# Strategies for continuity and growth in the family business

**By John Messervey**

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Let me describe one family's dilemma. They have six children, five daughters and one son. The father came up to me after attending one of our meetings, and he said, "John, I have a problem. I don't know what to do with this business I've built up." And he described his family sometbing like this.

The oldest daughter is leaving her job as a nurse to join her husband overseas in a Christian youth project. Daughter number two believes in the guru Sy-baba -a reincarnation of Cod-and is married to a citizen of India. The next and only son is a former minister who would like to join the business but whose wife is not liked by the son's mother. Daughter number three is living with a drug-abusing husband who believes in reincarnation and since he worked hard in previous lifetimes, this is his "vacation" life.

Daughter number four bailed out of the family system and also moved to California, married a prominent doctor 22 years older than she is who reminds her of Dad. They are millionaires and raising two small children. The youngest child believes her father is a racist so she married a black Ethiopian, has low self-esteem, is bulimic, and has no interest in the business,

Yesterday, I got a letter from the mother saying, "Don't talk to the m-laws" in all this mess. What to do? Sell the business?

Our focus is on continuity. We want your business to remain healthy. We have 12.9 million family businesses in this country in contrast to about 300,000 corporations that are publicly traded. So, we're all a part of family business, the magnitude is so great whether its the family that owns the Hyatt Hotel across the street or the guy who owns the corner restaurant.

We've discovered there are no perfect families and no perfect family businesses. Many are good and getting better. So the orientation is one of wellness.

Most family businesses don't end up like "Dallas" and "Dynasty". We believe every relationship in the family business can be improved and every business can be made a more satisfying place to be. We're going to look at the components of this.

First area is understanding family management and ownership. The forgot ten key is ownership. People just think it's family and business. No, it's family management, and business. You can have a management succession problem and not have an ownership succession problem, or vice versa.

A behaviorial look at families would include entrepreneurial rivalry between father and son, sibling rivalry, and how to increase the commitment of non-family members into your family business. There's a model for conflict resolution to apply which we'll discuss later.

A preventative look at family business spotlights what goes haywire most often in a family business and how to cure it.

And, there are some characteristics of successful family businesses. There are groups that are doing most of the things right.

Recognize that all organizations face the drama of succession. Family businesses, although they make up so much of our nations wealth, have a miserable ratio of success in succession. The most optimistic study we've been able to find has been done by a colleague of mine, John Ward at Loyola University in Chicago, and it shows for the average generation of 24 years, the first generation passing it on to the second generation makes it 40 percent of the time, the second generation to the third makes it only 15 percent of the time, and the third generation to the fourth makes it less than one percent of the time.

There are really seven positions if you own a family business. You are part of the family, you are part of the management group, and you are part of the ownership. Where the circles overlap, some people are family members and managers. Some might be owners and family. Some may be part owners, part managers, and part of the family.

We don't teach people how to be owners in this country. And most of us don't pass ownership on very well.

What I've discovered after 11 years of organizational consulting and six years of family business consultations is that the technically correct solution to succession may not be the emotionally appropriate solution.

A case illustrating some of this includes a strong-willed entrepreneur with a daughter and four sons. Plus there's the son-m-law who exhibited what I call in-law behavior. Often, we find m-laws are in charge of the most. They tend to accumulate and make themselves indispensable. This son-in-law was a very talented individual and was president of Dads company Dad became very successful and a multi-millionaire.

Mom doesn't like the son-in-law. Daughter is not getting along with her husband, the president of Dads company. So the son-in-law is looking over his shoulder and seeing four other sons coming up behind him.

Mom and Dads marriage was in trouble and they were pushing the problems of their marriage down into the relation-

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ship of daughter and son-in-law. Mom didn't care for the son-in-law and had a very contentious relationship with the daughter. Dad loved the son-in-law as a business partner and loved the daughter.

Who did Mom want to be president of the business? The25yearold son who was totally incapable.

