Family Business Magazine's

The Family Business
Mentoring Handbook

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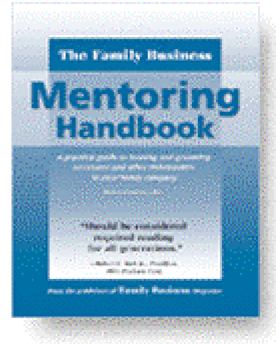

Teaching protégés to be proactive

To ensure continuity of the family business in the next generation, mentors would do well to guide their charges in adopting 'The Seven Habits of Highly Successful Successors.'

By Dean R. Fowler

How can a mentor help to ensure the success of a family business successor? One effective way is by encouraging successors to emulate behavior that fosters continuity of the business from one generation to the next. In consulting with numerous family businesses over the past 20 years, I have identified seven habits of highly successful successors (with apologies to Stephen R. Covey, author of *Seven Habits of Highly Effective People*). Good mentors promote these best practices and guide their protégés in adopting them.

These seven habits encompass the three distinct roles of successors in family businesses: family membership, company management and business ownership. The first two -- establishing independence and re-shaping communication dynamics -- nurture healthy family relationships and typically develop during the protégé's 20s. The next three -- demonstrating competency, participating in strategic decisions and clarifying boundaries -- provide the framework for management responsibilities and grow during the protégé's 30s. Finally, by developing liquidity strategies and assuming financial risk, successors are transformed from passive shareholders into proactive participants in ownership of the business. This final stage of mastery typically occurs during the protégé's late 30s and 40s.

1. Establishing independence

The first habit -- establishing adult independence -- serves as the foundation for the other six by transforming the relationship between the two generations. Mentors should encourage their protégés to establish their own adult lives, separate from and independent of their family and its business. In many cases, this means working outside the family firm. Outside experience helps a young adult to gain technical competency and business experience. More important, this experience helps next-generation members to overcome emotional dependence on their parents and to prove to themselves that they can function independently of their parents' financial resources.

As an alternative to working outside the family business, mentors can help their protégés to identify key projects over which the protégé may exert leadership. Taking charge of a project enables young people to succeed in their own independent efforts. For example, one successor identified an opportunity to provide additional services to customers of the family business. Under the tutelage of the chief financial officer, she developed a formal business plan that outlined the financial viability of her business proposal. Using "family venture capital," this successor started a separate business. As president of this venture, she had full authority and responsibility for future success.

2. Re-shaping family communication

It's the successor's responsibility to reshape communication dynamics within the family and to break the patterns of childhood. Two skills are critical to achieving this new pattern of interaction. The first is the ability to avoid what's known as *triangulation*. This unhealthy communication pattern often occurs when conflict, anger, resentment or frustration has built up between two people. To alleviate this build-up, one of the people "downloads" the negative feelings by sharing them with a third person instead of discussing the conflict directly with the other party. For example, if a daughter disagrees with a decision made by her father, she might complain about the situation to her mother, although the issue would be best resolved if she raised the issue with her father.

Non-family employees and managers are often caught in the dangerous pull of triangulation. Rather than be drawn into this scenario, a mentor can impart a valuable lesson by refusing to participate as a triangulated party. Instead, the mentor should encourage the two people in conflict to address their issues in an open and straightforward manner.

The second communication skill is active (or empathic) listening. The power of this skill rests in the listener's ability to really understand the perspective of another person. Family members must recognize that everyone needs assurance that he or she has been understood. Mentors must master active listening in order to really understand the needs of their protégés. For example, one daughter was frustrated because she felt that her father didn't really listen to her. Her mentor, the vice president of human resources, helped her to develop her own listening skills. Building on the communication principles the VP taught her, she created a code -- "A or O" – and presented it to her father. When she wanted his acceptance, she told him the conversation was an "A"; when she wanted his opinion, she told him it was an "O." With the help of her mentor, she took the responsibility to re-shape communication dynamics with her entrepreneurial father.

3. Demonstrating competency

The third habit to teach your protégé concerns competency. This habit has two dimensions: technical competency in some area of the business and demonstrated leadership capability.

Training and development programs for successors are often designed to give them limited exposure to several different aspects of a company. While this broad-based exposure is helpful, it doesn't enable the successor to develop any detailed technical expertise. More important, the successor isn't given the opportunity to develop as a leader through management of direct reports.

