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Succession Planning and Craft Brewers: Transitioning Your Legacy

You've spent the last 20 years working hard brewing great beer, providing a living for yourself and your employees, and establishing a conscientious reputation in the community. Now, you're starting to ask yourself, what's next? Or perhaps, how do I protect what I've worked so hard to build? Or, maybe you haven't been at this for 20 years, but you've been watching the increasing consolidation in the craft brewing industry and are wondering what it means for you. In either event, time spent focusing on your succession plan will be time well spent.

Recognize the Differences. A succession plan is a plan to transfer management responsibilities, legal control, and economic ownership to one or more successors upon your retirement, disability, or death. When you started your brewery, all three of these hats (management, control, and economic ownership) were likely worn by you. As discussed below, these hats can be worn by different people, which provides a great deal of flexibility in the succession planning process. (While the following discussion refers to stock, the same principles apply to membership interests in limited liability companies (LLCs)).

Give Yourself Time. Establishing an effective succession plan (particularly if it does not involve a sale to a strategic buyer or non-craft brewer) takes time. Allow yourself ten years for a smooth transition. With proper planning, a succession plan can protect your retirement income, promote family harmony, preserve your craft culture, retain key non-family managers, provide continued employment for your employees, facilitate a management buyout, and save taxes.

Keep It in the Family . . . or Not. A stumbling block for the owners of many closely held businesses is the desire to treat children equally. Treating children "fairly" is not the same thing as treating them "equally," and, in the closely-held business context, fair treatment is the recommended course.

If your children are too young for you to know whether they have any interest in your brewery, your succession plan should focus on selling the brewery to an outside party or identifying and retaining key non-family management personnel who can continue the brewery until your children are willing and able to run the brewery. Your plan should also include independent board members to serve as stewards of your legacy.

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If your children are willing and able to run the brewery, the focus of your succession plan will shift to transferring the brewery to your children at the lowest transfer cost, while ensuring your own financial comfort. If only one of your children is working in the brewery and if you have sufficient other assets in your estate, you could leave the brewery assets to the child who is active in the brewery and leave other assets of equivalent value to your other children. If your non-brewery assets are not sufficient to allow for such a division, options may include separating the non-operating assets (for example, real estate) from the brewery or having the child who is active in the brewery buy out the children who are not active in the brewery.

If you have multiple children working in the brewery, family dynamics may intensify other challenges the brewery is facing. A co-leadership structure is often impractical and unadvisable. Instead, control should be given to one child. In some cases, it may be possible to explore spin-off or split-up opportunities (for example, separating the distributorship from the brew pub).

If none of your children are interested in continuing the brewery, the brewery can be sold. Potential purchases include competitors or strategic buyers (including another craft brewer) (see Lucid Brewing's acquisition of American Sky Brewing, June 2015), key management personnel, an employee stock ownership plan ("ESOP") (see Left Hand Brewing, July 2015), local investors, or a noncraft brewer (see AB InBev's acquisition of Elysian Brewing, January 2015). In many cases, a sale does not have to be an all-or-nothing proposition and can, in fact, be a combination of these strategies (even if you are considering transferring part of your brewery to your children).

Who Will Manage Brewery Operations? Transferring management responsibilities is often the most difficult part of a succession plan. Establishing requirements for managers, evaluating and selecting successors, designing incentives to motivate nonfamily managers, and defining the role of nonfamily managers are all essential elements of a transfer of management responsibility.

Who Will Vote the Stock? Transferring legal control (i.e., the right to vote your stock) can take place in a variety of ways. You can immediately transfer voting control to a family member or an outside party by selling or gifting a majority of the voting stock, or some combination of the two. The transition of voting control can also happen gradually by selling or gifting the stock in minority increments over time.

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Before any transfer of stock occurs, the founder should execute a shareholders agreement. A well-drafted shareholders agreement will address a variety of issues, including stock transfer restrictions, planned and unplanned owner exits, stock valuation methodology, and drag along and tag along rights.

If you are not ready to transfer voting control, another option is to recapitalize your stock. When stock is recapitalized, voting and nonvoting shares are issued for each share of stock currently owned. You can then transfer the nonvoting stock to the new owners, while retaining voting control for yourself. You can also consolidate voting control by placing the voting stock in a voting trust or entering into a voting agreement with the other owners of voting stock.

Who Will Reap the Financial Rewards? The owners of stock (voting or nonvoting) are entitled to the economic benefits of that stock (e.g., S corporation distributions or C corporation dividends). Ownership can be outright or in a trust, which may be particularly desirable for asset protection purposes.

Protect Your Cash Flow. When transferring management responsibilities and/or stock, the founder's cash flow from the brewery will likely be a key consideration. Current sources of income for the founder may include salary, bonuses, S corporation distributions, C corporation dividends and partnership/LLC income. After the founder's employment by the brewery and/or stock ownership terminates, the founder's income may come from one or more of the following sources: rental payments (for real estate rental), salary continuation payments, consulting fees, deferred compensation, noncompete fees, and installment payments from a stock sale. A properly structured succession plan will take each of these into account.

Although there is a lot to consider in creating a succession plan, don't let it overwhelm you. The plan can be implemented in stages and will evolve over time, as your brewery does. The most important step is getting started.