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Family business succession

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FAMILY BUSINESS SUCCESSION

by

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ABSTRACT

Family businesses are a major economic force, providing jobs to half of the working people in the United States. However, family business research is a relatively new field. Interest in family business has steadily grown over the past ten to fifteen years. Business owners want to know how to capitalize on family ownership advantages and protect against the disadvantages that cause business failure and loss of asset ownership. Service providers also realize that more information and education is needed to better serve their family business clients.

This paper examines six categories of thought that are influencing the development of paradigms for the family-owned business. Each category has contributions and limitations. Further research in all areas of family business is a necessity to gain an appropriate level of understanding in order to meet the needs of all the stakeholders.

Chapter II describes three approaches to family business research in general. The rational approach and the focus on the founder can be considered micro aspects of the systems approach, which provides the macro model. The common thread is the notion that family processes and business processes exist in a continuous relationship with one another.

Chapter III describes three approaches to research on family business succession. All three approaches tend to focus on the micro level of the family business: resistance to succession by the founder; phase and stage concepts, which is a set of assumptions about how change and growth occur over time; and the focus on the next generation.

Chapter IV offers recommendations to family business owners, managers and service providers, based on the review of literature in the previous chapters. Four recommendations are offered to family business owners: introduce and educate all children to the business at a young age; establish a board of directors; develop high expectations for accountability of family members who work in the business; and develop and execute a written succession plan.

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Family businesses are a major economic force, providing jobs to half of the working people in the United States. However, family business research is a relatively new field. Interest in family business has steadily grown over the past ten to fifteen years. Business owners want to know how to capitalize on family ownership advantages and protect against the disadvantages that cause business failure and loss of asset ownership. Service providers also realize that more information and education is needed to better serve their family business clients.

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CHAPTER I

INTRODUCTION

Family business is the predominant form of organization in the modern economy. Over 90 percent of the 15 million businesses in the United States are family businesses (Bensen, 1990). Family businesses generate half of the gross national product, and employ half the work force in this country. These firms range from the small, "mom and pop," businesses to approximately one third of the Fortune 500 companies (Shulruff, 1992). Although there is considerable diversity in size and industry type among family businesses, there are many similarities among them, which relate more to the combination of family and business than to size and industry.

Despite their prevalence, systematic analysis of the unique contributions and strengths of family businesses is relatively new in business research. In the past, research has focused primarily on dysfunctional patterns in family firms. Only recently have authors begun to address some of the positive attributes of family ownership and management.

The commitment of family members to the business is a source of strength that often allows them to outperform competitors with greater resources (Benson, 1990). In a study of fifty family-owned and controlled businesses, researchers found that the majority outperformed their industry groups in profitability by a ratio of nearly two to one (Bowman-Upton, 1988). Daily and Dollinger (1992) conducted a field study which compared the performance of family-owned and managed with professionally managed firms. The researchers found differences between the two groups on both structural and process dimensions. For example, professionally managed firms are significantly larger than family businesses. Professional managers grow the firms for the sake of growth and personal gain. Family business owners work toward increasing the value of their enterprise, not just making it larger. Family-owned and managed firms exhibited performance advantages as a result of the unification of ownership and control. It can be presumed, then that these firms have learned to run their businesses based on management principles which serve the family and the business effectively.

Conversely, common types of organizational and managerial problems threaten the productivity and stability of many family businesses. Therefore, significant attention is being given by researchers, business consultants, and family business owners to identifying and attempting to solve the problems which consistently plague family businesses.

Providing for succession is problematic for any organization. It is well established that succession is a major problem for family-owned businesses and research shows that failure to provide for succession is the primary cause of the demise of family-owned businesses (Handler and Kram, 1988; Lansberg, 1983). Ward (1987) found that only thirty percent of family-owned businesses make it to the third generation, and fewer than fifteen percent reach the fourth. According to Cohn (1990), the typical family business has a life expectancy of only 24 years.

Periods of management transition or succession are the most critical in terms of conflict, and therefore, put the family business in danger of failure. Because of the high rate of business failures which occur during or shortly after management succession has taken place, management succession is a crucial issue concerning family businesses (Sales, 1990).

The most profound and disruptive struggles in family firms usually originate when the offspring of the founder enters the business. In other words, the beginning of the succession process is frequently the beginning of significant interpersonal struggles among family members working in the business. Family members begin fighting with each other, to the detriment of both business and family relationships. The emotions and tensions that are carried over from family to business and back again are major reasons for the high mortality rate of family owned companies. One major cause of the family conflict is often a lack of planning by business owners. Cohn (1990) asserts that if a business owner does not plan where the business is going, the odds are overwhelming that the business will not survive beyond that generation.

Purpose of the paper

This paper describes the significant developments of theories in family business and family business succession, pointing out six major areas of focus. Chapter two describes a general review of family business literature as it relates to three areas of focus: the rational approach; the focus on the founder; and systems theory. Chapter three describes a review of succession literature as it relates to three approaches: resistance to succession by the founder; phase and stage concepts; and focus on the next generation. Chapter four offers guidance to family businesses, specifically in succession planning, as well as the conclusion and guidance for more research.

CHAPTER II

RESEARCH ON FAMILY BUSINESS

For the purposes of this paper, a family is defined as a group of persons related by blood, marriage or adoption. A family business, family-owned business, or family firm is defined as a privately held business which is owned and primarily managed by two or more family members. Succession is defined within the context of a family business as the on-going change in management and control in a business from one generation to the next.

Family business research is a young but rapidly growing field. The family firm is gaining legitimacy as a unique business form because of the attention which is coming from academics, researchers, consultants, the media, and family firm members themselves. Before 1980 very few doctoral dissertations were written on the topic. Now, many appear each year. In 1985 the first academic courses were offered as part of a business curriculum. The first journal published on family businesses began in 1987 (Ward, 1987).

Until recently, neither organizational nor family theorists have paid much attention to the dynamic interrelations between the two domains of family and business in family businesses. Two factors have contributed to this omission. First, researchers who are trained in one field or the other find it difficult to study both the family and the business simultaneously. Second, theorists have assumed that work and family exist as two separate and self-contained institutional settings, a belief which is widespread in modern industrial society (Lansberg, 1988).

Two changes now taking place are increasing our collective awareness of, and sensitivity to, family business issues. First, the number of business owners confronting the realities of succession and retirement will accelerate throughout the 1990s (Sonnenfeld & Spence, 1989). Second, because of the increasing incidence of succession transitions, the demand for professionals who can give advice to those who are facing this transition is increasing substantially. Lawyers and accountants as well as business consultants and family therapists are seeking to learn more effective ways of helping their clients (Lansberg, 1988).

Family businesses present distinct challenges for organizational researchers. McCollom (1990) claims that family businesses can be differentiated from other organizations on four points: *structure; task; culture;* and *roles*, each of which presents dilemmas for researchers accustomed to working in other types of organizations.

Structure in a family business is different than other organizations because the business system itself is intermeshed with another system, the family. Family firms are differentiated from other organizations by the degree to which system boundaries overlap, as well as the extent of the interdependence of the two systems. All organizations have ownership structures, but only in family businesses are they tightly linked to a family system.

Task and product goals are the primary cohesive force within business. However, the family as an institution has goals and values which are not specifically related to tasks. The primary goal of the family is nurturance and continuity; the primary goal of a business is usually profitability and the production of services or products.

Because of the emotional intensity of family relationships and their centrality to individual identity, the *culture* of the family system has enormous affective power within the business system. Many family businesses appear to have more of a family culture than a business culture.

In the family business, a number of individual managers, employees, and owners play *roles* simultaneously in the family. These family roles may complement their work roles, but they can also create confusion and role conflict because of the differences in goals and values between the family and business systems. Family members are frequently hindered from effective role performance at work because they cannot separate themselves from family roles.

