TEPAP UNIT I
FAMILY BUSINESS MANAGEMENT

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Family Business Lifecycle

What stage is your family business in or between?

**Survival**
Start-up, Struggle for financial stability, Financed by owner’s compensation (or lack thereof).

**Stable**
Profitable for a number of years, growing, still owned by individual or couple. Net worth growth. Some offspring returning to business. Key employees.

**Professional**

**Institutional**
Mix of family/nonfamily shareholders. Family may not be involved in management, board of directors is governing body. Dividend income.

Succession Alternatives
Healthy businesses have healthy processes

Communication: input, feedback, discussion, & healthy conflict

Expectations of one another and of business performance clearly articulated.

Agreement on vision, goals, roles & strategy: Are we aligned?

Key people with development plans & self-awareness of individual impact – play to strengths
- Emotional intelligence

Processes to attract, develop & retain good people
- Job descriptions
- Evaluation & feedback
- Family employment policy

Accepted and respected decision making processes

Understanding of other businesses & management strategies
- Continuing ed investment

Commitment to work through conflict & agreements / processes to help
- e.g. buy-sell agreements

Understanding of financial information, performance & drivers

Recognize the value of being a family business...but act as if you are not one!
Power in the family business

Who has the power? Power is…

- Entity control, power of attorney = legal authority
- Information
- Proximity to decisions or decision-makers
- Family influence and relationships
- Money
- The ability to create chaos!
The Three Circle System in a closely held business

Management (Compensation)
Ownership (Return)
Family (Relationships)
Confusion and Potential Conflict

HR, Finance, Agronomy, Purchasing, Legal, Public Relations, Risk Mgmt.

Shareholder, Partner, Heir, Investor, Director

Son, Daughter, Sibling, Parent, Lifelong Friend
Three systems have different values and logic

**Family**
Mutual cooperation, loyalty, unity, permanence, stability
= Relationship

**Management**
Competition, less loyalty, rewards based on profit and performance, impermanent, task-oriented
= Performance

**Ownership**
Financial metrics like ROE, liquidity, dividends, access to capital, risk-oriented
= Building and/or transitioning wealth
<table>
<thead>
<tr>
<th>Family</th>
<th>Business</th>
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<tbody>
<tr>
<td>Emotional</td>
<td>Rational</td>
</tr>
<tr>
<td>Inward looking</td>
<td>Outward looking</td>
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<tr>
<td>Kinship based</td>
<td>Merit based</td>
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<tr>
<td>Generational authority</td>
<td>Positional authority</td>
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<tr>
<td>Develop individual</td>
<td>Develop products</td>
</tr>
<tr>
<td>Transfer values</td>
<td>Transfer Profits</td>
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What do you believe about your family and your wealth?

- Those that are working in the business should own it.
- My assets should be owned by my heirs regardless of their involvement.
- The next generation should have to buy the business.
- The next generation should not have to “recapitalize” the business with their wealth – it should be a gift to them.
- Being transparent (letting people know your thoughts) is important
- Keeping my thoughts and information private/hidden, to be revealed later, is preferable.
- Any family member can come back.
- Only those that pursue additional education, work somewhere else for awhile, and have a skill set that fits our business’ needs have a place here.
- Only family members can be owners.
- Ownership can be used to attract and retain the best talent.
- In laws should participate in discussions
- Only family members (blood relatives) should be involved in the process.
- Land will only be farmed by family members.
- Family members must perform in order to retain the right to farm the land.
- You will take a discount on your equity if you leave.
- Using insurance to pay an estate tax liability is an acceptable strategy.
- Giving some of my estate to charity is important.
Guiding Principles

Write down 3 “guiding principles” you believe (not necessarily your parents’).

Share with someone you haven’t yet spent time with (get up, move around)
Assumptions

- We sometimes believe that someone is too fragile to discuss sensitive issues. (Not telling them is best for them.)
- We think communicating will make things worse. (Better to fear conflict than experience it!)
- We think our feelings about something will go away. (This too shall pass…although the opposite happens. It builds then blows!)
- We think they should “obviously” understand our actions. (We forget that others in the business were not brought up with our experiences or relational and communication styles.)
- We think they already know what we know, or that what should happen is straightforward.

