

Employing Family Members as Vendors and Suppliers

By: Stephen L. McClure, Ph.D. and Christopher J. Eckrich, Ph.D.

As businesses and families grow over time, it is highly likely that, at some point, a family member will ask or be invited to provide services or be a supplier to the family business. A variation on this theme is a family member who seeks to own a franchise or an independent distributorship. While this practice is not inherently either good or bad, we see businesses split on whether using family members or their firm as vendors is a good idea.

Consider this. Your sister Karen has just gone into the catering business. You want to champion her business and encourage her by hiring her firm to cater all company entertainment functions that impact your reputation and image in the marketplace. But you pause. What will you do if her firm's product or service is substandard? You have a duty as the CEO to protect your business's reputation for quality. Furthermore, you begin to wonder whether your cousin, a small minority shareholder who works as a CPA, will now expect to handle the firm's tax work. You already have an experienced and trusted accounting firm that is delivering a good product at a good price.

Scenarios like this often lead family business owners to implement a policy that family cannot be used as vendors or suppliers of any kind. This firm rule avoids the potential conflicts identified above and is a popular policy for many family business owners. But what if you already employ a family member as a vendor or believe that a family member's firm can provide a superior product or service?

Family businesses that engage family members as vendors are encouraged to consider the following:

1. Clearly state expectations for quality and service, as you would for any other vendor. To reinforce the

expectation of a business-to-business relationship, rather than that of a family member to family member, put your expectations into a friendly but clearly worded memo. The memo should clarify the expectation for a successful business relationship and identify quality and service expectations so that they are clearly stated by the other party. This memo can be shared with others — with affected managers and employees in the business, as well as with family members — to accomplish the next point: transparency.

2. Seek transparency among family owners about the nature and scope of the work provided. All interested parties should be aware of any business relationships between family owners/members and the family business. Talk openly about the effectiveness of the business relationship in whatever forum makes sense for your family business. In some cases, the right forum is a family meeting with the principals on both sides of the business relationship. Or it might be a management meeting. These discussions work well as long as there is an effective supplier/customer relationship. If something has gone wrong, however, see below.
3. Put the services up-to-bid to multiple vendors on a regular basis (usually every one to two years) to assure that pricing stays competitive. This does not have to be a cold approach that sends the message that you do not value an existing business relationship, rather do it in a way that simply allows you to assess your needs. If you are paying a little more for the relationship and value doing business with a trusted relative, understand that and make sure everyone else does too. If you are paying less

because the family vendor is giving you a deal, be clear, but beware. This kind of arrangement can backfire if there is an assumption on the family vendor's part that reduced quality and service is okay because of the financial consideration he or she is giving. If you find that you are paying too much, you will have valuable information for a negotiation discussion with the family vendor. Another good practice is to initiate a contract term and let the family vendor know that the services will have to be renegotiated at the conclusion. At that time, evaluate the business relationship and consciously decide whether to continue or make changes.

4. To minimize conflict, present the proposal to the board (independent, objective outsiders on the board help here) for review and approval. A family vendor, knowing that this is a step in the process, will increase his or her own attention to the professional nature of the business relationship.
5. Annual reviews of existing family vendor relationships at the board level also are a good practice. In larger family firms, consider appointing a committee of several outside directors (two to three) and key managers (one to two) to review all family vendor and supplier relationships. Some

family firms already may utilize a compensation committee to review family member hiring and compensation decisions, and this committee's scope could be expanded to include family vendors.

6. Use the normal method of making changes to your family employment policy to add a policy statement about family supplier and customer relationships. We hope your process involves a meeting of family members so that expectations are communicated and broad acceptance is promoted.
7. Fix the relationship if it's broken. A severed business supplier relationship can be like a divorce. It is either messy or not, usually depending upon the civility of both parties, not just one. However, after exhausting all genuine efforts available to fix the relationship, make a clean break if that is the only remaining option. In many cases, severing a business relationship with a family vendor is like firing a family member. (See the following article by Bernard Kliska on firing family members.)

Finally, we hope your business-to-business relationships with family members are successful. We frequently hear of the mutual benefits received when they are working well. But the key to this success is a professional and formal business relationship on both sides.

