Family business – to sell or not to sell?

In this article, the first of the new Families in Business debate section, Dennis Jaffe argues the benefits owners can expect from selling while Tom Davidow fights for the non-sale corner and keeping the business together for the next generation

YES - SERIOUSLY CONSIDER SELLING

For many families, a family business is like the preferred child. It gets lavish time and attention while the other siblings are relegated to the background and the parents may seem to be living their lives through it. The trophy business brings them renown, status and importance in the community. With such a deep emotional connection to the business, it is unthinkable for many families to consider selling it, and none of the other "siblings" would dare bring up this option. For this reason, selling the family business is hard to consider for many families.

"The sale of the family business is not the end of the family as an economic or shared enterprise unit"

But there comes a time in every business family's life cycle, where a sale will have to be seriously considered. To resist taking this seriously endangers the very enterprise the family has spent years growing and nurturing. Consider a recent example of a family with a strong car dealership that had lasted nearly a century. The family was dedicated to keeping it in the family, and had begun to develop a next generation to run it. Then they received an offer from a large company that was acquiring many dealerships, representing a price more than the family thought the business was worth. The message from the buyer was simple - sell to us, or we will buy your close competitor and, with our deep pockets, we will run you out of business. The family hung on proudly and declined the offer. Within 10 years, the franchise was fighting for its life. Is this a family tragedy where emotion should have been challenged by business reality?

There are external and internal pressures for a sale. Externally, the global marketplace is changing, with offshore competition and roll-ups of smaller businesses, and a family business that has been successful in a small market niche for many years is not guaranteed success in the future. When an offer emerges, the business has to look seriously at its future prospects, not its successful past. Also, the business may need an infusion of capital at the very time when older family members want to be assured of retirement income, and younger family owners want returns on their investment. How can they balance these competing needs?

Internally, as the older generation leadership ages, they have to look at the capability and desire of the next generation to lead the business where it needs to go. If neither will nor skill are there, they should consider passing the business outside the family. If there is a family leadership candidate, they should be sure that this person can deal with the future challenges. Another internal challenge is in the area of ownership, where some family owners want to have access to the capital that is locked up in the business, and the other owners have to figure out how to buy them out.

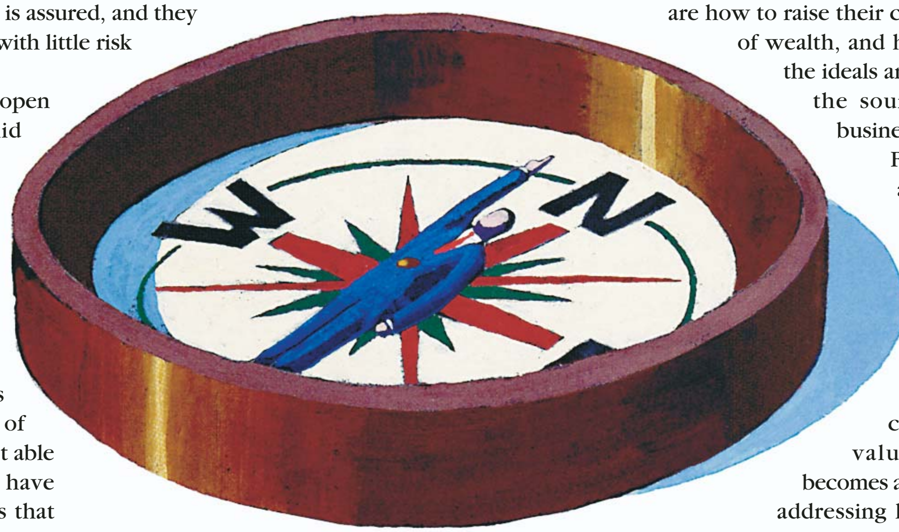
In one family, there were capable leaders in a family branch that wanted to take over. Another branch wanted to exit the business. The marketplace was such that there were several buyers who had expressed interest in the business. Rather than hide or jump to a decision, the family considered its options carefully. They quietly listened to offers, with the understanding that the family successors could also make a bid, and that their bid would be somewhat privileged. But in the end, it was decided that the best option was to sell. Each of the family branches had good business ideas, and each branch soon became involved in new ventures that were successful. In some ways, they build on the family legacy of entrepreneurialism: in other ways, they were freed from the past and able to move forward in new directions.

The growing number of family members who want returns on their ownership adds more pressure to the business. So when a family tries to hold on to the family's legacy business, it will have to deal with these issues. If the family leaders are holding on to the business for emotional reasons, they are likely to run into trouble. Now, consider the benefits if a family decides to sell the business when there is an offer on the table. First, the family cashes in its success. Second, it does not have to deal with the awkward issue of making sure that family leaders can develop the business to the next stage of growth. Finally, the business does not drain capital from the family.

The freedom from the business allows the family to come together as a new generation and reinvent itself in a new form. Many of the conflicts in a business family over income and management of the business arc ended, and the family has a new playing field where the next generation can make its mark. And most importantly the legacy and retirement income of the founding family is assured, and they can live comfortably, with little risk for their own futures.