Stevens (1990) asserts that the combination of the family system and the business system creates many conflicts. Problems and conflicts arise when the goals, behavior patterns, and rules which maintain the family system overlap the business system in a dysfunctional manner. In other words, conflicts may arise between parent and child, between siblings, or between husband and wife when roles assumed within the family system are also assumed within the business system.

"Family business systems theory" is emerging as an interdisciplinary approach which combines theories from two distinct theoretical research areas: management and family systems. The discipline is in the initial phases of formation. It is important to understand the earlier writings in the area of family business in order to understand the move toward a systems approach in the form of the family business system. In considering the development of thinking about the family firm, six major areas of focus emerge: the rational approach; focus on the founder; systems theory; focus on founder in terms of resistance to succession; phase and stage concepts; and focus on the next generation.

The development of these six approaches has not been completely sequential. Writings across time occur in each approach. There is currently a tendency toward systems thinking, although little has been written on the topic of succession based on the systems perspective. One common theme in each of the six approaches is that the two entities, family and business, are connected. Recognition that the family business contains two blended and powerful components and that the events that occur in one component can dramatically influence the other, has become a primary feature of the contemporary thinking in this field (Hollander & Elman, 1988).

The rational approach

The family business began to emerge as a topic of interest and research in the early 1960s. The earliest literature on the family business reflected an intense sense of frustration with the family component of the business. Writers were primarily concerned with the purpose, function and structural properties of the business. The influence of behavioral scientists was conspicuously absent in this intellectual and rational approach to family business (Hollander & Elman, 1988).

Writers who subscribed to the rational approach generally objected to the fact that family firms were not operated in a more "business-like" way. Theorists claimed that family members were not capable of managing a family business. Business and family were seen as opposites, in conflict with one another. The complexity and high rate of failure of family businesses led some writers to recommend surrender of the business to outside management. Others advocated placing the firm's interests before the family's interests and condemned family emotional processes as the source of difficulty. Cohn and Lindberg (1974) state that the problem with family firms is that family issues take priority over the more important administrative needs.

Hollander & Elman (1988) assert that one theme emerges from an analysis of these early writings, namely that two parallel organizations exist in the family firm: the family, which is the nonrational component, and the business, which is the rational component. When the two organizations conflict, the rational component loses to the power of the family. Most of the early writers were business consultants whose goal was to increase rational decisions in the business. The family firm proved to be a frustrating client, which was very different from management structure described in the business text books.

Contributions of the rational approach. Despite their narrow view of the family firm, writers who recommended excluding the family from the business made a significant contribution to the evolution of understanding about the family firm. These writers recognized that the family-owned business consisted of two parallel and influential components, the family and the business (Danco, 1991). Even though the rational approach commands that the family and the business be separated, proponents of this view made visible the need for boundaries between them. By separating family and business issues, it is feasible to identify what falls into the business category and what falls into the family category, which can help to clarify the decision-making process. The rational approach forces distinctions between family and business and, therefore, helps to define respective roles and goals in both family and business (Hollander & Elman, 1988).

Limitations of the rational approach. The proponents of removing the family from the business failed to recognize that the presence of the family is integral and enriching for the family business. The approach is based on the assumption that the family business should be driven purely by profit motives. Hollander (1983) asserts that the family business is equally, if not primarily, driven by family patterns, values, and considerations about people.

The rational approach left a legacy of negative stereotypes about the family firm. For example, it implied that the family business is not a real business, and its managers are not real managers. Negative stereotypes continue to plague family business managers.

Focus on the founder

Considerably more thinking has focused on the founder than on any other aspect of the family business. The founder is viewed as the most important person concerning the destiny of the business. It is apparent that the stages of development of the business and the inflexible nature of the founding personality can come into conflict. For example, the firm may grow beyond the founder's ability to be involved in every detail of the operations yet the founder may be unable to give up the appropriate amount of control (Hollander & Elman, 1988).

Some of the most colorful explorations of the family business have focused on the motivations and characteristics of the founder as the initiator and vital life force of the business (Danco, 1991). Efforts to understand the founder have included analysis of his personality characteristics which contribute to a paternalistic and often enigmatic leadership style. Until recently, research has focused primarily on male entrepreneurs of the 1940's and 1950's; thus this section describes the literature on men of that generation of founders.

A number of writers seek to understand decision making in the business by examining the personality development of the founder. Men who began businesses in the 1940s and 1950s that became family firms are by definition entrepreneurs. Therefore, much of the writing about founders addressing the entrepreneurial personality describes the profiles of entrepreneurs drawn in the studies by Collins and Moore (1970). These studies describe men currently reaching retirement age who have driven personalities, are emotional distancers, and have experienced tumultuous childhoods. The founders emerge as loners who have escaped from poverty, with insatiable egos. Bork (1986) characterizes founders as men who have been highly deprived. The founders were often orphaned or alone, fathers were frequently absent through death or emotional withdrawal, and mothers were long-suffering and deserving.

In this school of thought, examining the personality characteristics of the founder becomes a way of understanding the development and culture of the business. The notion of "paternalistic culture" (Dyer, 1986) captures the extent of the relationship between the founder and the business. In the paternalistic culture, relationships are arranged hierarchically, with the founder or other family leaders retaining all decision-making authority and the key information about the firm's operations. Family members are given preference over nonfamily employees. There is considerable distrust of people outside the family, and the founder closely supervises the employees, who are given little discretion in performing their tasks.

The founder assumes multiple roles and, as the business grows, he continues to be involved in every aspect of the business. He is usually not a planner, does not delegate and reserves the right to intervene at all organizational levels at any time. Revealing his strategy or delegating responsibility is a frightening prospect which signifies a loss of control. The founder is frequently autocratic with a need to be in control of both family and business. The organization is highly informal and resembles an extended family. There is rarely an effort toward training and development of management personnel. This inhibits the development of strong subordinates resulting in the first-generation business being a one-man show (Benson, 1990).

Conflict begins at the point when the requirements of the business diverge from the founder's need to control every aspect of the business. Difficulties are likely to emerge when the expanding organization requires more formal administration. The need for planning and delegation can conflict with the hands-on style that worked well in the early founding stages. Ward (1987) identifies factors including personnel practices, such as hiring, evaluation and promotion, termination, retirement, and managerial training and development as those that need resolution in order for the business to survive beyond the career and life of the founder.

According to Guzzo and Abbott (1990), leaders of family firms often derive their authority from two sources, as head of the business and as head of the family. According to Dyer (1988), 80 percent of first-generation family firms have a paternalistic culture characterized by authority centralized in a charismatic family member, usually the founder. Such a culture can benefit the small, struggling business. But a paternalistic culture can leave the firm in jeopardy if the leader dies or becomes incapacitated, especially if a succession plan is not in place (Lansberg, 1988).

Contributions of the focus on the founder. The founder plays a critical role in the formation and destiny of the family firm. He is often the major or sole owner and in control of every decision. Examining the personality and style of the founder can help to predict difficulties in the transitions that the business must face.

Limitations of the focus on the founder. Relying solely on an analysis of the personality of the founder for explanations of the development of a family business system can be limiting. It exaggerates the influence of one individual to the exclusion of all other elements of the complex family and business system. The interaction of variables and forces are absent. Little recognition is given to problems in the marketplace or to the influence from other internal and external factors which affect the family and the business (Lansberg, 1988). In other words, the founder is only one figure in a total system.

The literature on the founder tends to create a negative, one-dimensional portrait. It is unproductive to approach the family business with expectations based on such a limited stereotype. The literature described in this section is of a particular generation of male founders under one set of historical and economic conditions, which fails to take the contemporary founder into account. Founders of high-tech businesses that evolve into family businesses or founders who are women do not fit the type that is frequently described (Hollander and Elman 1988).

