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Obstacles and Challenges of Business Succession in Central Europe

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ABSTRACT

The transfer of a business to the next generation is a very important issue entailing several different social and economic influences. Failed business successions cause a loss of jobs, company knowledge and innovation potential. Creating an environment where business transfer is supported should therefore be of major importance for company owners and for policy makers. For better succession planning it is important to know the obstacles and challenges associated with business succession. Especially Eastern European countries face many challenges as these countries have no experience in business succession. To analyze the obstacles and challenges of business succession in Central Europe, three Eastern countries (CZ, SK and PL) with no experience in business succession were analyzed and compared to Austria where half of family businesses are at least in their second generation. Literature analysis and two focus groups with stakeholders (local public authorities and private entrepreneurs) were undertaken in all four countries. The results show that one of the main obstacles and challenges for business succession is the absence of a successor. Especially in Austria, this is recognized as the main obstacle. The Eastern countries (CZ, SK and PL) face different challenges to Austria that can mainly be explained by the lack of experience and supporting schemes for business succession. Especially knowledge and awareness related obstacles play an important role in Eastern European countries. Business succession is an individual process involving many emotions; therefore psychological and social issues are perceived as a huge obstacle in each analyzed country. Austria has a lot of experience with successful business transfers and offers various support mechanisms. However, many similar problems to Eastern countries were detected. A change of the business succession environment and the raising of awareness of the topic is therefore necessary in all investigated countries.

1. Introduction

One of the biggest challenges for family-owned businesses is the intergenerational transfer (Griffeth et al. 2006). The transfer from one generation to the next is becoming more important due to the ageing population in most industrialized countries (Levesque and Minniti 2011).

Each year about 450,000 firms are transferred affecting two million employees in Europe. Another 150,000 companies are not transferred due to system inefficiencies (European Commission 2011). If business takeovers fail or do not take place due to the absence of successors, the business will cease causing a loss of economic business value, employment, entrepreneurial experience and economic growth (Block et al. 2013). Business succession is therefore one of the key issues studied in the family business field (Sharma 2004; Zahra & Sharma 2004). One of the main challenges in analyzing business succession is the complexity of the topic. Business succession encompasses top-level management, legal and financial considerations, social/psychological factors, leadership development, and exit strategies (Jacobs 2006). Another point is that entrepreneurs usually have no personal experiences in business succession as it is a "once in a lifetime" experience (Viljamaa et al. 2015). Early planning and preparation (Sharma et al. 2003) as well as a well- developed business succession environment are necessary for a successful and easy ownership transfer (Viljamaa et al. 2015).

Countries in Eastern Europe have not yet developed a business succession environment mainly due to historical reasons. Business owners in Eastern Europe who established their business in the 1990s and now want pass on their business have no support mechanisms available. However, also in Western countries with well-established support mechanisms many obstacles and challenges occur during business succession.
The main objective of this study is to identify the obstacles and challenges of business transfers in four different Central European countries. Austria is chosen as a country due to the

experience and available support mechanisms in business succession. The Eastern countries of the Czech Republic, Slovakia and Poland were chosen as these countries have economically strong SMEs but no experience in business succession. This paper analyzes if these countries have identified the same obstacles and challenges and if these are perceived with a similar relevance in each country.

2. Research Methodology

This study concentrates on business succession in small and medium sized companies. We define business succession according to Jacobs (2006, pp. 326–327) as:

"… the transfer of a business that results from the owner's wish to retire or to leave the business for some other reason. The succession can involve a transfer to members of the owner's family, employees, or external buyers."

Austria represents a Central European country with a great deal of experience in business succession and several available and well-established mechanisms which support business succession. The results of this country will be compared to Eastern countries in particular the Czech Republic, Slovakia and Poland.