We take a multi-generational look at your family business. The four of us-1 work with a psychologist, a family therapist, a strategic planner most often-could sit down with the father and mother and almost predict what was going to happen in the next generation. It is eerie. I wouldn't have said that seven years ago, but it's getting really spooky on how children will turn out like or opposite of their parents

Families have varying degrees of enmeshment. Enmeshed families are where when anyone sneezes, everyone offers a Kleenex. Everyone's kind of in to each other'stuff-a pile of puppies.

The other type is the Disengaged Family, equally a problem and the opposite of enmeshment.

What do the young people in family businesses want, if they're destined to take over some day?

I happen to be of the school of psychology that believes all human behavior is based on needs. That is, we are need-driven. Your family's commitment to your family business is based on the extent to which they perceive their needs are being met. Their commitment to any organization is based upon the extent that organization is meeting their needs.

So, the task of the owner of the family business becomes merging the individual needs of the family members with the overall business needs of the farm or ranch.

How to do that? We've discovered people want to be treated well and they want to be utilized well. The trick is in number two-utilized well. That's where the payback is, number two. People love to be utilized well. If they're treated well, and most family businesses do a good job of treating people well. If they're treated well, you get longevity. They may not be the most talented nor the most productive, but they stick around.

But, if they're utilized well, there's much more coming back.

What kind of jobs does it take to utilize people well?

Three things must be in place. One, the job must be complete, the job has an A to Z to it. A beginning, a middle, and an end. It's not some kind of never-ending mush. It has distinction, it has lines around it.

Two, it offers some kind of significant decision-making. The son or daughter has the responsibility for making choices about the "howness"of the job-how the job is done.

Third and most important (and so diffcult for family businesses), the manager-owner must give the son or daughter feedback directly. You must let them know where they stand. I have so many clients who say--Why, my daughter, she is the best in this business." And I've asked them, "Have you ever told her that?' And then their face just kind of glazes over. They cant get that out.

No discussion of family businesses would be complete without a discussion of entrepreneurs. Most entrepreneurs are first born. We don't know where entrepreneurs come from, but one clue is that they come from other entrepreneurs and that's generally the oldest son.

Entrepreneurs are generally in excel-

# Some other considerations...The Will

**By John Alan Cohan, Los Angeles, California, Attorney at Law.**

A will is a document by which you may dispose of your property at your death. Legal experts agree that procrastination concerning making out a will is one of the main reasons why an alarming number of people die "intestate", or without a will. If you die without a will, your property will pass in accordance with the appropriate law of "intestacy" in effect in your state. This means that your property will be distributed according to a fixed formula, and even remote relatives whom you do not care about could benefit from your death. It's important, then, even if you have a relatively small estate, to make sure this does not happen and you prepare a will as early as possible.

In recent years many people have recognized the effective use of "living trusts", which permit you to avoid probate of most, if not all, of your assets. However, for several reasons, even with a living trust, a will is also important. First, it is not always possible to anticipate and thus to exempt from probate every last asset you may own by using a living trust, and those assets would have to be distributed according to the law of intestacy if you did not leave a will. Second, it is possible that you might die of injuries in a misfortune such as an auto accident, and if this happens your estate is entitled to sue for damages. Unless a properly drafted and executed will is in place, damages may have to be awarded to heirs determined by the law of intestacy.

Another important reason for having a will concerns minor children or grandchildren who may survive you. Unless you name a guardian for them in your will, your children will become a ward of the court, and the court will determine who would serve their best interests by appointing a special Guardian to be custodian of their property as well as to take care of them. It is usually irresponsible for parents with minor children to postpone implementing a will.

A will does not have to be complex, and frequently it can be simple, brief, and to the point. It is your right to leave a will and to thereby insure exactly what will be done with your property. For many people a statutory will, available in California, Maine, Wisconsin, and Michigan, may be appropriate. A statutory will comes in a standard form which, when completed, signed and witnessed, has the same power as a detailed will drawn up by an attorney These forms are available in many stationery stores.

