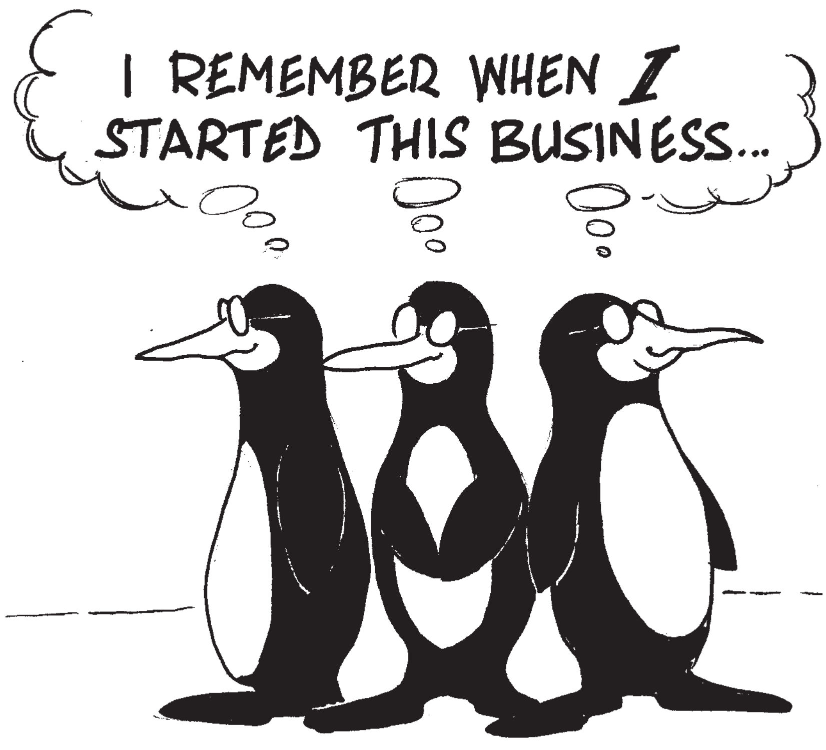
CHAPTER 3

Your Family Business History: Past and Future



Most good accountants and other professional business advisors will have at least a rudimentary understanding of your industry, but they will likely want to know more about the specifics of your particular business. By understanding what has occurred in the past, your professional advisors can more easily help you chart your future course.

Your starting point in a new relationship with any professional advisor is to provide a business history or company overview. Your advisors will sit with you and briefly chart changes in the business and profitability over time. They will likely ask you about your original motivation for starting the business, your greatest obstacles and concerns, and your key milestones along the way. Early in the life of a business, the story is usually about finding the right mix of products and services, and achieving growth. Along the way there might be technology changes, acquisitions, family members coming into the business, and more.

Your Trusted Business Advisor

While people sometimes think that accountants are only skilled at addressing financial issues, in fact the highest-value use of your accountant is to involve him or her almost as a member of your team. While we do our best to remain impartial sounding boards for your business, we find it beneficial to work with you over time to understand your business from the inside, as well. As professional advisors, we have worked closely with a wide variety of businesses over the years and we can offer an objective perspective on issues as diverse as human dynamics and new products. Sometimes we can see the proverbial forest more clearly while you may be distracted by day-to-day management issues.

It is in your best interest to help your professional advisor understand your goals for your business. Knowing where you want to be in five years can be important when making decisions on a daily basis from both a financial and strategic point of view. We can help with business planning on a number of dimensions. For instance, your accountant is trained in certain business methodologies like the SWOT analysis taught in business schools for decades. Looking at your Strengths, Weaknesses, Opportunities, and Threats from an outside perspective can often help you decide how to use your strengths better to take advantage of opportunities in your industry. Or from a competitive perspective, you may be able to anticipate threats or exploit the weaknesses of your competitors to find new niches or expand markets.

Unfortunately, many family businesses only think to call their accountant in as a business advisor when they are in crisis mode or face management transitions. And, of course, transitions in family businesses are often seen as fraught with peril. After all, the statistics say that most businesses won't make the transition to a second generation of family management. (*Forbes* magazine recently said that only 30% of businesses do.) For this reason, your accountant can be most valuable to the family business as a long-term trusted advisor. There are many issues that we can help with, long before or after a transition is at issue.

The Human Factor

Despite the stereotypical portrayal of accountants as "number crunchers," many human factors impact the success of your business operations, so naturally we consider them in our general consulting. It may sound odd, but an accountant can act almost serve as a therapist in some situations. As the owner or senior manager of a business, there are some issues you just can't discuss with employees, competitors, or even family members. An accountant who understands your business can act as a sounding board and advisor.

Family Roles vs. Business Roles

Running a business is a daunting task. And family businesses have their own set of unique issues and dynamics. Many of the issues that family businesses face occur because of the confusion between family roles and business roles. For instance, in a family business, the roles can differ greatly from the traditional roles within the family unit. In a family, the oldest child has a clear role, as does the youngest, and so on. But in the business, the oldest may not necessarily be the boss-in-training. The oldest may fit better in a finance or sales capacity while a younger sibling may possess the qualities of a good candidate for the leadership role. And then there are sons-in-law, daughters-in-law, cousins, aunts, uncles, and other relatives. How do *they* fit into the family and business dynamics?

