

LEGACY MATTERS

Family Stewardship: Walking the Fine Line Between Legacy & Change

THE 2004 OUTSTANDING LEGACY SERIES

Enable your family to be successful into the next generation: Use the 3 circle model to identify the web of relationships and understand the structures, policies and mechanisms that can secure a long term outlook.

The Business Families Centre extends our sincere thanks to BMO Harris Private Banking for their support and their vision in providing the opportunity to learn from Dr. Fredda Herz Brown at the second annual Business Families Centre "Outstanding Lecture". Her research in examining successful first to second generation transitions and more than twenty years of working with families who share substantial assets provided the foundation for the Oct. 27th lecture. Participants found themselves immersed in a rich discussion about how long term success of your family enterprise stems from the ability of the family to put in place structures, mechanisms and leadership which support both the family's legacy and its ability to look to the future and change. Dr. Herz Brown stressed that the foundational strength of commonly held beliefs provide a framework for how children are raised, business decisions are made and leaders are developed in the family enterprise.

The intensive, full day workshop the following day moved the topic from discussion to execution. Dr. Herz Brown focused on the transmission of values and mission by development of capable next generation stewards. She examined the complexity of leadership and development; provided a view of a new model for leadership; and gave participants at the workshop the opportunity to apply the model to the development of their family's next generation leaders.

Three Circle Model

Dr Herz Brown used the Three Circle Model, which includes the family, business and ownership, to describe the complexities that a business family faces. Becoming clear on how you're going to manage each of these circles is critical to the success of the family and the business.

Through the use of case studies and video clips, Dr. Herz Brown offered examples of mechanisms and structures that can be established to meet the needs and to give a voice to the various constituency groups and their concerns. For example, a Family Council or Family Charter can be implemented to address the family concerns. Shareholder meetings and a Board of Advisors or Directors can be developed to ensure the ownership processes are addressed. Business structures can include mechanisms such as a Management Development plan and a compensation plan for key non-family executives and family member employees. Where there are overlapping memberships in the three circles, regular and formalized information sharing processes should be put in place.

For long-term success of the family enterprise, the family structure will take on the greatest degree of importance as through it will come the transfer of values, mission and vision to the business and owner circles. In order for family members to effectively steward the values and vision, it is important to be knowledgeable and educated and prepared for their roles.

This issue of Legacy Matters is proudly sponsored by:



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Family Stewardship, cont'd.

Leadership Challenges

The unique characteristics of families who share work and assets result in leadership challenges for the steward of the family enterprise. Because it is a family enterprise, there is an additional layer of complexity. Dr. Herz Brown offered several reasons for why it is so difficult to separate business and family:

- ♦ The fact that the family is in business together defines their relationships. Money and work has the potential for organizing (or disorganizing) family relationships.
- ♦ Transitions are more complex. Governance issues, cousins working together, and retirement are examples that may present more challenges and issues as a result of owning and sharing assets as a family.
- ♦ Closeness increases intensity; and the potential for triangulations and polarization between family members, leading to more stress. Families often resort to old patterns when emotions are involved and when conflict arises.

Developing Stewards

Leading a family enterprise means that you are entrusted with your family's wealth. The question is, "How can you develop stewards?" Dr. Herz Brown stressed that leadership development has to be an intentional process. Leaders need to have a strong sense of emotional intelligence regarding self and others. The requirements of next generation of leaders are quite different than those of the generation before them.

Values, Mission & Vision

The next generation leader must have a vision and focus that is forward directed, based on history and is inspiring. Having a 100-year view means that the steward has to know what they value and

where they want to get to. To become a steward of the family wealth, they need have the values and mission articulated, or they will not have a clear sense of direction in which to go. Being clear about the mission and goals will help you determine the kind of leader you want and need.

Best practices for the Long Term Survival of the Family Firm

Through the use of a case study, the participants of the workshop had a chance to explore what it takes for a leader and steward to meet the challenges and issues for long-term success. Some of the processes and structures that are considered to be "best practices" are to:

- ♦ Establish Family meetings and develop a family charter
- ♦ Include the 3rd generation in the meetings, depending on age and interests
- ♦ Create guidelines for attendance, communication and behavior at the meetings
- ♦ Create guidelines for educational expectations; and entry and exit for employment in the business
- ♦ Have shareholder agreements
- ♦ Create career and leadership development plans for family members in the business
- ♦ Establish a board of directors or advisory committee that includes non-family members
- ♦ Articulate in writing and promote the family values that you want to instill in the next generations
- ♦ Ask the question "what is the money for?". Kids, founder and business owners may have different expectations of what will be done with the money i.e. dividends, put back into the company, etc.