If you are going to have a very complicated situation, there is some concern that the form might not be suitable for you or it might not be filled out properly, and therefore it would be prudent to consult an attorney instead. Also, certain functions cannot be served by statutory wills, as for example, if you wish to postpone the timing of certain dispositions of property or implement a testamentary trust to benefit certain heirs or organizations. Also, for larger estates, it can be disastrous to use statutory wills because they are ineffective with respect to avoiding estate taxes.

For most people, a will is a permanent document that might not require any changes except where a new child or grandchild is born when a family member dies, or when there is a significant change in your assets or new property tax laws are enacted. Wills should be reviewed periodically, Amendments or changes can frequently be made by a simple codicil rather than drafting a completely new will.

If you have property located in different states, or if you lent health and possess high energy. They're really tuned up, all the time. One thing about entrepreneurs: as soon as one project is finished, another is sure to follow.

Entrepreneurs are generally engagecl in solitary sports. I don't know of any entrepreneurial bowling leagues. They also usually have a strong relationship with one parent, either love or hate basis. And that opens the primary entrepreneurial rivalry.

Sons or daughters say, if I inherit this business and I screw it up, then people will say, "they couldn't cut it". Or, if I inherit this business and I clo better than Dad, people will say, "look what he or she started with." It's a Catch-22.

The entrepreneurial rivalry is to outclo Dad. Or, to win your father's approval. It's been said the family business is where the children continue their struggle with their parents. Entrepreneurs avoid equilibrium. They will create chaos to solve chaos. Such offers the entrepreneur the chance to be a hero, over and over again. You get into a mess to get yourself out, but you never get into too much of a mess.

Finally, entrepreneurs have had a number of jobs for pay by the age of 15. J. C. Hall, founder of Hallmark Cads, had 11 jobs by the age of 15.

Why are we in the cattle business? There are fundamentally four reasons: wealth creation, build an empire in real estate or cattle, to make a monument to my family or myself-the name on the door syndrome (like many car dealers in the city who want their name everywhere), or self-fillment.

So, if Dad wants X from the business, Mom wants Y, and the children want Z, it isn't going to work especially if these parties don't know their objectives. The family needs to discuss and rank the priorities on these four. If you don't get this settled, then everything else that follows is going to be confusing to the people in the family and other owners.

Families should recognize there are eight stages of career development in a family business. The first is "dirty reality"-what am I doing here? This entry stage may last a few hours, a few days, a few weeks, perhaps even a lifetime.

The second is, do I really want to do this? Do I really want to be here. Third is what we call surrender-you've decidedl'm going to learn about this; I'm going to lean this business. After this the steps move along very quickly,

The competitiveness stage: can I be as good as the Olcl Man? Can I keep up with him?-that fundamental entrepreneurial rivalry. Then assertiveness: I want to run this ranch, this farm. Most people don't remember the day they came to that conclusion. It's a process. Then there's the fearful stage-can I a0 it? Then follows the longest stage of all, the mastery stage -I am doing it. Some never leave stage seven and adopt what we call the "feet first" strategy which means there's only one way they're going off that ranch and that's feet first.

Lastly comes the most satisfying stage of all and that's the mentor stage, the stage where they pass it on. Not just the wealth-that's the easy part-but where they pass on the knowledge, the values, the opportunities that made that stage great. That's the stage people have told us is so nourishing.

A study by Gail Sheheey illustrates both men and women's level of happiness becomes highest and climbs more or less constantly during the mentor stage from ages 52 through 70 and on up as there is a feeling of completion, fulfillment, of a passage, gratefulness of having lived such a life. That's what we hear most often from people who have passed on their business.

All family businesses have conflict. A model of conflict resolution can be illustrated by a son wanting to convince his father of the need to buy more land. If you're the son and you're trying to sell that idea to Dad, you're going to get one

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move to a new state, special caution must be taken with regards to preparation of a will, in consultation with your attorney.

It should be noted that certain kinds of property are not subject to testamentary disposition by will. Property held in joint tenancy, for example, automatically goes to the surviving joint tenant and cannot be disposed of by will. Life insurance proceeds, likewise, usually go automatically to the designated beneficiary, unless the policy states that the proceeds are payable to your "estate".

