When the Family Takes Care of the Business, the Business Will Take Care of the Family

By: David Karofsky, The Family Business Consulting Group

Family businesses, no matter how large or small, require active family involvement and attention to keep them functioning and prosperous. If families begin to see their family business as an endless supply of wealth and resources, they risk quickly depleting them. There are times when the business will serve the family, providing them with financial resources, employment opportunities, and other benefits. But there are also times when the family needs to serve the business, putting the business's needs first, even above the family's own.

In my experience working with family businesses of all shapes and sizes, I have encountered this exact dilemma multiple times. Families find themselves in a situation where they are forced to prioritize the business over the family in order to preserve the business and ensure that it can, in return, take care of the family in the years to come. This can often demand a difficult decision in the moment, but one that will positively impact the business moving forward. Ultimately, these challenging decisions to put the family business first will be the choices that best serve the family itself in the future.

Let's look at four different situations that each address a different aspect of working in a family business: family employment, business leadership, ownership, and governance. In each case it was paramount that the family take care of the business first.

Case Study 1: Seeking Family Employment

A technology sales company based on the West Coast had a small number of in-person employees at its central office, making it easy to identify inefficient employees. Unfortunately, for this particular client, one of the inefficient employees was the exiting CEO's son-in-law.

The business was previously 100% owned by a father, John, but he had recently transitioned 50% to his eldest

daughter, Jessica. His other daughter, Anna, had been living on the East Coast with her new husband, Dan, but they had recently moved back west for Anna's job. Dan, however, had been unable to secure work, putting pressure on Anna and their family. To help his youngest daughter, John offered his son-in-law Dan a job as a client representative at the family business.

Dan quickly proved to be a mid-level worker. He wasn't a liability, but he wasn't an asset either. As a client representative, he wasn't proactive, instead waiting for the problems to arrive on his desk and sit before he addressed them. This behavior was quickly noticed by the rest of the small in-person staff, most especially Jessica. As the current vice president of sales, a five-year transition plan had been developed for Jessica to buy out her father and take over as CEO.

However, Jessica was rightfully concerned about keeping Dan on their staff, given his work style. In a company of this size, anyone who was not actively benefiting the business was potentially costing the company opportunities for growth. When Jessica voiced these concerns to her father John, he shut her down, saying that taking care of the family was one of the reasons for having a family business.

This situation put real pressure on both the business and family systems. On the business side, Jessica was faced with the prospect of inheriting a lackluster employee whom the current CEO seemed keen on keeping around. On the family side, Jessica's dissatisfaction with her brother-in-law as an employee was putting tension on her relationship with him, her sister, and her father.

What this family really needed was a family employment policy. This kind of policy would protect both the business and family interests by defining the expectations for employment, compensation, a performance review process, and the consequences for poor performance of a family member. The process of creating this family employment policy allowed the family to reset expectations for family members' work performance and accountability, enabling the family to have in-depth discussions as to what was best for the business and the family going forward.

Case Study 2: Righting the (Leader)Ship

Putting the business first isn't always the course of action that feels the best in the moment, even if it is ultimately the right thing for both the family and the business. Making the difficult decisions necessary to keep everything going in the right direction can be challenging emotionally for the family, as it often means addressing emotional situations with a logical mind.

A large car-part manufacturing company based in Detroit was run by Diane, who had inherited a relatively small factory from her father and had since grown it into a country-wide operation with multiple locations. Diane had always been at the helm of this operation, and it was "her way or the highway." The business had done extraordinarily well under Diane's leadership, and her husband Carter and two daughters, Delilah and Linda, who also worked in the business, had lived comfortably due to its success.

Diane had been diagnosed with a rare degenerative disease that was gradually impacting both her physical and cognitive functioning. Despite this, Diane had remained in her position as CEO for the last several years. Unfortunately, Diane's health challenges were beginning to accelerate. Her disease was starting to impact her decision-making ability and this was being reflected in the company's performance. Delilah and Linda knew they had to move quickly or the business would be put at risk.

It wasn't easy, but the family, in consultation with advisors and their attorney's help, achieved the desired outcome of transitioning Linda to CEO immediately and having Diane relinquish legal control of the business. This transition of leadership, which would have already been challenging given Diane's personality and character, was further exacerbated by her cognitive decline. The family's decision to not act sooner had led the business in a dangerous direction. Luckily, they could come together, put the business ahead of the family, and right the ship's direction.