Systems approaches

A family system is a relationship oriented system, which is emotionally based, with emphasis on loyalty and the care and nurturing of family members (Benson, 1990). A business system, in contrast to a family system, is a task oriented system, which is objectively based, with emphasis on performance and profit (Hollander, 1983). These differences between family and business goals contribute to the difficulties associated with family members working together. These differences cause ambiguity, confusion, and stress for most family members, which is the reason that systems theories are being applied to family businesses.

The development of systems thinking has contributed significantly to our understanding of the family business. Hollander and Elman (1988), trace the genesis of systems thinking to the work of Ludwig von Bertalanffy (1968):

> Von Bertalanffy first applied his notions of systems to biology and subsequently to human systems. The underpinnings of the systems approach include an emphasis on the whole as the unit of focus, interrelatedness of parts, hierarchy, openness, and interactiveness (p. 156).

The origins of systems thinking can be found in the rational approach and the approach that focuses on the founder. Recognition that two components affect the dynamics of the family firm and the notion of interaction underlie both approaches. The issue of the coexistence of family and business is thematic in the rational approach. Those who focus on the founder have emphasized that the founder's and the firm's needs can conflict.

While the other two approaches contain the fundamental components of systems thinking, the systems approach to family business is a comprehensive approach which is distinct in its conceptualization of the functioning of family businesses. The first systems models used open-systems theories as a conceptual base. Open-systems thinking emphasizes the interrelationship between the organization and its environment. The focus is on understanding the context within which the organization must function.

Davis and Stern's classic work (1980; reprinted in Family Business Review, 1988) facilitates understanding of the interrelationships of three components: the business or task system, technology and the marketplace, and family processes. Davis and Stern identify several systems requirements for the healthy family business, one of which is clear and consistent boundaries that locate problems and issues in the appropriate context, either family or business, for resolution. Another requirement is social structures and processes in the family that can contain and resolve family problems. The final requirement is an appropriate task structure in the business and an organizational structure that accepts and values the centrality of the family in the business.

Beckhard and Dyer (1983) propose a scheme of the family business that includes the business, the family, the founder, and linking mechanisms, such as the board of directors. Each component is perceived to have an identity and culture of its own, often with needs and values that compete with those of the other components. Dilemmas raised by decisions about continuity at various phases of the family business create problems at all levels of management within the business and often reach beyond the founder and the spouse to extended family members across several generations.

The approaches of these authors contribute significantly to the development of a systematized way of thinking about the family firm as a highly complex, open system of interactive elements. Their reasoning makes the business the central focus. Intergenerational and nuclear family emotional processes are forces that either impinge on or support the functioning of the system. Appropriate boundaries can constrain the negative intrusions. Here, there are echoes of the rational approach.

According to Swartz (1989), it is possible to create change in a family business only when both the family system and the business system are addressed directly and concurrently. The reason is that in a family business there is a high degree of reciprocal interdependence between the family and the business. Consequently, it is impossible to intervene in the business without affecting the functioning of the family, and vice versa. Swartz refers to this as the dual systems approach.

At the heart of this approach is the recognition that there are four fundamental differences between families and business systems. First, while family systems are fundamentally emotional systems in which membership is involuntary, businesses are predominantly rational systems in which membership is voluntary. Second, while family systems tend to be oriented inwardly, toward the nurturance, development, and protection of members, business systems are predominantly oriented toward securing a profitable position in the market place. Third, while the behavior of family members is mostly viewed in the light of norms about loyalty and fairness, the behavior of people in business systems is assessed in terms of their ability to contribute to the delivery of the goods and services that the business produces. Fourth, while family systems tend to actively resist change in the interest of perpetuating a sense of safety and security for family members, business systems more readily recognize change as an opportunity for growth and advancement.

The work of Kepner (1983), McWhinney (1984), Hollander (1984), and McCollom (1988) represents another shift within the systems focus. Each of these authors emphasizes the power and importance of family and the permeability of boundaries between family and business. The family processes are not viewed as external but as central. The first three authors cited also advocate the use of family systems theories in diagnosis and interventions for family business. Family systems theories provide a number of concepts useful in understanding organizational processes and relationships. These theories do not seek to explain behavior by particular character traits or individual needs (for example, "she's depressed," "he's unmotivated"). Among the several accepted family systems theories, behavior is understood as functioning in a specific interrelational context and as adaptive within that system.

Kepner (1983) asserts that the systems view is progress in conceptualization of the family business. She cautions, however, that the family firm models are dualistic and potentially polarizing. The danger is that the family will continue to be pitted against the firm. Kepner traces the negative and positive effects of business decisions on the various subsystems of the family.

McWhinney (1984) also emphasizes the power of the family and the need to attend directly to the family in management or consultation. The goal is to help family business members become aware of historical emotional patterns, such as patterns of dominance and submission and strategies used to maintain security, emotional stability, and social responsibility, that can impede the effectiveness of the business.

Hollander (1984) offers an integrative model that incorporates both systems concepts and developmental phases. She delineates three major interactive components: the family, the business, and the environment. Behavior and transactions among any of the three components of the system respond to five elements: family culture, organizational culture, and the three intersecting life cycles of individual, family and business. Hollander seeks to capture the complexity of the family business system by showing individual, family, and business development across time, in the context of accepted and automatic patterns and processes that comprise the cultures of the family and of the business.

Components of the business culture are core beliefs, values, rituals, and artifacts. Family culture includes the historical emotional processes transmitted from generation to generation, such as rules, roles, myths, patterns of power and control, and ability to support autonomy and individuation. Throughout, Hollander emphasizes the interaction and interdependency of family, business, and individual life cycles. For example, a workaholic father can be balanced within the family by a son who accepts the role of clown. The son's process of entry into the business will be affected by the family's and his own perceptions of the role and by the ongoing and pervasive complement to the father's workaholism.

In reporting data from research on a rapidly growing family firm, McCollom (1988) explored how the family system can perform a key integrating role for the business, which in turn meets needs for the family. The discussion suggests that intervening in family firms with the intention of promoting managerial efficiency by removing the family can be dangerous if the interdependencies between the family and business systems are not understood.

Culture is an integrating mechanism in organizations. Culture is defined as a set of conscious and unconscious beliefs and values held by a group of people and the patterns of behavior, language, and symbols that express those beliefs and values, provide identity, and form a network of meaning for that group. McCollom states that culture and formal systems are the primary integrating mechanisms that make most organizations work. Formal mechanisms are usually in the form of a managerial hierarchy within an organization, and are used as a basic tool for coordination and integration in that organization. The family system performed the role of integrating the operations of the company that McCollom studied, and there wasn't a managerial hierarchy that performed that function. One lesson that McCollom reported was that care needs to be taken when passing judgement about "correct" or "appropriate" management systems. While management consultants might be appalled by the lack of formal systems in many family businesses, when the arrangement works well for both the business and the family, it may be inappropriate to recommend changes toward formal systems.

As Kepner (1983) states, another significant issue raised by present family business systems approaches is that they tend to be dualistic. Dualism tends to support opposition and polarization. Some writers place the family issues outside the business as forces that are environmental and that may be screened. Others subscribe to the notion of a joint system: two subentities, family and business, that together comprise the family business system. Both approaches assume that it is both possible and appropriate to separate family and business.

The notion of a joint system is rooted in the rational approach. It may be an outgrowth of the need for conflict resolution and clarity about complex relationships. The potential for conflict between family and business has led some to assume that there must be two components rather than one unit.

