



Family Business 101: Essential Family Business Practices

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Kathleen is a Principal in the Consulting Services Team at MCM CPAs & Advisors. She has had extensive experience helping and advising firms with their growth, development and passing enterprises to the next generation. Her areas of focus include business strategy; family and business governance; family and business policy development; succession planning; leadership development; next generation career coaching; family education and communication; and exit planning that allows owners to exit their businesses on their terms and conditions.

Before working at MCM, she was the Director of the Family Business Center at the University of Louisville and Director of the Small Business Development Center for North Central Kentucky. She also created the Vogt Invention and Innovation Fund for the Vogt family in Louisville, which provides seed stage support and capital for inventors and product developers as well as co-launching the award-winning radio series This I Believe on NPR.

Kathleen is a frequent presenter at family business and trade conferences, educational programs and meetings covering topics such as family governance, change management, succession planning, exit planning, leadership development and family communication.

Education& Certifications

- University of Illinois – Master’s Degree, Urban Planning and Policy
- Valparaiso University – B.A., Communications and World History
- Certified Exit Planner (CEP)
- Advanced Certificate in Family Business Advising (ACFBA)
- Certified in Family Wealth Advising (CFWA)

Professional and Community Associations

- Family Firm Institute (Fellow)
- Business Enterprise Institute (BEI)
- Psychodynamics of Family Business (PDFB)
- UofL Family Business Center
- Greater Louisville, Inc.
- Goering Center for Family and Private Business
- Old National Center for Closely Held Business

Lecturer and Author

- Regular Presenter, Psychodynamics of Family Business Conference, Chicago
- 2016, Family Firm Institute Annual Conference Presenter
- Family Business Magazine
- 2014, Entrepreneur Magazine, 7 Lessons in Harmony for Family Startups
- 2010, Business First, Family Businesses are the Cathedrals of our Economy
- 2008, Business First of Louisville, Bound by Synchronicity: Varied experiences poised Kathleen Hoyer to lead the Small Business Development Center
- 1994, Crain’s Chicago Business, That Cando Attitude Group Floats Small Start-up Loans



Housekeeping

- + Put your “burning questions” in the chat
- + Let us know the name of your family business and what Generation you’re in
- + Feel free to raise a hand to ask a question
- + Email me if something isn’t addressed Kathleen.hoye@mcmcpa.com
- + Family Business Peer Group: Interested?



“Family Business” is a Paradox


Family

Love
Inclusion
Equity
Collaboration
Legacy
socialism

Business

Money
Merit
Profit
Competition
Innovation
capitalism

paradox

[ˈperəˌdäks] 

NOUN

a seemingly absurd or self-contradictory statement or proposition that when investigated or explained may prove to be well founded or true.

"in a paradox, he has discovered that stepping back from his job has increased the rewards he gleans from it"

synonyms: contradiction · contradiction in terms · self-contradiction · inconsistency · incongruity · anomaly · conflict · absurdity · oddity · enigma · puzzle · mystery · conundrum · oxymoron · antinomy

- a statement or proposition that, despite sound (or apparently sound) reasoning from acceptable premises, leads to a conclusion that seems senseless, logically unacceptable, or self-contradictory.
"a potentially serious conflict between quantum mechanics and the general theory of relativity known as the information paradox"
- a situation, person, or thing that combines contradictory features or qualities.
"the mingling of deciduous trees with elements of desert flora forms a fascinating ecological paradox"



Did You Know?

The number of family businesses that make it to the second generation is.....

DROPPING!

Before: 1 in 3 (30%)

Now: 1 in 5 (20%)



What is a Family Business?



What is a Family Business (FB)?

TECHNICAL DEFINITION

A family business is an enterprise in which:

- + the majority of the votes are held by the person who established or acquired the firm (or by his or her spouse, parents, children or children's direct heirs)
- + at least one representative of the family is involved in the management or administration of the firm
- + the person who established or acquired the firm (or his or her family) possesses 25% of the voting rights through his or her share capital
- + and at least one family member sits on the board .



What Makes FB's Different?

REAL LIFE DEFINITION

- + The presence of the family
- + The owner's dream to keep the business in the family
- + The overlap of family, ownership, and management
- + The competitive advantage derived from the **positive** interaction of family, management, and ownership



Top 5 US Family Businesses

1. Wal-Mart - \$421 Billion
2. Ford Motor Co. - \$128 Billion
3. Cargill - \$107 Billion
4. Koch Industries - \$100 Billion
5. Carlson Companies - \$38 Billion



Family Business Overview

- +90% of all businesses in North America
- +78% of all new job creation
- +35% of fortune 500 companies (not just mom n pops)
- +30% make it to 2G; number is dropping (20%)
- +90% of families control or contribute to more than one firm (family enterprise model)



2019 Update: Family Firms

- + 1 in 10 of current FB leaders are Female (18% WW) ☹️
- + 2 in 10 have a robust succession **plan**
- + 4 in 10 have a retirement **plan**
- + 4 in 10 worried about digital disruption
- + 6 in 10 **plan** to pass to next generation of family
- + 6 in 10 of the next CEOs will be MILLENNIALS
- + 6 in 10 have an emergency/contingency **plan**
- + 8 in 10 expect steady growth in next two years
- + 8 in 10 involve directors in strategic growth **planning**