Thom and Zaugg (2005) identified nine possible succession alternatives such as family internal transfer, company lease, management buy-out, management buy in and so on. For this study we do not differentiate between different succession forms but rather analyze general obstacles and challenges in Austria, the Czech Republic, Slovakia and Poland. For this study, a literature analysis was done to identify the main obstacles and challenges related to business succession. Based on this literature review a guideline was created. This guideline was used for two focus groups with relevant stakeholders in each country. The focus groups were separated in meetings with representatives from local public authorities and entrepreneurs experienced in business succession. The discussions were recorded, transcribed and analyzed in order to answer the research questions. This was done in order to find out obstacles and challenges in different European countries. In particular, the research questions are:

RQ1: What are the obstacles and challenges for business succession in Austria?

RQ2: What are the differences in obstacles and challenges for business succession in Austria and in the Czech Republic, Slovakia and Poland?

3. Status Quo of Business Succession in Europe

In Central Europe, "start-ups" are far more popular than taking over an existing business Figure 1 shows that on average in the EU-27, a majority would rather set up a new business (54%), while more than a quarter (28%) would favor taking over an existing business" (Eurobarometer 2012). A trend can be seen between Western and Eastern countries. The countries with the lowest proportion of people not willing to set up their own business are Germany (40%) and Austria (43%). More than three out of 10 respondents say they would rather take over an existing business in 12 Member States, with the most people favoring this alternative in Austria (40%) and Germany (39%).

"If you currently had the means to start your own business, including sufficient funding, would you rather set up a new one or take over an existing one?"

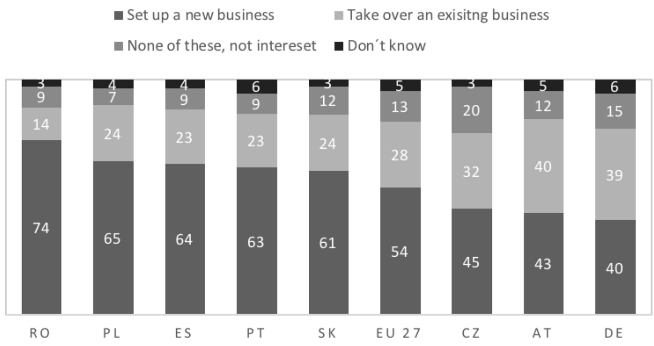

Figure 1: Proportion of people who would rather set up a new business than take over an existing one in selected European countries; Total number of respondents: 42,080
Source: Slightly modified with all information from Flash Eurobarometer 2012

While the German speaking nations have the highest proportion of people who would rather take over a business than set up a new one, the eastern countries Poland and Slovakia have one of the highest proportions of people who would rather set up a new business. However, the Czech Republic is rather similar to Austria and Germany with 32 % of the respondent ready to take over an existing company and 45 % who would rather set up a new business. (Flash Eurobarometer 2012). In the Czech Republic, an increase of 13 % of people willing to take over an existing business occurred from 2009 to 2012. The number of people not interested in any business is quite high in the Czech Republic.

3.1 Austria

About 90% of Austrian companies are family businesses. Half of these family businesses are in their first generation, 20 % are in their third generation, 20 % are in the third or even fourth generation and 10 % of the family businesses are a mixture of different generations (BMWFW 2014).

This shows that many business transfers were successful in Austria. Most of the transferors and successors are generally satisfied with the environment for business succession in Austria. However, according to a survey from 2014, finding a new suitable successor is very difficult. The survey also mentions administrative and tax related burdens as very challenging. (Ziniel et al. 2014)

3.2 Czech Republic

In the Czech Republic, the topic of succession is new and started to be actively discussed around 2015 (Navláčil 2016). The main reason for this is that most family businesses were founded after the collapse of communism about 25 years ago. This is the main reason for the absence of business succession mechanisms in all former communist European countries These business founders are approaching retirement age in recent years and are experiencing the first generation of exchanges (Weikert 2015; Deloitte Česká republika 2014).

Every fifth company is a family business and accounts for more than a quarter of the GDP of the Czech Republic (Navláčil 2016). About 2/3 of the companies face the challenge of business transfer within the next five years. The process of handing over the company often takes more than two years. The majority of company owners (2/3) want to hand over the business to a family member. (AMSP ČR 2016).