However, it is conceivable that the concept of a joint system derives from notions of what should or could be, not from what actually exits; it is perhaps an idealized form. The description of a family business system may be deficient when resemblances between a few individual parts are extended to the whole.

The notion of the joint system is also supported by the application of two separate sets of theories: family systems theories for the family aspect and organizational systems theories for the business aspect. For the most part, these theories have been advanced by advocates of the particular discipline to which they belong.

Contributions of the systems approach. Conceptualizations of the family business as a system provide the most complex framework to date. The focus on the centrality and influence of both the family component and the business component as they interact provides an expansive net that attempts to capture and view all processes, both historical and immediate, simultaneously. Change in the emotional life or needs of the family, the impact of the business on the family, the simultaneous impact of the marketplace, and developmental phases are all contained within one model.

Contributions of the systems approach include viewing open-systems theory side by side with family systems theory which provides a way of seeing the family business as a whole. Family systems theory affords increased clarity in describing the emotional issues that affect rational functioning. Open-systems theory explains the interaction of business with environment. One is incomplete without the other.

Systems constructs validate earlier approaches rather than negate them. For example, from the rational approach comes the awareness that two entities comprise the family business and that the boundaries between them have to be managed. The founder can be understood as the earliest point in a systems process that carries his imprint and that grows over time into a complex system. The assumption among those who use a systems approach is that the total system is the client, although the call for help may have come from a single person. The systems approach emphasizes adaptation and potential for change rather than pathology and dysfunction.

Limitations of the systems approach. It is a limitation that the systems approach emphasizes the macro level. The underlying assumption is that it is important to see the forest rather than the individual tree. Nevertheless, there are times when it is valid and desirable to focus on individual components within the configuration. Systems intervention occurs at the micro level. It is unrealistic to contemplate and deal with all systems forces and components simultaneously. This raises the question that there may be a gap between theory and practice in the application of systems thinking. According to Hollander and Elman (1988), family business professionals need to engage in a dialogue to work out ways of using theories developed at different levels of analysis in a complementary manner.

Joint models have been based largely on dysfunctional family business systems. In order to understand how family and business work together, researchers may need to observe healthy and adaptive family businesses to understand the functional interweaving of family and business. It is possible that the failure of the subsystems to interact constructively distinguishes dysfunctional firms from functional firms. For these reasons, researchers need to look closely at the way the functions of family and business interact in a particular family business situation.

CHAPTER III

RESEARCH ON FAMILY BUSINESS SUCCESSION

The focus of this chapter is the literature that is specific to the succession process in family businesses. The approach that focuses on the founder deals with succession regarding the founder's resistance to succession. Phase and Stage concepts and the focus on the next generation are by nature concerned with succession issues.

Focus on the founder - resistance to succession

One of the most difficult and important transitions for family businesses is management succession. The founder plays a key role in whether succession is adequately planned for and executed. Many founders resist the succession process, which increases the chances of the business failing shortly after that person's death or retirement (Cohn, 1990).

The founder definitely plays a critical role in the formation and destiny of the family firm. It is impossible to deal with transitions or succession in the first generation family firm without considering the founder and his needs and preferences. It is generally accepted that the transition from first to second generation is the most difficult, due in large part to the founder's need for centrality and control (Beckhard and Dyer, 1983). Resistance to succession planning and the succession process has also been identified as one of the most important reasons why many first-generation family firms do not survive their founders (Lansberg, 1988). In many cases the logical management succession period coincides with the need to change the management style in the business from entrepreneurial to a professional management structure. At the time when the founder should be letting go of control, his age may cause him to fear a loss of control and the inevitable changes in the business.

Business founders often have difficulty giving up that which they have created or developed. They fail to prepare for succession even when competent and qualified offspring work in the business. Explicit planning for succession is rare. The failure to plan for succession is due to resistance that exists on many different levels. For the owner, factors associated with resistance include lack of other interests, psychological identity with the firm, and fear of aging, retirement, and death (Handler, 1990).

The entrepreneur's resistance to letting go of the organization is illuminated by studies of retirement. The lives of adults in their 50s, 60s and 70s are filled with much daily continuity of skills, activities, roles, and relationships. Retirement is threatening because it represents a change from the continuity of one's daily routine. For the entrepreneur or CEO, barriers to retirement and succession include the loss of heroic stature and mission (Sonnenfeld, 1988).

Attitudes about retirement and succession are reinforced by behaviors at the interpersonal level. At this level, members of families often have difficulty communicating openly about succession issues. The generation of founders who are retirement age are known as a group to have poor interpersonal communication skills. Minimal trust, power imbalances and family conflicts also contribute to resistance at this level. Specifically, succession can be sabotaged when conflicts within the family permeate the business, resulting in the downfall or sale of the firm.

Organizationally, certain characteristics, such as culture and structure, will further influence resistance to succession. For example, if change is generally viewed not as a threat but as an opportunity, resistance to succession may be minimal. Environmental instability, turbulence, or depression may also reduce resistance to succession.

There are several types of unexpected factors that can decrease the founder's resistance to succession. Two of these factors include the founder's development of poor health, and the advent of new technologies changing the nature of the operations of the business (Handler & Kram, 1988).

Contributions of the focus on the founder. It is predictable that founders will experience difficulty with the succession process, for a variety of reasons. Writers who describe these difficulties help family business managers and consultants to understand some of the inner conflicts the founder experiences. This understanding can facilitate a dialog between family members.

Limitations of the focus on the founder. The behavior and motivation of the founder is only one part of the whole family business dynamic. The founder may not be the only member of the family business who resists succession. It is too easy to generalize the motivations of the founder, blaming him for the lack of successful transitions, to the exclusion of other important people who also play key roles in the process.

Phase and stage concepts

Another important area of research and thinking about the dynamics of family business succession is the work done on developmental phases and models of growth. The analysis of stages of development identifies patterns that offer some predictability in alternating periods of stability and transition which occur over time.

All of the developmental theories share a common set of assumptions about how change and growth occur over time. A prevailing theme in these studies is that there are predictable periods of stability and intervening periods of stressful transition. The theories describe developmental tasks that need to be addressed during each stage; issues that are inadequately resolved recur in later periods. Theories pertain to individuals, to families, to organizations, and to a combination of all three. In the family business field, the various writers on development can be differentiated by the parts of the family business that they elect to describe (Hollander & Elman, 1988).

One approach has been to relate the firm's developmental stages to the family's generational progression. The study by Hershon (1975) is representative of this point of view. A second approach focuses on the interaction between the firm's developmental needs and the stage of life of various individuals crucial to the firm. McGivern (1978) views the intersection of business phase and individual life stage in the choice of an appropriate successor. Davis and Tagiuri (1989) look developmentally at father and son pairs attempting to manage the succession transition. A third approach, stated by Handler (1990), focuses on a four-stage mutual role adjustment process between the founder and next-generation family members.

Hershon's (1975) classic study, which includes an explanation of phases in the life cycle of the family business, is based on an analysis of seventy family firms. Hershon traces the development of three management patterns congruent with three generations of the founding family. The Pattern A firm is characterized by paternal dominance and entrepreneurial management. It is the typical first-generation firm, which functions as an extension of the founder. The Pattern B firm, which Hershon calls "collaborative," is a second-generation firm characterized by fraternal management. It is likely that the sons of the founder head divisions of the organization. The firm is expansive, probably branching out into new products, increasing its emphasis on marketing, and finding new distribution channels. The Pattern C firm is dominated by collective or family network management. At this point, the firm has probably passed to the third generation and is managed by brothers, cousins, and other family members. Hershon identifies a model for the successful family business which illustrates the simultaneous progression through family generations and sequential managerial patterns. He notes that stable and transitional periods alternate such that, during the stable periods, the business and the family managers tend to become more mature.

