Family Business Succession and Transfers: Challenges and Opportunities

EFB
EUROPEAN FAMILY BUSINESSES

Family Businesses are the Backbone of the Economy

Family businesses (FBs) make up more than 70-80% of all European companies, encompassing a vast range of firms of different sizes and from different sectors. Most SMEs (especially micro and small enterprises) are FBs and a large majority of family companies are SMEs. FBs also account for an important part (about 40 % - 50 %) of European employment. FBs are active in all sectors of the economy. Nevertheless, studies have shown that FBs are more prevalent in traditional and labour-intensive sectors such as agriculture, manufacturing/crafts, construction, tourism, or retail trade. FBs are important, not only because essential economic contribution, but also because of their values which form their DNA. FBs bring long-term stability through their commitment to local communities, and the responsibility they feel as owners to society as a whole. FBs focus on long-term sustainability of the firm rather than the realization of short-term profits.

The Transfer of Business

The European Commission estimates that 450.000 enterprises, representing 2 million jobs are transferred yearly in Europe. There is clearly a huge stake for society that these transfers are managed successfully. In light of growing evidence, the issue of business transfers has been steadily growing in significance:

1. In 1994, the European Commission publishes recommendations on the Transfer of SMEs[1] - it clearly recognises that Member States should prioritise family succession. The recommendations encourage the Member States to:

- ✓ ***ensure the successful transfer within a family by seeing that inheritance or gift taxes do not endanger the survival of the business,***
- ✓ ***encourage the owner, through taxation measures, to pass on his business by selling it or by transferring it to the employees, particularly when there is no successor in the family.***

2. In 1998, the Commission encouraged Member States in a second communication to increase their efforts[2];
3. In 2006, the EC releases communication Transfer of Businesses - Continuity through a new beginning[3];
4. In 2009, the first ever expert group on family businesses publishes it recommendations - the importance of business transfers features throughout[4];
5. In 2012 a dedicated expert group on business transfers is assembled;
6. In 2013, European Commission Entrepreneurship 2020 Action Plan[5] states that, **'Transferring a business from one generation to the next is the defining feature of a family business and the greatest challenge that it can face;**

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[1] http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:31994H1069&from=EN
[2] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31998Y0328(01)&from=EN
[3] http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52006DC0117&from=EN
[4] http://ec.europa.eu/DocsRoom/documents/10388/attachments/1/translations
[5] https://ec.europa.eu/growth/smes/promoting-entrepreneurship/action-plan_en

7. In 2015, the European Parliament resolution on 'Family Businesses in Europe'[6] calls for the improvement of the business transfer environment;
8. In 2017, a dedicated conference on this issue was organised during the Maltese Presidency.
9. In 2018, the OECD ministerial gathering on SMEs, discussed the issue of Business transfers, and in particular the issues surrounding family Business transfers[7].

Family Business and Succession

Family businesses, as all business entities, face challenges - one in particular stands out as the most important. 'The transfer of business ownership, together with the transfer of management from one generation to the next, is the greatest possible challenge facing family businesses'[8]. A family business transfer must be **considered as, not only a transfer of management, but a transfer of ownership,** where that ownership is not a liquid asset but something which is built up and developed by the family over generations, including values, traditions and know how. As a result, because of the inherent complexity of family business succession, it is crucially important that the environment, where the transfer takes place, gives a family business the best chance of survival.

How to support Family Business Transfers

As mentioned above, the institutional recognition of business transfers, and its gradual rise in importance, has made a difference. Significant regulatory improvements have been made for family businesses in Europe. They enjoy more support from experts and dedicated organizations when they go through the transfer process. But, despite all the progress, it is obvious that significant improvements can be made to the transfer of business environment for family businesses. Below EFB underlines the most important issues that need to be addressed by policy makers to facilitate the transfer process for family companies in Europe.

1. Family business transfers must be recognised

The transfer of business is not just about buying and selling. Family business transfers for the potential they represent to the European economy, must not be ignored.