3.3 Slovakia

Almost all Slovakian registered active businesses are small and medium sized enterprises (99.9 %). The majority of the SMEs are micro-enterprises with 0-9 employees providing employment for nearly 75 % of the active workforce and account for more than 50 % of gross output and value added. (Statistical Office SR)

Slovakian family businesses are in a period when they are mostly undergoing or preparing for the first generational exchange. A survey of family businesses in Slovakia by PwC shows that only one third of businesses will handle this generation exchange process successfully. (Krošláková 2014)

3.4 Poland

In Poland, 68 % of the enterprises can be defined as family businesses. Due to systemic transformation (from a centralized economy to a market economy), Polish family businesses are mainly the effect of the functioning of the economy over the last 25 years and their managers are actually the first generation of entrepreneurs. (PARP 2014)

4. Obstacles and Challenges of Business Succession in Central Europe

The literature analysis revealed that multi-dimensional problems occur involving personnel management, law, financial, organizational and psychological factors (Thom and Zaugg 2005). Therefore, this paper classifies the obstacles and challenges into four different fields related to:

- Management and knowledge
- Social issues
- Economic and financial issues
- Governance and legislation

The stakeholders from public authorities and those from companies experienced with business succession identified similar obstacles and challenges in their countries. The main obstacles and challenges in each country are listed in Table 1.

Table 1: Obstacles and challenges of business succession in four different Central European countries

Obstacles & challenges related to …	AT	CZ	SK	PL
Management/ knowledge	Absence of successor	No available market for succession; no knowledge due to lack of experience	Absence of successor, limited knowledge due to lack of experience	No awareness of the topic; no knowledge due to lack of experience
Social	Lack of Communication	Different values between generations	Problem of “letting go” of the seniors	Different values between generations
Finances	Wish for more financial support mechanisms	Minor importance	Minor importance	Minor importance
Governance/ legislation	Too many regulations which change frequently	Minor importance	The whole system does not support business succession	Many legislative barriers

4.1 Management and Knowledge Related Obstacles

Overall, in all the analyzed countries one of the most crucial obstacles is the absence of a possible successor. Although Austria has EU- wide the highest proportion of people willing to take over an existing business (Figure 1, Flash Eurobarometer 2012), “finding a potential successor” is the main obstacle and challenge in Austria.

Local Austrian authorities mentioned that the absence of a potential successor has far- reaching consequences for the company and the economic situation of the country. Those entrepreneurs who have a potential successor and know that their company will survive behave differently along the life cycle of a company to those who have problems finding a successor. In Austria, there is a problem that “older” companies are not innovative any more mostly due to lack of investment. A logical consequence of an entrepreneur not having a successor is that they stop investment as they might have to close their company and the investment will disappear. Investment increases the value of a company, however, very often people are not willing to pay these costs and it can turn to an uneconomic situation for senior entrepreneurs. Those entrepreneurs who have a successor aim to handover a stable company and continue with investment and are more open to innovations.

As the Eastern European countries do not have much experience in transferring companies to the next generation, it might not be as obvious as it is in Austria that a lack of a successor leads to a high degree of investment and innovation lack in the life cycle of a company. However, it can be assumed that this is also true for Eastern countries.

In the Czech Republic people think that a reason for the absence of a potential successor is the fact that there is no market in which to sell the (family) company. The situation in Austria shows that setting up a market for business transfers is a useful tool but will not solve the problem of having no successor. (ENTER- transfer 2017a) There is a huge difference between Western (Austria) and Eastern European countries (CZ, SK and PL). In Austria, entrepreneurs and local authorities do not see any problem in the education and knowledge of the young generation. It is a common opinion that the young generation was never as well educated as nowadays. The only "knowledge" related problems in Austria is that children are so well educated and keen on gaining knowledge and experience it is difficult to keep them in the family business. However, this can also have a positive influence as many descendants work many years in different companies and gain valuable experience they would not have acquired in their family business. Many of the children decide to take over the family business at a later stage based on their own decision.