- ♦ Encourage the 3rd generation to apply their interests and to think more broadly than what the firm is currently doing. Encourage them to use their interests to pursue research and development in other products, services or business opportunities.
- ♦ Think about creating an ethical will - a will that identifies what values and wishes for the future. What's important for the next generation to know about me?
- ♦ Plan social gatherings for the family. This helps develop trust and positive relationships
- ♦ Create opportunities for younger generation to "shadow" the older generation
- ♦ Identify a family philanthropic cause that everyone can be involved with - all ages
- ♦ Create a junior board - allow the younger generation to learn
- ♦ Assign a mentor from the older generation or from another family business
- ♦ Create systems for providing feedback and performance evaluation to family members working in the business
- ♦ Provide opportunities for the next generation to lead, to meet challenges, to make mistakes, to handle crisis, to make decisions

Constituents in each of the three circles must understand what their responsibilities are and what kind of information they are expected to share and to learn about. Using the 3 circle model to identify the web of relationships - where family, business and ownership overlaps, and then understanding the structures, policies and mechanisms that can be used to secure that long term outlook will enable your family to be successful into the next generation.

by Edie Doecker

Director - Business Families Centre

UPCOMING EVENTS & PROGRAMS

Registration

online:
<https://www.secure.commerce.ubc.ca/bfc/regform.cfm>

by telephone 604.822.0102

Visit our website at www.sauder.ubc.ca/bfc for more information about these educational programs for business families and their advisors.

February 17, 2005 (Full day)

Bringing the Family Together: Strategies for Family Meetings, Councils and Communication

Presenter: Dr. Dennis Jaffe

March 3, 2005 (Full day)

Addressing Conflict in the Family Enterprise

Presenter: Dr. Tom Knight

March 18, 2005 (Full day)

Women in Business Leadership

Presenter: Dr. Nancy Langton

April 8-10, 2005 (2.5 days)

The Road Map, Part One: Navigating the Business Family Relationship

Facilitators: David C. Bentall and Dr. Nancy Langton

May, 2005

2005 Family Legacy Series Dinner

The fourth annual gala dinner

Breakfast Briefing Series

February 16, 2005

8:00-to 9:30am

Governance & Strategic Planning for the Family Business

Presented by: Dr. Dennis Jaffe

Advisors Series

January 20, 2005

4:00 to 6:00pm

Addressing Conflict in the Family Firm

Presented by: Dr. Thomas Knight

February 16, 2005

4:00-to 6:00pm

Governing the Family Business:

Boards, Family Councils, Leadership and Family Agreements

Presented by: Dr. Dennis Jaffe

A Word from the Chair

DAVID BENTALL REPORTS ON DR. HERZ BROWN'S VISIT

This fall, Dr. Fredda Herz Brown was invited to Vancouver by the Business Families Center. She came to deliver our annual OUTSTANDING LECTURE. But in addition, we invited her to lead several workshops, and attend a dinner with our founding families. Over the course of several days, she stimulated us to think about many topics from refreshingly new angles. Below are some of the new insights and perspectives I found through my interactions with Dr. Brown, one of the true Pioneers in the field of Business Families:

1) ON LEADERSHIP

Many successors in business families have leadership potential. Unfortunately, too often they don't develop their potential, because the elder generation is too busy leading to make room for other "would-be" leaders. Too often we think of leadership simply in terms of executive assignments, and these are hard to create, just so successors can learn. However, by being more creative, we can create opportunities for leadership development in a host of areas. "Lots of people have leadership qualities, but without context", noted Dr Fredda Herz Brown. We can change this by artfully searching for and creating new opportunities for successors.

2) ON FAMILY HARMONY

Tragically, family members too often spend much of their time wrangling for position or power. To avoid this, some leaders try to get everyone to think alike, hoping this will prevent strife. Unfortunately, this tactic usually leads to increased tension, as family members are encouraged to sublimate their true feelings. Rather than try to "homogenize", as my dad used to try to get our family to do, Fredda pointed out that "...The way to get consensus is to allow time for individual thought." What a profound, counter-intuitive insight!

