Enterprising Rural Families™

This newsletter is an instrument of the *Enterprising Rural Families: Making It Work* program of the University of Wyoming Cooperative Extension Service. For further information concerning the Enterprising Rural Families program or on-line course contact *information@eRuralFamilies.org* or go to *http://eRuralFamilies.org/*.

TIPS OF THE MONTH:

- Regardless of our best efforts to maintain a perspective on life and remain calm in a frantic world, there are days when we feel smothered by to-do lists and overwhelmed with the need for decisions. A support team can help us to stay on track and prevent isolation.
- "We want to be sure that all we have is passed on to our children and grandchildren without causing personal or financial difficulties…"

  Consider a *beneficiary controlled trust.*
- Leaving a legacy that everyone can love depends on generations being able to bridge the communication gap. All persons should be included from elders to grandchildren, especially adult children. These issues are examined in detail in the two disk course titled *A Lasting Legacy*. For more information go to the *Right-Risk.org* website and click on "Products."

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SUCCESSION IN THE FAMILY BUSINESS

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Family businesses have characteristics contributing directly to the difficulty of transferring management to the next generation. Of particular interest are the characteristics which distinguish the management succession issues of family businesses from those of non-family businesses. Most of these characteristics are related to human interactions among family members and their inability to isolate family issues from business issues.

Family businesses mix business and family. For example, family social occasions can involve more business talk than family talk. Tranquility in a family that is in business together requires acceptance of the double lives everybody is living. Family problems and decisions are mixed with business problems and decisions. Solutions to problems are rarely pure business or pure family in nature so attempts at complete separation are counterproductive.

Business continuity requires generation to generation transition. Timeliness in the transition is essential. However, the parents may be unwilling to give up control and authority at the time the next generation wants it or should have it. On the other hand, the next generation may not be ready for their responsibilities when they have to assume them.

Continuous change in the external and internal environments accompany business management succession. The changes are diverse and pervasive: technology, public policies and regulations, growth and aging of people, and economic opportunities. Change must be managed simultaneously with attention to management succession.

The Role of the Founder

The founder as the most influential person in the organization sets the tone for management succession, makes the "rules" and, more than anyone else, determines success or failure of the succession. Each family

business will eventually have a different generation of managers or it will no longer exist. The founder's acceptance of this reality undergirds and fosters management succession planning. Rejection of this reality stifles the planning.

If the founder does not have a viable business that gives the next generation a chance at success, the issue is transfer of assets to the next generation rather than transfer of management. Understanding and communicating the current status of the business is a primary role for the founder.

Ideally, the founder integrates management succession concerns into strategic planning. The founder has the responsibility of involving all members of the management team in strategic planning. The founder must also deal with the integration of plans for the business and plans for the family because "family issues ultimately shape the business strategy." Updating the mission statement causes the management team to continuously answer the question, Why are we in business? This question can easily be expanded to deal with questions of business and family values, human resources including employees, role in the community and industry, and long-run aspirations. Answering these questions requires careful communication within the family business. Improvement of communication skills may need to precede strategic planning. A family commitment rather than just a founder commitment to improved communication increases the chances of success. For more on strategic planning in family businesses, visit the Enterprising Rural Families website at eRuralFamilies.org.

In the absence of strategic planning and written mission statements, each member of the management team is allowed to generate her or his own reasons for being in business. Conflicting strategies for success, misallocation of resources and failure to deal with management succession then characterize the business. The founder's top management role is thus compromised on critical strategy decisions.

The Perspective of the Next Generation

The next generation has multiple perspectives owing to its composition: sons and daughters who enter the business, their siblings who do not enter the business, the spouses of the founder's children and the founder's employees. For each of these four groups, there are issues of career and financial planning, career opportunity and career satisfaction, fairness of treatment by the founder, and family relations.

Regardless of how the founder may have conducted the affairs of the business, the next generation of managers in agriculture faces the certainty that success of a business is dependent on more than hard work, sacrifice and adoption of new technology. The next generation's success after gaining management control depends on a complex milieu of financial, management, interpersonal and external factors. Assuming that management control over the founder's resources and personnel assures success may instead leave the next generation poised for failure. Maintaining the business at the founder's level challenges the new manager. However, matching the founder's level of operation and expertise probably will be inadequate. A business cannot stand still and have long-run success. Changing and growing the business to have a chance at long-run survival is a challenge the new management team may not be able to handle. Competition, inflation, shrinking profit margins, changing technology, and new customers with changing expectations will challenge even the best managers.