When some family members work in the business and some don't, it can become even more complicated. For instance, family members working in the business may receive higher salaries and better perks than they would receive in the job market. This can cause resentment from family members not involved in the business — and from non-related employees of the business. Sometimes these issues only surface when the business is passed on to heirs. But the solution in either case is to keep a clear distinction between the role of owners and the role of employees. If you work in the business, you should draw a salary that you would earn in a similar business. If the business distributes profits and you own a share in it, then you are entitled to an owner's dividend as well. But family workers in the business are not entitled to "milk" the business to the detriment of outside family owners.

Your Business History: Past, Present, and Future

As mentioned earlier, an effective professional advisor applies their knowledge of your business's history to help you achieve your future goals and objectives. Often the variables that were significant in the past for your business success will continue to be important in the future as well. But the future will also bring new variables as conditions change in both your industry and your family.

Passing Your Business On

One of the future business issues covered in other chapters is succession. It's worth mentioning here that when you plan your future, succession is a major event that must be considered. If you do not plan for this process well in advance, you'll be at a great disadvantage. After all, as the old saying goes, if you fail to plan, you're planning to fail.

There are only four ways you can make a transition out of your business: (a) die, (b) go public, (c) sell to outsiders, and (d) sell to family or employees. We can't do anything about the first case. However, dying without a succession plan is like dying without a will — it can only cause problems for those who survive you. We won't cover going public and selling to outsiders here. We'll focus briefly on transitioning the business to family members.

Years of experience have taught us that entrepreneurs usually have a difficult time relinquishing control — of anything. Many people who start businesses don't make an easy transition to managing their own businesses. The entrepreneurial personality is different from the managerial personality. However, you've built a successful business, so you've learned some middle ground.

The same issues are in play when considering your succession or retirement. Some people dread even the thought of retirement while others take to it immediately. However, there is a middle ground between giving up *all* control and retiring "down south" that can also help with succession. In many public corporations, the former president or CEO becomes Chairman of the Board. This allows the company to tap into your experience — and you to maintain some control of the company — while giving a new CEO a bit of room to "stretch their wings."

As Chair, you can selectively choose business projects that are of interest to you, but which you never had time to get around to while running the business. This can be a high-value activity in any organization. When you're busy running a business, often you don't have the time or focus to step back and look at the big picture. Having the time to finally drain the swamp instead of fighting alligators can be a very valuable benefit to the business. By focusing primarily on special projects, you can contribute to the business, be available as a consultant, protect your own interests, and enjoy a flexible schedule.

Examples Of Transitions

A fairly typical family situation illustrates several of these points. The founder of a mid-sized manufacturing business had a brother and a daughter who were both involved in the business. He also had two sons who were not interested in joining the family business. Over the years, the founder did not make it clear who would succeed him or what each person would inherit and the daughter assumed that she would be overlooked when the business was transitioned in the future.

When the founder finally faced the issue of succession and discussed it with his family, he announced that he would like his daughter to assume the role of the next CEO. The founder's brother made it clear that he was happiest as a CFO and was not interested in becoming CEO. The founder was not ready to leave the business altogether, so he found a niche area to explore, which he'd had no time to pursue when he was CEO. Once all the parties were clear on their roles, they spent over five years transitioning successfully.

One of the sons who was not involved in the business was an artist and needed financial support. All the children were to receive equal ownership. By clarifying the separation between ownership and control, dividends were paid to all the children, independent of whether they worked in the business or not. (Those who worked also received salaries, of course.) By opening the lines of communication and clarifying the roles of each family member, the transition went smoothly and, as a bonus, the business expanded in the new niche profitably.

On the contrary, a lot can go wrong when a good plan and communication are not established, as illustrated by the case of another manufacturing business. Again, the business was founded by the father who built it up over a length of time spanning nearly three decades. His three sons worked in the business all their lives. They started on the loading dock as teenagers and worked their way up, through the different areas of the business.

The business eventually went public but the family maintained control. Sadly, the father died suddenly — without a succession plan. There was no plan for resolving disputes and there were no strong, impartial, outside advisors. The three sons had equal ownership and poor communication. They argued over every decision to be made. The business manufactured high-tech stereo equipment and the market was changing fast. Technology and outsourcing decisions were among many that didn't get made on time. They lost market share and profitability. Because the business had always been profitable, the brothers had enjoyed luxury lifestyles that they weren't willing to give up. Within ten years the business foundered and it was sold out from under them.

Some of the differences between the two cases are obvious and widely applicable. Some will vary depending on your situation. Most family businesses don't survive to the second generation. If you want to be on the positive side of that divide, plan your transition ahead of time.

Conclusion

No matter how effective you are at running your business, you need trusted business advisors who can offer outside expertise and perspective. And when you pass on the business, your successors may need even more help in order to make a smooth transition. An effective and respected outside advisor not only offers a different perspective and can help with decisions, but can act as a counterbalance and deal with the difficult family issues that must be addressed.

Although accountants are not "real" therapists, they should be aware of family dynamics in order to help you reach your goals, taking into account the numbers, the management information derived from the numbers, and the human elements needed to make a business successful for years to come.

Questions To Ask Yourself

1. Do I have a transition plan and, if so, does my family know about it?
2. When will I be willing to give up some or all control?
3. Am I comfortable that others have the ability to run my company?
4. Have I arranged for family members to receive necessary training in the business?
5. Should I involve a non-family manager as a transition or to help the family?
6. Are there business projects that I'd like to work on if I had time?
7. Are there new areas where I could develop the business?

Questions To Ask Your Accountant

1. What is your experience with businesses like mine?
2. What is your experience with family businesses?
3. How have you helped your clients with the management transition process?
4. What does your role as a professional advisor encompass?
5. How can you help us be more successful now and in the future?