BY JUSTIN FISHER & SCOTT SWEARINGEN

THE CFO'S ROLE IN PLANNING *a Company's Future*

When an owner considers the future – that is, his or her succession, retirement, or financial liquidity event – there is often one of two options:

1) Internal succession through the sale or transfer of ownership to the next generation of family, existing management, or the employees, or
2) Sale of the business to a third-party strategic or financial buyer.

Regardless of the direction, it's important for a company to not only maintain but also increase its value to stay competitive. Equally important is to ensure the right people are leading the charge to prepare management for ownership.

While PMs are often viewed as future owners who need to be developed, a CFO should be seen as the bridge between operations and finance. As a financial participant who understands internal processes, a CFO can help develop the right people as well as knowledge of sales, growth, and revenue. A CFO has a unique view of operations that helps identify the people who are thriving within various departments as well as the business as a whole.

Build Value

Grow Talent

An effective way to build value in any organization – especially one that's privately held – is to attract, develop, and retain talent by engaging and motivating them. In a time when being progressive is often the key to retaining talent, contractors will need to find nontraditional ways to stay competitive and attractive to younger workers, in addition to bringing disenfranchised workers back to the industry.

Bridge the Gap

All too often, companies neglect to focus on people or succession as they relate to workforce demographics. If a company's management team has an average age of 65, then that team may have a difficult time making a cultural connection with its Millennial workforce. All the while, that younger, very qualified workforce wants a transparent, collaborative, free-flowing environment; if that environment doesn't exist, then it creates doubt about whether there's opportunity for a younger leader to move forward. The gap between that up-and-coming leader and management is simply too big.

In addition to not attracting or losing good people, there's a lot at stake if management doesn't have a clear succession plan or vision for how it plans to manage that middle gap. When people start to leave, a company is left with loyalty and morale issues, and competitiveness in the marketplace and profitability can take a hit.

Prioritize Progress

While it might seem daunting, breaking away from tradition can be a positive turning point. Take flexible scheduling as one example: While it's popular among some firms, contractors historically start work early, and the culture of construction emphasizes being physically at your desk or on-site rather than flexible work hours.

The Importance of **Succession Planning**

A plan helps build a lasting legacy for the company, an owner's family, and employees. Additionally, a plan can eliminate the sense of uncertainty with employees who desire stability and vision for the future.

For privately held firms, it's central to the longevity of the business. Part of any long-term plan is understanding how a company can compete further down the line. If strategic planning around management is done properly – and early – there are many benefits, such as:

- Providing owners control over their legacy and the future of their business
- Building a leadership pipeline
- Incentivizing employees and key managers
- Modernizing the organization's approach to its people
- Boosting competitiveness in the marketplace
- Increasing future value of the business
- Achieving long-term goals
- Informing lenders and other stakeholders who seek assurance of business continuity

To stay competitive with its staff and those looking to join, management might consider these types of initiatives:

- Telecommuting and other flexible schedule options for qualifying employees
- Open-concept offices
- Revamped internship program that carefully considers how to onboard new people
- Investments in workforce development and early education that lead to construction industry careers
- Alumni programs to stay connected with former employees

Plan Preparation

Once an owner begins to think about succession planning, a CFO must consider numerous factors related to the business and personal finances and legacy. Planning starts with written goals and a schedule to track progress and guide decisions for when an owner anticipates stepping away from the business.

Next, identify successor candidates, evaluate their strengths and weaknesses, and benchmark them against an inventory of the ideal skills, talents, and abilities required for a management position. This will clarify the action steps – such as training, mentoring, or personnel changes – needed to build the new management team.

Prepare for Ownership

CFOs typically help management understand the financial picture of projects and communicate how the company is doing over time. They understand the internal processes – skills that new owners, or those preparing for ownership, must acquire.

In this regard, CFOs are well suited to advise owners on the training needed as well as the personal and business aspects of succession. Beyond providing straight financial analysis, a CFO can pose strategic questions that can help secure the company's future:

- What growth trajectory do we want to achieve over the next 5-10 years, and how do we get there?
- How are we thinking about disruption in our markets to aide our growth?
- How and where will we source talent over the next 5-10 years?
- What technology will we need across our enterprise to disrupt in our markets and achieve our growth targets?
- How will our brand evolve to connect with future employees and a changing customer base?