McGivern (1978) proposes a three-stage model of the succession cycle that corresponds roughly to the periods before, during, and after the succession itself. During the first stage of the succession process it is recognized that the chief executive must be replaced in the foreseeable future. At this time there is usually discussion of whether the business should continue or be sold, which creates feelings of insecurity and rivalry. The second stage begins with the decision to appoint a successor, which begins the process of selection and training the successor. This is also the beginning of the retirement process for the current chief executive. The third stage begins after the formal succession and transfer of titles has taken place. This is generally a period of the successor taking control, developing management skills and dealing with the retired chief executive.

These three stages are influenced by five factors: the stage of the business development, the motivation of the owner-manager, the extent of family domination, the organizational climate, and the business environment. The way in which these five factors influence the family business depends on the firm's life cycle stage and needs.

In coordinating succession with other developmental issues of the business, McGivern (1978) states, "It would therefore seem reasonable to suggest that it is necessary to look at the successor in terms of whether he conforms to the role requirements of the chief executive at whatever developmental stage the firm has reached" (p. 38). For instance, a second-generation firm may need a person skilled in systematizing, organizing, and institutionalizing rather than a person who starts new ventures and is entrepreneurial in style.

Davis and Tagiuri (1989) studied the quality of work relationships of father-son pairs working together in family companies and determined periods when the life stages of the members of each pair were more likely to produce either problematic or harmonious work relationships. They examined the intersections of the life stage needs of the two individuals as they influenced the functioning of the business and particularly the succession process. This application of life stages does not focus specifically on the phases of growth of the business. The authors conclude that some intersecting points of the life stages of father and son are more favorable than others for the formation of effective working relationships. Complementary needs are more positive than similar needs. For example, a father who is in his fifties and a son who is between his mid-twenties and mid-thirties are likely to have a more effective working relationship than other pairs. The authors draw implications for planning in such areas as decisions about the transfer of responsibilities in the business.

The respective life stages of the two men is an important influence on the quality of father-son work relationships. Seven factors strongly influence the quality of any work relationship: the two men's agreement on the formal purpose of their work relationship; the degree of clarity and overlap in the responsibilities of the two men; the type and level of power that each man has in the relationship; the similarities and differences between the objectives, activities, traits and work styles of the two men; the sentiments that each man holds for the other; the ability and willingness of each man to send and receive messages; and the costs and benefits that each man perceives in the relationship measured against his expectations and possible alternative work relationships. The position of the father and son in their respective life cycles influences all seven determinants of the quality of the work relationship.

When the father is in his forties and the son is between seventeen and twenty-two, the work relationship is relatively problematic. A man in his forties realizes that there is an end to life and begins to feel that time is running out, which makes it an emotionally charged time. Young men in their teens and early twenties are still in the process of separating from their family. They are trying to establish their own identities, and they are often still engrossed in their childhood conflicts with their parents. At this time, energies and instinctual drives are at a high point, which make this an emotionally charged time for the son. The father's and son's respective life stages have much in common: identity questioning, high energy, and the appraisal of life. Unfortunately, these similarities create tension within the relationship, and they result in work interactions of relatively poor quality. Because this is an emotionally charged time for both men, it is possible that each will distort the other's messages and feel threatened by the other's actions. At the very least, communication between father and son at these life stage intersects is likely to be poor.

At this point in the son's life, he most likely feels that he has many career options and, therefore, does not feel a sense of urgency to make the work relationship with his father succeed. Sons who join their fathers directly out of college are likely to have unrealistic expectations of immediately putting into practice some concepts and "book learning" that may be unrealistic for the business. At this mid-life point in the father's life, work can be a source of stability, and the son's insistence on change may be perceived as testing the father's competence and authority at work which can be extremely threatening.

When the father is in his fifties and the son is between twenty-three and thirty three, the work relationship is relatively harmonious. It is generally recognized that the period between the mid-life transition and age sixty is a time of tranquillity. Men beyond mid-life transition tend to be less competitive, need less to idealize and condemn others, are more objective and philosophical. It is in this period that men have both the experience and the inclination to teach younger people and to become effective mentors.

The period between ages twenty-three and twenty-eight is not considered to be particularly stable. Work relationships during this time tend to be of relatively good quality because young men in this period search for mentors who can help them to define and work on their dream or life plan. The desire for competence increases beginning around twenty-two, and the primary task of men between twenty-five and thirty is attaining success and mastery.

The period between twenty-eight and thirty-three is another transition time when men feel some urgency to focus their lives. Around thirty, a man usually makes a lasting occupational choice, and before the end of the age twenty-eight to age thirty-three period, he has begun to commit to some choices for a new life structure. During this period, men become more settled. They strive for competence, and they are increasingly in need of recognition and advancement.

There are two key reasons for harmonious father-son work relationships in this period: The father is emotionally able during this time to understand and tolerate the son's instability, and the son wants to learn and grow in competence at precisely the time when the father wants to teach and help those in the younger generation to develop. Both men are less emotional, and communication between them should be easier during this time. As the son increasingly focuses his life, he is likely to become more committed to making his working relationship with his father succeed. The father is also less concerned about recognition while the son is becoming more eager for recognition. It is probably easier for the father in this period to reward and recognize his son. Another important factor is that both men are likely to be physically and intellectually strong in this period and capable of contributing to the business. Therefore, father and son are more likely to feel that rewards, recognition, responsibilities, and authority are divided fairly between them.

When the father is in his sixties and the son is between thirty-four and forty, the work relationship is relatively problematic. Many men have difficulties coming to terms with their retirement. Men approaching sixty-five and seventy are reminded of the eventual loss of meaningful activities and relationships when they leave their companies. Therefore, since retirement is not prescribed by corporate structures for the owner-manager, it often occurs only with his death. This period was found to be the most problematic for the father and the son, compared to the other periods.

Men between age thirty-four and forty strive to attain competence, recognition, advancement, and security. As men approach forty, these goals become very pressing, including struggles with dependence, sexuality, and authority. The resurgence of strong emotions in a man regarding his dependence on his father can stimulate very negative emotions toward the father, such as a lack of trust.

It seems likely that the father-son work relationship in this coincidence of life stages will be difficult, since the son's struggle with authority overlaps with the father's desire to demonstrate the continuing value of his skills, ideas, and leadership. The son's emotional state may well distort communication between the two men. Sons probably feel held back in their desire to change aspects of the organization, and fathers feel unappreciated. They may have serious conflicts over the goals of the company, the father wanting to keep the company on a steady course and the son desiring to steer the firm in a direction that the father considers reckless.

Davis and Tagiuri assert that the overriding issue for sons in their late thirties is not one of displacing the father by taking over the company but rather one of escaping the father's shadow and reach. It may be that fathers and sons can coexist in the family company well into the father's seventies if the father relinquishes some authority in the company to his son.

Handler (1990) focuses on the role of the family business owner, and suggests that the owner and the next-generation family member progress through a mutual role adjustment process associated with succession. The role of the successor is shaped by the role of the founder. Specifically, the founder seems to progress through various phases of lessening involvement in the business over time. At the same time there is a parallel adjustment process as the successor moves through phases of increasing involvement.

The first stage of the four phases of role adjustment is when the founder is the "sole operator." This is generally the start-up phase of the company. At this time, the future successor does not have a role in the company. During this period, the owner usually performs nearly all the operational tasks of the business, and is frequently the only family member in the organization.

The second stage is marked by the founder's role moving from sole owner to monarch, as the future successor's role becomes helper. During this stage, the founder begins to have preeminent power over other family members. The future successor usually is working full-time in the business by this time, and tends to have limited but functional duties usually associated with one or more departments but not involved with business strategy.