What might you be assuming about how other people will act or handle tough issues?
# Sharing Information In the Family Business (preventing assumptions)

<table>
<thead>
<tr>
<th>Financial</th>
<th>Relational</th>
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<tbody>
<tr>
<td>Balance sheet, income statement, cash flows, upcoming purchases, compensation, expenses, investments, debt</td>
<td>Events with vendors, family, neighbors, friends, employees, customers, landowners</td>
</tr>
<tr>
<td><em>How is the business doing? What changes, concerns or opportunities do you see?</em></td>
<td><em>What’s happening with those we know or interact with? What are your expectations of others? Are they meeting your standards?</em></td>
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<table>
<thead>
<tr>
<th>Attitudinal</th>
<th>Future</th>
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<tbody>
<tr>
<td>Feelings about the business, relationships, events, people</td>
<td>Opportunities, decisions, ideas, plans</td>
</tr>
<tr>
<td><em>How are you/we feeling? What is your perspective right now?</em></td>
<td><em>Where are we headed? What is your plan? What could derail it?</em></td>
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Conflict and communication

• Many challenges to family & business come from not managing conflict (note: it is seldom “resolved”).

• The key to managing conflict is to promote good reflection, emotional intelligence and communication skills.

• All families have their own style of communicating.

What is your family’s level of “unmanaged” conflict?
What is your family’s level of and process for communication?
What is your family’s “style” of communicating? (Bury it or Blow?)
The Process of Managing Conflict

Admit: Conflict exists!

Assess: Is it worth resolving?

Assemble: Is the other party willing to work on it?

Listen: How is the other person feeling? What's their story? (Watch tendency to react!)

Demonstrate: Can you articulate that you understand why they are upset?

Reflect: How have you contributed to the conflict? How might your actions have been perceived?

Tell: Explain your side of the story. How have you been hurt? How were you misunderstood?

Agree: We've both been hurt. Do we want the relationship to be better?

Answer (both): What do you need to See or Hear from the other person in order to move forward?
Ground Rules for Discussions

- Be willing to listen and be open minded
- Feel free to share without retribution; don’t be combative
- Don’t interrupt
- Assume the best; good intentions
- Respect
- Turn off phone for this meeting
- Be on time
- Value is when everyone participates
- We want everyone’s perspective; don’t dominate
- Say it here, not later
1. Differences and/or uncertainty in the future direction of the business.
2. Unexpressed expectations of family members and business partners.
3. Compensation philosophy differences among family members.
4. Lack of clarity and discussion regarding future transitions.
5. Lack of understanding about business or structure and big picture “flow” of money.
6. Inadequate sources for retirement funding so transitions are feasible (lack of planning).
7. Lack of a family entrance policy.
8. No strategy for dealing with unexpected – or planned – departures (buy-sell).
9. Unexpressed frustration/concern with income tax or inheritance philosophy.
10. Lack of regular communication/assumption-based activity.
Managing Family Relationship Risk
(An approach to succession planning)

• Assess the key stakeholders: Roles, Values, Power, Concerns. Who needs to be involved at what level, and what are their positions and concerns?

• Keep a focus on business planning: future focused & framed more objectively
  ▶ Vision for the business and the family
  ▶ Specific goals and strategies for the business
  ▶ Each person’s potential role over the next few years (incl. entrance/exit)
  ▶ Expectations about changes that may occur
  ▶ Regularly revisiting business performance and the plan

• As a group, create a list of key responsibilities/organizational chart – forces a discussion about expectations.

• Determine functional areas for gradual transitions of control: timeline, percentages.

• Clarify what you expect - particularly around knowledge, skills and results.

• Seek out and encourage experiences (formal education, workshops, training) to learn & interact with peers. Create a forum to discuss the results of your learning.

• Consider using a structured advisory board setting to challenge your business to become more professional and remain accountable to progress.
What, specifically, are we planning for?

<table>
<thead>
<tr>
<th>Estate Plan</th>
<th>Succession Plan</th>
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<tbody>
<tr>
<td>The process of determining a plan to transition financial wealth from one generation to the next.</td>
<td>The process of “co-creating” psychological ownership of the vision, strategy, goals, roles, decisions, performance and results of the business enterprise between two or more generations.</td>
</tr>
<tr>
<td>Often parents determining how to get X assets to Y people.</td>
<td>Often all family members in business determining where you are headed, how best to get there, who will do what, and how that should be rewarded.</td>
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Estate vs. Succession: Different areas of focus

