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Thomas Schwarz
Grand Valley State University

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Will Your Family Business Survive to the Next Generation?

Thomas Schwarz, Ph.D., Director
Family-Owned Business Institute
Seidman School of Business



Family-owned businesses of all sizes are an integral part of our economic past, present, and future. They are the premier type of business form in the free world and a primary source of GDP, tax revenue, job creation, and the high quality of life we enjoy in the Greater Grand Rapids area. In spite of this significance, national statistics show that only 30% of family businesses survive past their first generation (Dyer, 1986) and that only 10 to 15% survive to a third generation (Applegate, 1994). This article outlines a process you can follow to increase the chances that your firm will continue to support your family and community for generations to come.

While a portion of the low succession rate may be attributed to the competitive challenges facing any business, family-owned or not, there are unique factors that family-owned businesses encounter. Facing these challenges in the same professional manner used in other business decision-making can strengthen the firm and enhance its ability to survive to succeeding generations. This process involves a 3-step approach: 1) becoming informed about the issues, 2) developing a multi-stage strategic plan, and 3) implementing and monitoring the plan with continued alignment.

Becoming Informed

Emerging competition; reduced barriers to entry through technological development; the globalization of markets; unpredictable regulatory, tax, and legal environments; and changing consumer/customer buying habits are common issues facing most firms today. Family-owned businesses face these issues in addition to others unique to family firms. Some of the more important issues are summarized in Table 1 (right).

One of the well-noted risks to family business survival is the transfer of leadership and/or ownership to the next generation. In a recent national survey of more than 3000 family-owned business owners, 42% of the CEOs expect the leadership of their firm to change hands in the next 5 years. Of that group, only one-third of these firms have written strategic plans outlining how this transition will take place (Arthur Andersen/Mass Mutual, 1997). What are the issues facing your family firm? Is the family unit strong? Are the offspring interested in joining the firm? Has adequate mentoring been in place over the years? Is there a plan for tax-advantaged ownership transfer and cash flow distributions? Will customers and employees remain under the new leadership? What would happen if the entrepreneur unexpectedly becomes ill, retires, or dies? Has a successor been groomed?

And, what is the impact of changes in our society upon the family unit itself? Increasing divorce rates, single-parent families,

Table 1

Central Issues Facing Family-Owned Businesses

1. Vision and Communications

- Has a written vision/mission statement for the family/company been developed and communicated?
- Are family members communicating openly and effectively on business matters?
- What type of communication should there be between active and inactive family members?
- Does the firm consider how to communicate effectively between family and non-family employees?

2. Leadership and Company Flowchart

- Who is in control and is everyone on board?
- Is there a clear chain of command/responsibilities for each family member?
- Are non-family professionals' roles clearly articulated/communicated?

3. Family Employment, Compensation, and Ownership Policies

- Which family members are employed, what do they do, and what is fair and equitable compensation?
- How are cash and other company value transfers determined?

4. Family Specific Issues

- Is there dominance by a parent(s)? any sibling rivalry?
- How are non-active family members, cousins, in-laws, and spousal issues addressed/resolved?
- How have social trends and pressures on the traditional family affected your family and firm?

5. Succession Leadership

- Who will take the helm at transfer? What is the intent of next generation?
- What will be the impact of a new leader on other family members, customers, employees?
- Will there be a continuation of family advisors/service providers?

6. Succession Cash Flow

- How much will be due for taxes and where will the cash come from?
- How much is the business worth and what methods can be used to transfer wealth effectively?
- What is the best method for distributing wealth and ownership among multiple offspring/employees?

7. Community Involvement, Relationship, and Representatives

- What is the firm's plan for community involvement, who decides, and what are the cash guidelines?

spousal role reversals, two-income families, gender equality and career activity, and other similar issues all serve to change the inner workings of the family unit from that upon which it was likely founded. In a study of the impact of these trends, Michael Gilding (2000) found that heightened desires for individual autonomy and democratization presented challenges for the stability and continuity of family-owned businesses. Yet, he also found that the most successful families developed new methods to facilitate communication and trust to enhance firm survival. These are some of the more important issues that should be reviewed in examining your family business. Careful and honest analysis will expose the vulnerable spots in your firm and set the stage for developing a strategic plan to minimize these risks and, quite possibly, even turn them into strengths.