Case Study 3: Fair, Not Equal Ownership

In some cases, putting the business in a position to take care of the family is a long-term play. For a fourth-generation wholesale food distribution business in the Midwest, this meant reexamining and restructuring the shareholder agreement to create fairness across the ownership group.

This business was originally founded by a married couple with two sons. Each of these sons had two children of their own, resulting in an equal ownership percentage up until the fourth generation, in which one branch of the family ended up with five fourth-gen children and the other had only two. This created a vastly uneven number of shareholders on each "side" of the family.

Ever since the founder of the business had drawn up the first shareholder agreement for his sons, this business had a "one person, one vote" approach to shareholder decision-making. This worked fine for the second and third generations but was sure to cause problems for the fourth, fifth, and subsequent generations, as the bloodline unevenness of shareholders would only grow.

In consultation with advisors, the family reconstructed the shareholder agreement into a percentage-based voting structure, thus reducing the ownership voting percentage on the side of the family with more fourth-generation children and increasing it on the side with less. While it eliminated the "equality" of the individual votes, it created more fairness across the shareholder group, as the voting percentage was now representative of their equity shares.

This decision required unanimous agreement across the entire shareholder group, a task which took several months of intensive discussions. Some members were understandably concerned with diminishing the power of their vote, although they eventually all came to see how this choice would only benefit family harmony. Their decision was a perfect example of going through some short-term change for the long-term health of the current family and future generations.

Case Study 4: A Seat at the Table

Sometimes, the decision that will best take care of the business so that the business can, in return, take care of the family means saying "no" to a member of that family.

A US-based, fifth-generation construction business that was netting over 150 million dollars annually had established a performing fiduciary board of directors for approximately three years. The board was a majority independent board made up of three family members and four non-family members who were independent leaders in their own businesses. It was an incredibly well-performing board of directors, something that the family was very proud of.

At one point, a family member who currently sat on the board decided to step away, meaning that a family seat would be available. A nominating committee was established to decide which of the family members who put their names forward would take the open spot on the board.

One family member, Max, put his name forward, as he hoped that this could be his first chance to serve on the board. In some ways, he felt that the nominating committee was a formality and that he would obviously be given the seat on the board, as he was the exiting board member's eldest child. Max was ambitious and mindful, but also young and inexperienced as a board member. The nominating committee made the wise yet difficult decision to not immediately offer him a seat on the board. Max was disappointed but understood that if he wanted to contribute to the business, he needed to bring something to the table, not just his name.

A few years later, another family seat opened up on the board. Max, who had spent the past several years gaining business experience and serving on a different company's board of directors, was supported by the nominating committee and ultimately voted onto the board by the shareholders.

This family business made it clear that ownership does not constitute a seat on the board. The ownership group knew that they needed to protect the integrity of the board by ensuring that whoever sat on it did so for a reason, and not simply because they were family.

Running the Family Business Race Together

The choices necessary to take care of the business aren't always the easiest for the family to make. They can often mean prioritizing the needs of the business over those of the family, setting the stage for difficult emotions that will need to be processed and worked through. Here advisors can be critical to effective decision making. But when a family relies on their family business for wealth creation and desires to create a sustainable legacy for generations to come, it often needs to be the thing that comes first. Think of the family business as a relay race and as the baton transitions, and you need to have the best people positioned at every milestone to win the race.

Questions to Consider if Your Family is Taking Care of the Business

- Does your family business have a family employment and compensation policy?
- Does your family business have clearly defined roles, responsibilities, and decision making?
- Does your family business have clear lines of delineation with respect to the roles between family, ownership, governance, and management?
- Does your family business have a defined leadership transition plan?
- Does your family business have a defined ownership transition plan?
- Is your ownership group clearly aligned on goals for Growth, Risk, Profitability, and Liquidity?
- Does your family business have a clearly defined governance structure?
- Does your family business board have a clear mission, vision, and purpose with defined criteria for board membership?

David Karofsky is a principal consulant with The Family Business Consulting Group.

The Family Business Advisor.

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