However, social obstacles can result from the increased knowledge of the young generation. An Austrian stakeholder mentioned:

"We are the first generation senior entrepreneurs who can learn even more from the young generation than the young from the old. The main reason for this is of course digitalization in which young people are generally more sophisticated. However, naturally, this is not easy to accept for the older generation who grew up believing that knowledge is mostly gained through life experience."

In the Czech Republic, the situation of knowledge related obstacles is very different to Austria. Stakeholders think that it is a huge challenge to find highly skilled successors (in their own family and for hired management). The main reason for this is that there is no history in management education and training. (ENTER- transfer 2017a) A study also mentioned that it is a huge barrier that there are no schools focusing on family businesses in the Czech Republic (AMSP ČR 2016).

In Poland the lack of awareness and knowledge of entrepreneurs and governmental about business succession is one of the main obstacles. An additional problem is that Polish family business owners have a distrust of external people (i.e. managers, advisers and experts) and low interest in external training. Additionally, there are almost no external "advisors" available in Poland. (ENTER- transfer 2017c)

Similar to the Czech Republic, stakeholders are worried that the children of entrepreneurs may not have enough competences to take over and maintain the business in Poland.

4.2 Social Obstacles

An entrepreneur defines his company very often as his "life's work" which easily makes it clear that many emotions are involved in handing over a company.

Negative tensions in the relationship between successor and transferors are one of the main reasons for a failed business succession. The mutual respect of the business partner and also the relationship to other involved persons in the succession must be considered during a succession process. Also, the desires as human being and business person must be considered. (Baumgartner 2009; Ziniel et al. 2014)

Harmony within the family is one of the most critical factors during business succession. Most old entrepreneurs wish that their (established) business stays within the family in all analyzed countries. Sometimes the will and the competences of the descendants are only of minor importance for the transferor. An early succession planning therefore is of high importance as it allows the descendant much time to think about their motivation and gain extra knowledge but also to find other suitable candidates. Besides early planning of succession, open communication is of special importance in family internal succession. Open communication before and during the planning of the succession is the basis of a good family harmony and the success of the transfer.

In Poland, senior owners do not want to consider succession in their companies as they think they still have time and they want to do everything by themselves. In their point of view they are still able to work and they postpone the moment of the succession further and further. When the moment comes, it is already too late, because the children do not want to take over family business in Poland. (ENTER- transfer 2017c)

A common challenge in family businesses discussed by Czech stakeholders was the struggle to distinguish between company management and family life. Some participants mentioned that owners of larger companies often have difficulties to fulfil their responsibilities as parents. In the Czech Republic, companies experience conflicts between generations as a huge obstacle. The main underlying reasons are different values, life styles, and expectations of the different generations. The "young" generation prefers group decisions, focuses more on human resources and on motivation. The senior generation has applied a totally different management style as they founded their companies mostly in the 1990s when it was necessary to have an aggressive, goal-oriented, focused and straightforward management in the Czech Republic. The huge differences between the young and the old generations were intensively discussed in the Czech Republic but only mentioned as an aside in other countries. However, the differences between generations are similar worldwide. The desire for a great "work life" balance and the importance of "time for themselves" is not just a trend in the Czech Republic- this trend can be seen worldwide. (ENTER- transfer 2017a)

Also in Slovakia, different values between generations was observed as huge challenge (ENTER- transfer 2017 b). Another social/psychological obstacle is that companies are often identified with the owner. After a succession the new owner is not always accepted by the employees and/or business partners. An additional problem is that the senior owner does not always leave the company and still has influence. Many successors in Central Europe feel they are the owner without management power. However, some entrepreneurs also think it is very beneficial if the senior owner supports the new owner in the family business.

4.3 Economic and Financial Obstacles

Economic and financial issues were not perceived as obstacles in the eastern countries (CZ, SK and PL). The companies usually utilize tax and financial advisory services assisting the process of succession.