**Estate Plan**

What you **have** – Assets
Easy to identify (balance sheet)
Solved by an expert
Responds to compliance/gov’t regulations
Solutions implemented quickly
Involves **financial** ownership
Determined by senior generation
Activities occur at set times
Major transition often occurs at death
Opportunity for conflict limited time
In-laws generally “passive” recipients
Strategy tends to be clear

**Succession Plan**

What you **do** – Skills, Activities, Decisions
Hard to clearly describe…lots of hats
Solved by you, assisted by advisors
Involves business environment, strategy
Solutions evolve over time
Requires **psychological** ownership
Collaborative between generations
Takes place daily in the business
Major transition occurs during lifetime
Opportunity for conflict every day
In-laws often “active” voices
Strategy can be very messy
### Technical Problems & Adaptive Challenges

**Technical Problems** | **Adaptive Challenges**
--- | ---
Easy to identify | Difficult to identify (easy to deny)
Often lend themselves to quick and easy (cut-and-dried) solutions | Require changes in values, beliefs, roles, relationships, & approaches to work
Often can be solved by an authority or expert | People with the problem do the work of solving it
Require change in just one or a few places; often contained within organizational boundaries | Require change in numerous places; usually cross organizational boundaries
People are generally receptive to technical solutions | People often resist even acknowledging adaptive challenges.
Solutions can often be implemented quickly—even by edict | “Solutions” require experiments and new discoveries; they can take a long time to implement and cannot be implemented by edict

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“*The single biggest failure of leadership is to treat adaptive challenges like technical problems.*”

Succession plan is psychological ownership of…

- **Vision**
  Where are we headed? What do we want to look like in 10 years?

- **Goals**
  What do we specifically want to accomplish over the next 1, 3 or 5 years?

- **Values**
  What are our core values? (e.g. “Faith, family, farming, fun”…)

- **Structure**
  Will the entity structure and ownership plan facilitate succession – and do people understand it?

- **Roles**
  What contribution do participants want to make to the success of the business? Are they playing to their strengths or working against the grain?

- **Expectations**
  Are performance expectations clear for both family and employees? Do people know where they stand?

- **Results**
  Is our financial system providing good information and are we using it to set goals and make decisions?

- **Transitions**
  Do people know what transitions are coming and when (generally) they are happening?

- **Communication**
  Do we communicate well? On a regular basis about key decisions? Do we talk as a family about things other than business? Do we communicate well with non-family employees?

- **Governance**
  Is it clear how decisions are made? How will they be made in the future? Do people feel included?
Planning as a process, not an event

Corporate (Family and Closely Held) Decision Making Model

Assumptions
Confirmation

“I” to “WE” Knowledge

Action
Reflection
Planning
Mutual Education

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1. Committing to a “Process” versus an “Event”

2. Getting people to say what they need and/or want: How do they see the future?
   - Vision and Goals: Professional or Institutional Business? Where do they want to end up?

3. Understanding what role people will play in getting there.
   - Senior Generation: There every day? On call? Don’t call?
   - Spouses: Involved? At Meetings? Stay away?
   - Next Generation: Calling all shots? Oversee certain functions? Qualifications? Performance?
   - Governance: How will decisions get made?

4. Identifying the best strategy / structure to transition wealth
   - Advisors: Get good ones who will work collaboratively
   - Clarify your goals – and let advisors propose methods/options that fit

5. Resolving the conflicts along the way: you can’t avoid them.
   - When tough: talk it out, balance against alternatives, make decision to move forward

6. Educating and Developing as Family Members
   - Spending time on individual development – watch for people getting “stuck”
   - Personal and professional development, family away-time, philanthropy
   - Understand how business and assets are performing

7. Checking in on the plans: Occasionally revisit goals, roles, performance, expectations, plans
Transition Mistakes

- Inability to let go – financially, identity, etc.
- No Plan or No talk about the plan
- Missing Passion or Performance: “Continuation Guilt”
- Lack of perspective or understanding of common business and ownership issues
- No talk about performance expectations (asset or role)
- Transitioning “single-owner” mindset to “partner” mindset
Reasons one might avoid an exit discussion

1. You love your work – and don’t want to quit. What else will you do?
2. You are not ready to deal with your mortality.
3. You aren’t sure you can afford to step away.
4. You feel the business depends on you – no one is capable of taking over.
5. You are concerned you will lose prestige with community/peers.
6. Staying in is a good way to control the kids!
7. You have strong loyalty and commitment to long-term non-family employees and landowners and the next generation may not.
8. Your marriage might suffer.
Letting go: Exit Concerns

**Usually Identified**

**Financial Security:** Is there enough money?

**Preparation:** Is the next group ready to lead?

**Need:** Can the business survive without me?

**Family Glue:** Will they hold it together?

**Identity:** Who am I and what will I do after leaving?

**Not Usually Vocalized**
Business change is situational, and often easier.

- Adoption of a new system
- New equipment
- New land
- New farming practices

But role transition is psychological, and often harder.

