

## ENTERPRISE Family Business

# No successors? Treat the business as an investment

Mike Cohn

What happens when there are no successors to take over the family business? Is selling the company the only option?

Families can successfully own, and grow, a family business even when the next generation doesn't work there. It takes a change of focus but can be a way to maintain a family legacy. The key: Treat the company as an investment instead of as a career.

Some reasons to keep the business:

**1. Unrealized growth opportunities:** Many family businesses have plateaued as the current generation approaches retirement and becomes risk averse. The company may be poised for next stage growth but lacks leadership and strategy and sometimes the capital to get to that next level.

**2. Family legacy and a competitive advantage in the marketplace become intertwined:** In a 2003 BusinessWeek report of European family-controlled public companies, they dramatically beat their rivals on all European stock indexes

**3. A committed and competent top team:** Key management who knows the business, can run it, and are dedicated to the business and to the owning family.

**4. Good cash flow:** Timely financial information and management, budgeting and



planning produces consistent earnings. The same reasons that someone else would like to buy the business also are good reasons to keep it as a family investment.

So how do you make a shift in focus?

Start by evaluating whether the family can learn to be "smart owners," whether leadership can be cultivated or needs to be recruited, whether corporate governance exists or needs to be developed, whether there are sufficient sources for capital needs, and most importantly, is there time?

The owner-investor model emphasizes family governance over family management. In other words, the family decides to hire the best and the brightest to run their family business, which might be a family member but might not.

A plan is developed for the company, outlining goals and needs and a chief executive or chief operating officer may be recruited to accomplish those goals.

Family education is required so that proper oversight can be created to monitor and track performance against goals. In addition to family education, a board often is appointed by the family, with experienced outsiders, who can represent the family's interest.

Some questions should be resolved to become a successful owner-investor:

- **Ownership education:** How can uninvolved next-generation owners be informed and educated about the responsibilities and risks of ownership? Or, as one family described it: "How can we keep our noses in, but our fingers out of the business?"

A commitment to understanding business risks and opportunities, and the industry in which the business operates, is critical.

- **Change:** Status quo won't work for future success. How can the family respect the company's culture and values, while implementing needed changes? What experience does the family have in consciously working together to create and manage change?

- **Governance:** Will family members commit the necessary time to understand the business and its needs? Will a board be bold enough to make tough decisions or will it become a caretaker? What governance policies should be implemented to balance family and business needs?

A family council may represent family interests, interfacing with the board on strategic and policy issues.

- **Ownership structures:** A family entity may be formed to hold family business stock, keeping ownership consolidated for the future. Multi-generational

trusts or family limited partnerships may be formed for this purpose.

Multi-generational trusts have additional advantages since assets in the trust are creditor-proof, divorce-proof, and protected from estate taxes. Trustees of family trusts or general partners of family partnerships may have substantial powers over this family asset, therefore policies and procedures to protect the rights of beneficiaries or limited partners are important.

Benchmarking should be implemented so family owners can compare family business performance with its peers.

An appraisal of the company can educate family members about its fair market value and how it compares to peers in the same industry.

Incentive compensation plans for key executives can tie pay to performance and may help family owners and execs who run the business align their goals and expectations.

Involving family members in addressing these thought-provoking questions may provide some surprising answers and lead to a course of action the whole family can support.

Owning a high-performance family business can be a source of pride as well as a great investment.

*Mike Cohn is a nationally recognized succession planning consultant with CFG Business Solutions LLC, in Phoenix. He can be reached at 602-468-9667.*