It is important to carefully select and designate an executor of your will, and it's recommended to designate a successor or alternate executor. The executor shoulcl be someone who is likely to survive you and who can be trusted as significant powers are reposed in an executor in terms of administering your estate and dividing up personal property. Because of the broad powers given an executor, he is in a position to go through all of your property for the purpose of making an inventory, and if anything is later "missing", it is extremely difficult to actually prove any wrong doing. Accordingly, extreme care should be exercised in naming your executor.

In addition to preparing your will as early as possible in life, legal experts advise that you should not keep your will in a safe deposit box unless a second person also has legal access to your safe deposit box. (Your bank can arrange for a joint tenancy safe deposit box or a power of attorney designation for that purpose.)

Because quick access to your will is necessary in the event of your death, the original might best be kept in an accessible place at your home or in your lawyer's office.

Funeral instructions should not normally be set forth in a will, contrary to popular misconception but should be stated in a separate written document. The same may be said concerning provisions regarding disposition of organs to science or the use of life-sustaining procedures. Most states have procedures (outside of your will) for implementing your wishes in those respects.

**...The Living Tust**

One of the most important issues facing agricultural families is how to draw a lifetime economic map that will permit transfer of accumulated wealth from generation to generation with the least amount of tax consequences. How might a family optimize the benefits to be enjoyed by the accumulation of wealth, enhance financial and mental security, promote family harmony, and perhaps most importantly plan for an orderly transfer of property from one generation to the next smoothly and economically?

An estate plan regarding transferring of your ranch or farm to the next generation should be as integral a part of your life as having a deed to real estate, keeping bank accounts, or having insurance policies. It is a plan for living rather than a hurried program to be implemented in contemplation of death. An estate plan shoulcd be drafted and implemented early in a farmer or rancher's career and must be reviewed on a regular basis to meet changing needs.

The most highly recommended procedure for planning on the orderly and gradual transfer of a farm or, for that matter, any business, really, is the implementation of a family living trust, which is possibly the most cost effective and money saving family planning tool that you could ever encounter. Most attorneys are not familiar with the extraordinary capabilities of a family trust in connection with a family business of two responses. You are either going to get, an unconditional "yes" or you're going to get some other response. Any other response other than an outright yes should be regarded as a conditional "no".

When your hear that conditional no, your instinct is to try to sell that idea again. Don't do that. Trying to sell the idea again tends to reinforce the no, and second, it's like you weren't listening the first time.

We suggest this. Step one: ask an open-ended question. Open-ended questions cannot be answered with a simple yes or no. They allow people to talk. Ask Dad why and let Dad explain, let him talk. Now, he's going to say some things you might not agree with, they might even be inaccurate. Just shut up because you have to let Dad talk.

Why **let Dad talk?** Because people change their minds when they're talking, not when they're listening. My theory is when you're talking, your filters aren't up. When you're listening, you build up your filters and you push the stuff back you don't want to hear

When Dads through talking, you go through the next step which is an elaborate re-statement of the problem citing all his objections and so on. Then ask a closed auestion such as "Is that all of your concerns?" If he says no, then you've got to go back and get all of them out. Be patient. This process takes more than a few minutes. It might take months.

Then when all the objections have been aired, you restate your belief in the idea being a good one, asking, "How can we work this out?" Guess who will help? More than likely he will. It isn't guaranteed, but you're more likely to get his help as you've avoided conflict and have at least the prospect of arriving at some kind of shared solution to the problem. Why? Because you've made sense. you've been patient, and you have been reasonable.

The **last step** is to propose some kind of action plan that you work on together. The process is called exploring differences. Open-ended questions, listening, restatement, and seeking solutions jointly. Don't get bumped off at the beginning when you hear that conditional "no". Don't get upset, don't let it eat you up inside.

Now, people are more likely to carry their emotional baggage in a family business than in other careers. In a family you can't run away. And parents have ambiguity, You can keep things vague for a long period of time. Children, being a bit more impatient, want clear and crisp direction. Parents possess long gestation periods for decision-making. They can take their time. Children want decisiveness. They want clarity.

