

## The Dark Side of Being Too Generous to Family Employees

By: Barbara Dartt, The Family Business Consulting Group

“I feel trapped,” said Charles. “I don’t trust my sister as my partner or as my co-worker. My dad knows I love the business — he can’t understand why I don’t just suck it up and put up with what I think are bad behaviors. He said my perks look like a good trade-off to him.”

“Have you looked elsewhere?” I said. “It seems that this relationship with your sister is having really negative consequences on your marriage and your health.”

“Yes. And I realized there is no way I could make what I’m making here and I wouldn’t have the flexibility, either.”

Charles’ situation isn’t that uncommon. His salary and benefits were set by his father who, at the time he made the decision, was the leader of the family and the business. It would have been more effective and caused less long-term discord if Charles’ employer had set the pay instead.

### The Real Trap

Charles’ father fell into a classic trap that wrapped a family employee’s compensation with a lot of emotion and role confusion. The amount of compensation may have been adjusted by Dad’s:

- Care as a father;
- Guilt as an absentee parent;
- Experience that family employees bear unique responsibilities and pressures;
- Desire for convenience because it allowed child and parent to have similar standards of living; and
- Generosity of wealth sharing since the business performance allowed it.

Dad set his son’s pay at about 140% of market at his entry to the business. He also allowed Charles considerable benefits above and beyond those provided most non-family employees including extended vacation time,

flex hours, use of a company vehicle, extra travel perks and a bonus that was decided more on need than on performance.

Dad was interested in his son returning to the business and he felt there ought to be some advantages to being a family employee. But he didn’t quantify the full value of the pay and benefits, explain or document the reasoning behind the above-market offer, nor did he let Charles know that he knew the offer was well above market value. Before Charles returned to the family business, he’d been employed by other companies for seven years. He knew that the offer was generous, but didn’t ask his dad why he felt Charles deserved the pay.

### Actions with Unintended Consequences

As I lay out this scenario, the pitfalls of Dad’s decision (and Charles’ acceptance without communication) may be pretty clear. And yet my colleagues and I regularly see cases of parental generosity and informality cause feelings of dependence, dissatisfaction, anger and bitterness. These emotions can exacerbate other relationship tensions within the business, including sibling rivalry, and get in the way of effective governance of a family business.

Overlapping roles in family businesses — like father and CEO — are always tricky to manage. But when dads (or moms) allow the *family want* rather than the *business need* to guide compensation levels, they create a non-sustainable process that often hamstring the next generation’s independence and objectivity.

- When next gens (and their families) are dependent on a pay rate that isn’t hooked to their value in the business, how is the family employee able to make clear, unbiased, business-focused decisions?
- How do they develop, implement or support an existing job family and pay-grade system for non-

family employees that are based on fair market value when their compensation isn't?

- How do they rationalize their pay to non-operating family owners, especially siblings?
- If other family employees join the business, how is their compensation determined? Value? Or need?

## Actions for Mid-course Correction

To address this unsustainable approach, the next generation can lead the challenging work of unwinding the family-driven, need-based “structure” by creating a rational, professional and objective compensation approach. The shift in behaviors means addressing tough issues like quantifying the different levels of value family employees bring to the business, personal financial responsibility, lifestyle expectations and employee performance.

Of course, it is best if you set up the rational, objective process from the beginning. But, in the case that you find yourself some way down the road of a more need-based, senior-generation driven compensation approach, here's how you can begin the shift:

1. Communicate to the family and particularly, to family employees, that the compensation approach will be changing.

- Share the rationale for taking on the change and the process that will be used as well as who has the final decision on the new approach, and, on anyone's change in pay.

2. Develop a compensation philosophy for your family business – a summary of the values and principles that guide decisions on compensation and benefits.

- Gather input from family, family employees and family owners.
- Be sure to discuss what was agreed upon and include the basis on which compensation will be determined. A market-based approach is the most objective and justifiable. However, if your family business has used another basis for a long time, an

abrupt switch to market is not advisable. Sometimes a hybrid model must be adopted to transition from the current approach to fully market-based.

- Outside facilitation is often helpful to support open dialogue, hear different viewpoints and come to a consensus on a statement that represents the family and the business.

3. Get an objective assessment of family employees' current compensation and benefits packages relative to the market. You may also include non-family employees in this process.

- Again, be sure to be clear on who has the final decision authority over how this data will be employed to change compensation and benefits.

4. Adapt the market-based findings to your current situation.

- It may take several years to transition to a fully market-based approach.

## Keep Communicating

Continue to remind stakeholders of the process and where your business is at within that process.

- Let folks know that the process is hard now but this pain is being endured to provide the family and the business a stronger, long-term foundation.
- Be sure to emphasize that no abrupt changes will happen. All adjustments in pay and benefits will be done over time and with lots of notice.

This transition will produce emotional reactions and stress in the short run. If your goal is a sustainable family business that has the highest probability for family harmony and business success, this short-run pain is essential to avoiding a more divisive future.

Aronoff, C., McClure, S., & Ward, J. (2011). *Family Business Compensation*. New York: Palgrave Macmillan contains additional depth on the challenges and traps that exist in compensating family employees.

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