Preparing for Transaction

While many CFOs may have experience with succession transactions, not all business owners and managers do. CFOs can help prepare these leaders for what will take place in a transaction.

As an example, a CFO can assist the management team by leading it throughout the due diligence transaction process. In particular, a CFO can share with owners and managers what a potential buyer looks for – something of which they might not be aware.

Through this critical process, current and future owners can gain a complete picture of the business and how an external buyer will assess value in such areas as business finances, forecasts, cash flow, contracts, marketing efforts and branding, customer base, people, and management strengths and processes.

Plan Formation

The five elements of succession planning focus on: business financial planning, personal financial planning, management succession planning, estate planning, and ownership transition planning.

A CFO is often the person within a company who has insight into each of these elements. Within each element are practical approaches a CFO can take to initiate a conversation or action. As a link between the business owner, the business, the advisory team, and the next generation owner, a CFO plays a key role in connecting all of the elements together in the succession plan.

Business Financial Planning

Without a succession plan in place, it's difficult to realize the value of a company's greatest asset – a quality workforce and management team, which is a major indication of enterprise value.

It's important to consider a company's long-term vision and how succession fits into that plan. CFOs should discuss the answers to strategic long-term questions with the owner or CEO. A CFO can jump-start the succession conversation with such questions as:

- Does our company have the right people in the right positions?
- Are there holes that need to be developed and filled from within? Or is it better to find someone from the outside?
- Is compensation for our key personnel competitive in the market?
- Do our top managers want to be part of the business's future? If not, how can we build a culture where key personnel want to stay? (This will help drive our long-term success as well as economic viability of overall transition planning.)
- Does our company have an effective coaching and mentoring philosophy and program with adequate training opportunities?
- If needed, what's the financial statement capacity for leveraging a succession plan?

Personal Financial Planning

While a CFO is often defined as a senior executive who oversees the financial actions of a company, don't underestimate the value of a CFO's insight when it comes to advising owners on personal finances. He or she can help ensure an owner has sufficient personal liquidity and net worth to tend to his or her family's needs and interests after stepping down.

Closely held business owners tend to keep two balance sheets that are intermingled – the business books and their personal financial statement. The CFO often plays a critical role in the interconnectivity and flow of assets between both balance sheets, and can help the owner assess transparency and risk.

Transparency

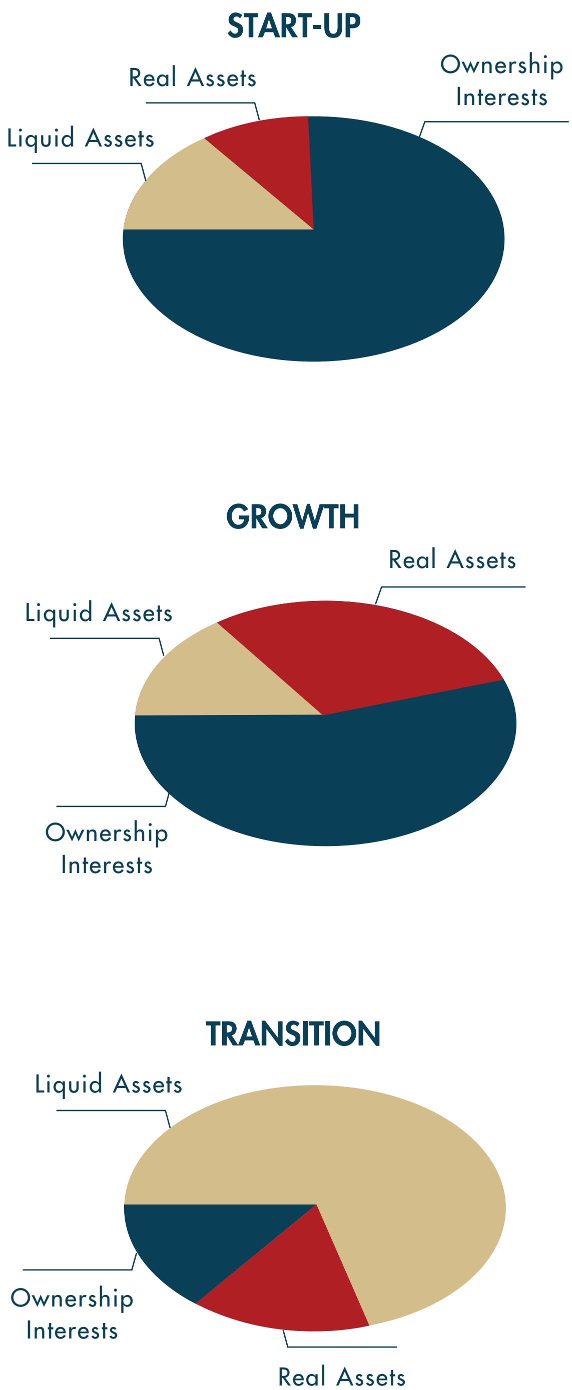
Owners are most interested in the value of their assets and the cash flow these assets are generating. CFOs can play a huge role in helping owners clearly assess value and cash flow that's being generated by their comprehensive asset base, which helps owners make a comparison decision between assets. Questions a CFO can ask include:

