DECODING FAMILY BUSINESSES

Josh Baron & Rob Lachenauer

Who cut down Mom's rosebushes?

Rosebushes! This fight nearly derailed a successful second-generation family business.

We had scheduled a meeting with the company's owners to discuss whether to retain their underperforming nonfamily CEO. Instead they spent almost the entire time arguing over whether one of the brothers had the right to "prune" or "kill" (depending on whose version you believed) their mother's prized rosebushes at the family cottage. Despite our efforts to change the subject, they couldn't move past the rosebush incident. The meeting ended in a deadlock, the group unable to make any decisions together.

It's hard to imagine a public company's board coming to a standstill over landscaping. Outsiders often scratch their head at how family businesses seem to defy conventional business rules. That's because family businesses are different. If you're part of such a business or working for one, the business's uniqueness will be no surprise to you. But that doesn't mean you always understand how and why the business operates the way it does. You just know that conventional business wisdom doesn't always apply. But what are the rules?

We have good news. Family businesses can be understood if you stop scrutinizing them like conventional businesses. Unlike conventional enterprises, family businesses have three defining characteristics:

- Some individuals, especially owners, have a huge impact.
- Family businesses are held together by relationships, which are multidimensional and interlocking.
- Everyone's behavior is shaped by system dynamics, some of which you may not even realize.

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THE IMPACT OF INDIVIDUALS

For all the talk of "imperial CEOs" of public companies, these executives can't touch the influence of a family business leader backed by ownership power. The owners, a relatively small number of people (most family businesses are owned by far fewer than a hundred people), have ultimate authority over every decision in the business. They can fire the CEO, add or remove board members, change the strategy, sell the company, decide who can be an owner, and even redesign the corporate logo, to name just a few things in their control. Family ownership keeps power in the hands of a few individuals. Who these individuals are and what they want will have a profound impact on their family business. And that impact will vary, of course, from business to business and family to family.

The average CEO tenure in a family firm is at least thirteen years, compared with five years in publicly traded firms. With both more time in the seat and more decision power as an owner, these family CEOs put their personal stamp on their companies.

But owners are far from the only people who, as individuals, make and shape important decisions in family businesses. Though they may not show up on the company's organizational chart or the ownership documents, spouses, children, cousins, in-laws, nonfamily executives, and board members can all influence a family business's direction. In a public company, it matters little who the CEO's spouse, parents, siblings, or friends are, but in a family business, these people matter greatly.

People's personal character plays a key role in directing the fate of a family business. The seemingly irrational decisions of family businesses often reflect rational choices of thoughtful people who value things beyond higher profits. And since they own the company or influence those who do they can "want what they want"—be it growing through a personality-fitting strategy such as those that Frederick and Ian applied, or focusing on distributing money out of the firm, or directing the firm to combat climate change and poverty. As individuals with unique goals and desires, they get to chart their own course.

MAKE-OR-BREAK RELATIONSHIPS

You can also decode your family business by examining the **relationships** inside it. Unlike in a nonfamily business, where clear boundaries usually separate professional and personal relationships, a family business involves multidimensional relationships that influence each other in profound, often unexpected, ways. In fact, three distinct types of relationships are simultaneously at play.

In **family relationships,** the members usually try to treat one another equally. Families are at their best when they are inclusive, forgiving, protective, and supportively challenging. They "trade" in emotions—love and some more negative emotions at times. Families are emotionally connected. And family relationships are the longest relationships of most people's lives.

Business relationships, on the other hand, are hierarchical; there's a boss and a reporting structure. They are usually meritocratic. If you don't make the cut, you are fired or you leave. The average tenure of US employees is now less than five years. Businesses "trade" in competencies. You hire a vice president of manufacturing for the executive's knowledge and experience in the business issues you face. And the person is in the role only as long as the mutual investment makes sense for both parties.

Ownership comes down to who has the voting control of the firm and who can influence through their voice, even without a vote. Owners "trade" in power and are part of an exclusive club: you are either an owner or not. In family businesses, unlike, say, at Apple, ownership is sticky. Most shares have limits on whom you can sell your shares to, and how. Exit and entry are not simple, quick options.

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In your family business, each big decision you make—to curtail a dividend payment to your mom to protect your balance sheet, to buy out your cousin, to skip your family reunion, or to fire your brother—can reverberate for years, or even generations.

SYSTEM DYNAMICS

A family business is a *system*, meaning that the people who are part of it exist within an interconnected environment that affects everything that happens. Yes, individuals and relationships drive much of the dynamic in a family business, but each business faces legal, cultural, geographical, and other circumstances that also affect its dynamics in fundamental ways. Four main system dynamics are at play: sameness, mutuality, competing interests, and unintended consequences.