The last two stages of this role transition appear to be most critical to effective successions. The third stage consists of the founder's role moving from monarch to overseer/delegator which enables the successor's role to change to manager. This is a very sensitive transition, which depends on the founder's capacity to trust, share, and delegate. During this process of delegation, it is not uncommon for the roles of the owner and successor to overlap and blur. Also during this stage of role adjustment, the founder typically starts taking time off from the business, or working fewer hours per week in the business. The founder's functions in the business also become limited to those tasks that require experience and expertise. Obtaining financing, considering options for growth, and other longer term strategic decisions and capital improvements are typically the focus of the owner at this stage.

The fourth stage of role adjustment is characterized by the founder's role moving toward being the consultant, while the successor's role is moving into the leader/CEO position. At this point, the founder is no longer actively involved in the organization although he may serve on the board of directors of the company. It is necessary for the founder's role to change to consultant in order for the successor to be able to take on the role of leader/CEO. A critical aspect of the founder's transition to a role as consultant is disengagement or retirement from the organization and the simultaneous pursuit of other interests. Retirement is a particularly sensitive and difficult issue for owners and family business members. Not only do successors have difficulty believing their parents will retire, they are not eager to accept this reality. During this period, successors often conceive of the parent as a stabilizing force in the business. Once the parent moves out of the business into a consultant role, the family business system has to accommodate to this loss.

Another critical aspect of this stage of role adjustment is the transferral of management and ownership rights. Often this process of stock transferral is accomplished slowly or even avoided in order for the founder to maintain control. However, the successor does not generally believe that the business has completed the succession process until the voting stock has been passed down as well.

The timely transferral of stock is necessary not only from an emotional or sociological perspective, but also given the tax implications. Delay in transferring stock often indicates the founder's desire for high control and tendency toward limited estate planning. As a result, upon the death of the founder estate taxes may be significantly higher than they would have been if portions of the business had been transferred in the founder's lifetime. Thus, minimal planning for succession may affect the ability of the firm to survive the transfer of power.

Contributions of the phase and stage models. The writers who have sought to clarify the workings of the family business through models of growth have made a significant contribution. Phase and stage constructs offer predictability and normalization and facilitate an understanding the interrelatedness of individual, family and business life cycles. Predictability evolves through understanding that the typical individual or entity will progress through expected phases. Understanding the inevitability of phases offers possibilities for control and effective planning. Movement from one phase to another requires transition, which is accompanied by turmoil. By marking off segments and ongoing life cycle phases, the models have highlighted the importance of the transitional periods central to organizational and managerial change and the need to deliberately manage times of transition (Ward, 1987).

From a developmental perspective, crises and change can be viewed as normal and predictable rather than pathological and as opportunity rather than threat. The models are, therefore, normalizing, which can reduce anxiety for both the individual working with the family business and the family members themselves and thus allow and enable clarity in the decision-making process. Hollander and Elman (1988) assert that pathology or dysfunction tends to occur when individuals, families, or businesses fail to negotiate the transitions and, therefore, get stuck in a particular stage.

<u>Limitations of the phase and stage models</u>. The phase and stage models also have limitations. They are basically time oriented. They do little to explain the ongoing interaction and reciprocal influence of the family and the business. For example, when a family business reaches a transition point, the family's

values and priorities dictate whether the family resists or supports the transition and influence the ability of the business to make the transition successfully. The selection of a successor serves as a key example. If primogeniture (successor being the eldest son) has been the basic operating rule, a decision to select a more competent younger or a female family member may be blocked by powerful emotional forces from within the family. Stages of development do not fully explain these reciprocal interactions. Phases of development are universal. However, phase models do not capture the historical emotional processes that affect the family's mode of acting or its ability to manage transitions (McCollom, 1990).

Focus on the next generation

It has been established that succession is critical to the future of a family firm. However, little is known about how the next generation actually experiences the process of succession. Handler (1992) conducted a biographical study of next-generation family members, and the results of the study indicate specific factors critical to succession. Handler's approach is in contrast to other traditional literature which focuses on the founder as the central person in the family business system.

There are several reasons for considering the members of the next generation associated with family businesses. First, the motivation, desires, and concerns of next-generation family members are probably different from those of the founders or owners in family businesses. Secondly, the participation of the next generation in the organization is critical to the transfer of power between generations (Dumas, 1989). Finally, the most practical reason for studying these individuals is related to the statistics that exist on family firm succession: only thirty percent of family firms survive the transition to the second generation (Beckhard and Dyer, 1983).

The major product of Handler's study of the next-generation family members is a framework that describes the factors shaping the succession experience from their perspective. A major implication for practice is the potential use of the framework as a diagnostic tool for evaluating next-generation family members' experience of succession.

On the individual level, the study suggests that next-generation family members judge their experience in the family firm in terms of the degree to which needs associated with individual development are satisfied. Specifically, the importance of meeting needs associated with one's career, psychosocial development, and life stage are critical for the next-generation family member. The ongoing assessment of these needs through personal reflection and planning is necessary for next-generation family members.

In terms of career needs, individuals must answer questions related to their future, such as identifying the ways in which working in the family firm satisfies specific career interests. In addressing their own psychosocial development, individuals must consider the extent to which they are capable of their own accomplishments and accountable to themselves while involved in the family business. Finally, in meeting life-stage needs, individuals must consider the ways their needs change over time, and how those needs can be satisfied through the family firm. Individuals also must determine whether they can exert personal influence in the context of the family business.

On the family level, the study suggests that mechanisms are required to strengthen family relationships through improving communications both within and between generations, as well as to manage boundaries between family and firm. Working on communication between family members is necessary to institutionalize succession planning in family firms by reducing the resistance associated with succession planning. Increasing awareness in families of the existence of an overlapping system between family and business is also necessary. Related to this is the creation of family values associated with the business mission or goals and the establishment of norms for minimizing the interference of family issues in business.

Finally, the major implication for succession planning lies in recognizing the perspectives of the next-generation family members. Strategic planning associated with succession should incorporate their needs. These individuals should be actively involved in planning for the future, particularly given that the leadership of the organization is likely to depend on them. Thus, Handler's study suggests that the challenge for organizations lies in managing succession as a means of enhancing the continuity of organizations as the quality of experience of the individuals involved.

Resistance to succession by the successor. Succession from one generation to the next takes place within a complex web of dynamic family relationships. The complexities and nuances within these family systems pose a number of potential obstacles standing in the way of effective succession. For the most part, however, academics and practitioners concerned with the problem have placed the burden on the founder or owner (Sonnenfield, 1988). This person decides when the process will begin, who the successor will be and when the transition will take place. A common assumption of much contemporary thinking on the subject, therefore, has been that a founder's resistance is the primary hurdle to effective succession.

While recognizing the complexity of family systems and the importance of the founder, Levinson (1983) suggests that the successor is the key person in the succession process. The characteristics of successors are important determinants of how succession takes place. Goldberg and Wooldridge (1993) assert that there are two common experiences shared by successors. First, resistance to succession is generally evident and there seems to be a period of tension between the two generations of management during the succession process. Second, at some time it is necessary for the successor to stand up and take charge of the company in order for the succession process to be successful. Each case studied by Goldberg and Wooldridge seems to suggest that succession outcomes are determined by the actions of successors as well as by the initiatives of founders. While a founder's resistance can be anticipated, it does not seem to be the determining factor in how succession takes place.

The literature on resistance to succession suggests that numerous forces work against successors, such as lack of succession planning, lack of external support for both founder and successor, and the successor's need to establish credibility with the founder and other family members and employees.