Source: University of Louisville, PWC,



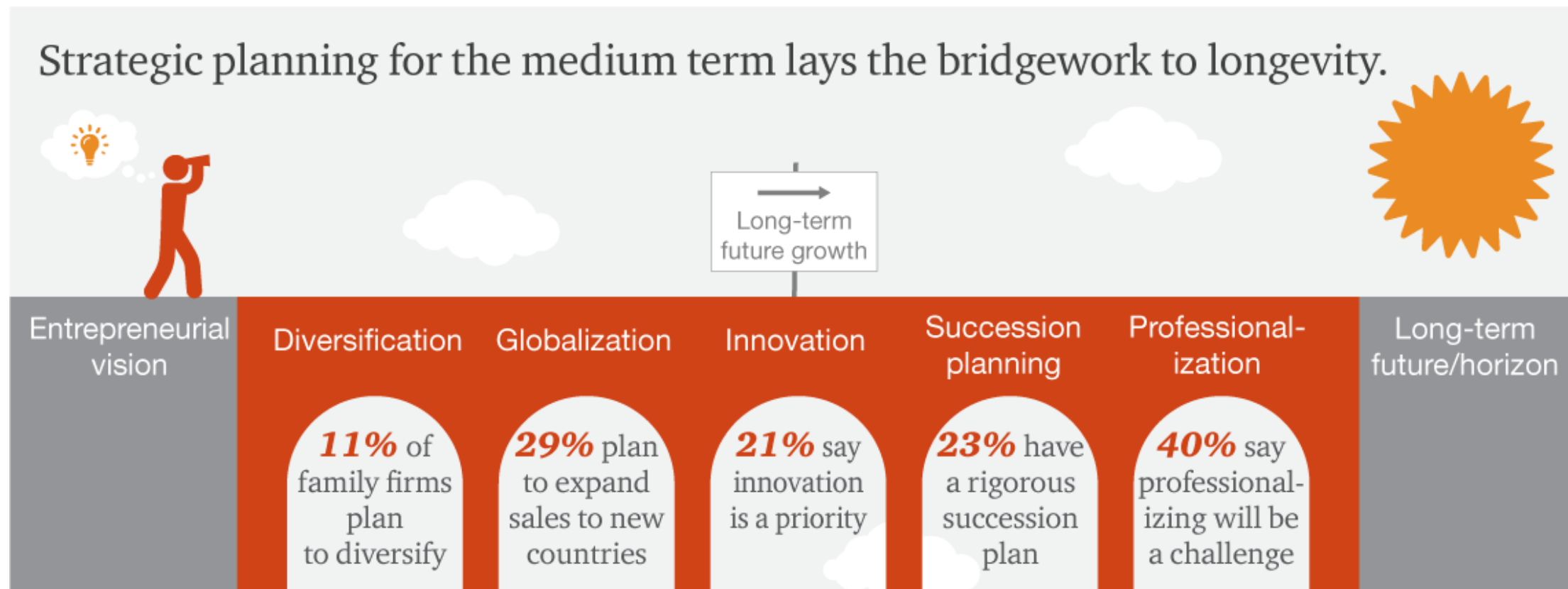
The State of US Family Businesses

For many family firms, the *missing middle* is the *strategic bridgework* spanning the mid-zone between two visions —

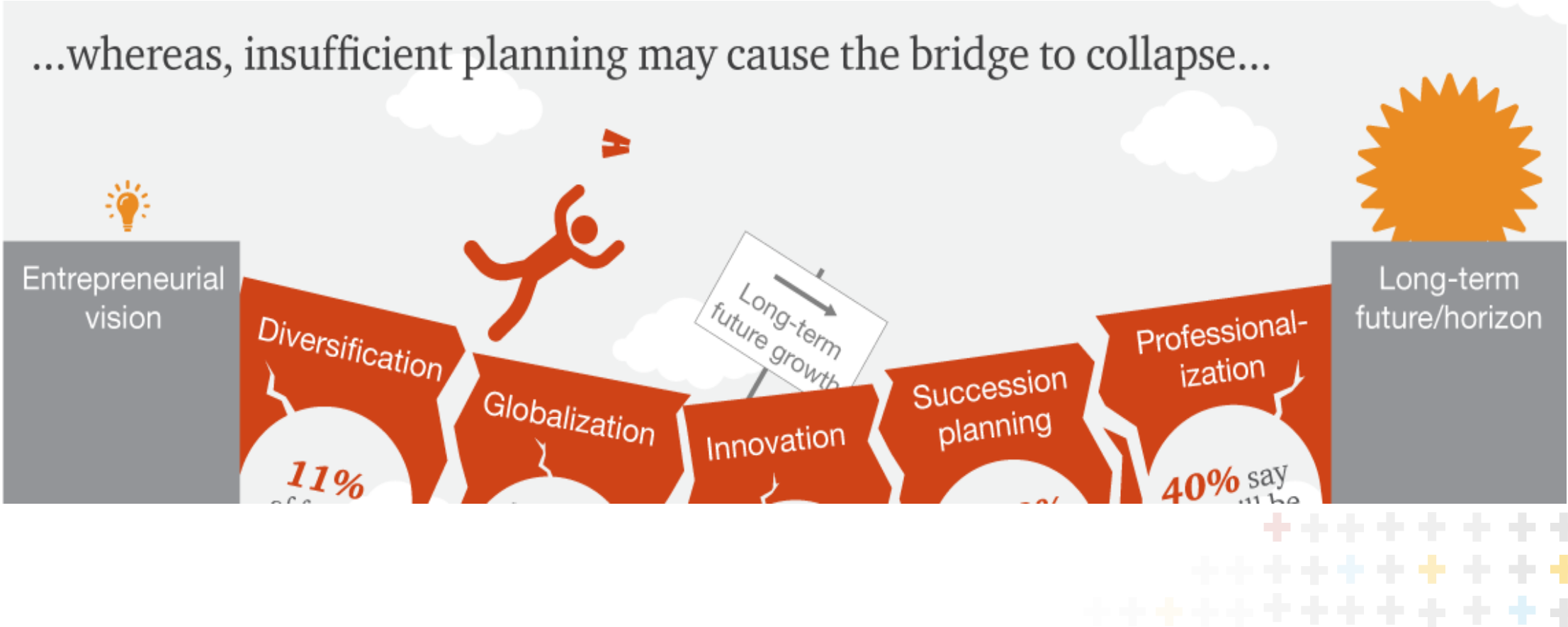
the **entrepreneurial vision** that sparks the formation of a business and

the **long-term vision** that allows family firms to pursue goals far into the future.

Planning: The Missing Middle

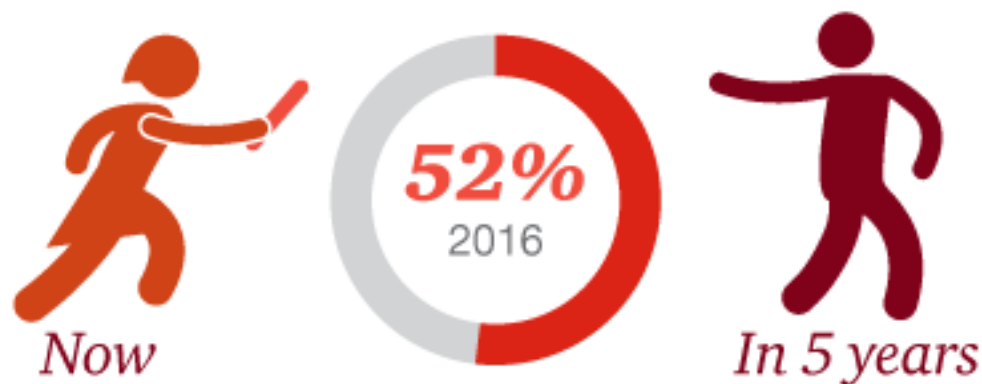


The Missing Middle



Planning is Hard

Difficulty with strategic planning may be why fewer firms plan to **keep the business in the family**.



Among firms planning to change hands in the next five years, only about half of them intend to pass ownership to the next generation.



... but it's not impossible.

The longevity of family firms depends on sound **succession planning**. Firms that have made it to the 3rd generation and beyond are more apt to have a succession plan than younger firms.

