The Family Business Advisor

THE FAMILY BUSINESS CONSULTING GROUP

# Family Ownership Strategy: Generating Family Currency

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As families and their family businesses evolve on their multi-generational journey, there is a transition from the entrepreneurial phase of the founder to the longer-term family enterprise stage that carries the family business into the future. Many founders of family businesses started with a "right place, right time, strike while the iron's hot" mentality. During the entrepreneurial phase, founders often rely on instinct with minimal formal planning. The ownership and business strategies, while not explicitly defined, are inherently connected and focused on serving the founder's and their immediate family's interests.

As the family business transitions from the centralized authority of a founder to being governed by a group consisting of parents, siblings, and cousins, it's important for the family to focus on developing and implementing a family ownership strategy. This strategy aims to build family unity and is a hallmark of achieving multi-generational continuity.

Put simply, the family group's functioning and success become more influential in perpetuating the enterprise than any individual's capabilities, including the founder. Determining how the family ownership group will function well is the essence of a family ownership strategy to build what we call family currency: the intangible and non-financial investment made and value received by the family and individual family members. This is the emotional connection between individuals, family members, and the enterprise itself.

## Family Ownership Strategy

A family ownership strategy to grow family currency involves identifying and periodically renewing a family's intentions for their enterprise. This includes clarifying their purpose for working together, defining the relationship between the family and their enterprise, agreeing on how the family will work together as a group and behave toward one another, and determining the family's goals for the continuity of their wealth. They also need to align their expectations for such matters as enterprise growth, how much risk the family group wants to take, what is an appropriate rate and level of profitability, and how will the enterprise provide liquidity to individual family owners.

Growing family currency in the face of an increasing amount of diversity as the family grows is naturally challenging. An increasing number of family members brings geographic dispersion, an array of talents that may or may not apply to the family's enterprise, and varying personal dreams and goals, to name a few aspects of diversity. A well-developed and articulated family ownership strategy builds family currency and provides support and guidance to family business leadership.

## Why Family Ownership Strategy and Family Currency Matter

Let's start with a tangible business reason. To the extent a family can build family currency through the implementation of a family ownership strategy, families can effectively reduce the cost of equity capital since more engaged and unified owners are more likely to desire to keep their capital employed in the family's enterprise and be supportive of business leadership. All other things being equal, the lower the cost of equity capital is, the more valuable the enterprise becomes in terms of financial currency. Building family currency in turn builds financial currency.

Another tangible reason for this is clarity for family business leadership. In one situation, a client approached us about working with the business leadership team to develop their business strategy. During our initial discussion, we asked, "A business strategy in support of what?" as well as "What does the family ownership group want to accomplish with the business, and what do they expect from the business?" The CEO paused thoughtfully and said, "I am not sure. Perhaps we should know that."

The result of this discussion is that the business strategy project was put on hold as the family ownership group came together to develop and articulate their family ownership strategy. With the family ownership strategy in place, the business leadership team was in an optimal position to develop a business strategy that supports achieving what the family wants in a way that meets their expectations. In effect, having a family ownership strategy helps ensure that the business will function in service and support of the family.

A tangible family reason for developing a family ownership strategy is that it opens opportunities for family owners, whether working in the business or not, to participate, contribute, and positively influence family relationships and build family currency. An important element of relationship building is to engage in meaningful and purposeful work in service of others, the broader family. Doing so can bring joy to individual family members as they work in support of their family. "By participating in the working group that developed the family ownership strategy recommendation for the full ownership group, I can now see how I can contribute even though I do not work in the business," shared one family owner. "This brings me a lot of energy for our family's and business's future."

## When to Start Developing a Family Ownership Strategy

The work of developing the family ownership strategy is that of the family. The matriarch of one of our clients once said during a family meeting, "We can hire the what and the how (business strategy), but only the family can decide the why."

When a founder and their spouse start considering the passing of ownership to the next generation, it can be a great time to begin considering a family ownership strategy. When this happens, the founder and spouse establish an ownership group with forethought and planning as to why and how the group will function, which can increase the odds of achieving multi-generational continuity of their enterprise and wealth. Often, however, ownership starts to pass to siblings, driven by an all-out focus on estate planning and too little forethought as to how the family ownership group will function. This frequently results in setting precedents and practices that eventually come to be seen as unfair and challenging to sustain once the influence of the founder and their spouse wanes.

Consider a scenario where a sibling group that owned a private-label food manufacturing enterprise had never addressed a family ownership strategy and eventually could not agree on one. They were ambivalent about keeping or selling the business, had not given any thought to transitioning ownership, and had not engaged the third generation in developing plans for the future.

Over time, the lack of a clear family ownership strategy led to a decline in the family currency, resulting in a lack of interest from the third generation and continued divisiveness among the siblings. The family's cohesiveness deteriorated, leading to the business leadership team, a combination of family and non-family leadership, struggling to articulate and execute a coherent business strategy. As a result, in the later sibling stage of the business, family relationships deteriorated further, the company's performance continued to drop, and the business was eventually sold at a significantly diminished value.