To become competent, successors should assume long-term responsibilities that require leadership. Initially, this may involve the responsibility of overseeing a significant project and heading the project team. As experience grows and develops, successors should take on departmental leadership roles or divisional responsibilities, where profit and loss results may be measured and evaluated. In one family firm, the vice president of operations was asked to develop a comprehensive training program for the family successor. The president of the company considered mentoring to be an important part of the VP's responsibilities. These duties became part of the VP's primary goals and objectives and were measured as part of his annual performance review. Working closely with his protégé, the VP developed a four-year program that culminated in the protégé's ascent to management responsibility for a major division of this international business.

In addition to financial measures, a "360-degree" leadership performance review is an effective tool to identify strengths and weaknesses as protégés develop their leadership capabilities. In this review process, managers, peers and direct reports of the protégé all complete a questionnaire that evaluates the next-generation member on several key dimensions of effective leadership. The questionnaires are compiled anonymously in order to ensure frankness and pinpoint areas of leadership development where the protégé needs additional mentoring.

4. Participating in strategic decisions

The fourth habit mentors teach their protégés relates to the development of business strategy. Successors are frequently involved in day-to-day operational issues without participating in strategic decisions. They must learn about strategy early in their careers by defining how their own projects fit into the broader strategy of the business. Typically, one of the senior executives who participates in the corporate strategic planning process helps the successor to develop project management skills. The mentor guides the protégé in determining how best to align the successor's projects with the strategic goals of the business, rather than simply to develop day-to-day tactics in reaction to business circumstances.

Successful successors take the strategic process one step further; they partner with the senior generation to define future strategies that fit the passions and competency of the successor generation. In one family business that specialized in long-haul trucking, a successor recognized that the company's communication technology and logistics expertise could also serve other businesses in managing their own private fleets. The vice president of operations helped him to prepare a strategic plan that outlined how these core competencies could be leveraged to create a separate profit center for the business.

In another situation, a family business founded by a mechanical engineer grew through its proprietary products, designed and patented by the founder. The son, who had expertise in computer systems, was not sure how he would fit into the mechanical engineering focus of the business that had been developed by his father. A long-term trusted adviser who served on the company's board of directors worked with the son to identify the son's career goals and ambitions. Together, the board member and the successor recognized that the son's expertise in computer systems could be used to serve the customers' hardware and software needs. As a result, the strategy of the business was transformed not only to meet the strengths of the senior generation, but also to build upon the competency and expertise of the successor generation. Family businesses can redefine their strategy so that the business becomes the "home" for the passions of the successor.

5. Clarifying boundaries

Perhaps one of the greatest challenges facing business successors involves clarifying the boundaries separating operational responsibilities, the development of strategy and corporate financial decisions. Effective mentors help their protégés negotiate these boundaries, which are typically complicated by role confusion between family membership and company management. Parents, as the primary shareholders of the business, usually maintain control of the major strategic and financial issues that affect the company while delegating operational responsibilities and accountability to their direct reports, including their children with management positions in the company.

Conflicts between the generations are often rooted in two distinct issues. First, the senior generation will delegate operational responsibilities without defining clear expectations and performance measures and then will step back in to take control when the outcomes don't meet their undefined expectations. Second, the senior generation is often risk-averse, while the successor generation wants to implement strategies to grow the business for the next 20 years. When conflict and tension exist between parents and their children working in the business, mentors play a very important role as mediators between the two generations. One non-family president was given the challenge of balancing two alternative strategic solutions to a current business situation. With sales declining, the father wanted to reduce overhead expenses in order to bring the company back to profitability. The son, on the other hand, wanted to hire a sales manager to build future business opportunities. The mentor worked with both the father and the son to objectively evaluate the pros and cons of each alternative. The alternatives were then presented during the formal strategic planning process, so that the entire executive team could determine the best strategy to pursue.

6. Developing liquidity strategies

The first five habits that protégés must master define key characteristics of any successful manager (family or non-family) who may be considered for executive responsibilities and leadership of a company. The next two habits -- developing liquidity strategies and assuming financial risk -- involve areas where family membership, management expertise and ownership dynamics intersect.

While most family businesses have an estate plan, which addresses financial issues in the event of the leader's death, very few develop liquidity strategies to restructure the capital of the business while the senior generation is still alive. With life expectancy now in the late 80s to early 90s, more successors are recognizing the need to design a mechanism for buying the business from their inactive siblings or cousins, as well as from the senior generation.