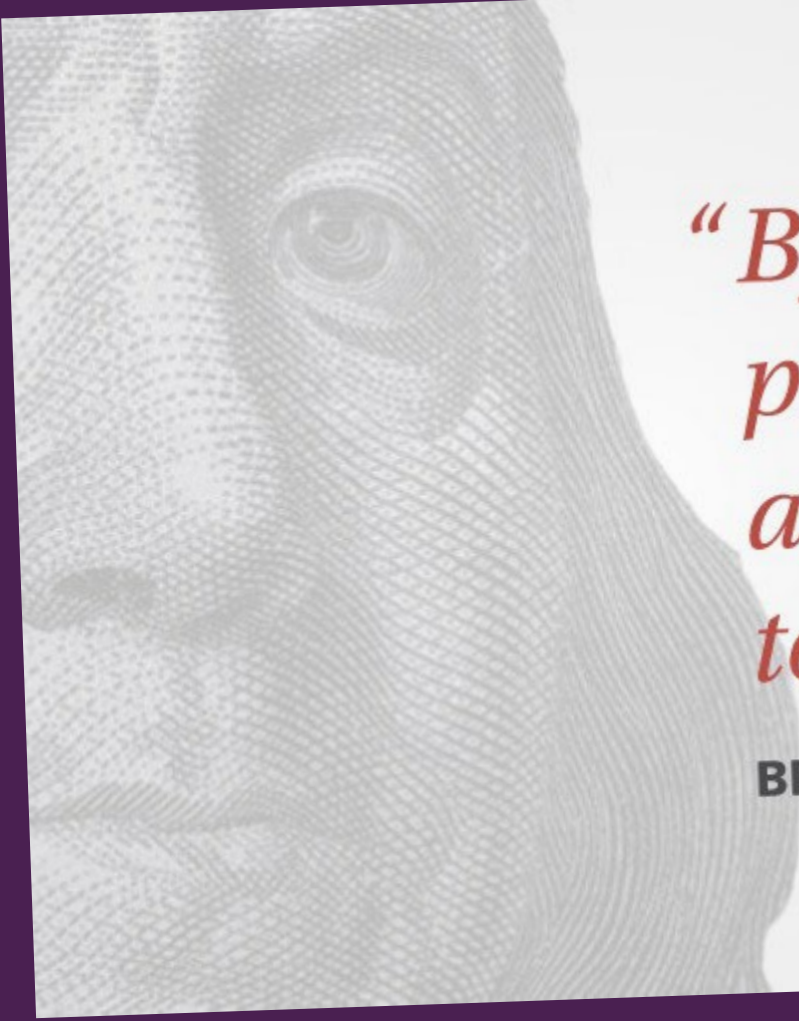


75% of 3rd+ gen firms have a plan



62% of 1st/2nd gen firms have a plan





*“By failing to
prepare, you
are preparing
to fail.”*

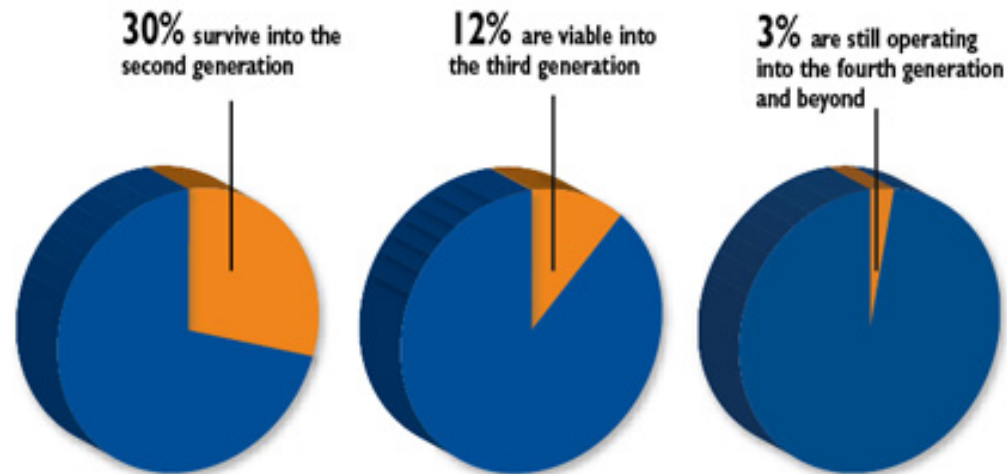
BENJAMIN FRANKLIN

The Problem



PASS IT ON?

Family-owned firms make up 80% to 90% of all U.S. businesses, yet only 3% of all family businesses survive beyond the third generation.



Source: Family Firm Institute, 2005



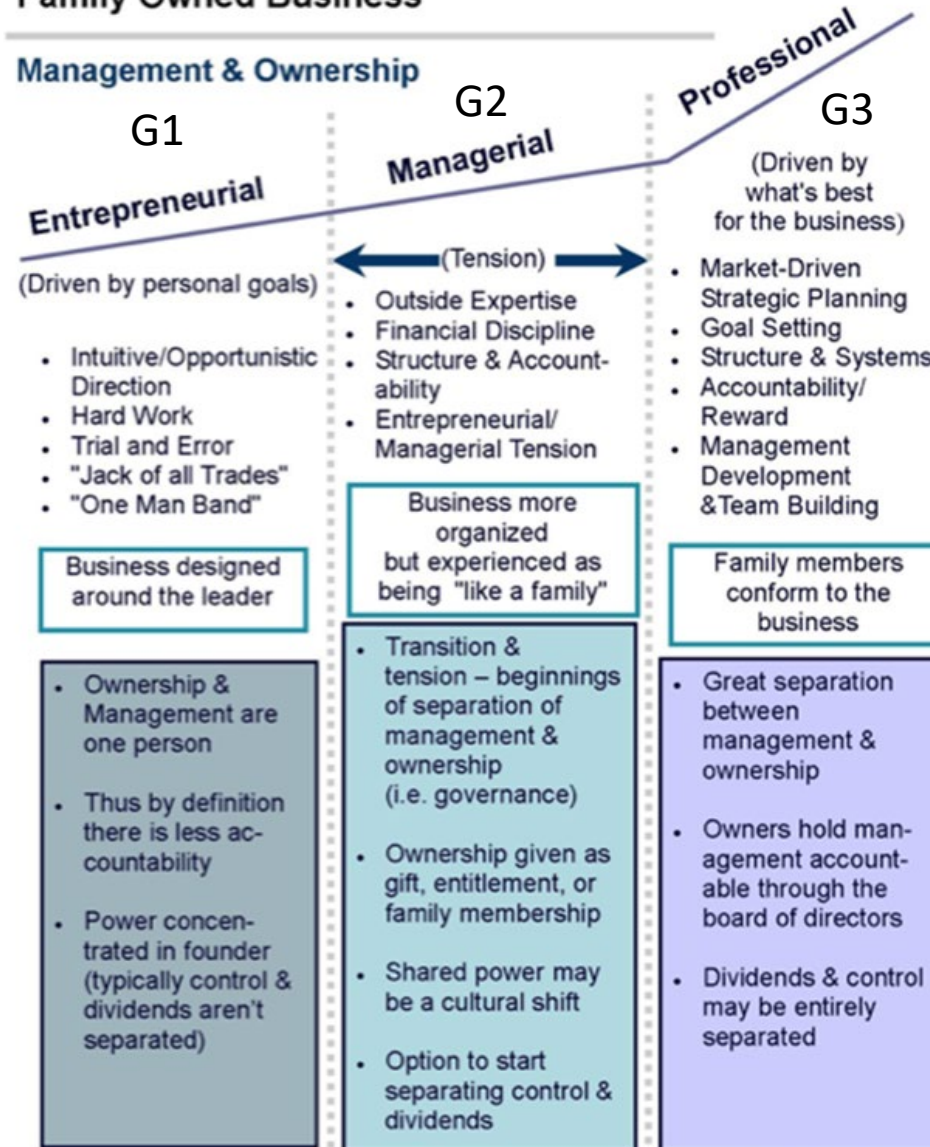
Generational Tension Points

G1: Entrepreneurial/Founder

G2: Managerial/Sibling Team

G3: Professional/Cousin Consortium

Stages of a Successful Multigenerational Family Owned Business



17 Family Business Pitfalls

1. **Growth limitations.** Lack of capital and resistance to re-investment in the business or pursuit of outside resources artificially stunts growth.
2. **Non-business issues.** Family problems, including health issues, marital affairs, addiction and financial problems create difficult political situations for other family members.
3. **Soft structure.** The frequent lack of clear policies and business norms for family members may lead to operational confusion.
4. **Limited vision.** Lack of outside input on how to operate the business, as well as competing visions held by various family members may limit new opportunities
5. **No written strategy.** Long and short-term plans often remain undocumented.