Developing a Plan

It has often been stated, “those who fail to plan, plan to fail.” The issues outlined above have been well researched, documented, and publicized. Nevertheless, it is common for firms who are keenly aware of the issues to fail to lay out specific plans in many of these areas. Some of the most common reasons for failing to plan include: 1) an unwillingness to address the issues, 2) an inability to devote the necessary time, and 3) a reluctance to spend the necessary money to create and administer the plan.

What can you do if any of these refer to your situation?

Fortunately, there is a growing number of resources that can help:

- Service Providers. These not only include your lawyer, banker, accountant, insurance agent, and the like, but also the emerging profession of family business consultants.
- Peer groups. These not only include local Chambers of Commerce, CEO Roundtables, the Rotary Club, and the like, but should also include an independent board of directors for your firm.
- Universities and Community Colleges. Most institutions have numerous resources available to address family business issues including faculty, staff, curriculum, and students. In addition, many institutions have courses or workshops on family business issues, and their libraries and data resources are enormous.
- Local SBDC (Small Business Development Centers) provide free or low cost one-on-one counseling on planning.
- Conferences on Family Business are commonly offered internationally. There is likely to be one offered in a city or vacation spot you visit.

The participants listed above have developed numerous tools to aid you in your planning and implementation. Many of the most common are listed in Table 2 (right).

Why not do these things? Not enough time, avoidance of the issues, or a need to have a facilitator/leader make it happen. Each of these items can be overcome. You need to take the first step. If you need help in doing this, use the resources listed and find someone to take the lead for you.

Table 2

Tools for Planning and Implementation

■ Family Council

—family members that serve as an advisory and communicative forum.

- Develops the Family Mission Statement/Family Plan
- Defines purpose, goals, leadership, compensation, and other issues of family involvement
- Regular business meetings

■ Independent Board of Directors

—either advisory or authoritative leaders that provide high level analysis and planning skills.

- Bring in successful professionals who have industry knowledge but are not competitors.
- Look for expertise outside of yours.

■ Written Strategic Plan

—a detailed analysis of the business, markets, players, goals, and activities of your firm.

- Could include separate plans for the family, company, and succession.
- Covers all issues of the company, including governance, industry competition, marketing and sales, and human resources

■ Written Company Policies

—a clear written document that outlines how things are done in your firm.

- Shareholder Agreement—Buy/Sell Agreement
- Family Employee and Compensation Agreement
- Policy on company philanthropy and community involvement
- Peer groups
- YPO (Young President Organization), CEO Roundtables
- Mentoring opportunities
- Chamber of Commerce user groups
- Continued education plan
- Classes, workshops, conferences
- Periodicals, books, tapes, websites

Family-Owned Business Additional Resources

Recent Books

You Family, Inc.: Practical Tips for Building a Healthy Family Business, by Ellen Frankenberg. New York: The Haworth Press, Inc., 1999.

You Can't Fire Me, I'm Your Father: What Every Family Business Should Know, by Neil N. Kownig, Ph. D. Franklin, TN: Hillsboro Press, 1999.

Guide to the Family Business, by Peter Leach and Tony Bogod. London: Kogan Page, 1999.

Strategic Management for Small and Growing Firms, by Peter M. Markulis, David Szczerbacki, and Barbara J. Howard. Central Point, Oregon: The Oasis Press, 1999.

Websites

Family Firm Institute:
www.fambiz.com

Fambiz.com:
www.ffi.org

Canadian Association of Family Enterprise:
www.cafeuc.org

Mass Mutual Family Business Network:
www.massmutual.com/fbn/index.htm

Local Centers

Grand Rapids Chamber of Commerce
Family-Owned Business Council
Phone 616-771-0300

Family-Owned Business Institute
Seidman School of Business, GVSU
Phone 616-332-7200

Small Business Development Center
Seidman School of Business, GVSU
Phone 616-336-7310

Implementation

Sometimes in business we get so wrapped up in the immediate needs of the business that we don't step back and plan the overall strategy for the long term. And even once we have a plan, we lack the discipline to implement it. Here are some recommendations for steps in ensuring implementation:

- Write things down. Good business is good family business.
- Have a Family Council that provides for accountability in implementing the plan.
- Enhance communication in every way.
- Deal with real issues. Respect everyone's right to discuss topics.
- Adopt a Board of Directors with outside members.

Often, the best intentions never get executed. Time, lack of knowledge, and costs can be culprits. To overcome these, it is often helpful to get assistance. Those facilitators that helped generate the plans can be the most effective to see the implementation through to its completion. Additional resources can also be found in Table 3 (see following page).

References

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