- If an owner holds a raw piece of land, how is it appreciating over time?
- What are the expectations for that asset, and is the owner achieving those expectations?
- What are the capitalization rates – the cash flow being generated and value – of the real estate assets, and what are the expectations for those rates over time?

Risk

Regardless of whether a company is in the start-up, growth, maturity, or transition phase, all owners hold three buckets of wealth: liquid assets, real assets, and ownership interests. CFOs can help owners evaluate risk across this asset base so they can determine how to reallocate the cash flow.

Wealth Allocation for **Business Owners**



If owners can assess risk at any point in time, then they can make educated decisions to reallocate cash that is generated back into assets to fit the overall risk profile. Continual rebalancing or asset redeployment is not only normal, but also important for the company.

Management Succession Planning

The foundation of a company's growth and legacy hinges on having quality employees to enhance long-term performance, value, and transferability. The CFO is uniquely positioned to look at the leadership matrix and succession in each key position to understand who's ready to move up to the next spot.

Historically, the industry has offered a limited talent pool. Creating opportunity for employees and keeping them engaged and motivated is a critical role for everyone on the executive team, including the CFO. Build a culture where the organization is willing to promote from within and offer opportunities and responsibility.

Once you've identified who to groom for ownership, keep in mind that this transition is a big step. It's no longer about getting concrete poured at one job or keeping a project on schedule. Through training and mentoring with a CFO, potential owners can begin to shift their focus to a company's overall financial health.

This might include:

- Keeping salaries competitive
- Looking at the financial feasibility of leases
- Reading and understanding the financial statements, including the balance sheet, income statement, and statement of cash flows
- Knowing what to consider when assessing financial health
- Being aware of requirements or red flags for bonding, surety, or banking
- Grasping cash flow and entity structure
- Understanding income tax

During this phase, collaboration is also an important option. A CFO might consider joining or assembling an advisory board of CFOs outside the industry to share ideas on how to innovate and handle disruptions. Being involved in a peer network outside of construction allows CFOs to expand their resources and business acumen in order to be more effective in such areas as technology trends, disruption, or strategic planning.

In addition, expanding a peer network within the construction industry (e.g., through construction associations) can further benefit CFOs by taking such general topics to a more granular level and adapting them to their needs in construction.

An outside advisor can also provide additional data, help counsel the team, and discuss options with the owners.

Estate Planning

An estate's prosperity depends on much more than accumulating wealth. Taxes, family issues, fairness, asset protection, and effective wealth transfer factor heavily into estate planning decisions. Usually tapped for the business aspects of succession, CFOs are well suited to advise owners on the personal aspect of planning for the family legacy while helping to reduce the estate tax burden.

Ownership Transition Planning

There are five key factors that shape an ownership succession plan, all of which can be overseen by a CFO:

1) *Understanding choices* – A plan begins with identifying potential successors, which might include current management, family, or third-party purchasers.