17 Pitfalls (continued)

6. **Compensation issues.** Compensation and benefits for various family members may not reflect their actual participation or may conflict with non-family compensation packages.
7. **Who's in charge of what?** Poor definition of roles and responsibilities limits accountability and efficiency.
8. **Skills and talent.** Family members may lack the skills and abilities necessary for their positions, but it may be impossible to fire them.
9. **High turnover.** "Outsider" employees may sense that family members will always advance quicker; also, they may become frustrated with family-directed management.
10. **Succession planning.** Uncertainty as to if, how and when the next generation will take control is the omnipresent elephant in the room.



17 Pitfalls (continued)

11. **Poor training.** Integrating family members into the company is often automatic rather than systematic.
12. **Paternalistic leadership.** Tradition and family respect tend to override the pursuit of improved management practices, including the integration of women into leadership roles.
13. **Resistance to change.** The desire to keep the status quo can frustrate younger family members and prevent the adoption of new ideas. (i.e. Technology)
14. **Communication problems.** Relationships within the family, rather than a clear process, drive communications, leaving them subject to motivation by anger, frustration or envy.

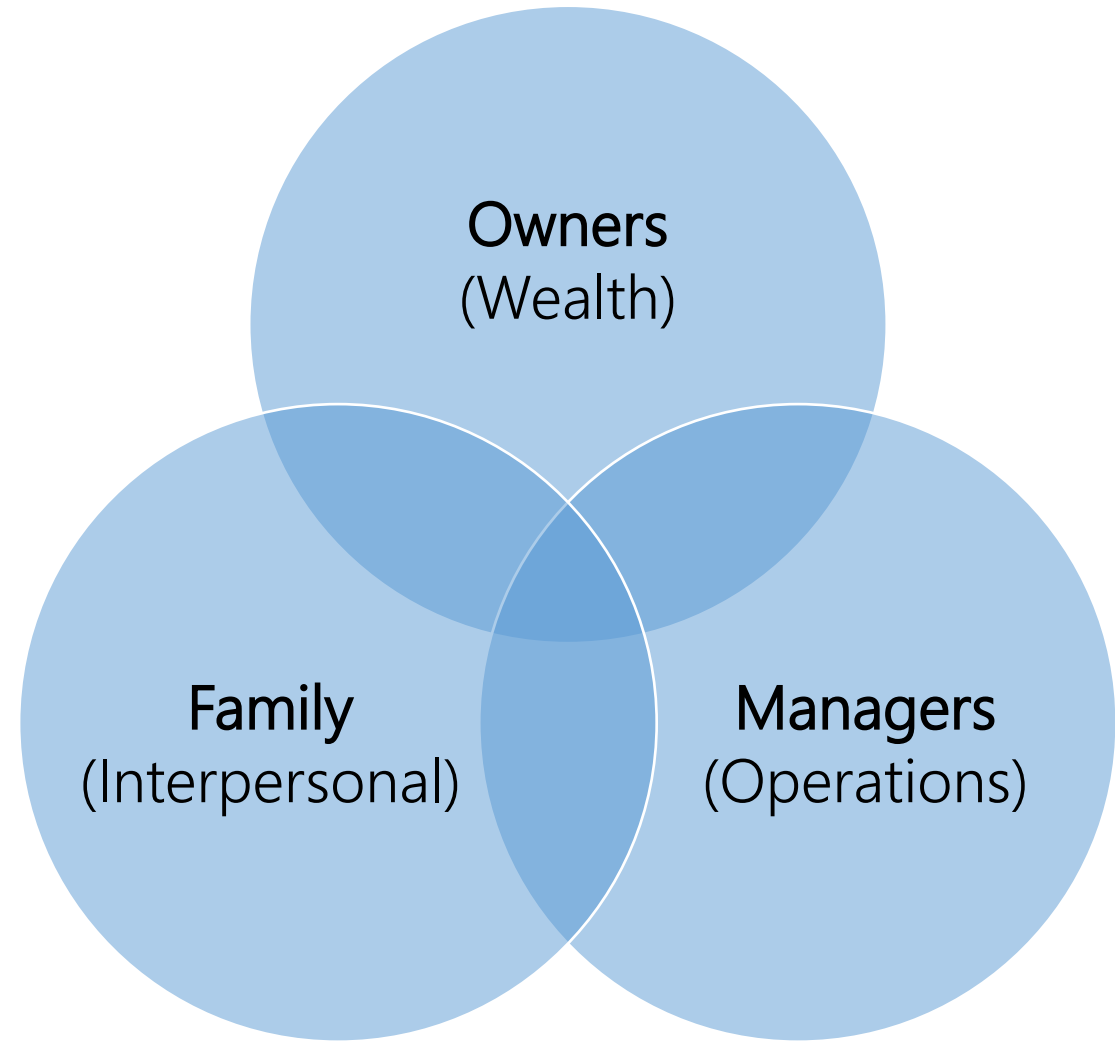


Still More...