Mentors must discuss with their protégés various approaches to financing a smooth intergenerational transition. Successors should take a proactive role in learning about effective strategies for recapitalization of the business. For example, one family is wrestling with the question, "Should we sell our business to a strategic buyer?" A non-family president manages the day-to-day responsibilities of the business and has explicit instructions from the board of directors to serve in a mentoring capacity to the successor generation. As part of their quarterly board meetings, the successors have been investigating several alternative scenarios. Under the guidance and direction of the non-family president, they have explored an ESOP to create diversification and liquidity for the senior generation, new buy/sell agreements among siblings to structure future redemptions, funded non-qualified retirement programs for the senior generation, and finally, the pros and cons of selling the business to a strategic buyer. Guided by the non-family president, the successors have been given the responsibility of meeting with their parents, advisers and other experts to identify the best possible options and then make their recommendations to the board of directors. The board will take the successors' recommendations under advisement and make a decision about the future ownership of the business.

7. Assuming financial risk

In most family businesses, successors are owners by virtue of being gifted non-voting stock. In this respect, the successors are essentially participating in estate planning tactics rather than assuming the responsibilities of ownership. Mentors must encourage their protégés to become involved in the financial aspects of the business as a way of transforming themselves into responsible owners. Early in a protégé's career, this involves teaching the young person how to read financial statements and explaining the impact of this financial information on business decisions. Mentors should introduce successors to bankers and other trusted advisers and should explain that developing a relationship with these key people will help establish successors' credibility.

To move from being passive recipients of a gift to active owners of stock, successors must be willing to take their own financial risk. For example, in one family business that acquired a competitor, the bank asked all family members to personally guarantee the loans. Some family managers were unwilling to co-sign such a document, thereby demonstrating their lack of commitment to taking financial risk. The willingness to take on personal financial liability demarcates the difference between management and ownership roles.

Financial risk is often linked with the development of liquidity strategies. For example, when one of my young clients was ready to assume the risk of buying the company from his family, he took a proactive role. He requested his father's permission to meet with attorneys, accountants and other advisers. With their help, he developed a proposal to purchase the business and presented it to his father. The father worked side by side with his son to present this liquidity strategy to the rest of the family, in order to promote a smooth transition of ownership from one generation to the next during the father's lifetime. The process of developing intergenerational buyouts is facilitated most effectively when the company operates with a formal board of directors. Members of the board are normally the best mentors in helping successors design ownership transition plans. To structure such transitions and to take on financial risk, protégés must learn in detail the financial aspects of the business and alternative funding strategies that can be pursued to finance these buyouts.

Liquidity strategies and corresponding financial issues are rarely addressed in family-owned businesses. Most mentoring activities focus on the first five habits.

Patience is a virtue

These seven habits of successful successors can't be developed all at once; they represent a gradual process, with each habit building on the previous one, over a time span of about two decades. As family members, successors must first take the initiative in developing adult independence and re-shaping family communication patterns. In their role as managers, they must develop technical competency and demonstrate leadership; they must also help to shape the business's strategic plan and must clarify the boundaries that distinguish operational, strategic and financial roles. As owners, successors must be proactive in designing liquidity strategies and then be willing to assume financial risk to consolidate ownership for their generation.

Successors must be patient as they navigate their way through these seven steps. Mentors must demonstrate patience themselves by embodying this virtue in their interactions with their protégés. Mastery of these seven habits is a challenging process. The senior generation and other family members must be willing to accept and encourage the transition of the business from generation to generation.

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Successful Habits of Successors

Lessons Learned
from

Forums for Family Business™

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- Nationally 70% of family businesses fail to transition with family ownership

- Of over 60+ Forum companies, 94% transition successfully with family ownership

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Rate Company for Succession Success
1 - Poor → 5 - Excellent

☐ Habit One: Establish Adult Independence - psychological and financial

☐ Habit Two: Reshape Family Communication

☐ Habit Three: Develop Competency

☐ Habit Four: Design Strategy

☐ Habit Five: Clarify Boundaries

☐ Habit Six: Coordinate Liquidity Strategies

☐ Habit Seven: Take Financial Risks

☐ TOTAL

31-35 Excellent
24-30 More Work Needed
Below 24 Danger Zone

For information, please call 262-789-7367 or email dean@deanfowler.com