Succession Success

Eight steps to help transition your family business to the next generation.

*by **Kindra Gordon***

If you know a family business that is being run by its third or fourth generation (or beyond), tell them congratulations. Then ask how they did it — because the odds were stacked against them.

On average, about 40% of family businesses succeed in the second generation, and only 13% are successful in the third generation, reports Beth Adamson, director of the South Dakota Family Business Association. Businesses that succeed into the fourth, fifth and sixth generations are in the single digits.

The association, based in Vermillion, S.D., aims to help people realize and continue the dream of families in business. It is funded through a private family grant and is operated as an outreach program of the University of South Dakota (USD) Business School. Members include a wide array of family businesses, from the ag industry to plumbing contractors.

Adamson emphasizes that family businesses contribute a great deal of economic vitality to the private enterprise system in America — accounting for 50% of our gross domestic product (GDP) and 62% of jobs. Thus, she says it is critically important that family businesses are successful at succession — passing the family business to the next generation.

But that's a process that doesn't often come easy. "Not only are you trying to run a business, but you've got the dynamics of family, and that can be good or bad," Adamson says. "It comes down to communication."

Additionally, she reports that about 50% of family businesses today are operated by sibling teams — which can further complicate succession plans and make communication even more crucial.

Difference in dynamics

Adamson points out that mixing family with business tends to mix emotional and rational feelings, which can often complicate the family business — and make it more stressful.

Adamson shares a list of traits that are characteristics of families and those that are business-based. She says recognizing these differences can help families realize why communication is so critical to keeping a family business together.

- Family choices are based on emotion; business relations tend to be rational.
- Individuals are born into a family, whereas individuals are usually hired into a business.
- Family is based on relationships; business is based on results.
- Family is built on unity/support; business is based on competition.
- Family seeks security; businesses must take risks.
- Family is about equality; business is about equitability.
- Family tends to focus inward; business must focus outward.
- Family is based on status quo; progressive business should be all about change.

Based on these differences, Adamson says it's understandable why problems can emerge when you overlap family and business. She says a common mistake is that family businesses get "hung up on tradition and not changing and planning for succession."

But Adamson says if families want to see their business move to the next generation, they need to plan for it, communicate about it, and take action.

"Succession should never be an event," she says. "It should be a process."

Two other ideas

Beth Adamson of the South Dakota Family Business Association suggests the following two additional steps to help with family business succession:

1. Have an active board of directors containing experienced, nonfamily business leaders, and use your board. Adamson shares that some family businesses establish a board to help in decision-making processes, which may help minimize family conflicts.

2. Empower an organizational transition team. This team may take the approach of acting as shareholders to assist with facilitating ownership, directorship and management. Establishment of policies, processes and structures that promote professional business structures and that clarify roles is a key to a smooth transition, Adamson says.

8 'How-to' steps

Adamson's first observation in planning for succession is that it starts very early — when that next generation is still children. The things they hear about the business when they are young will have a great influence on their attitude toward the family business in the future. Thus, she cautions against having negative conversations regarding the business — and then adding comments such as "someday this will all be yours."

This is not to say that young people should be left out of knowing the financial side of the business, but it needs to be communicated in an appropriate manner.

She also suggests children should know they have a choice to pursue other dreams if they are not interested in the family business. She grew up in a family with only one boy, and from the time he was born, it was expected that he would take over the family business. Her brother felt forced into the position, and it resulted in he and his father not speaking to one another.

Keeping those points in mind, Adamson suggests these steps for transitioning a business from one generation to the next:

1. Establish a mission statement that expresses the desire for the family business to continue. This helps keep that goal top of mind.

2. Conduct family meetings. Adamson calls this an "essential practice for long-run health of the business." She advises that these meetings should include everyone involved in the business and/or family. She also recommends that these meetings should be for the purpose of information and discussion of goals and challenges. They should not be focused on management decisions.

3. Establish a family participation policy. The purpose of this policy is to plan ahead for how family members will come into the business, thus making that transition a little smoother when the time comes. Adamson suggests addressing such issues as:

- whether working in the family business is an entitlement or an opportunity;
- whether positions will be created especially for family members;

Dealing with disagreements

University of Nebraska's Ron Hanson has offered estate-planning advice to farm families for three decades. He says simple misunderstandings often cause breakdowns in communication among family members, especially during periods of stress.

Hanson concedes that every family has its moments of disagreement, but he says it's not the disagreement that ruins a relationship. Instead, it is how that moment is handled.

He cites some unfair fighting tactics, such as:

- Refusing to admit a problem exists, or pretending there is no issue with which to deal.
- Walking away from someone or giving them the silent treatment.
- Storing up all your gripes and complaints and unloading them at once on your spouse or the rest of the family.
- Spending more time fighting or figuring out who to blame instead of putting energy into finding a solution.
- Taking sides.
- Fighting about the same old problems and issues.

"The trick to improving family relationships is learning how to have your disagreements without being disagreeable," Hanson says.

"Fairness is the key to solving any type of conflict," he adds. "People don't get upset or angry when they are treated fairly."

Hanson suggests communication can be enhanced between family members by being willing to share personal feelings with others, admit mistakes to someone, and to listen to others rather than doing all the talking.

- how evaluations of family members will be conducted; and
- the steps that a family member must take to be considered for a job (college degree/work experience, etc).

Another issue to consider as part of the policy: If a family member leaves the business, can he or she return to the business? If so, what's the process?

Having such a policy in place should help the business and family operations run more efficiently. Adamson says, "Without policies you have ambiguity, and when you have ambiguity, you have chaos."

4. Design a leadership development plan. This is a plan for passing knowledge from one generation to the next. "It's moving from the intuitive to the intentional by writing things down," Adamson says. "The next generation doesn't know what's in your head."

5. Clarify a business strategic plan. This should encompass transitioning current resources into the future. Adamson likes to use the comment: "If you take a resource to the grave, you will dramatically impact your company's ability to compete."

6. Fund parent's personal financial security.

7. Identify successor or a successor selection process. This may tie back to the family participation policy.

8. Complete the transfer of ownership control. Of this, Adamson says, "Letting go is the final test of greatness. Trust and independence are the most generous and courageous gifts parents can give."

For more about the South Dakota Family Business Association, visit *www.usd.edu/fambus.*

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Impact of the family business

Why is survival of family businesses important? Family businesses have a significant economic impact.

- Eight out of 10 businesses are family businesses.
- They contribute 50% of our gross domestic product (GDP).
- 37% of Fortune 500 companies and 60% of publicly traded companies are family-owned.
- 62% of jobs in the U.S. are through family-operated businesses.
- 88% of businesses plan to stay in the family.

Source: 2003 Mass Mutual Survey and FFI.org.