

BUILDING THE FAMILY OWNERSHIP TEAM

PART II ON FAMILY OWNERSHIP

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As a result of a family's strong desire to pass ownership to all family members regardless of their interests or capabilities, most family ownership groups include a minority of family members who know a lot about the company and are loyal to it, family members who want to be good owners but don't know how, family owners who only care about the money they will receive, and maybe one or two who are discontented. Your job as a family or family business leader is to manage and develop this group so that most of the owners are good stewards (guardians) of the family business that know their responsibilities and rights as owners and have the information and skills to perform well. Many years of working with family companies demonstrates that this can be done and it's highly worth doing.

Developing skilled and supportive family ownership groups takes time and requires building *just enough* trust, pride, talent and money with the owners. You certainly don't want too little of these resources, but it is true that owners can have *too much* trust, pride, talent or money.

Too much trust (blind trust) by the family owners of management or of each other reduces accountability in the system. Everyone (even a founder and controlling owner), in a family business system needs to feel accountable to someone. I have seen owners of the family business have so much pride in the company or its leaders that they think they can make no mistakes. Such hubris can lead to humiliating mistakes that can wreck companies and destroy fortunes.

Families need to constantly build their talent, but families should never feel so internally talented that they believe they do not need help from non-family managers and advisors. Families that succeed in business for a long time believe in partnering with others outside their family.

Finally, while family companies tend to do better when its shareholders have strong individual balance sheets, and I want my clients to live well, families shouldn't have a lot of money that can be spent, because they tend to spend it too freely, and this can lead to a number of problems. It's better for families (and family companies) when family members are reasonably conservative about spending money, and invest most of it wisely.

So, with these important principles in mind, how do you build strong family shareholder groups? Let's start with money.

MONEY

Managing a relationship involves managing the person's expectations of what you can do for them. Family owners need to have realistic expectations about the financial needs of the business and the income that the family company can reasonably provide to them. By the third generation and often by the second, there is tension between the reinvestment needs of the business and the financial needs of the family.

To solve this financial problem and support a competitive business, especially after the first generation, most families must reduce their financial dependence on the family business or they will drain the business of critical capital. This sensitive issue requires careful analysis of family and company financial needs, sympathetic setting of new expectations by the leader, and sensitive implementation of new financial policies.

It makes sense, given the typical limitations of the family business to support a growing family, for families to build other assets to help financially support the family. Even with other cash producing assets, most family members also need to be financially self-reliant (by working and largely supporting themselves) and living within their means. This is a challenge that requires strong family leadership.

But the business can and in most cases should provide a reasonable dividend or another kind of distribution to the owners after the needs of the business are addressed. Our experience shows that most owners (especially smaller owners) appreciate receiving

predictable and fairly constant dividends over time, rather than having dividends fluctuate. This is usually possible to do when management plans ahead adequately and communicates effectively with the owners.

Family companies also need to establish an internal capital market to allow owners to buy and sell their shares when the owners' liquidity needs or other issues make that useful. This requires having a clear buy-sell agreement, set in advance, with share price determined by objective measures and the selling process fairly and transparently managed, usually by the board.

Getting family owners to support a dividend policy and shareholder policies that support the continuity of the company requires that the owners trust management and each other, and that they have pride in the company and their own efforts as guardians of the company.

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TRUST

Business leaders build trust with shareholders by operating the business with transparency so shareholders can see that they are managing the company professionally. They communicate openly with owners about the business, providing useful information about the business and how it is performing, and discussing plans for the business. While owners do not have the right to take part in many business decisions, they should be included in some discussions about the business. Effective leaders also use and support governance structures to engage owners' views on the business—shareholder meetings, a family council, and a board of advisors with both owner and independent members.

Having clear, fair agreements (such as buy-sell agreements) among the owners also encourages trust among them and with the management of the company. Perhaps most important, leaders build trust when they listen to the owners' views about the company and about their own personal needs, and respond to these views and needs in their actions.

PRIDE

The owners' pride in the business motivates the owners to expect fewer financial rewards as long as the business performs well. In well-managed family companies, even owners who never worked for the company generally feel a sense of pride and identification with the business. Typically they grew up seeing or hearing about the business and the family members who ran it, and they feel personally invested in making sure the company is successful long into the future. That's a huge asset for a business and should be nurtured through informing owners about the business and engaging them in discussions about the business, showing them how family talent and family values have made the company successful, and reminding them of the role of the owners and the family in building something they are proud of.

TALENT

Which brings us to the important role of family talent. Managing the money, trust, and pride elements that build strong family ownership groups is immensely easier when family members understand their roles as owners and are committed to being skilled owners. Building the talent of the ownership group is much easier with a strong foundation of professionalism in the overall family. If family members are committed to being capable supporters of the family business and in other aspects of their lives, they will not only appreciate being educated and developed as owners, they will help lead this effort. Well-educated owners are a business leader's best ally because they understand and appreciate the efforts he or she has made on their behalf.

Building trust and pride, managing the money issues, and educating and developing the ownership group might sound like a lot of work, and it can be. But these efforts generally have great rewards. Think of all the effort you put into carefully selecting, compensating, communicating with and developing your employees. The owners are a vital resource for your business too. Don't you want to have a top performing ownership group as well?

ABOUT THE AUTHOR



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John A. Davis is a globally recognized pioneer and authority on family enterprise, family wealth, and the family office. He is a researcher, educator, author, architect of the field's most impactful conceptual frameworks, and advisor to leading families around the world. He leads the family enterprise programs at MIT Sloan. To follow his writing and speaking, visit johndavis.com and twitter [@ProfJohnDavis](https://twitter.com/ProfJohnDavis).

ABOUT CAMBRIDGE INSTITUTE FOR FAMILY ENTERPRISE

The Cambridge Institute for Family Enterprise is a global research and education institute dedicated to the real issues facing family enterprises. It is a place where progressive members of family enterprises come to learn, exchange ideas, develop themselves and position their enterprises to be not only successful, but sustainable over generations. Its sister organization, Cambridge Advisors to Family Enterprise, advises multigenerational families around the world on strategies to sustain their success over generations.