2) *Integrating personal and business goals* – This starts with defining priorities and developing a strategy to incorporate the business and personal financial plans and goals.

3) *Maximizing value* – Many owners have no idea how much money they'll need upon the transfer of their business ownership. They also have unrealistic expectations about how much their business is actually worth.

4) *Coordinating with the estate plan* – A detailed analysis of a company's strengths and weaknesses will yield valuable insight for increasing cash flow, reducing risk, and creating a solid foundation for growth. Recommendations based on this information will complement planned transition objectives.

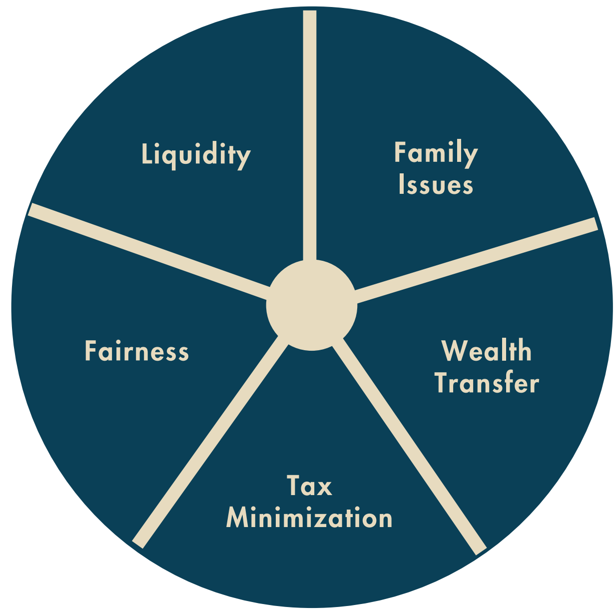
5) *Achieving liquidity* – This ensures an owner has the money needed for retirement and their desired lifestyle.

External Considerations

Potential Legislation Changes

Congress is currently discussing eliminating minority interest discounts for transitioning family-owned businesses. An IRS hearing on proposed regulations in IRC § 2704 took place in December 2016. If it isn't blocked, it will likely take effect in

Five Factors of
Estate Planning



Five Factors of Ownership
Transition Planning

early 2017. However, there's more uncertainty with the timing of these regulations considering President Trump's pending tax proposal to eliminate the federal estate tax.

It's critical for CFOs or owners to reach out to their tax professional to assess how these changes might affect them. If owners are considering making a transfer, then they may want to complete it prior to the new regulation becoming final. If the proposed regulations become law, the owner's family could pay more in estate taxes in the long term if mitigating steps aren't taken.

Market Factors

From a construction standpoint, there are limits to merger and acquisition (M&A) activity. At any time, a construction company can have contracts in place that last anywhere from six months to five years (or longer); replenishing these contracts creates a continuous backlog.

A strategic or financial buyer will focus on when those contracts run out and if there's any assurance they'll be replaced. Contracts being replenished often come down to who has a relationship. Management and people with those key relationships create value. It's important to replicate and improve on what they've done in the past.

Start Planning Today

First, begin by forming the strategic and business plan as well as setting goals for both the owners and the company. Some questions to jump-start this process:

- What does ownership want to accomplish?
- What are its goals?
- What are the business goals over the same time period?
- Does the strategic and business plan allow for congruency?

Ultimately, look at the business goals and objectives to determine what can be achieved over the near and longer term.

Then, make some business projections. Look at the marketplace and the company's financial position. Develop at least three possible future outcomes: aggressive, conservative, and moderate. Identify what levers influence achievement of one more than the other. Also consider if the workforce can accomplish set goals.

Finally, set definitive goals. Offering diversified experiences for employees creates value in different ways. While the adjustment period might be a little painful, shaking things up can ultimately help a company achieve its business goals.

Conclusion

While many business owners avoid important succession issues due to their sensitive nature (e.g., family dynamics, legacy, retirement, or mortality), an effective plan can be good for both the owner and the company.

When CFOs begin to lead these conversations and ask questions, it might feel uncomfortable at first, but that's when the opportunity for improvement is at its peak. ■

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