AVOIDING THE

3 BIG PITFALLS

WHEN TRANSITIONING YOUR FAMILY BUSINESS

A pocket guide to doing it right
(and not worrying about it at 3am)

WHO IS THIS FOR?

Are you involved in a family business, and wondering "What happens next?" as the time approaches for a generational handover?

Are you wondering "How do we get the right person leading the business, without starting World War III?"Or "What should we consider when planning this?"

Then this guide is for you. It's intended to give you clarity about how to do this well, and how to start.

The transition is hard, and it often fails. You can avoid that failure.

We've written this quick guide because we've seen too many family businesses close, or be liquidated, when everyone assumed they would somehow continue.

Someone must initiate the conversation: maybe the founder, now thinking of stepping back; maybe their partner, wanting them to take some reward for the years of hard work; maybe a son or daughter, considering their own life plans; maybe indeed a daughter- or son-in-law, who can often see what the family overlooks.

If you are that person, wondering how to get the change started, this guide is for you. We'd like you to start the journey with confidence. We'd like you not to be awake at 3am.

Enjoy.

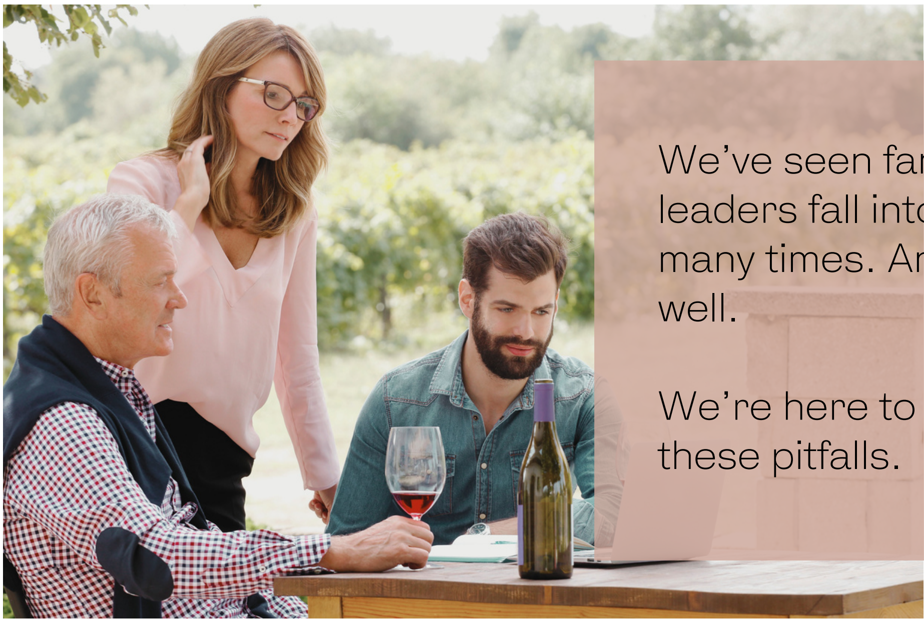
WHAT ARE THE 3 PITFALLS?

This is where we see things go wrong, too often.

1. Assuming a family member (or several) will take over the business. That may not be the best road to take, for the business or the family.

2. Not planning. Assuming "We'll cross that bridge when we come to it." Guess what? It will be too late by then.

3. Not seeking professional help. This is too complex, and too emotional, to work through without a skilled independent advisor who specialises in family business.



We've seen family business leaders fall into all of these, many times. And it doesn't end well.

We're here to help you avoid these pitfalls.

WHAT ARE THE OPTIONS?

Ken and Janet were successful farmers, with three talented daughters. All three of the girls went to Uni, and were on their way to successful professional careers. When I met Ken at a business function, he explained to me that the family had long been discussing their future. None of the girls was interested in taking over the farm. They had decided as a family that when the youngest, Lucy, finished Uni, they would sell it. Ken and Janet would put some money in trust for each of the girls, to be spent on long term benefits such as their own kids' education. The rest of the money would buy Ken and Janet a pleasant retirement home on the coast, near enough to their old farming community for occasional reunions. Ken was looking forward to a lot of fishing.

A neighbour had already agreed to buy the farm at a fair valuation when the time came - he wanted to expand his holdings and was looking for an opportunity.

This was an emotional time. Ken had inherited the farm from his father, who died young, and the girls had grown up there. But the family had talked it through over some time, in depth, and they were all mentally prepared for what would happen when Lucy graduated.

A family business transition can go many diffent ways, with many different outcomes. Here are three (de-identified of course) to get you thinking.

Kurt and Helen started a specialist wholesaling business many years ago. As a young man Kurt decided, after a matter of weeks, that the profession he trained for was not for him. Since then, he had tenaciously carved out his own place in the world, all the way to building the family home with his own hands. He built the business in the same fiercely independent spirit. Helen participated, but kept a place in her own profession.