More than the capacity to manage the business affects the next generation. The following factors impact the next generation: personal need fulfillment, career interests, personal identity, life stage, personal influence, mutual respect and understanding between generations, sibling accommodation, commitment to family business perpetuation and separation strains due to family involvement.

The mix of management, financial, family and psychological factors affecting the next generation creates need for expertise beyond that occurring in the typical family business. The next generation can be helped greatly by a diverse external advisory committee as well as individual consultants. The narrowness of consultation from a single perspective, e.g., financial planning, estate planning, family relations or business growth is likely to generate a false sense of security in the next generation.

Succession as a Process

Management succession can be a process taking place over many years requiring cooperation of all people on the management team. The succession steps involve planning, selection and preparation of the next generation of managers, transition in management responsibility, gradual decrease in the role of previous managers and finally discontinuation of any input by previous managers.

In contrast to the above process, management succession can be by crisis. The crisis may be brought about by the death or disability of the founder, divorce, threat of departure by the heir apparent, or hiring of an outside manager in an attempt to "finally fix things gone wrong." In the absence of design and implementation of a process, succession will almost certainly be by crisis. Preferably, management succession is a process not motivated by crisis nor characterized by a single event nor marked by a single date on the calendar.

Whether succession is a process or a crisis depends on several characteristics of the business, senior managers and family. Growing, profitable and successful businesses cause managers to think about expanding opportunities and continuity. Stagnant businesses with disappointing profits cause managers to concentrate on today's predicaments. An attitude of, "I've got to solve today's problems before I can worry about the future." makes treating succession as a process difficult, if not impossible.

Senior managers garnering the payoff from strategic planning are more likely to see the benefits of succession planning than managers who muddle along day to day. The knowledge and self-discipline to do strategic planning, expansion planning, human resource planning, financial planning and market planning, for example, certainly can extend to succession planning. Optimistic, systematic and business oriented managers are more likely to plan for and follow through on management succession than pessimistic, unsystematic and production oriented managers.

Family characteristics also influence whether management succession will be a process or a crisis. As the number of adult children and their children in the business increases, the complexity of management succession increases. Similarly, difficulty in management succession is likely to increase with an increase in the number of heirs expecting cash from their parents' estates. Tightly knit families with strong commitment to honoring their parents' wishes about business continuity should face fewer problems than fragmented contentious families.

The Characterization of Effective Successions

Thirty percent of family businesses in this country survive to the second generation and only half of these first generation survivors make it to the third generation.

Following are five actions for management succession success consolidated from a list of more than 15 factors extracted from the research literature on management succession:

1. Select managers for the next generation. A person can rarely be successful in declaring himself or herself the new manager.
2. Put in place a comprehensive development program for these managers. There needs to be some combination of formal training, self-study, mentoring, communication, performance evaluation, strategizing about overcoming specific weaknesses and employment outside the family business. Manager development comes through an active process rather than simple assimilation through

watching "mom and dad do it for years."

3. Provide opportunities for next-generation managers to fulfill their personal and career goals. Delegation of specific responsibilities and the necessary authority is also important.
4. Develop plans for management succession, strategies for the continued operation of the business, retirement of the current managers and transfer of assets before and through the estate. Base plans on realistic assessments of the past and present, and reasonable expectations for the future. The plans need to stay flexible while providing for timing of the transfer, responsibilities of family members during and after the management succession, the specific arrangements for a testing period and financial security of current owners. As mentioned previously, the plan is for a process not a single transfer event.
5. Develop positive associations and good working relations among the family members in all generations in and out of the family business. Strained relations makes the inevitable need for compromise difficult if not impossible. As a practical matter, family business managers are unlikely to use a long check list to guide their actions. Identifying key actions which affect the management succession process can be a helpful starting point in developing a strategy for management succession that is responsive to the specifics of the case. The succession strategy will be evolutionary as changes occur in family members and employees, the culture of the business and the external business environment. Moreover, at any point, a health, marriage, weather or economic calamity may divert the best planned strategy for succession.

Reference: Erven, Bernard L., Professor and Extension Specialist, Department of Agricultural Economics, Ohio State University. *Management Succession Issues in Family Business*. 2005, www.fambiz.com/Orgs/Cornell/articles/real/erven.cfm

Planning for Successors

Successful Successor Traits

- Self-confident and optimistic
- Able to take calculated risk
- Respond positively to changes
- Flexible and able to adapt
- Knowledgeable of markets
- Able to get along well with others
- Independent minded-energetic and diligent
- Creative, need to achieve
- Dynamic leader
- Responsive to suggestions
- Take initiatives
- Resourceful and persevering
- Perceptive with foresight
- Responsive to criticism