- Involves not just doing, but feelings about what you do
- Touches one’s vocation (calling) and thus their identity and value.
- Happens in close proximity to one’s history and community, making it particularly difficult.
Changes succeed or fail based on whether people do things differently. The decision to change is only a part, behavior/action is what makes the difference!

1. Sell the problem, more than the solution. Everyone try to “see” the consequences. (What happens if not successful?)
2. Identify specifically what people must stop, keep and start doing. (Plan)
3. Keep focused on why the transition is important. (Outcome)
4. Identify who stands to “lose”. Focus on them.
5. Increase communication/meetings during process (especially when in the “neutral zone”).
6. Change reward models to reward adoption or change. What motivates the person transitioning?
7. Identify a champion/change manager - provide coaching or training.
8. Mark the ending (have a transition celebration!).
9. Increase the feedback loop. Recognize that not all feedback needs a solution!

The consequence of not making a change when the time is “ripe”? Slow future development; More conflict; Missed opportunities.
The Exit Process

1. Reflect: Are you ready? What are your goals, principles, concerns and blind spots? Are you and your spouse on the same page?

2. Assess the key stakeholders: Who needs to be involved at what level, and what are their sources of power, their positions and their concerns?

3. Assess your advisors: Have they completed similar plans and can they work collaboratively? Do they understand your goals?

4. Commit to a communication process and get the right people around the table. Commit to managing conflicts when they arise.

5. Discuss goals.


7. If working in the business, determine areas for gradual transitions of control.

8. Set timetables for anticipated transition milestones.

9. Check in on progress.
Splitting Up: Observations

• We are increasingly being asked to help people “get out” of business together.

• The request often comes before families have instigated a legal process or litigation – they want to unwind “collaboratively.”

• The request often comes after families have tried to work together, make decisions, or co-exist in the business.

• Sometimes is isn’t a request; it’s a recognition of the long-term problems that have existed or will continue if not dealt with. In short, it’s a reality.

• The “unwinding” often leaves one or more family members in place to operate the business, or may divide the business into smaller operating segments. Seldom does it mean “sell it all.”

• If done well, the change to the ownership and management structure can leave the family structure intact and in a position or future improvement
How did the families get into business together?

- Generational repetition
- The estate tax tail
- Head-in-sand
- The equality paradox
- The parents’ hope
- Continuation guilt

**Being in business together often wasn’t a deliberate choice:**

*Do we want to / Should we be in business together? Why?*
What caused the families to want to end their partnerships?

- Different vision and goals
- Different management styles and expectations/practices
- Poor financial performance (or lack of agreement on financial expectations)
- Growing disconnect between business enterprises (livestock/crops)
- Discomfort/lack of trust of current or next generation
- The “last person standing” is in sight! (No one returning.)
What can we learn from their reasons for splitting up?
What makes us stronger?

Take the time to talk about what you want to accomplish in the future.

- Do you want a bigger farm than you have today? How big? At what rate? Clarify your approach to opportunities.
- How leading edge do you want to be? Talk about the cost of the approach.
- How professional? Talk about the level of structure, processes, bureaucracy you want.
- What are your profitability/financial/leverage expectations? Define “pressure” from a financial standpoint.

Go around the table:
- What’s most important to you?
- What should the farm look like 3 years from now?

CAN YOU FIND CONSENSUS AROUND THESE QUESTIONS?
Clarify your expectations for business management

- What do you expect of a manager? What do others expect of you as a manager?
- How will land be cared for?
- How will employees be treated?
- How will equipment be managed?
- How will landowners be dealt with?
- What culture do we want?
Discuss financial performance and commit to / agree on changes.

1. Develop a process for discussing financial performance and upcoming decisions.
   a) Find a time to talk finances.
   b) Use budgets and marketing plans – even if basic.
   c) Clarify goals around working capital, leverage, etc.