By the time their three children, Martin, Rachel and Gerald were adults, the family had experienced many internal conflicts. To Helen's dismay, in particular, they could hardly converse without recriminations. All three children had tried taking a place in the family business, but this did not work out for Martin or Gerald, and only in part for Rachel.

When Kurt reached his seventies, the question of "what next" for the wholesaling business could not be ignored. There was a real risk that the value built up, over so many years of such hard work, would be lost.

After some difficult conversations, the three children met together, without their parents, to consider what outcome they wanted. They decided that they could (a) be in the family business together, or (b) remain friends. They chose (b). The business will ultimately be sold. It is unlikely to realise the value it would have as a going concern, with a new generation of managers in place; but the family will be happier.

The Hampden business

had become well-known, and very profitable, for its range of home and commercial hardware products. George and Mary Hampden started with little but enthusiasm, and created a well-known business, finding time along the way to bring five children into the world. George was getting on, and ready to retire, before the family started a serious conversation about "what next?" Two of the children, Sam and Carla, had loosely structured roles in the business. The other three had their own careers. But a long kitchen-table meeting had established that everyone wanted to see the business continue in the family, and everyone was prepared to help. With the help of professional advisors, and after long negotiations, the eldest daughter, Naomi, became the agreed successor to her father as managing director. Sam and Carla had their roles formalised, and the other two, Nicholas and Tim, joined the board of directors while continuing in their outside careers.

George and Naomi joined an executive development program together. The others agreed to formalise the skills they would need to continue the success and growth of the Hampden business after George's retirement.

Today the company is not run as it was in George's day, but it remains well-respected and profitable, building on opportunities that became apparent only as the younger generation re-structured the business.

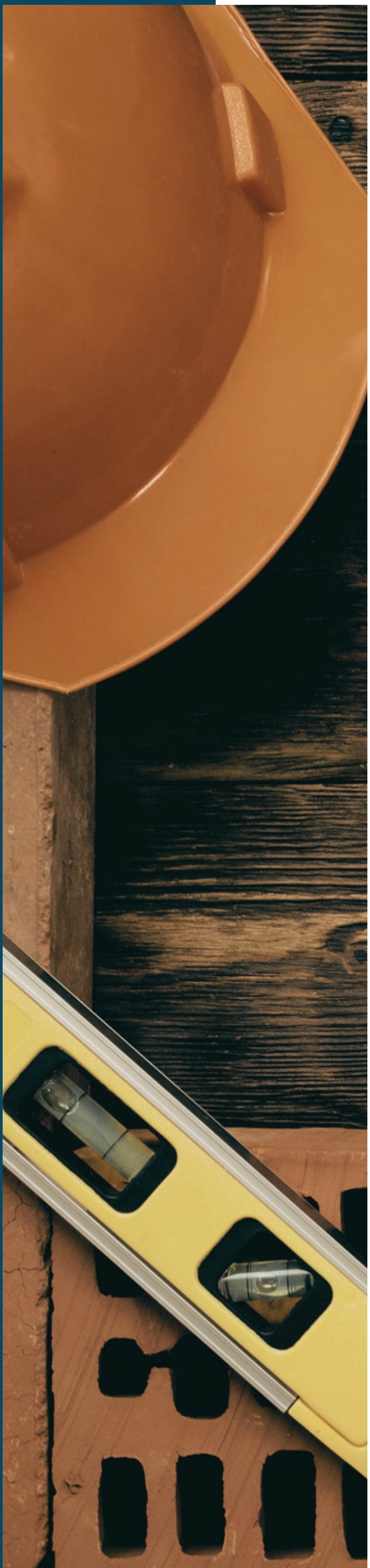
PAUSE: WHAT'S A FAMILY BUSINESS ANYWAY?

Without getting bogged down, it actually matters how we define a family business, and there are many definitions out there.

We prefer a flexible view that a family business is one that is under the effective control of two or more members of the same family. The husband and wife team running a tradie business? Yep. The traditional family farm? Yep.The third-generation enterprise owned and run by a "cousin consortium"? Yep. The firm where a patriarch or matriarch holds all the cards, and dictates terms to everyone else? Probably not, but it could become one.

Does your business fit? Quite likely. It is estimated that 90% of the world's businesses pass muster on this test or a similar one. In Australia, the majority of private-sector business activity, and jobs, come from family businesses. They are collectively worth $4.3 trillion, with a "T". So, we'd better get this right, agreed?

WHAT ARE THE FOUR DILEMMAS?



We see family businesses up against one or more of these four dilemmas, regularly. You need to be aware of them, and you'll need to work your way through them.

The most critical time, and often the most vulnerable time for a family business, is the transition to the next generation. Knowing about these four dilemmas can help you avoid the mistakes:

1. How do we honour the legacy of the founding generation, without being trapped in their business model as the world changes?
2. How do we make provision for everyone, old and young, without crippling the business?
3. How do we get the right people in the right roles, for the good of the business, without starting World War III?
4. How do we give the older generation confidence that they can hand over without losing their retirement nest-egg?