At some point, however, the successor needs to take charge. This point is reached when transfer of leadership occurs and the successor becomes the legal or rightful head of the family business. Most of the literature covering this period describes the incumbent as agonizing over the decision to let go. The role of the successor during this period is unclear, mainly because too little has been written. This juncture in the succession process is precisely where the successor is in a position of influence. Longenecker and Schoen (1991) suggest as much when they describe the period as one of testing, in which the potential successor demonstrates the ability to lead and manage and thus earns the right to increased leadership responsibility.

Although some of the problems inherent in succession can occur early in the process, a number seem to occur at later stages when the potential successor has the title of president or general manager of the business. It is during this period that the successor has the opportunity to gain the trust and confidence of the predecessor, employees, family members, and important outside constituents, such as attorneys, bankers, accountants, and customers. Many are biased against successors during this period, and hence many successors fall short in meeting others' expectations.

Goldberg and Wooldridge assert that the degree to which effective succession takes place is determined by the founder's perception of the potential successor's performance during this period. Further, perceptions of performance during this period are determined largely by the attitudes and image that the successor projects.

In particular, four sets of attitudes seem to play an important role in determining how the successor is perceived. First and most obvious is the successor's attitude toward the founder. Successors who are intimidated by the founder or who cannot transcend a parent-child dynamic are likely to project this fact to others. Second, attitudes toward the business are likely to color important interactions. For example, successors who feel that they were forced to join the business are likely to project resentment toward family members and others. Third, for similar reasons, the successor is likely to project attitudes toward the family; unfavorable attitudes create an unfavorable image of the successor in the minds of key constituents. Last, the successor's attitudes about himself, particularly his self-confidence, are usually evident. Successors need to believe in themselves and in their ability to make the right decisions. Thus, Goldberg and Wooldridge assert that attitudes concerning the founder, the business, the family, and self differ among effective and ineffective successor groups.

<u>Contributions of the focus on the next generation</u>. The next generation is obviously a large part of the equation in the whole succession process. Consultants as well as all family members should consider the qualifications, needs and desires of next generation members. It is helpful to understand the common difficulties which are faced by those in the next generation in order to begin a dialog about solutions to those difficulties.

<u>Limitations of the focus on the next generation</u>. The body of research on the next generation is extremely limited and needs to be expanded upon in order to draw sound conclusions. At the same time, it is necessary to look at all aspects and members of the entire family business for solutions, instead of looking exclusively at the next generation.

CHAPTER IV

RECOMMENDATIONS FOR FAMILY BUSINESS SUCCESSION AND CONCLUSION

Family businesses tend to share similar types of organizational and managerial problems. It has been established that the problems predictably arise with the most force during times of transition. Therefore, the most critical issue for the continuity of family businesses is the management of succession. One approach to the solution of family business conflicts is to remove the family from the business operations and move to professional management. While outside control of the family business is an available alternative, the majority of family businesses tend to keep control within the family for as long as possible. This is usually due to family pride in the business, a sense of loyalty and heritage, and a need for continuity. That so many family-managed firms are successful sustains the viability of retaining management control by family members. While it would appear that the nepotism associated with family business would weaken it in a competitive environment, this is generally more than overcome by the commitment of family members who have a serious stake in the success of the business.

Many business advisors specialize in consulting with family-owned businesses and should periodically be utilized to facilitate planning and difficult transitions. These consultants have a variety of recommendations to share with family business owners which include topics such as conflict management, succession planning, estate planning and hiring practices involving family members.

The problems outlined in this paper can be addressed through systematic succession planning. Successful succession planning includes the accomplishment of four key tasks. These tasks are not necessarily completely chronological, but are in many cases concurrent activities. The four tasks are as follows: 1) Introduce and educate all children to the business at a young age; 2) Establish a board of directors; 3) Develop high expectations for accountability of family members who work in the business; and 4) Develop and execute a written succession plan including estate planning.

1. **<u>Introduce and educate all children to the business at a young age</u>**

Most owners of successful family businesses want their firms to survive after they retire. They want to perpetuate what they have created and pass its economic value on to their children. Successfully interesting the off-spring in the business may depend upon the early orientation of the children to the firm. It is important to let the children know about the business at an early age. Make the children feel that the business is part of family life. Provide for gradual and meaningful involvement of the off-spring in the family operation. During their early teens, show the children the behind-the-scenes planning, decision making, and the risks involved in the job.

Many parents who own businesses believe that all of their children deserve equal treatment, including equal opportunities to work in the business, or at least to own stock. However, it is extremely difficult to treat all family members equally, much less convince all members that there is fair treatment. Develop an atmosphere of clear and direct communication about the rules concerning the children working in the business, beginning at a young age. When children are told that, if capable, they someday may have the chance to own and run the family business, they tend to be much more reasonable as adults. This also encourages parents to begin planning early so stock ownership and estate planning matters don't split the family.

Family members should be given preference in part-time and temporary or summer job positions while in high school and college. This provides the children with a view of the business in general, and will be helpful when they are selecting a career in the future.

2. **Establish a board of directors**

There is a certain point in the life of a growing business when a transition must be made from entrepreneurial to professional management. There are significant changes that must be made to the company's structure such as accountability by function, strategic planning, financing, operations, and marketing activities. One important part of the transition to professional management is to establish an active board with outside directors. Most small family corporations have a board of directors in name only.

A board consists of individuals who serve as active directors of the corporation and who meet together at regular intervals to review the performance of the chief executive and to provide advice and counsel about plans for the future. Many family businesses have not established active boards. A board that never meets may exist in name only for legal purposes, or a set of authorized people may gather irregularly for the purpose of granting formal approvals without review or discussion of the firm's past performance and future plans.

There are many benefits of having active, outside boards. Many owner/managers reach a point in the growth of their business when they need expert advice in making difficult decisions. Properly chosen outsiders on the board can provide the least expensive form of consultancy available. Directors on small company boards average between $6,000 and $8,000 a year for retainers, including meeting fees, and they are available on an as needed basis. A good board can lift the business owner's aspirations and confidence in the business by sharing in the risky decisions. Effective boards open communications and stimulate effective action on sensitive family business issues. An active board increases the accountability level of the chief executive, raising job performance expectations for all members of the organization. The presence of respected directors can also resolve many disputes or disagreements among family members connected with the business.

The role of the active board is to assist in setting the course of policy formation, in developing long-range objectives, and in monitoring the strategic plan as it is carried out. In the privately held family business, a key role of the board is to assist in the strategic decision-making process. Leadership succession is the most important responsibility of the board. Rather than managing the day-to-day details of the business, the board has the ultimate responsibility for directing the management of the corporation. The board reviews and approves or rejects the recommendations of management on major decisions and in doing so holds management accountable.

To determine how to find and utilize directors, a business owner identifies the strengths and weaknesses of his or her current management and current board, determines the desired goals and the type of expertise that is needed in order to achieve them. The owner then identifies successful business people in the company's geographic area who are admired and respected for their success and who might make good role models. Ideally, the owner interviews a number of board candidates before selecting those people who compliment the owner's abilities and personality. A seven-member board with three insiders and four outsiders should fit the needs of most companies regardless of size, but each company must design a board to meet its particular circumstances.

Board meetings can be held as often as necessary, depending on the company's size and needs. A recommended schedule is about six times a year or every other month. At the very minimum, a board should meet quarterly. Frequent meetings help to keep the board active and well-informed.

3. **Develop high expectations for accountability of family members who work in the business**

The family business is an increasingly attractive career choice for the children of business owners, even when more than one child joins the business. Consequently, more families than ever intend to pass on the leadership of their business to multiple offspring. As more family members become involved in the business, either as employees or stockholders, the potential for conflict increases. There is often a conflict between family and business priorities and without the accountability that applies to most nonfamily businesses, many function in an informal and undisciplined manner. Questions about who will lead the business, work in it, own stock, and how family members will be compensated are usually the major causes of conflict. Many families find a balanced approach where the best long-term interests of both the family and business may be served. The family recognizes that, if the business is to succeed, it must be managed according to sound business principles and that a successful business is in the best long-term interests of the family.