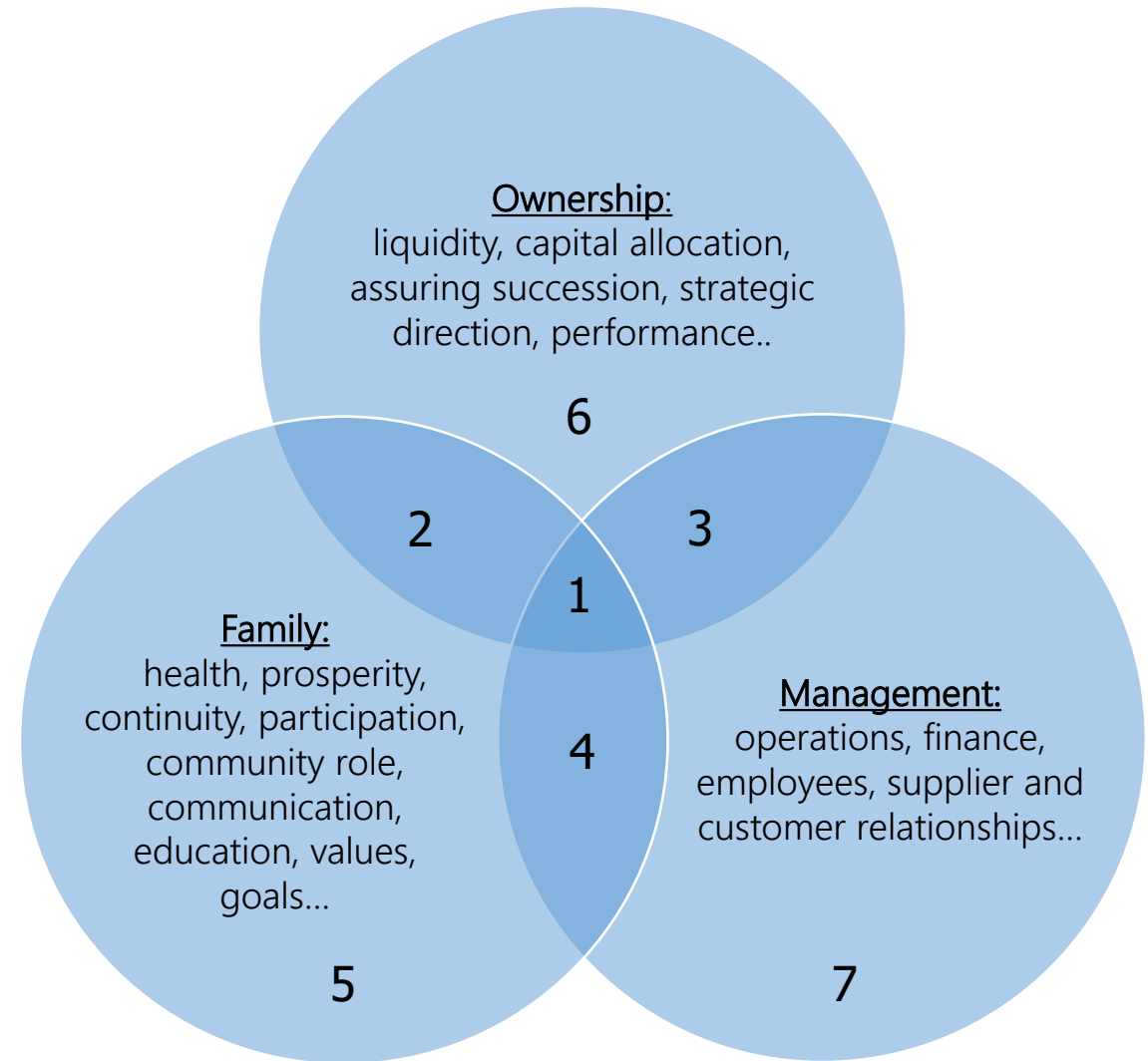
- 15. **Exit strategy.** Little or no attention may be paid to how to sell, close or merge the business.
- 16. **Valuation questions.** No focus on what the business is worth or what will make it more or less valuable puts family members at odds with the marketplace.
- 17. **Control issues.** Family members with little day-to-day participation may have unusually high levels of control.