SAMENESS | Though your family business is unique, it will behave in predictable ways that are similar to some businesses and different from others, no matter your industry or the size of your business. For example, the stage of development of your family business will shape how it operates. In the seminal family business book *Generation to Generation*, Marion McCollom Hampton and coauthors describe three main configurations of these stages: controlling owners, sibling partners, and cousin consortiums. The distinct patterns of behavior for each configuration are similar the world over. The laws and taxes of your country and the culture your business operates in will create important similarities with other family businesses in your area.

All of these factors can mean that businesses in a wide variety of industries and sizes have much in common with one another in particular contexts. Your situation probably has more in common with some other family businesses than you think. You can learn from their experiences.

MUTUALITY | Long-term success requires collaboration. The interconnected nature of a family business means that people can achieve some outcomes, arguably the most important ones, only by working together. Even the most powerful people in a family business must learn to compromise if they want to accomplish goals that depend on the actions of others.

In the long run, family businesses succeed by mutuality—making decisions that are of mutual benefit to family members.

For example, spouses can play a significant role in how the next generation sees the family legacy and business. If they are not treated well, they can find ways to keep their children less involved with the family. Unhappy in-laws can discourage their children from attending family gatherings or accepting internships in the family business. They could also advise their children against seeking a career in the business.

COMPETING INTERESTS | System dynamics create competition inside a family business. *Fundamental attribution error* is what social psychologists call the human tendency to attribute people's actions to their personalities rather than any other causes, such as their situation. You might be quick to dismiss the objections of a family member who is the odd one out and you think this person is always just trying to be a contrarian. But in reality, they might be looking at a business decision through a different lens and are just expressing an objection in a clumsy manner. The family member might have a worthwhile point that you will never consider, because you assume they're just being stubborn. Perhaps a better way to understand behavior comes from the expression "Where you stand depends on where you sit."

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People's wants depend significantly on their position in the family business. Since those positions will differ—consider, for example, the controlling owner versus someone uninvolved in the business but dependent on its dividends for financial security—different individuals will have competing interests.

Competing interests typically emerge over time. Well-intended people can want plenty of things—dividends, company growth or its sale, status, love, recognition, and jobs for themselves and the next generation, to name a few. Competing demands are put on the business, the owners, and the family.

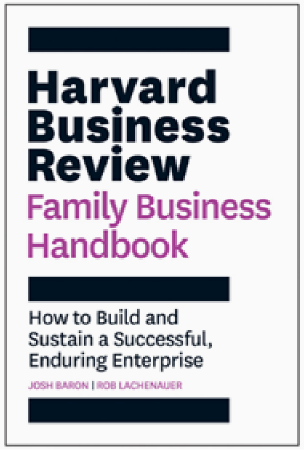
UNINTENDED CONSEQUENCES | You can never do just one thing. Does this saying sound familiar? You try to fix one problem but, in the process, create a bigger problem elsewhere. We worked with one family business run by three brothers who wanted to avoid a situation where any two of them could gang up on the other. So, they set a rule that any major decision required unanimity. This approach worked out fine when it was just the three of them in the business and their interests were more or less aligned. But it broke down when the next generation entered the company and each brother became more narrowly focused on what was best for his children. Since any of the three brothers could block a decision, they often ended up in a deadlock.

In a complex system, actions have ripple effects. A well-known example is the butterfly effect, where a hypothetical butterfly flaps its wings and sets off a series of events that cause a typhoon on the other side of the world. This hypothetical property of chaotic or complex systems suggests that when actions are interconnected, small things can have major impacts that are nearly impossible to see until much later. You can never really just change one thing in a family business; a single change almost always triggers other consequences as well. When you take a stand or make a major change, you will often create an outcome that is different from, or even the opposite of, what you originally intended.

Family business is a team sport. You win together, and you can lose together. To understand the rules of your system, you have to recognize that individuals, their strengths and weaknesses, and their preferences matter. So do the multifaceted relationships on your team. Family businesses are deceptively complicated. Consider the family arguing over rosebushes at the beginning of this article. As we worked with the family, we quickly came to realize that the fight wasn't really about the roses. It was about years of slights, power plays, and lingering wounds, but also about everyone's deep desire to preserve their parents' legacy. The battle over the rosebushes was merely a proxy for their difficulty making decisions together as a group. The family members were eventually able to see this problem for themselves.

Once you grasp how family businesses work, you can see how an apparently irrational decision might make perfect sense in your family business. More importantly, you will come to understand your family and your business better. In a family business, it's easy to attribute challenges to individual personalities. But every business system is made up of individuals and relationships. **Focusing on the right problems can help you maintain both a great business and a great business family. And hopefully, you will then avoid wasting precious time arguing over roses.**

Info



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