Let's contrast this with another situation with a family-owned wholesale distribution business. A sibling group, influenced by the founder's foresight, involved the siblings in formulating their family ownership strategy early on. This proactive approach allowed the cousins to contribute to the family's ownership strategy in the latter sibling stage. Despite only a small fraction of the 40+ family members working in the business, implementing their family ownership strategy and the resulting family currency has helped keep the family unified and their capital together.

This, in turn, has enabled the business leadership team to develop and implement a business strategy that aligns with the family ownership group's expectations. As the family CEO stated during their latest round of strategic planning, "Clarity about our family's ownership expectations puts our leadership team in a great position to figure out how to meet those expectations. After all, if we did not know what our family's owners expect, meeting their expectations would be nearly impossible."

## Building a Plan for Family Currency

At times, certain family owners in subsequent generations will need direction in finding paths to engagement. Below are some examples of elements of family ownership strategy goals that family enterprise systems use to create family currency within their family enterprise systems. These examples may be different from the roles of parents or grandparents, where the investment of family currency occurred naturally due to the hands-on involvement and associated investment of "blood, sweat, and tears." In those cases, failure wasn't an option, nor was the investment of family currency. Subsequent generations may continue those traditions but often find new and different ways to put their fingerprints on the family enterprise system.

| Family Ownership Strategy Element or Goal | Family Currency Investment | Family Currency Return |
|---|---|---|
| Engaged Family Discussions | Purposeful sharing regarding the challenges and successes | Shared understanding based on first-hand experience and modeling for future |
| Family Member Internships | Young adults invest time and take personal risks working in the business | A lifelong connection to the business, deeper understanding, and a sense of pride |
| Family Member Employment | Personal investment in gaining valuable education and/or outside experiences | Continued personal development and a deep contribution to business successes |
| Family Senior Leadership | A commitment to high-level personal and professional development | Direct family business leadership with shared values, culture, and brand |
| Awareness of Family, Owners, Board, and Management Roles | Dedication of effort to understanding the complexity of family enterprise systems | Opportunity to see varying paths for all members to contribute in the future |
| Family Board Members | Developing skills for the stewardship roles needed by a functioning director | Putting "fingerprints" on the family enterprise's future goals, strategy, and results |
| Family Meetings | Work together with other family members to organize purposeful family gatherings | Build memories, connections, and practice decision-making and communication |
| Family Education Process | Learning and skill development related to family, ownership, and business topics | Foster connections, shared experiences, cultural awareness, and a shared vocabulary |
| Family Policy Development | Engaging with other family members to develop policies regarding family policies | Fairness process, joint decision-making, communication, relationship building |
| Family Governance Processes | Serving and supporting structured family governance processes | Develop and share a "unified voice" for the family via the governance process |
| Individual – Civic, Charitable or Philanthropic Involvement | Individuals invest time, talents, or personal finances in the community | Developing as a person while feeling pride and joy related to having given back |
| Collective – Civic, Charitable or Philanthropic Involvement | Collective process that engages family members in investing in community efforts | Create connections, shared experiences of joy, giving back, family/business pride |
| Conversations on Family Ownership Responsibilities | Thoughtful and serious attention to the "who" and "how" for future ownership | Increased likelihood of longevity resulting from filling roles with skilled family owners |

## Comparison of Family Ownership Strategy to Business Strategy

The family ownership strategy should focus on the investment and return of family currency. The focus of the family ownership strategy will differ from that of the business strategy.

The family ownership strategy:

- Addresses a 10-30 year time horizon.
- Focuses on developing paths for ongoing family stewardship opportunities, family connections, and family harmony.
- Measures success by the ways in which individual family members lives have been enhanced in non-financial ways as a result of their engagement with the business systems — whether in support of the business, by interacting within the family, or through efforts to give back to society.

In contrast, the family business strategy:

1. Addresses a 2-5 year timeframe.
2. Considers future business markets, products, services, investment, and human resources.
3. Measures success with value creation and financial measures like profit, growth, margin, cash or debt levels.

Elements of the family strategy also may influence business strategy by:

- Offering guidance to business leaders regarding family currency goals, family vision, mission, and values — the "whys"
- Stating goals for family members' engagement in governance or employment roles in the business, or offering other goals related to financial or non-financial matters.

## Conclusion

As you consider strategic planning for your family enterprise system, ask yourself whether the process includes two separate but connected paths: 1) the development of a family ownership strategy to build family currency and 2) the development of a business strategy to build financial currency. Your efforts will ensure that the words "family business" remain closely connected under your watch and will allow succeeding family leaders to do the same.

Your children and grandchildren will appreciate your planning to invest their own "currency" into the family's enterprise. To the extent that future generations experience a life well lived, it may have been made possible by the return on their investment into the family systems and the resulting family currency, which contributed to their sense of self and gained wisdom.

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