A family that is not open to considering a valid offer for its business runs the risk that a healthy and productive business can suddenly hit a crisis and lose a great deal of its value. Or a family can place its future into the hands of a new generation of leadership who are not able to compete, or they have handed off a business that does not have the capital to develop and innovate, which are equally scary choices.

The sale of the family business is not the end of the family as an economic or shared enterprise unit. Rather, a sale is a moment of rethinking and balancing of the past with the future. At the same time, with a liquidity event, the family has the option of allowing “free choice” of family members, so that the next generation does not have to be a captive partner. Some can go their own way, while others can take what they have inherited from the family, and build for the future.



Selling the business allows the family to move in a new direction

NO - KEEP IT IN THE FAMILY

Like “Pascal’s Wager”, which states that the benefits of believing in God outweigh the consequences of being wrong, holding onto the family business instead of selling it demonstrates a conviction that the benefits of continuing the business into the next generation are greater than the financial risks of doing so. In the end, choosing to hold on to the family business is based on one's values and one’s desire to preserve the family itself.

Even in the best of circumstances, when selling the family usiness creates a liquidity event that would provide financial security for the family and lets its members to maintain their life style, the family will risk other losses associated with dissolving hard assets into more liquid ones. In addition to the obvious loss of the psychological benefits associated with being a family business owner, the next generation will face an even more significant one: the crucial opportunity to experience its family’s values as expressed in the family business.

An enormous amount of liquidity has flowed into the marketplace in ihe last decade, accompanied by large numbers of private banking and family offices lining up to serve the post-liquidity family. The primary concern of those families are how to raise their children in an arena of wealth, and how to teach them the ideals and values that were the source of the family business’s success.

Family businesses are the most reasonable and natural configuration of how to survive and thrive in the world. When a family is strongly committed to its values, its business becomes a training ground for addressing life's never ending problems, both inside and outside the business. Essential ingredients for successfully overcoming those problems, be they physical or emotional, are the love and support found within the family system. Corporations and professional firms, for example, have recently instituted flexible time and job sharing to hold onto valued employees who are trying to balance family and careers, a concept that has been forever present in the family business.

“By the time a family business has survived for generations, it has developed a powerful sense of family”

By the time a family business has survived for generations, it has developed a powerful sense of family. Things may not always have been pleasant or easy, but the very fact that the business has survived indicates that the family is an admirably strong one. Moreover, family businesses do not survive for generations by making the same mistakes over and over again. Rather, they develop models that are then refined from one generation to the next. Those models succeed because they rely on a set of values which have been internalised, generation after generation, through the experience of owning a family business.

Home is where the heart is: the family business keeps family members united

A client of mine recently made it clear why 85% of businesses in the US and one third of the Fortune 500 are either family-owned or controlled. We were discussing how to set up a foundation and develop structures that could include members of the next generation. There are seven siblings in his generation, the second, including five of my client's brothers and one brother-in-law. They have been working together before and since the original founder passed away. The number of years they have spent working in the business ranges from 35 to 25.

"Where better can a family pass on their values to their children, while experiencing the fullness and richness of life, than in the family business?"

No members from the next generation work in the business nor do any of them appear to be interested candidates. I suggested that when the business eventually gets sold, the foundation would be a terrific place for the continuation of the family legacy. He politely explained that the experience of coming to work everyday, and struggling along side his brothers to make the business survive and prosper could not be duplicated through the quarterly (at best) meetings of a family foundation.

He then went on to talk about how happy he has been working with his brothers. He even told one brother, who has been only an owner, that while he loved him equally, he did not have the same feelings towards him that he did towards his other siblings. (He included the brother-in-law in the same category of closeness as his siblings). Every other brother in the room thanked him for describing his feelings. And each of them absolutely agreed with him.

Another client of mine, who is 84 years old, is watching his business transfer from his children to his grandchildren. The transition involves all the risks and challenges, financial and emotional, that one might expect in any generational transfer. His attitude about selling is simple; all that money could destroy his family. What would they do with it, anyway?

While continuing the family business into the next generation is a risky proposition - the odds of success can be daunting - the odds of succeeding are improving every day. The key lies in realising that both the family system and the business system can be governed by the same criteria: performance. When families learn to accept performance with quantifiable goals as their ultimate criteria for success, they teach their children an important value: accountability.

All parents want to teach their children good values, including a sense of responsibility, solid ethics, and sound judgment. The opportunity to provide a healthy and safe environment for children to learn the most important lessons in life is a precious gift for both parents and children. It ought not to be squandered. Where better can a family pass on their values to their children, while experiencing the fullness and richness of life, than in the family business? When it comes to deciding whether or not to hold on to it. the wisest choice, given the long-range potential benefits, is to keep it in the family.

Dennis Jaffe is a founding partner of Relative Solutions.
Tom Davidow is founder and principal of Thomas D Davidow & Associates, based in Brookline, MA.