So, You'd Like to Keep Your Business in the Family

What owners can learn from successors who have completed the journey….

By: Edward A. Lopit

Ninety percent of businesses in the United States are family controlled and many owners have a desire to keep it that way. If you're exploring the prospects of passing your business to a daughter or son, do so with eyes open. The challenges with transitioning a business within family are significant. "Less than one third of family businesses survive the transition from first to second generation ownership. Another 50% don't survive the transition from second to third." [1] For many, there is a high personal cost as well. As noted by successors interviewed for this paper:

> "My dad and grandfather had a strained relationship. They'd go months or longer without talking after arguments about work. Since my dad bought out my grandmother they barely talk anymore."

> "My father's ego and self-worth were significantly tied to the business. While I felt I was saving the business and keeping my parents from becoming impoverished, he saw me as the bastard child who stole his business. Dad never fully accepted his role in the relational dysfunction his actions had produced. On his deathbed, he asked why we hadn't been closer."

Yet there is hope. When handled properly, keeping it in the family can be a win-win for all involved. Not just to the generation the business is passed to, but to subsequent generations to follow.

> "The proceeds of the sale provided the capital to fund my parent's retirement. It was heavily front loaded, and the rest was paid off in a bank note. They might have considered other options, but succession to a family member was something they had worked on for years. It was a good business opportunity for me too, and Dad hoped I would want it."

For the business owner much is on the line and the ultimate success or failure of this endeavor will be dependent upon the ability of your successor to take the reins and lead the business forward. Interviews with successors in small to midsize businesses revealed insights for how an owner might tip odds for success in their favor. What do successors feel worked? What advice would they give to a business owner and parent wanting to effectively transition their business to the next generation?

Here is what they had to say.

I. Take Charge

While there are many things a business owner can delegate to others, transitioning the leadership position to a successor is not one of them. Ignore this eventuality and the implications can be far reaching and leave a tremendous burden on your family.

[1] Forbes 7/31/13 – "The Facts of family Business". https://www.forbes.com/sites/aileron/2013/07/31/the-facts-of-family-business

> "My grandfather worked right up to the day he died at the age of 86. He had done no succession planning. It was all very complicated. My dad, grandmother, and aunt had to figure out who was going to do what, who owns what, and what the next steps were going to be."

> "My parents took over when my grandfather was tragically killed in an airplane crash. They got a telegram telling them of the tragedy. Suddenly they became owners of a business. Neither had business experience. My mom had only worked in the business as a young child. As the only living heirs, they took over the business by default."

It is surprising how often otherwise principled, hard-driven, entrepreneurial, and decisive individuals struggle when thinking about their ultimate succession.

> "The business was my dad's thing, the means to his survival, it took care of the family. It was incredibly hard for him to let it go. Even though it was going to family, it took an emotional toll on him."

> "It got to a point where my grandfather, who had other interests and loved to travel, slowly gave the job of running the business over to his sons. He was spending less and less time in the business. Ultimately the sons came to the decision that they needed to retire their father."

As owner you must take charge - embrace the inevitability of succession and take steps to ensure your successor and organization are positioned to execute a successful transition when the time comes.

II. **Start Early**

The timeline to transition ownership within family can be extensive. Preparing a successor takes time. Family members capable of leading the business must be identified and develop needed skills and experience.

> "My succession path to CEO was over 5 years. While I had management experience, it was in a different industry. They needed to see me progress, yet have the time to make a change if I wasn't. If it went sideways, or I decided I didn't want to do it, they needed time to find someone else."

Family transactions are complicated. The methods to pass control of equity, fund transactions, and deal with tax implications are time sensitive. Allow windows to pass and options narrow considerably.

> "As the transition plan was developed we learned many things. For example, someone asked if we had the resources needed to pay inheritance taxes if something happened. We learned we didn't and it took two years to fully get a handle on this one issue."

The transition of management and ownership must be completed while preserving the competitiveness of the business. Market conditions can change drastically as decisions drag out with implications to both you and your successor.

> "Waiting to start a succession plan was not good for either of us. The industry changed and there is immense pressure now to make the payment while keeping the business alive. If we had started earlier, he would have gotten all his money and the company wouldn't be saddled with debt. We could be nimbler and able to morph or change. But we're stuck."

Planning and executing an effective succession can take longer than you might think. Successors feel it is important that you start early to ensure there is adequate time to complete the handoff successfully.

III. Proceed Cautiously

While keeping the business in the family may be attractive, perspectives and judgement in these transactions can become clouded. "It is common sense that when managerial decisions are influenced by feelings about and responsibilities toward relatives in the business, when nepotism exerts a negative influence, or when a company is run to honor a family tradition rather than for its own merit and purposes, there is likely to be trouble."[2]

While your desire to keep the business in the family may be strong, the ability of your successor to lead the organization will determine the outcome. If your retirement is to be funded by future cash flows produced by the business, the personal impact can be a direct one. Given the implications, it is important that everyone go down this road with eyes open.