EFB recognises that the transfer of business is not limited to family succession. When a business is not transferable to family members, for any myriad of reasons, the transfer to employees or a third party is necessary. But, in many Member States family succession remains the predominant form of transfer, and as such, must be supported accordingly.

The European Commission must continue to communicate to national administrations, and internally, the importance of family businesses and the need for them to receive effective support when they go through a transfer.

[6] http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P8-TA-2015-0290+0+DOC+XML+V0//EN&language=EN
[7] http://www.oecd.org/cfe/smes/ministerial/
[8] http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+REPORT+A8-2015-0223+0+DOC+XML+V0//EN

2. The tax and regulatory framework must not hinder family business succession

In 2014[9] and 2016[10], EFB, in conjunction with KPMG, demonstrated that the fiscal environment, when it comes to transferring ownership, is highly complex. The analysis showed that there is a lack of consistency across Europe in the levying of tax and that, in certain Member States, it is essential to be 'tax literate' (those who are aware of exemptions and reliefs and that qualify for them) to give your family business the best chance of survival.

In addition, inheritance and gift taxes might create a substantial disadvantage for family businesses that have a long-term outlook. The different tax treatment of inheritance and retirement can also lead to changes to the families' behaviours. For example, the leaders of family businesses may hold on to control of the business for tax reasons, which can be frustrating for the next generation and act as a constraint on business growth.

Furthermore, in those instances where families and businesses have to fund tax liabilities arising as a result of events which are inevitable, and which result in no economic return to them, it is imperative that the **fiscal and administrative burden is proportionate to the associate risk of loss of activity for local communities**. Often, financial resources have to be used to fund these liabilities resulting in less money for future business investment. Investment of course drives increased employment and growth, key issues for all governments and economies.

As such, the European Commission is the ideal institution to monitor and review the legal, administrative, and fiscal environment that surround family business transfers across Europe. It should perform regular appraisals and it should submit recommendations to Member States when necessary. This could be done under the European Semester. In addition, under the justification for the better functioning of the Single Market, the European Commission should monitor the transfer of business situation in the cross-border context.

3. Accurate yearly data must be compiled on the transfer of business situation

As mentioned previously, data on the business transfers is sorely lacking. This can be equated to the fact that data on ownership is also limited, and as a result, tracking ownership evolution is complicated.

Policy makers are fully aware of this problem; the commissioned report for the Business Transfer Expert Group highlighted the need for accurate data on the Transfer of Business at the EU Level. Without this crucial insight informed decisions and policies are hard to make.

The European Commission should launch a pilot scheme to capture data surrounding the transfer of business situation in Europe, with the hope of creating a permanent data programme in the Member States.

4. The dissemination of best practices must be improved between Member States

[9] http://www.europeanfamilybusinesses.eu/publications/40/29/European-Family-Businesses-Tax-Monitor-2014 (ANNEX 1)
[10] idem

Many excellent best practices exist and have been outlined by the European Union to aid family business transfers. However, more must be done to promote exchanges of best practices between Member States to ensure that companies are not needlessly lost.

The Commission should create and moderate a permanent forum to increase the exchange of knowledge and experiences between public administrations and family-business-related institutions (such as associations and academic research institutes) in different Member States. This tool would be used both for the exchange of best practices, and for the promotion of new policy making initiatives at the European level.

5. More support is needed to help family businesses better prepare their transfers

A **transfer is not a single event, but a process** that must absolutely be planned in advance in order to succeed. As mentioned previously, EFB's Tax Monitor highlighted this necessity. Early planning is also needed to ensure that the successor has the necessary skills and motivation to continue the business.

In addition, family businesses all too often do not have access to the expertise that is required to prepare and initiate a transfer. This also applies to the non-technical components of the transfer (family communication, family expectations, family values, family competencies, family dynamics, etc.) which are just as important as the technical issues of a transfer (taxes, et cetera.)