Again and again, we've seen family business transitions come unstuck over one or more of these four dilemmas.

But even before tackling these, you need a clear, agreed decision on what kind of future your family business has. Let's look at the paths this might take.

HOW DO WE CHOOSE WHICH PATH?

Let's zip back to the 1800s for a moment.

If your father was a cobbler, you were (if male) going to be a cobbler too. If you were born into a family of merchants, you were going to join the family firm at an early age (if male), and you were going to learn the ropes so you could one day be a boss. If female, you were most likely expected to marry someone whose family business complemented yours.

Before the 20th Century, it made little sense for anyone to seek a livelihood outside a successful family tradition, unless they were an intractable black sheep or were excluded from inheritance.

But it's wiser now for the family to make a careful and considered choice of paths. You may dream of the family retaining and nurturing the business, and the wealth it produces, generation after generation.

That may happen, as it has with Coopers Brewery, founded in 1862 by Thomas Cooper and still in the control of his descendants. The current MD, Tim Cooper, is a 5th-generation descendant who started his career in medicine before coming back to the family business. Three of the other top leaders of the company are also 5th generation Coopers.

Such a line of succession may happen in your family.Or it may not. From where you stand today, you cannot guarantee it. Is it time to think about alternatives?

In family business work, research over many years gives us a rough rule of thumb: the Rule of Threes. Take 100 first-generation family businesses, where the founders are still in day-to-day control. Of these, about 33 are likely to finish up in the hands of the founders' children – the other 67 will be sold or closed. Fast forward, and only about 13 of the original 100 are likely to finish up in the hands of the founders' grandchildren.

In Australia, Darrell Lea chocolates, founded in the 1920s, fell apart in the third generation, and was subject to effectively a forced sale. The legacy for the family was bitter division and conflict. The brand still exists, but no descendent of the founder benefits.

So I urge you to consider this: assuming that the next generation will take on the business can derail you. Good sense requires us to evaluate all the options as the older generation step back to enjoy the fruits of their hard work. Liquidate the assets and invest the proceeds, is one, if the business holds a lot of capital – as Ken and Janet did with their farm.

Sell as a going concern, with the goodwill, either to a competitor or to a new entrant to the industry. That looks like the path for Kurt and Helen's wholesale business.

Or perhaps, indeed, bring in the next generation with the plan to hand over both management and ownership, as the Hampden family have been doing. Just make sure that everyone is prepared, trained and ready.

Whatever the path, the most important thing is to have that plan, clear, agreed and written down, well before the crisis arrives.

And the most important thing about the plan is to start.

And the starting point is a conversation.

Scary fact: 1 in 3 Australian families with a business have not yet thought about succession in leadership or ownership. You don't want to be in that position.

HOW DO WE GET STARTED?

Let’s be frank: you won’t get far without some professional help. The intersection of the business system with the family system is just too complex, too fraught, and too loaded with emotion for the family to navigate it unaided.

You do need to start with a conversation, as we’ve said several times. But if that conversation is just a shouting-match around the dinner table, you haven’t achieved anything. Have you?

Here’s what’s going to get you started the right way: a formal family meeting. That means, in a secure, neutral space, with clear expectations, agenda and rules, and a clear task to achieve. There must be time for all voices to be heard, and there must be rules to prevent any voice being over-dominant. Everyone needs to show up prepared and ready to contribute. Notes will be kept of what is agreed. There will be conflict and there may be tears.

You’re going to need a qualified family business advisor to facilitate and guide this meeting, or you’ll finish up pretty much back where you started. That’s where we come in.

Call us, in confidence, and we’ll set up a preliminary discussion, where we’ll work out if our services are a good fit for your needs. No cost, no obligation. If we find a good fit, we’ll propose a professional engagement. If not, we’ll wish you every success and we’ll always be here if you want to take it further.

Upland CONSULTING
HEAD HEART AND BOTTOM LINE

THEN WHAT?

It’s vital that your family meeting concentrate on what the family considers most important, and what it wants to happen. The many questions about ways and means come later. The first document to get right is a written, agreed statement of what the family wants to happen next.

Then, to make it all work legally and financially, you will need legal and accounting advice, and if the decision is to sell some or part of the family enterprise, you will need a business broker or other sell-side advisor. To plan for retirements and legacies, you will need a financial advisor.

Experts will be needed to help you correctly draw up wills, trust deeds, shareholder agreements and other binding documents.

Your family may already have some or all of these advisors. Our role is not so supplant or compete with them, but to help coordinate this multi-disciplinary team to get the best and clearest outcome. Our patch is the big picture!

BONUS

The Succession Readiness Questionnaire - online.

CONTACT US

Remember, no charge, no obligation while we figure out if we are the right people to help you.

Get in touch via our web site: www.upland.com.au

Or call our senior advisor, Iain, who is accredited with Family Business Australia, the peak body.

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Thank you!