Successors can attest that even in the closest families the mixing of business adds complications.

> "Running a family business comes with strains you don't have to face in other businesses. I try to turn it off when I come home and not drag my wife into things. If I had a tough day at the office with my dad, then have to see him at a barbeque over the weekend, it's tough."
>
> "There were certainly times of conflict between everyone. Times when I needed to shut the door. In fact, to this day my dad and uncle are not very close. Some pretty hurtful stuff. Personally, my role has been very difficult. I have felt in the middle at times, needing to be the peacemaker."
>
> "I was continually wrestling with a need to be respectful, a good son, fair and honest, and treat it as just business. This got very hard because of the way my dad's emotions were wrapped up in things."

The underlying motivations for keeping business in the family can be complex. Acting on emotion rather than logic may prove problematic. Once successors agree to step in it may be difficult to get out.

> "The surface reasons were certainly real. It was exciting to work with my dad. Then there are the deeper reasons that you may not realize without some deep soul searching – unresolved family dynamics, wanting to please, doubting you will ever be able to find a better opportunity on your own. A successor needs to be sure the business is their passion. It may be a great opportunity, but it will be hard work. If you don't love it, if it isn't something you are passionate about, you may be left wanting."
>
> "If you're family and you leave, it raises questions. Outsiders will wonder if the business is OK. Leaving can be destructive. Stepping in then stepping out sends a bad signal so you need to be committed."

While times are changing, if the successor is a woman the challenges faced may be even greater.

---

[2] "Conflicts That Plague Family Businesses" - by Harry Levinson, March 1971, Harvard Business Review. https://hbr.org/1971/03/conflicts-that-plague-family-businesses

> "When I walked in the room they thought I was there to bring in the coffee and tea. I was younger than most and 99.9% of the time the only woman at the table. It took time, but ultimately I earned their respect."

Successors want what's best for everyone. They need to know that your decision to select them has been well considered and they will be provided the support they need to be successful. They understand the issue of "earned" vs. "anointed" will be a big one for staff.

> "I think it's critical that you have the right individual. If they don't have the skills, the make-up for the job, it's not going to work regardless of the planning."

Successors understand it is only natural for a parent to want to be benevolent. But with so much on the line they recommend everyone proceed cautiously. While difficult, business logic must trump emotional desires.

IV. **Formalize a Plan**

Taking time to communicate and get everyone on board before acting takes effort. While most CEOs may acknowledge the importance, successors found needed planning often missing or inadequate. "Although two-thirds of family companies have some sort of succession plan, only one-quarter have a plan that is robust and documented."[3]

As a successful entrepreneur, you may not need a formal succession plan. However, the consensus of those in the successor role is it is essential.

> "My dad had mapped out what he needed financially with his departure, but when it came to the transition of leadership there really wasn't a plan. I had worked in the business most of my life, but that didn't really prepare me to take the leadership role".

> "My development plan was not formalized. Dad may have had an unwritten plan, I'm sure he did, but it was never communicated. He was entrepreneurial, a decisive leader, he didn't share decision making well."

> "There was no formal plan for how the transition was to occur. They had some ideas, but I think they were making it up as they went. I basically had to learn everything by trial and error. I've never really felt I was adequately prepared to be CEO."

To avoid misunderstandings, it is important that everyone's expectations are clear, preferably in writing.

> "Insist on a formal transition plan and clear expectations. Have tough conversations early and document what is said in writing, so everyone's memories are the same."

> "Take the time to map it out in advance and be clear on what you're trying to accomplish. We never went through that process. I was sort of thrown in the deep-end of the pool. Its worked out, but could have been easier."

---

[3] Up close and professional: the family factor Global Family Business Survey; ©2014 PwC
http://www.pwc.com/familybusinesssurvey

> "After the transition he wanted to stay out of my hair and, if anything, he stayed away too much. Knowing me as he does, it would have been good for him to make sure he checked in with me. There were times he just disappeared. This made it harder for us to work together. He always had ideas, but they connected less and less with what was going on. So, if anything, he left too quickly."

Act with purpose and with clear intentions.

> "I'm not sure how the decision was reached that I would take over… I don't know if we ever really had an official sit-down where we discussed things. It just became clear over time. In meetings, dad would introduce me as his son who would be the next generation taking over the business."

Communication is key. Those in the successor role expressed a need for clarity and consensus around key elements of the transition. Specifically:

> "What does my dad think the role should look like and how does that align with what I think the role needs to look like?"
>
> "How will I be prepared to lead the business – will there be training, mentoring, a career path?"
>
> "How will knowledge be transferred? Will I have an opportunity to pick his brain and understand where he spent his time and why? What did his workload look like?"
>
> "Will parents stay involved, or will they just ride off into the sunset?"
>
> "Can the founder let go and, if not, what will he/she try to hold on to. How might my authority be limited?"
>
> "What does the founder personally identify with and how is their personal self-worth and financial net worth tied to the business?"
>
> "If I bring change, how will that be perceived?"