3) ON STEWARDSHIP

Succession training typically focuses on the roles of management. What about training shareholders to be knowledgeable and wise? In a healthy business family there is a good balance between shareholder interests (such as return on capital and dividend flow) and management interests (including reinvestment for growth, and opportunities for leadership). As Herz Brown cautioned, business families should recognize that "...a leader who thinks he/she can do anything he/she wants with the company and the shareholder's wealth is a dangerous person!" It is important to create balance.

4) DEVELOPING HEIRS

The over-use of credit card debt vividly illustrates that many people today are not willing to wait for what prior generations had to save for. Similarly, in business families, successors are often able to live far above the standard of living they have earned. As a result, the necessary effort that used to be linked to achievement is often disconnected, by a generation of overly generous parents. No one can argue against parents working hard so that their children can have it better than they did. However, as Dr. Brown observed, "opportunity becomes a problem... when so much is given to successors, that they don't challenge themselves. The need for the butterfly to struggle to emerge from its cocoon should remind us to not "destroy" our children with kindnesses!"

Rarely does one have the opportunity to sit and learn from a true pioneer. I had one of those rare privileges recently, and am so thankful that our Platinum Presenting Sponsor BMO Harris Private Banking, in addition to supporting sponsors Business in Vancouver, Hemlock Printers, and Zlotnik, Lamb & Company participated with us to bring Dr. Herz Brown to Vancouver. It was an inspiring few days!

Independence and Succession

BY MARK A. ZLOTNIK, CA, CLU, TEP

Planning for the financial independence of the first generation should be an integral part of the succession of ownership, control and management to subsequent generations. If the current owners have all their assets tied up in the business, how can they feel comfortable about transferring ownership and/or decision-making power to their children? If this premise is true, then it is helpful to have a plan in place that segregates investment assets from business assets allowing the owner/manager to develop financial independence from the business. This might involve some of these steps:

- ♦ Segregating real estate assets into a separate holding company
- ♦ Building up financial assets in a separate holding company or personally
- ♦ Building up financial assets equally between spouses for income splitting later on
- ♦ Making maximum use of tax sheltered accumulation vehicles (e.g. RRSPs and IPPs)

IPPs can be a very useful vehicle for owner/managers to build up tax sheltered retirement assets. Like an RRSP, deposits to an IPP are tax deductible and all income earned inside the IPP is sheltered from current tax. The amount of annual contribution is based on actuarial calculations that allow significantly higher annual contributions than an RRSP.

The attractiveness of an IPP gets better with age as the annual contributions increase each year. Also, an IPP can allow for some lump sum past service contributions, based on age, earnings and service since 1991. For example, a 60-year-old male, owner/manager would be able to deposit

up to \$157,000 including past service compared to the current RRSP limit of \$16,500 for 2005.

There are some negatives. An IPP has more restrictive provisions than an RRSP in terms of access to the retirement funds while working and use of the funds for retirement income at retirement.

The IPP is just one method of enhancing retirement income and creating financial independence from the business. Start planning now and be disciplined. This will allow for greater retirement income as well as protecting assets from business risk.

IPP Examples for 2004

AGE	50	60
Net Past Service Contribution	\$78,246	\$132,027
Add: Current Service Contribution	20,780	25,069
IPP Contribution *	\$99,026	\$157,096

* Assumes maximum pensionable earnings (>\$100,000) since 1991, and maximum RRSP contributions throughout full period.

Mind Your Business Family: Adopt an Action Plan

AN ELEVEN-STEP ACTION PLAN BY JOSEPHINE MARGOLIS NADEL,
CHAIRPERSON FOR THE PROFESSIONAL ADVISORY COMMITTEE

Research in the field of family business clearly demonstrates that all business families want: *business prosperity, family harmony and personal well being.*

The growing literature focuses on the challenges and issues facing family business, however much of the commentary overlooks the benefits and resources. Family firms are widely regarded by some scholars as fertile ground for nepotism, self-dealing and vulnerability to failure beyond the founding generation. Other researchers consider family firms to be at the cutting edge of profitability, job creation, wealth creation, return on investment, flexibility and speed to market.*

Clearly, the unique problems facing the family firm provide sufficient reason to explore the factors contributing to their continued survival, health and growth potential. The goal of this article is to provide a preliminary Eleven Step Action Plan to ensure success.