Firing a Family Member

By: Bernard Kliska, Ph.D.

If you think firing a long-term employee is difficult, try firing one who is a family member. As daunting the task may be, sometimes it's necessary. Any major firing threatens to disrupt a business, creating fear, anxiety and shifting alliances among employees. But the disconcerting and disruptive ripples from firing a family member may spread throughout the family as well. Handling this difficult matter the right way can limit emotional damage to the family and business and, with good communication and a few procedural tips it can also ultimately strengthen them.

Prevention is always the best strategy. Because most terminations have long roots, it's advisable to know as early as possible whether a family member is developing into a healthy plant or troublesome weed.

The cultivating of prospective family members should begin before they enter the business. Avoid promising any future position. Constantly reinforce the value that performance, not family status, always determines a person's position in the company. No one is owned any company position—even after they're in it. If termination becomes necessary, the ordeal will be easier for everyone if these values have been firmly established.

Regular and honest performance reviews are essential. Although people disagree about their automatic use, 360-degree reviews—reviews that solicit input from both subordinates and superiors—are an excellent tool for family business members. Not only do 360-degree reviews help ensure the objectivity that is so difficult in reviewing family members, but if termination eventually

becomes necessary, they provide important backup that can help defuse emotional reactions.

Unfortunately, even the most conscientious prevention strategies can fail to offer foolproof protection against the day when a family member may have to be fired. If that moment of reckoning arrives, there are several ways to help everyone through it.

Keep the separation between business and family clear. It's difficult to profess the family values of love, loyalty and all-for-one-and-one-for-all while delivering a termination notice. The person receiving the notice may understandably have difficulty hearing and believing that those family values still include him, but those values should still be clearly stated. Although for the ultimate good of all family members, including the terminated person, the business must come first; firing a family member from the business does not mean firing him from the family. An unsuccessful manager still remains a successful and important father, sister, brother, uncle or daughter. An uncomfortable fit for the business does not have to mean an uncomfortable fit for the family. If a family affair is coming up, discuss it and state that you and everyone else hope the person will participate. Ask if there is anything you or others can do to make him more comfortable. If he refuses to talk about it, schedule a time to check back and keep that commitment.

Offer an honorable out. Consider offering the person a face-saving resignation. It won't cure an injured ego, but it can help. Avoid saving the person's ego by putting him into another position unless you genuinely believe that such a move is for the company's benefit. Remember that offering an honorable out must not short-circuit open, frank discussion of family issues and performance.

Use your board of directors wisely. Use the board for insulation, advice and support, not as a weapon, excuse, surrogate or proxy. While it's usually better for the family if the recommendation for termination comes from the

board, you should avoid hiding behind that. Make it clear that while the board has recommended termination, you have made the final decision. Remember, you want to enhance communication and the family relationship. This requires honesty.

Have an impartial third person present during termination. Sometimes a consultant can promote effective and clear communication helping to navigate the anger, shame, denial and sadness swirling around the room. In an emotionally charged atmosphere, it takes more than good intent to make sure that the important things are said, heard and remembered. Research shows that strong emotions significantly distort memories and recall. A third person can help keep the emotions in check while acting as an impartial witness in case disputes later arise over what was said.

Be alert for family brushfires. Every family has alliances and tensions, often subtle or covert among family members. It is strongly advisable to know how these affect the family and essential to know how these may affect the business. It is impossible for family members to perceive all the emotional and strategic ramifications of a termination. An outside consultant can help anticipate and handle these alliances and tensions. A family map or genogram is particularly useful in planning the termination interview. Charting each family member, including children and in-laws, going at least a generation back and then identifying alliances, tensions, similarities, differences and emotional patterns among family members gives a surprisingly clear picture of how each person is likely to respond. The genogram will provide ideas for how to avoid and handle problems and to bolster egos ahead of time.

Firing a family member may feel like the ultimate paradox in a family business, but by handling it clearly, honestly and with consideration and compassion, it is possible for both family and business to emerge from the ordeal even stronger.

To learn more about our firm and how we serve families like yours, call us at (773) 604-5005 or email us at info@thefbcg.com. There is absolutely no obligation.

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