

Changing Lanes

Transition planning for entrepreneurs and family businesses



LOFTUS ALLEN & Co.

CHARTERED ACCOUNTANTS and FAMILY BUSINESS ADVISORS

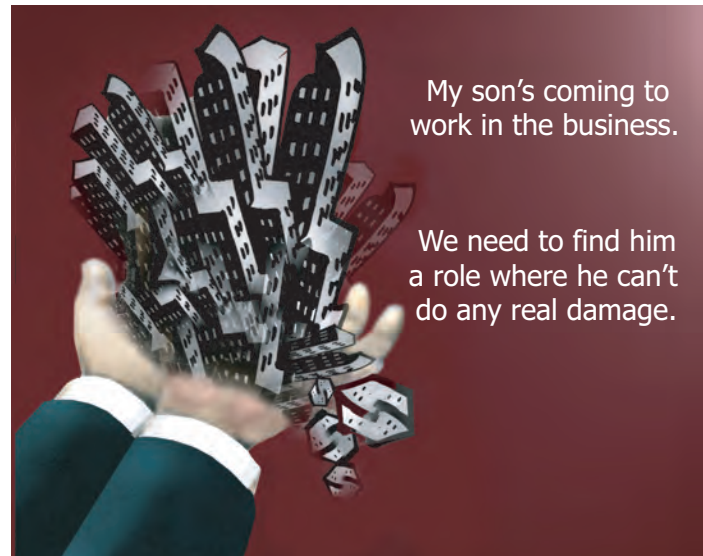
with compliments from



Terri Heggum-Allen, C.A.
Steve Allen, C.A.

When Family and Business Overlap


In an effort to keep their finger on the pulse, many SME (small to medium-sized enterprise) owners end up wearing many hats. Their roles in the business world might include those of majority shareholder, Chair of the Board, CEO, manager, salesperson, mentor, customer, supplier and colleague. In the family or personal circle, they play the role of offspring, sibling, spouse, parent, friend etc. Often these two worlds overlap and the business owner is faced with responsibilities to both, and some difficult decisions to make.



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Making decisions that impact both the family and the business are never easy. Sometimes an action that is tailored to meet personal or family obligations can negatively impact the business and vice versa. The most common example is when unqualified family members end up in key positions in the company, either from a sense of responsibility on the part of the owner, or a sense of entitlement on the part of the relative. Even entrepreneurs can find themselves in a struggle to perform in roles that are outside their core strengths. Is such a situation detrimental to their own well-being or the success of the business – or both?

Failure to professionalize the distribution of roles and responsibilities can breed a false perception of rights, loss of identity or role confusion, and considerable conflict. Addressing the lack of clarity around responsibilities, roles and rights – the last of the seven complexities – is the focus of this edition of Changing Lanes. 

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Rights and Responsibilities




It is widely acknowledged that to have rights to anything in life, we must also accept the responsibilities that accompany those rights. We all know that there are conditions or duties to uphold in pursuit of our rights to “life, liberty, and happiness.”

This basic philosophy permeates all areas of our lives. For example, both in business dealings and personal relationships we have an expectation of respect – but with the right to receive respect comes an obligation to show respect to others. If we ignore our responsibilities we must be prepared to accept the consequences.

Balancing rights and responsibilities isn't always easy. This is certainly the case for family-owned and family-run businesses where meeting the objectives and needs of the family circle can conflict with the objectives and needs of the management and ownership circles.

This complexity also spills over into the task of preparing your business for its inevitable transition.

Study after study shows that entrepreneurs fail to plan far enough ahead to ensure the continuity of their business. We believe that their fear and uncertainty about who will lead the business into the future is a large part of their reluctance to plan.

The key to addressing the uncertainty is to formalize each of the three key areas of the business. The development and maintenance of clear **roles** and processes will provide all generations with a vital link between the privileges of operating a family business and the responsibilities or obligations that accompany those privileges. 

I believe that every right implies a responsibility; every opportunity, an obligation; every possession, a duty.

John D. Rockefeller, Jr.

The Entitlement Virus

Through the success of his business, Thom has been able to more than adequately provide for his three children. Like all parents, he wanted his children to have a good start in life and a comfortable lifestyle. He supported them through college and helped the girls get established in their first homes.

Thom would like to see his business stay in the family, but right now he is very upset that the kids are more interested in what shares they have in the business, and in the case of Derek the youngest, how he can get a cash advance on those shares to finance his own business venture. Similarly, Diane isn't in any hurry to pay Thom back for the loan for the house because she feels that it is merely an advance on the inheritance that will eventually come her way. “Who do they think they are,” rages Thom. “It's my money, I made it. Where did they get this sense of entitlement?” Thom was shocked to realize they got it from him!