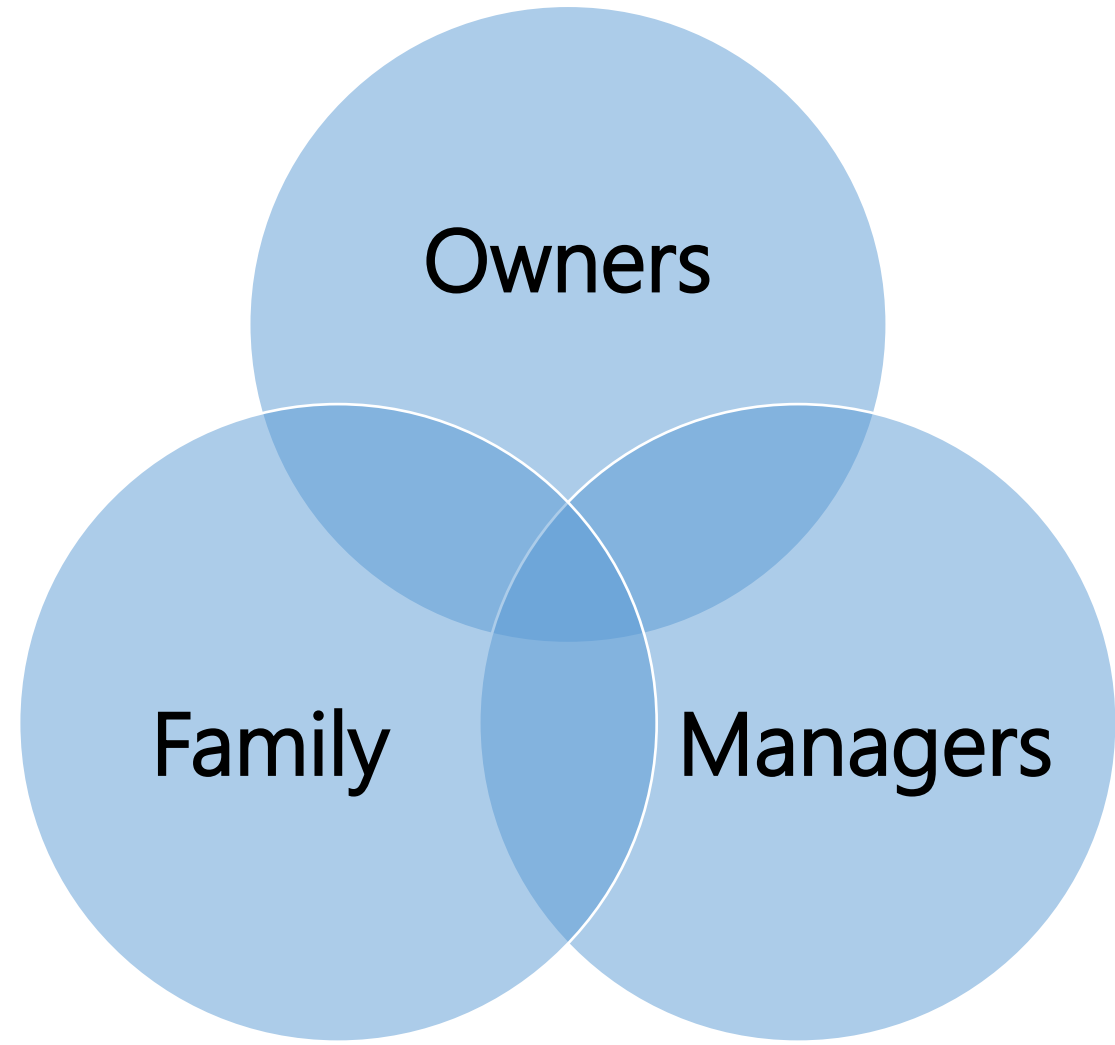
The Three Circle Model



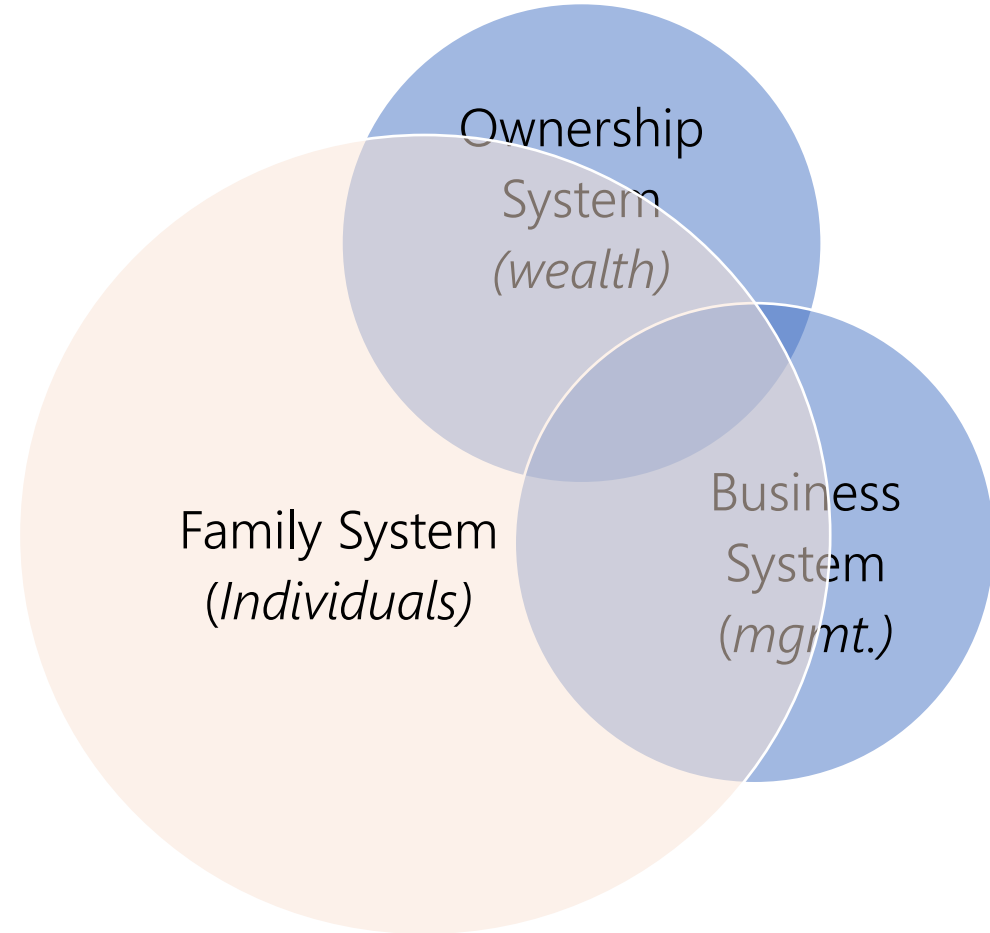
Primary Concerns



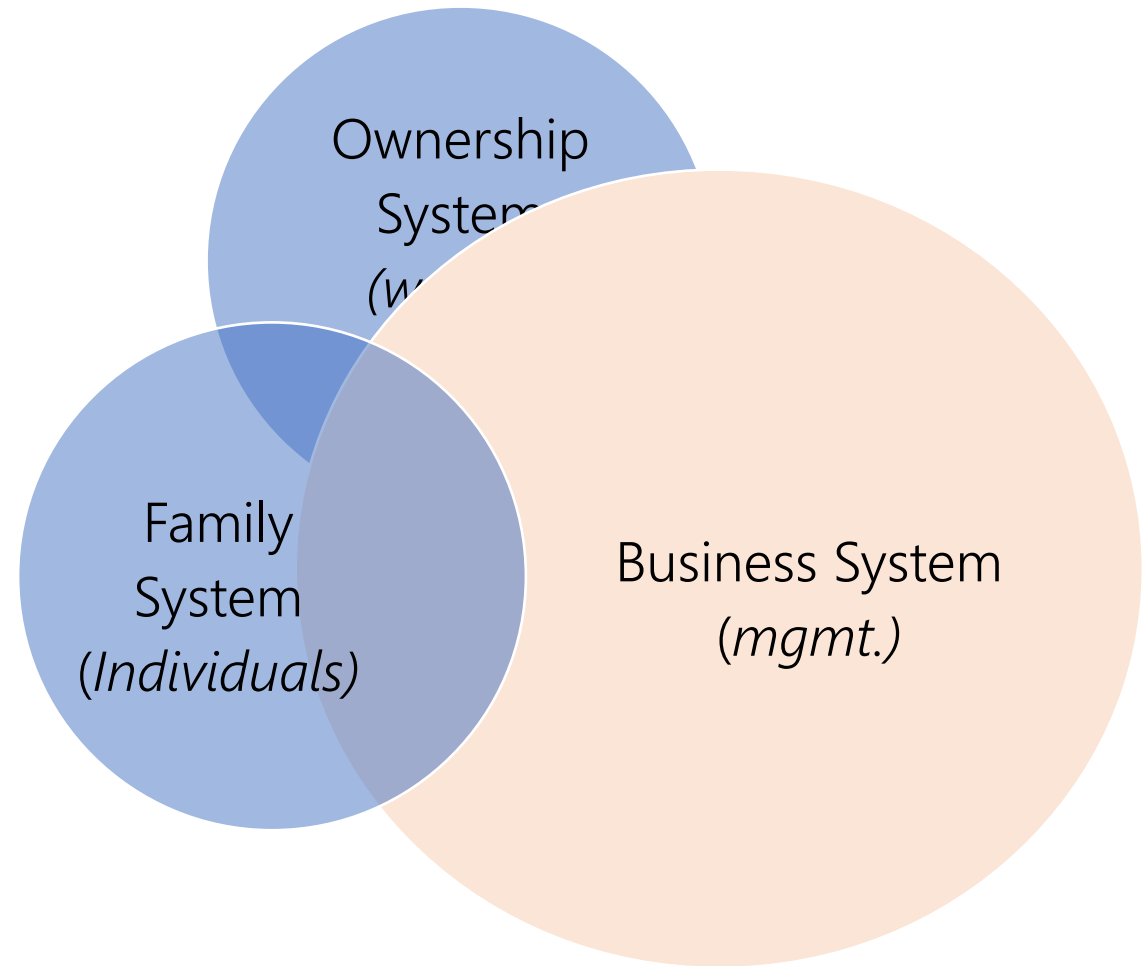
Dimensions of FB Governance



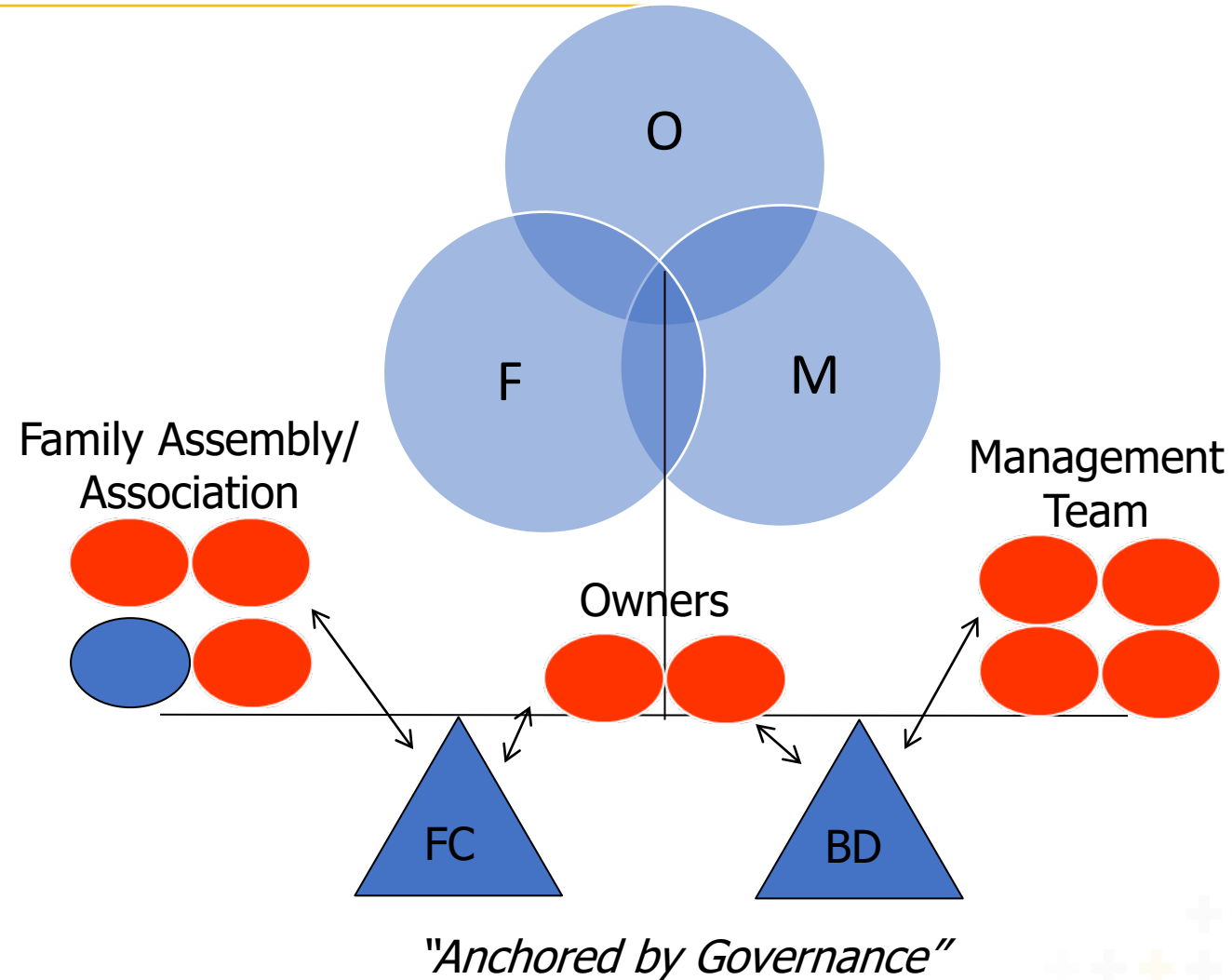