The European Commission should continue to act as the catalyst to ensure that family business owners are made aware of the resources and tools that are available to them to better prepare their transfers. Member States must enact national action plans to facilitate the transfer of business

European Family Businesses is a EU Federation of 14 national associations representing family owned companies. Our members represent a turnover of more than one trillion Euros, over 9% of the European GDP. We strive to raise awareness about the crucial role of family businesses in the European economy by pressing for policies that put family owned companies on a level playing field with other companies, and policies that favour and promote long term responsible ownership. Our field of interests include: the transfer of business; debt and equity financing; access to finance; gift and inheritance tax; growth; succession planning; entrepreneurship education; the future of Europe.

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ANNEX I

Figure 1a: Tax due without exemptions based on December 2013 rates

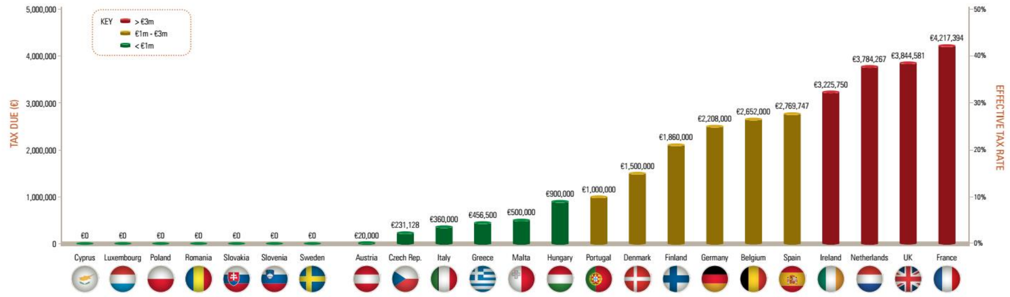

Figure 1b: Tax due with exemptions based on December 2013 rates

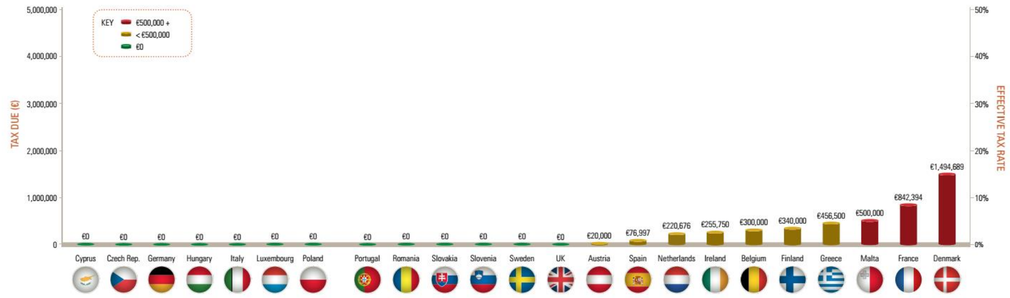

Figure 2a: Tax due without exemptions based on December 2013 rates

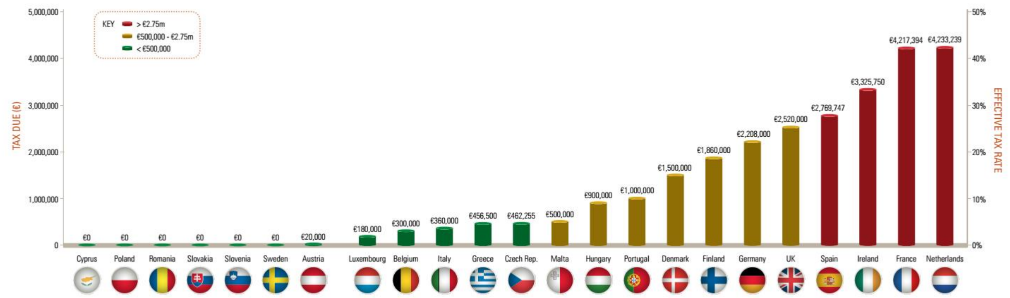

Figure 2b: Tax due with exemptions based on December 2013 rates