Children want perceived freedom and independence. Parents have ultimate control. As one son said to me, "John, every time I get near the end-zone, Dad moves the goal posts." Or it goes the other way. I had a father, owner of a food processing company, tell me: "I was hoping my son would blow it so I wouldn't have to worry about succession." That's how afraid people get. Talking about succession in a family business is tantamount to drawing up your will and talking about death.

And conflict goes beyond father - son. I had one brother tell me: "I spend a lot of time figuring how to get my brother's half of this business."

An **approach or** model one can use if you're an heir in the family business .... Ask yourselffour questions: One, what is most valuable to yourself? Are you going into the family business to win your parents' approval? The odds are you wont make it. The situation will be rife with conflict, submerged or direct. Second, what do you need to be truly happy? Have you been able to do enough, see enough sort it out? !lhree, what are you willing to pay for your happiness? What are you willing to give up? Are you willing to give up the family ranch? Or, are you willing to give up the job in the big city and come back home to the farm or ranch? Fourth, how do you remove the obstacles of getting there? How do you work those out?

If you're the parent, it works backward and is a little more difficult. First, what are your desires for the children? Second, how can your desires for the children be accomplished? Do you even know what those are? Third, can you give your desires up? Fourth, is it possible your children's desires may be more important than yours? can that be possible? If they want to move away, can you let that happen? And . . . can they move back if they decide to?Can you resolve those differences?

We've discovered that the best thing you can do for your children is to raise high esteem children? That's all there is to it. It isn't the money, I'm convinced of it. The issue is raising high self-esteem children-how do you do that?

You do that by allowing them to individuate, allowing them to adopt their own identity. What is our struggle in life? Our struggle in life is for separateness and identity. That is not to be implied that we're breaking apart the family The theory I believe in, is that the family is the smallest common denominator, not the individual.

One of common problems we see is artificial employment. That's hiring your children when there was no job there before they started and there won't be one there when they leave. And eveybody knows it, including them.

Another problem is inadequate training for new entrants. We strongly suggest young people in their twenties work somewhere else. Our experience has been that later in life, those sons or daughters that worked some place else during their twenties had much higher succession ratios and more successful families than those that have never worked elsewhere. Those wake up at 42 and wonder what it would be like to have worked somewhere else and it kind of eats at them, sometimes in a big way

Also, family businesses become very incestuous. We have in family business this elaborate training program called "Watch Me". Watch me deal with the bank, watch me deal with the government, watch me deal with our suppliers, watch me sell these cattle.

It's just good to work somewhere else-perhaps still in the industry-but for another firm, another perspective. When you're in your twenties, your father is likely in his forties or early fifties and in no mood to transfer the business.

because the probate-avoidance feature of such family trusts might detract from the high probate fees attorneys would otherwise realize upon the probate of your estate. Moreover, it's entirely possible few attorneys, nationwide, have sufficient expertise to competently draw up and implement a suitable family trust for your farm estate.

Now, let us review some of the pertinent issues regarding a family trust to see if it is suitable for your situation. Apart from the very substantial money-saving elements available because of probate avoidance, as mentioned, a family trust permits you to continue the operation of your ranch or farm, whether a sole proprietorship, partnership, or corporation in virtually the same existing `mannerIt permits you to eventually disengage from the business and move towards retirement. It permits you to have your son, daughter, or other heirs work with his father, to grow in and with the business, and to gradually shift responsibilities to the heirs commensurate with their capabilities, and to make it possible for your son or daughter to eventually have the business in their own name when it is felt that they are ready and capable of handling its continued profitable operations. It permits you to pay your heirs a sham of the net income as proper compensation for labor and efforts in connection with the business.

A family living trust permits you to utilize credit in farm estate building, establish additional reserves for the payment of existing loans on real property or other business loans, and to establish funds for future expansion and growth.

One important feature of a family living trust is that, upon the death of the mother and father, the business can be immediately transferred, absolutely, to designated heirs such as your son, without delays of anv kind. without probate. and without transfer fees. This means that, if your ranch business is worth, say $500,000, the net savings to you with such a trust will be about $50.000, or 10 percent of the value of the business.