Family First Model



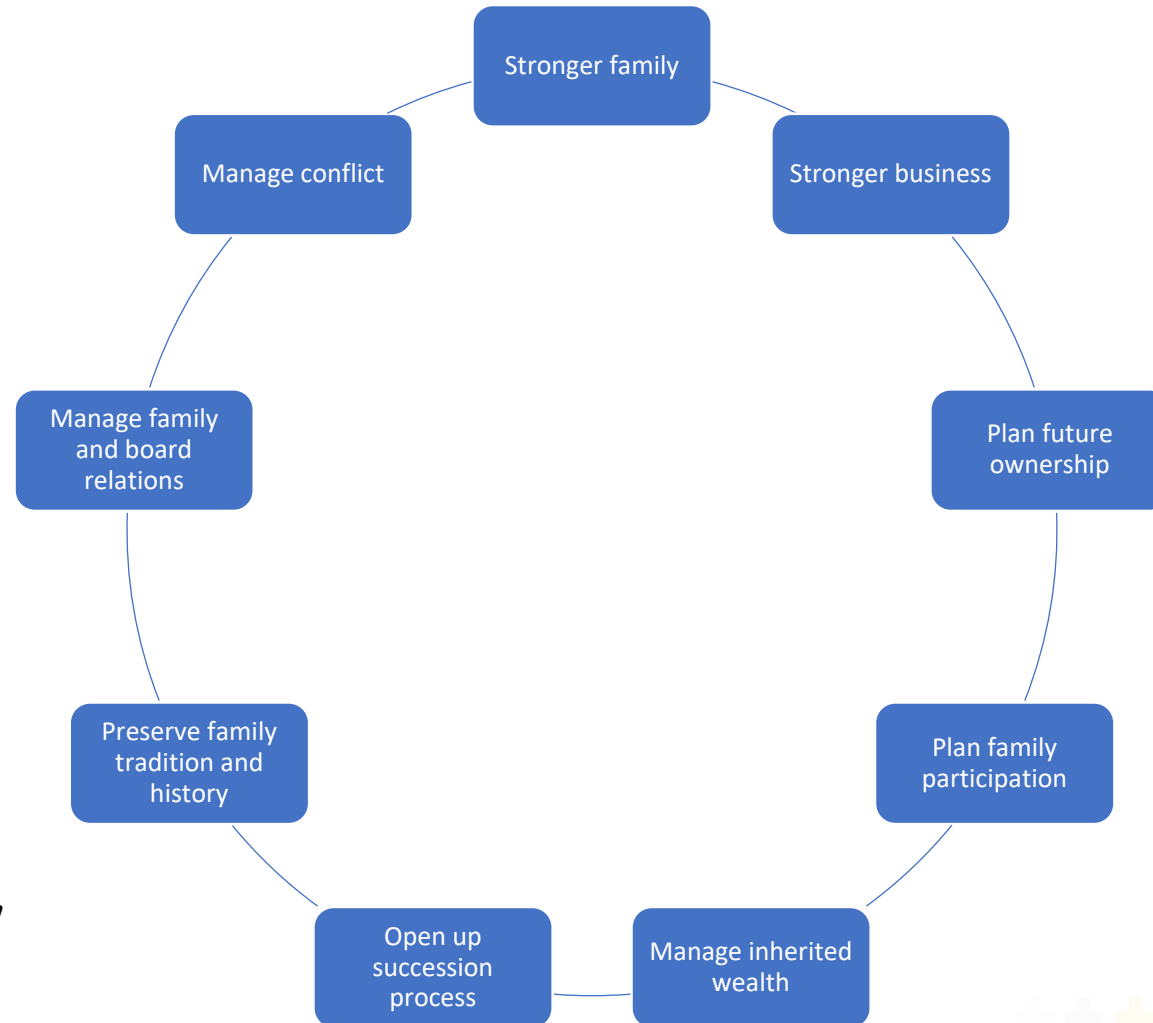
Business First Model



Dual Governance



Benefits of Family Meetings



Source: *Family Meetings: How to Build a Stronger Family and a Stronger Business*
www.efamilybusiness.com