2. Clarify individual financial authority vs. group decisions (dollar amounts and key decisions like employee compensation)

3. Agree on how to fund major tax strategies. Especially when you have off-farm partners. (Consider using the same advisor for coordination and reduction in misunderstandings.)

4. Include family members in meetings with accountants, lenders, etc.

5. Make family/partner compensation and benefits transparent – no side deals, or if so, approved!
Splitting Up: In Summary…

• Many years precede most decisions to end a partnership.
• Each of those years offers a window of opportunity to change or improve.
• Just like “little things” pile up and eventually cause a break, “little improvements” can also lead to a stronger business foundation.
• The key is to communicate.
• Ending a business partnership is sometimes necessary.
• If it is necessary, and you “end well” – you’ve still been successful!
Governance: The Role of Boards

Boards (advisory or formal) bring

- Higher standards for treating the business like a business:
  - Financial statements, preparation, planning, reporting
  - Focus on management or ownership (take heat off “family”)
  - A bridge between family and non-family

- Experience with other organizations/situations:
  - A “reality check” through questions, assessment
  - Credibility in guidance
  - Connections to others; a strong network

- Coaching potential for family and management team members:
  - Support for key decisions
  - Assistance during personal challenges

- Accountability: The pressure to “get it done”
Characteristics of Effective Family Business Board Members

- Honesty
- The willingness to challenge others
- The ability to challenge in an appropriate way
- Open-mindedness
- Interest in the company, enthusiasm for its mission
- Expertise in an area and the ability to make a contribution
- The ability to see various sides of an issue
- The willingness and ability to work with other board members
- The ability to deal with intellectually complex issues
- Able to ethically balance self-interest, organizational needs, laws
- Ability to assess their own performance, strengths, weaknesses
Qualifying your Advisors

CPA, Attorney, Lender, Insurance Agent, Wealth Manager

- Are they **competent**? Do they do good work for similar organizations?
- Do they **know agriculture** specifically?
- Do they **initiate** communication and bring ideas to you?
- Do they **collaborate** well with your other advisors?
- Do they have **other resources** in their firm or office? (Succession)
- Do they **admit** when they don’t know the answer? Are they willing to research or find others who do know the answer?
- Are they clearly / transparently **compensated**? How?
“Healthy” communication – input, feedback, discussion.

- Philosophy: Communication is important.
- Practice: Family meetings, agreement to address conflict.

Articulated expectations of one another

- Philosophy: People need to know where they stand with each other.
- Practice: Articulate strengths, write job descriptions and hold performance reviews.

Agreement on direction and goals and strategy

- Philosophy: We need to be on the same page about the future.
- Practice: Discussions at various intervals about the future: vision, goals, roles, plans, transitions in/out.

Accepted and respected decision-making processes.

- Philosophy: Turn “I Knowledge” into “We Knowledge” while also defining decision boundaries.
- Practice: Regularly scheduled board and management meetings. Consider an advisory board.

Professional development and emotional intelligence

- Philosophy: People need to keep learning and developing.
- Practice: Education, seminars, books, coaching, feedback.

Understanding of business performance.

- Philosophy: Owners need to understand business basics: accounting, marketing, HR, legal, insurance, etc.
- Practice: Use accountant, attorney, broker, insurance agent and others to educate.

Pick an area: What is your “First Next Step?”
Concluding Thoughts

• Timing has a lot to do with the outcome of a rain dance. (Is it the right time for a transition?)

• In the absence of a good story, people make one up. (Communication is the “oil” in the transition engine.)

• If you think a good advisor is expensive, try a bad advisor. (Use your advisors as a team.)

• There is no “one-size-fits-all” transition plan. Each plan reflects the history, culture, guiding principles, personalities, assets, perspectives and values involved.

• A succession plan needs both “technical” pieces (legal/financial) and “adaptive” (business leadership/family role change) approaches.

• If there is going to be a fight when something is “revealed”, let’s get to it so we have a chance to heal.

• You can’t “lop off” a family member!

• Aim for “Certainty” over “Agreement” and “Progress” over “Perfection”

• Recognize the value of being a family business…but consider acting as if you are NOT ONE (make explicit agreements).

• Planning is a process not an event. Things change and your plan will, too.

• Use the systems as a framework for activity: Ownership, Management, Family. Talk about your goals and expectations and strategies in each area to provide clarity.

• Consider how you will stay accountable to progress. Family? Advisors? Peers?