The best way to avoid problems with offspring working in the business is to develop written policies for hiring, promoting, and compensating family members. Clear, direct communication about high expectations of family members' job performance as a criteria for working in the business is necessary. The family members must work together as a team to accomplish common goals. It may be necessary, depending on the size of the family, to put limits on the number of family members allowed to join the business.

Family business owners need discretion in managing succession and perpetuating the family management of the business. The business also has an organizational need to maintain professional standards. Therefore, children of the owners can be placed in jobs at the discretion of the owners, but once in those jobs they must perform at least as well as professional managers.

Children of the founder who are interested in pursuing a career in the family business should be required to go through several steps in preparation for a management position. Upon reaching employable status, and having completed the appropriate managerial degree, the child works in a comparable or complementary business to that of the family business for a period of three to five years, receiving basic managerial training. Outside managerial experience offers a number of advantages. First, success outside the family business provides the child with a sense of self-confidence, independence and professionalism, as well as an opportunity to gain valuable knowledge. Second, outside training relieves the founder of the responsibility of instruction: a task which is often unsuccessful. Different sizes and types of businesses will offer unique learning experiences for the child which will help prepare him or her to work in the family business. Outside employment can be especially valuable when it is working for a competitor in another location. This experience would help the child gain knowledge of the industry, build a network of contacts, and develop a perspective into the way competitors operate.

Upon returning to the family business, the child should avoid an entry level position in favor of a position where he or she is challenged, is learning, and is contributing to the business. A program should be set in place for internal training to prepare the child to learn the management of the business. If the founder finds it difficult to train the child, an alternative trainer may be found within the firm. Characteristics of a high performing trainer include logic, commitment, credibility and an action bias.

It is a fortunate situation when the business is divided into separate, roughly equal parts, so that each child can manage his or her own business. In this way, more than one child can hold a leadership position within the parent company, avoiding some of the potential conflict because of competition between siblings.

The issue of stock ownership among offspring should be addressed as early as possible.

4. **Develop and execute a written succession plan**

Effective team development in a family business requires the ongoing definition of expectations concerning organizational goals, performance, and priorities. Integral to this process is succession planning for its future. There is typically a lack of succession planning in family businesses by founders and their families. Planning should begin many years before the actual management transition takes place. An orderly succession plan, in which leadership is delegated and gradually transferred over a prescribed time span, is basic to the ongoing success of a family-owned business. In order for the business to survive the succession transition, owners and the board must set goals, objectives, and a time frame in which to achieve them. A succession plan, in writing, is one good way to insure that control is passed on at the right time and to the right person.

The board can provide an objective forum to address succession, both how and whom to choose. The board can propose job assignments that help develop successor candidates in light of their strengths and weaknesses, as well as define the most important capabilities of the next chief executive, given the company's future strategic needs. The board can then assess potential successors' performance. Once the decision is made the board can assure everyone that the choice of leadership was fair and based on sound business judgement.

The successor evaluation process that the board designs may create an "executive team" of all the family members eligible for succession consideration. The sibling team can jointly assume the leadership of the company. Over time, the "natural leader" of the group will likely emerge - evident to the family, the organization, and the board. The best result comes when all next-generation family members achieve clear consensus on the choice through a process overseen and reinforced by the board.

A key element of a smooth transition is that all phases be timed. Time frames need to be established with regard to successor training and the eventual relinquishment of control. Utilizing these time frames also allows for the formulation of a retirement plan which provides a schedule of the founder's activities upon exiting the firm. This concept enables the founder to exit one job and enter another. However, the succession plan is not static. Since learning is a continuous process, the plan itself must be evaluated during implementation and proper adjustments must be made.

The cooperation of other key employees is often critical during the transition from one generation to the next. Non-family employees play a vital role in the family firm and are often ignored when succession planning or strategic planning is considered. These managers have to cope with both the benefits as well as the problems of working in a family business. They can be the critical factor in determining how successfully the next generation will enter and manage the family firm. Employees should know that, when possible, the top job will go to a family member.

A written succession plan with time frames is important to the process, however, the successor must ultimately take control. The critical stages during the succession process when this must happen is seen as the period in which the successor has the title of president or general manager. At the same time, the predecessor still holds the ultimate power and authority, either through his or her title or his or her presence at the workplace. The successor must be able to somehow assert himself or herself in the most opportune manner. Self-confidence and managerial autonomy are characteristics of effective successors. Therefore, for the incumbent, succession planning is a critical factor, because creating an environment for the successor that is conducive to experimentation and forgiving of errors will encourage the development of the successor's self-confidence and managerial autonomy.

Estate planning is an integral part of succession planning. Transferring company ownership can be accomplished a number of ways, all of which have significant tax ramifications. If the founder dies before succession planning has been done, there may be serious financial repercussions for the family and the business. This is an area in which outside professionals are a necessity.

Parents usually want to treat their children equally when it comes to the value of their estates. As a result, they often make sure each child owns an equal amount of stock in the family business, regardless of whether the child is active in its management. While structuring a plan for all children to share equally in the ownership appears to be a fair arrangement, it often creates more problems than it solves. Dividing stock evenly among the children may interfere with the management of the firm. Nonactive members may lack trust (whether appropriate or not) in the family managers. This is most likely to occur when the goals of the active family members are not consistent with those of the inactive members. For example, current family management may wish to achieve growth which requires additional debt or the retention of earnings. This strategy may be unacceptable to the nonactive members who see debt as risky and retention of earnings as punitive. Unless there is a forum for discussing the strategy and mutual trust and respect among the siblings, serious conflict may result.

In most cases, only the offspring who are active in the business should own voting stock. One solution to the dilemma of treating all children equally is to transfer stock in the business to the children who are active in the company and other assets to those who are not. If the owner has other assets that are significant relative to the value of the stock in the business, then treating everyone equally is not a difficult task. However, for many business owners the value of the business represents most of their net worth. Rectifying this situation can be accomplished in several ways. One simple option is to arrange the estate so the children in the business receive the stock and the others receive the life insurance proceeds. A second option is to give non-active children stock initially, but structure a program through which the corporation or other shareholders purchase the stock over a specified period of time. A third option is to carry enough life insurance so that at the death of the parents, the insurance proceeds can be used to purchase the stock that is owned by the uninvolved children. A fourth solution is to issue class B non-voting, income stock to children who are not involved in the business, and class A voting stock to those children who are working in the business. In most cases, the class B stock owners would receive a dividend before class A stockholders. In this way, nonactive children can receive some financial benefit without the conflict involved with running the business. These options should be considered with the help of the board and estate specialists.

Conclusion

Family businesses represent an extremely large economic force in the United States, which is the reason that increasingly more attention has been paid to family business issues in the past few decades. The most vulnerable time in the life of a family business is during management succession. This vulnerability can successfully be minimized by careful succession planning. The planning begins with introducing and educating the founder's offspring to the business at an early age. Establishing a working outside board of directors is extremely important in terms of succession planning, as well as guiding the overall operations and direction of the business. High expectations must be established for offspring working in the family business. The children of the founders must be accountable for their work performance in order for the business to continue to be successful. Establishing a written succession plan which is executed and monitored by the board will ensure a successful transition. The succession plan must include ownership transfer provisions, which are designed to support the management transition.

There is a need for more research in the area of family business succession, specifically in the area of non-traditional business situations. Most of the current research is based on male founders of businesses, being succeeded in management and ownership by one or more sons, with the eldest son usually expected to take the lead management role. Daughters and younger sons are successfully running family businesses, and there is a need for research to focus on those situations.

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