Benefits of an Active Board



Source: *Creating Effective Boards for Private Enterprises: Meeting the Challenges of Continuity and Competition* by John L Ward, 1991. www.efamilybusiness.com



Evolution of FB Governance

Stage	Family Organization	Coordinating Process	Board Organization
G1: Owner-manager or entrepreneurial	Informal Family meetings among nuclear family	"Kitchen to Dining Room Table" Fireside chats or mtgs.	Advisory council
G2: Sibling Partnership	Family meetings: Family members and spouses; family council or task force to handle projects	"Negotiating Table" Fireside chats, joint meetings, governing committee	Board composed of majority of outside directors and selected family members
G3: Cousin/ Collaborative	Family council Family assembly Shareowners subcommittees	"Board Room" Governing committee	Board, subsidiary boards, junior boards (as developmental tool)

3 or more = Higher Entrepreneurial Performance

Governance Practice	Global %	North America %
Women on the board	31	34
Formal succession process	16	18
Formal bylaws	16	21
Formal BOD	11	8
Board of Advisors	7	5
Different share classes	6	8
Mandatory retirement age	6	1
External directors on board	5	2
Majority external directors	3	3



Policies—Avoid the Nightmares

Anticipate future issues and decide how you will deal with them before they become issues. Consider these questions:

- *What happens if my brother thinks my nephew should be promoted but I disagree?*
- *What happens if my cousin gives his wife company stock and then they get divorced?*
- *What happens if we have to fire a family member?*
- *With 11 family members on the board, shouldn't some be getting off?*
- *How can I tell my son that he needs to get more work experience before joining the FB?*
- *Even if I'm not in the business, I own shares. Why shouldn't I get the same financial information as the family who are in the business?*
- *Why should your husband get paid more than mine?*
- *What do you mean, you took a \$100,000 loan from the business?*
- *Why can't I be on the board?*
- *How can your son work in the FB and own another business at the same time?*
- *Shouldn't the FB buy its group health policy from me? After all, I'm family*



Start with the Easier Policies

Easier	Harder	Hardest
Employment (when not facing it anytime soon)	Compensation	Governance (family council and BOD)
Code of Conduct	Publicity	Shareholder Agreement
Philanthropy	Dividends	Conflict of Interest



The Twelve Commandments of the Family Business Owner

*From: Beyond Survival, A Guide for Business
Owners and Their Families, Leon A. Danco, Ph.D.*

- + I. Thou shalt share thy dream with thy family.
- + II. Thou shalt inform thy managers and employees, "This company shall continue forever."
- + III. Thou shalt develop a workable organization and make it visible on a chart.
- + IV. Thou shalt continue to improve thy management skill and knowledge, that of thy managers and that of thy family.

The Twelve Commandments of the Family Business Owner

*From: Beyond Survival, A Guide for Business
Owners and Their Families, Leon A. Danco, Ph.D.*

- + V. Thou shalt institute an orthodox accounting system and make available the data therefrom to thy managers, advisors and directors.
- + VI. Thou shalt develop a council of competent advisors.
- + VII. Thou shalt submit thyself to the review of a board of competent outside directors.
- + VIII. Thou shalt choose thy successors.

The Twelve Commandments of the Family Business Owner

*From: Beyond Survival, A Guide for Business
Owners and Their Families, Leon A. Danco, Ph.D.*

- + IX. Thou shalt be responsible that thy successors be well taught.
- + X. Thou shalt retire and install thy successors with thy powers within thy lifetime.
- + XI. Thou canst not take it with thee—so settle thy estate plans—now.
- + XII. Thou shalt apportion thy time to see that these commandments be kept.

Succession Planning Checklist

- ✓ Estate Plan Optimized and Current
- ✓ Exiting Owners have sufficient liquidity and income for retirement without taxing the business
- ✓ Business system in good condition
- ✓ Family system in good condition
- ✓ Ownership system in good condition—particularly with multiple branches
- ✓ Key business relationships intact and all comfortable with successor(s)
- ✓ Emergency death and disability plans for all key employees, especially CEO
- ✓ Sufficient liquidity within business/cash flow
- ✓ Developmental plan for successors in place
- ✓ Sufficient time frame for executing succession plan (5-15 years)
- ✓ Buy-sell agreements ready for new owners-outgoing owner agreements ready to be transferred, adjusted or dissolved.
- ✓ Exiting owners have “tried out” retirement
- ✓ Plan B for everything that matters

Courtesy of Vaughan Scott, Axiom Financial Strategies Group of Wells Fargo



Recommendations

1. Create a Contingency Plan (hit by the bus)
2. Share it with persons affected
3. Have regular informal “family meetings” to discuss the future of the business and what you currently know
4. Consider setting up an advisory board
5. Figure out your exit strategy (see next slide)
6. Map out your growth strategy
7. Write stuff down/policies/procedures/agreements
8. Learn all you can about FB best practices
9. Embrace complexity
10. COMMUNICATE!



More to come...

You are *invited* to a

Family Business

Best Practices Series

The Five Behaviors of a Cohesive Team
Thursday, June 17, 2021 at 10:00 - 11:00 am ET

Register

What is an Exit Strategy and Why Do You Need One?
Wednesday, August 25, 2021 at 10:00 - 11:00 am ET

Register

Succession Planning Fundamentals
Tuesday, November 9, 2021 at 10:00 - 11:00 am ET

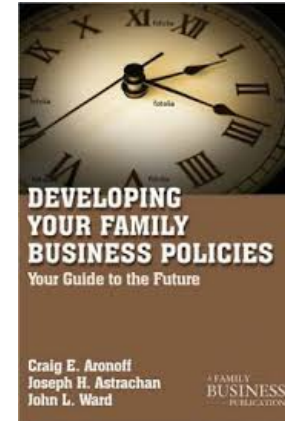
Register



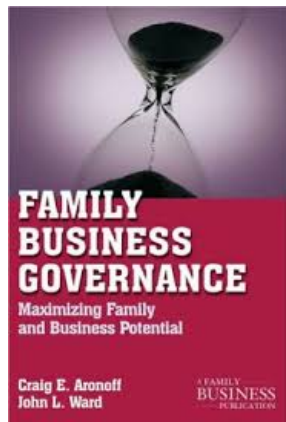
Bibliography



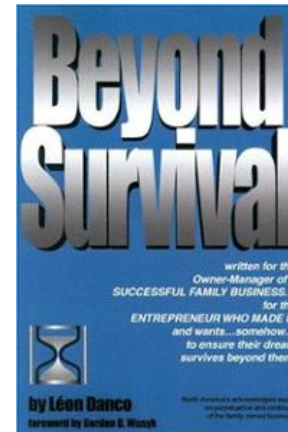
The Family Council Handbook: How to Create, Run, and Maintain a Successful Family Business Council, Eickrich and McClure, 2012



Developing Family Business Policies: Your Guide to the Future, Aronoff and Ward, 1998



Family Business Governance: Maximizing Family and Business Potential, Aronoff and Ward, 1996



Beyond Survival, Leon Danco, 1975





Thank You!

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PEOPLE
MATTER



LEADERS
INSPIRE



EXCELLENCE
RULES

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