STEP ONE: Conduct a Succession Readiness Check-up. Key stakeholders should complete the following checklist:

1. Do you know when you want to retire?
2. Are you financially secure and what does this require?
3. Could your business continue without you if you died today?
4. Do you know how much your company is worth?
5. Have you identified a possible successor for your position?
6. Have you determined to whom you wish to leave your legacy?
7. Is your chosen successor willing, groomed, prepared?
8. Have you developed an equalization strategy for children active in the business and those who are not?
9. Do you have a Shareholders Agreement?
10. Is the Buy-Sell provision of the Shareholders Agreement funded?

11. Have you developed a Contingency Plan in the event of the loss of a key person?

STEP TWO: Prioritize Critical Issues. Perform an exercise to identify the priority that your family business should give to the key issues. Rank each issue in response to the question: How important is discussing and resolving this issue to the survival of our business?

1. *critical;*
2. *family must address the issue to get on with its future;*
3. *not critical, but still important; and relevant.*

STEP THREE: Identify the issues, objectives and goals of each of the key stakeholders. Each stakeholder should consider his or her short/long-term objectives, professional/personal goals and management/ownership interests.

STEP FOUR: Design a Customized Process for the members of the business family to communicate, discuss and collaborate on their issues and objectives, and to implement steps five to eleven. Appoint a professional advisor or outsider to facilitate the process.

STEP FIVE: Develop a Vision Statement and a Mission Statement.

STEP SIX: Develop an Ownership Succession Plan. A plan that provides for a smooth transfer of ownership and management responsibilities. The options may include: sale to third party, family succession, management buy-out, other.

STEP SEVEN: Develop a Management Succession Plan. A plan that provides for smooth transfer of management responsibilities and may include a Management Development Plan.

STEP EIGHT: Develop a Contingency Plan. Such a plan stabilizes the business in the event of sudden death or disability of owner or key employees. It details what will happen in terms of business operations.

STEP NINE: Develop the Business' Strategic Plan. Key stakeholders meet, discuss and determine the future of the business, whether to maintain the current level of business activity or to expand the business. Discussion may include values, vision, and mission and should be aligned with the Ownership and Management Succession Plans.

STEP TEN: Develop a Successor grooming and development plan with timeline. Once the successor has been selected, a plan to train, groom and cultivate the successor.

STEP ELEVEN: Develop and Implement Appropriate Governance Structures for the Family, the Business and the Owners. Consider establishing Family Charter, Family Council, Family Participation Plan, Advisory Board/Committee, Outside Advisors on Board, Code of Conduct, Compensation Committee, Philanthropy Committee, Wealth Education & Responsibility Plan and other policies, as appropriate.

In addressing the challenges facing a family enterprise particularly in the area of succession, the approach, the process and the options must be customized. Although there are shared attributes and characteristics each family and each business is unique. You may feel somewhat overwhelmed or discouraged about the prospect of undertaking succession planning, however the lack of action may have an adverse effect on your family as well as your business. TO PLAN OR NOT TO PLAN is not even a question. Although you may be accustomed to responding rapidly, efficiently and successfully to problems you encounter, business family dynamics, present and future, can neither be rectified nor shaped with a mere quick fix. You need patience, a process and commitment of all stakeholders to embark on the journey which is necessary to bring prosperity and endurance to the business, harmony to the family and personal fulfillment to the owners. A legacy worth building is a legacy worth preserving for future generations.

* "Does the Family Business Interaction Factor Represent a Resource or a Cost?"

Ernesto J. Poza, Susan Hanlon, Reiko Kishida, *Family Business Review* June 2004, Volume XVII, Number 2.

Business Families Centre

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The Business Families Centre is a joint venture between the Sauder School of Business at UBC and the family business community. The BFC is committed to assisting business families, their advisors, and their enterprises through research, programs and academic education.

To find out more about:

- how your business family can become involved in the Business Families Centre at the Sauder School of Business at UBC
- how to make your tax deductible contribution to the Business Families Centre
- opportunities for sponsorship of BFC events and courses

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