In Austria, the public authorities discussed the importance of financial support intensively. They argued that the state has to provide more financial support especially if it comes to external succession. It is a fact that even small companies easily have a value of a few million Euros. The owner cannot and is not willing to give away the company below its value. However, an average person cannot usually raise such a large amount of money and/or is not willing to take the risk for such a high monetary value. This is one of the main reasons that successors are difficult to find in Austria. Family successors see no financial or economic obstacles in the transfer of the business, if it is a gift or inherited. There are no inheritance taxes in Austria.

4.4 Governance and Legislation Related Obstacles

The obstacles from governance and the legislative side were similar in the Eastern countries. In Austria, very different obstacles to these issues were found. The main reason for this difference is the absence of mechanisms due to the lack of experience in Eastern European countries.

Stakeholders from Poland criticize their system relating business succession. One of the main criticisms is that successors entering the businesses activity must immediately fulfill all legal requirements etc. This discourages people from becoming successors. The local Polish authorities ask for a reduction of taxes in a specified timeframe, counselling of professionals and support from the EU funds, etc. From conversations with the owners of Polish family firms it appears that even more advanced forms of business (e.g. limited liability company) do not guarantee safe transfer of ownership and power. However, many owners do not take into account rules and mechanisms ensuring the smooth transfer of management. Therefore, Polish companies are neither from the organizational side nor from the legal side prepared for business succession. (ENTER- transfer 2017c)

In Slovakia, legislative barriers can cause many problems in family businesses. According to Act No. 82/2005 Coll. on illegal work, it is illegal if a family member assists an entrepreneur without an employment relationship, from which criminal liability is imposed on the entrepreneur. Only family members registered as students under the age of 26 or family members with the status of pensioner or pension insurance are legally allowed to assist in a company. This often leads to illegal work in an effort to avoid taxation, but strips the person of social and health insurance, work benefits and support and other positive aspects of legal employment.

It is also criticized that "family businesses" are not a legal type of business in Slovakia. It is argued that substantial public support cannot be expected for the category of family businesses. On the other hand, some support is planned from the EU Structural Funds under the forthcoming Operational Program Research and Innovation 2014-2020. (ENTER-transfer 2017 b)

In the Czech Republic, legislative obstacles were not seen as a major challenge. There are many law firms on the market assisting with business succession. Most Czech companies have already taken steps to address legislative issues in the future. However, some of the companies are not prepared for unexpected and unfortunate events, i.e. death or fatal injury of the owner. (ENTER- transfer 2017a)

The legislative and governmental obstacles are perceived very differently in Austria. Although Austria is the country with the most support mechanisms in this study, legislative issues are seen as a huge obstacle. Austria has an extremely high number of regulations which have to be fulfilled and can change quite frequently. If a business transfer takes place these regulations are controlled very strictly and owners can be liable to fines if they are not fulfilled. Such "over- regulations" were not discussed in the other countries.

Conclusion

Literature analysis and focus groups with relevant stakeholders revealed how difficult a successful business succession is. The main reason for this is the complexity of the topic and the individuality of the enterprises and their specific situations. It seems to become increasingly difficult the further east one goes in Europe. Stakeholders attending the focus groups in Poland and the Czech Republic mentioned that they believe it is much more difficult to transfer their business in Poland than in Western countries.

In Austria, the main obstacle is the absence of a potential successor. Compared to the Eastern countries, Austrians have a high degree of awareness of the challenges of business succession and feel well educated to manage a business. This is mainly due to the long tradition and experience of business succession and the variety of support mechanisms.

The different stakeholder groups (public authorities and private companies) had very similar opinions about the challenges of business succession in their country.

Eastern countries have a strong need to set up mechanisms supporting business transfer. However, as we can see in Austria, support mechanisms like transfer markets etc. are useful tools but cannot reduce all obstacles and challenges. The whole environment of business transfer must be changed and better awareness business succession is necessary in all countries.

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