There are tax advantages, additionally to your son, daughter, or other heirs, in that normally there will be no tax liability to them upon your death, and they will obtain a "stepped-up basis" inconnection with the farm, which in itself is an extraordinary tax advantage. Moreover, the trust arrangement permits the heir to move into the farm operation, working with the father, without the burden of heavy debt. The father gets the opportunity to take it a little easier, and to take a little time off. Further, the heir enjoys a good and steady job and involvement in the business. The existence of the trust gives an incentive for the heir to inject, new ideas and enthusiasm in to the farm enterprise, and enjoy the shared relationship.

There are pitfalls if you do not arrange for a family trust. Quite often the relationship of father and heir in connection with working on the farm is casual and off-the-cuff. Sometimes, their understanding is oral and vague. The father fails to make it clear how the heir is going to grow in the enterprise. The relationship between the father and heir may deteriorate, and finally terminate in hard feelings. Also, without a trust, there can be disastrous tax consequences.

By contrast, with a family trust, the father retains all ownership of the enterprise (with proper ownership and income provisions for his wife), but the heir receives a share of the net income of compensation for the work The heir does not get ownership of anything-land or chattels-during the initial period of the trust. The trust can be revoked or amended at anv time.

Under this pattern the son or daughter gradually acquires a share in the animals, machinery, good will, and other assets of the business in accordance with the discretion of the father. Alternatively, provisions can be made for specific percentage transfers of the business at stated times in the future or upon the occurrence of certain events The transfer of the assets of the business, under a properly administered family trust, permits such transfers without payment of federal gift tax, which otherwise would impose significant tax burden on the parents.

The best trust arrangement is simple, clear and unambiguous, written in everyday, easy-to-understand language. Provisions can be made to either permit or prohibit the son or daughter heirs from selling the enterprise after both parents have died, if desired, thereby requiring the continued and profitable operation of the business for years to come. For further information on this important subject, please contact the author at (203) 557-9900.

There's all kinds of work that's been done to show, transfer is much more likely to occur when the father is 55-65 or 65-75.

Another problem is inadequate or unrealistic compensation. This is a ticking time bomb. Especially if you start having compensation based on need in the family rather than on performance. I've seen so many families where the son who is married and has children and needs a nice house makes three times more than the son who is single, who playsaround, etc. Yet, both may be working equally hard.

Finally, incompetent directors and advisors. Those are the people you've had around too long. Those are the people that play it back to you the same way they think you want to hear it,. Your CPAs, bankers, consultants, attorneys. The key is accountability. Put your work out on bid once, and you'll find suddenly you're getting more pertinent advice.

There are nine characteristics of successful family businesses.

1. You must articulate a clear mission for your family business. Where are you going, what do you believe in, what are your values?

2. Good family businesses have a history of family wellness. Well families beget well family businesses. The corallary is also true.

3. Successful family businesses encourage open communications. They encourage individuation. They encourage consensus. They have a system for making decisions.

4. Successful family businesses renew values, the family values, the business values, the methods of running the business at each passage of generation, each ownership change. You've heard it said, "shirt tail to shirt tail in three generations." That happens when they lose that work ethic in the second generation. Dad made it,, I spent it attitude.

5. They properly evaluate compensation and performance. Remember feedback? Good family businesses tell the kids how they're doing. They tell the children where they stand. That's the number one problem we find out there.

6. Successfulfamily businesses ruthlessly pursue training. The most valuable commodity in the next generation isgoing to be the well-trained, well-educated, articulate worker. The labor force is shrinking, as you know, and the major companies are picking off the bright and hard-working individuals.

7. They provide powerful incentives to non-family managers and employees. Those folks know their names are never going to be on that ranch or that farm or that business. They know that but they feel a part of the family. They're part of that wholeness and that wellness through incentives.

8. The family business should secure and challenge competent advisors. They don't let their advisors get stale. They keep them jumping.

9. Successful family businesses possess a long-term commitment. Farm and ranch families do this very well. You think in decades.

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