With a plan in place and communicated thoroughly, the likelihood for success increases significantly.

> "We put together a very specific year-by-year plan that had specific targets and success criteria. It went to a nominating governance committee overseen by the Board And there was an annual review. The thoughtfulness of the document, which we kept updating, helped the committee feel comfortable. They could follow and see the progression. They saw me at the annual meetings. It was a very deliberate, step-by-step process that really helped with the transition."

Failing to keep everyone on the same page can magnify negative dynamics and outcomes. Take the time to formalize a plan and include your successor in the process to the greatest extent possible.

V. Don't Go-It-Alone

No succession is perfect. When exploring factors contributing to success and failure, a common theme came up repeatedly. Those describing their experience as a success spoke to the contributions made by third parties throughout the process. Those who were part of a go-it-alone process questioned the wisdom in having done so.

A generational transfer of leadership is a high stakes endeavor for the successor. They have much on the line and big shoes to fill.

> "You hear a lot of horror stories about family businesses not making it past the second generation. That's always in the back of my mind. Am I going to be the guy that lets it all fall apart? I'm the youngest of the grandchildren on my dad's side of the family. I don't think anyone saw me taking over, including myself. Yet, here I am."

While there is a cost to accessing quality external resources, successors believed outsiders can deliver value to the process in three key ways.

1. Transactional Expertise and Best Practices

We all desire to keep things simple. However, the transfer of ownership of a family business is complicated. Outsiders can bring the specialized expertise needed to navigate valuation, regulatory, legal, and tax issues. Missteps in these areas can be costly.

> "We used our outside resources: legal, consultants, and accountants, to guide us through the transition. Our accounting firm was very involved in the transition strategy and planning everything out."

2. Detached Perspective

Mixing business and family is difficult. When familial patterns and dysfunctional behaviors seep into the workplace things can become toxic. Power positions between family members can tilt discussions in negative ways. Outsiders bring a detached perspective. When needed, they can effectively mediate disagreements and ensure a level playing field is maintained.

> "Working for my dad went well, but when it came down to this (succession) it was tough. I think you need to have an outsider shepherd you through this process."

> "Whether it's a formal board of directors, or a few outside people who can bring perspective to those involved, you need people who can be objective. When you mix up your hats (business hat, owner hat, family hat) things can get messy."

> "Be careful not to get drawn into a false narrative. 'Don't worry. We've got this. I'll take care of you.' I heard those messages for so long that I started to believe in them and I shouldn't have. After the deal was finalized my dad called and left me a message: It's business, not family.' And I had been thinking the opposite for 20 years. It was hard. I should have pushed the narrative to bring in third parties early on. If I got resistance, at least I'd have known."

3. Successor Support

Successors understand that they are moving into uncharted territory. Navigation of their transition into leadership will come with challenges and they need a solid support system of knowledgeable people who they can turn to for advice.

> "I would have developed better resources, advisors around me. A group I could go to for advice, support."

For those who have worked only in the family business or who have limited external work experience there is frequently a need to gain a broadened outlook as they prepare to take the company forward. Outsiders can bring industry knowledge and fresh insights that may be lacking in the firm.

> "I was in a bubble working for my dad. I didn't get outside mentoring or training. What I learned I learned from my dad. I learned his ways, his thoughts, and many times these were designed to benefit him. It wasn't until I started spending time outside the company that I realized some of what we were doing was not best practices and certainly were not good for me."

> "What I needed was different than what had been in place. I wanted a consultative team to help me run the company. Since I didn't have his experience in the business, I wanted to leverage the knowledge and experience of others. This meant we needed to change. It was difficult. It had its challenges. We did a lot of work with facilitators and that was helpful."

> "I'd like to add some new advisors to our board - people from my generation who might see things closer to the way I do. I respect the knowledge of the members of our board, but 3 out of the 4 are retired. The way business was conducted in their day was different, challenges today are different."

Conclusion

It is natural for an owner to feel apprehension when thinking about their ultimate exit. Building the business has taken years of hard work. Many challenges have been faced and overcome along the way. It has been a life work. But the last day on the job will ultimately come. To every owner it's inevitable. If you're thinking about keeping the business in the family after you move on, consider the wisdom shared by successors who have completed the journey. If you wish to increase your odds of success, you must embrace this last challenge and deliberately drive a transition that is a win-win experience for everyone.

About the Author*: Ed Lopit is Principal of E A Lopit & Associates, a provider of coaching, consulting, and interim services to small and medium size businesses (to 500+ employees). As advisor, confidant, and hands-on executive, Ed brings great ideas to life by building profitable, sustainable businesses that are the absolute best at what they do.*

Ed Lopit
(425) 478-0708
edl@ealopit.com
www.ealopit.com
http://www.linkedin.com/in/edlopit