Thom has never explained to his kids exactly what level of ownership they have. From the time they were little, Thom would spend “quality time” with each of them. He would talk proudly about the business and how it would someday belong to them. He had no idea that each child took that to mean he or she would be the sole decision-maker!

Being a responsible father, Thom taught his children to invest wisely – when to buy shares, when to sell and what dividends to expect. So why is he surprised when they apply the same rules to their ownership in Penmaenship Tool and Die?

When you add the fact that Thom does not formally share his plans for the future of the business with the rest of the family, it's understandable that the kids do not display the level of buy-in that Thom expects from them.

When a business leader holds all the cards close to his chest, the next generation will more often than not focus on what little piece of the puzzle they have ‘ownership’ of. In most cases, any “we-focus” deteriorates as family members fall back on their own agenda: WIIFM – what's in it for me! They have not been enabled to ‘give’ so they have no choice but to ‘take’ instead.

Yes, Thom is hugely responsible for the entitlement virus the kids have seemingly caught.

The Seven Complexities

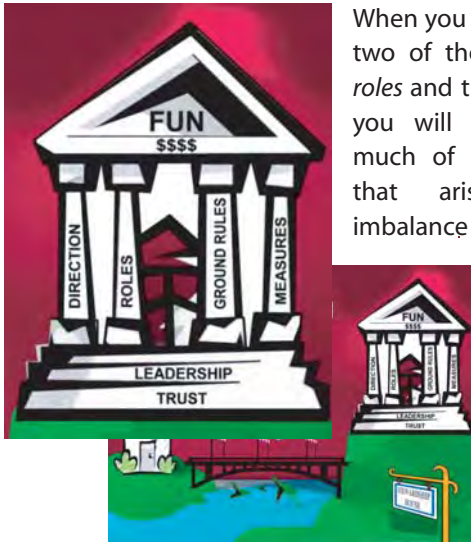
- 1 No clear definition between family and business
- 2 Family members can lose their personal identity
- 3 Unresolved conflict
- 4 No clear vision or direction - only dreams
- 5 Lack of trust or “we focus”
- 6 Lack of communication
- 7 Lack of clarity around responsibilities, roles and rights

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Erecting the Pillars

In a previous edition of Changing Lanes we used the analogy of building your house on the hill to explain the process of transitioning your business. Note the pillars that support the structure: the *direction, roles, ground rules* and *measures*.



When you consciously erect two of those pillars – the *roles* and the *ground rules* – you will actually address much of the complexity that arises from an imbalance of rights and responsibilities.

It is well documented that members of a family business have a number of overlapping rights and responsibilities, including management, ownership and directorships. This often leads to a lack of delineation between the respective roles which is exacerbated as more family members / generations enter the business. This heightens the need for agreements documenting the rights and obligations of shareholders, separate from those of employees and directors, and the role family plays.

2008 KPMG and FBA Study of Family Businesses

and *method of operation* is the critical step. Each should be placed in a role that utilizes their unique talents. Ongoing support can then be provided through a mentoring and personal development program.

At the same time, defining the **ground rules** for participation will ensure a balance between the rights and the responsibilities that can cause considerable complexity in family businesses. The best way to achieve this balance is through the establishment of policies and processes that address potential conflict situations before they arise.


Ground rules should be developed from the overarching family and business philosophies and should support the objectives for perpetuating the family unity, for participation in the ownership and management areas of the business, and for building family legacies. They can be shared through documents such as a shareholder agreement, a family charter and a family participation plan.

For each of the key roles, we recommend creating **ARAs** which map out the areas of:

Authority ~ the legitimate power given to a person to exercise discipline and use specific resources to reach an objective.

Responsibility ~ the ownership of duties or assignments associated with a function or position. Responsibility can be delegated but not shared and must be linked to accountability.

Accountability ~ answerable for the performance of duties within the assigned authority.

Essentially, these ARAs highlight the rights and responsibilities for anyone who plays a key role. For more information on how an ARA works, simply call our office. 

As the founder of Penmaenship Tool and Die, Thom Penmaen has the privilege – the freedom and the right – to take the business in whatever direction he chooses. However, as the employer of 150 people who depend on him for their lifestyle, Thom has bestowed upon himself a level of responsibility not only to those employees, but also the families and community they support.

So what can Thom do to meet his obligations and at the same time address the uncertainty that is distracting him?

Structuring a business that can survive under the next generation requires identification and designation of the roles that are essential to the continued strong leadership of Penmaenship Tool and Die.

Remember that people involved in a family enterprise often wear multiple hats. This crossover adds to the complexity and confusion. It is important to develop guidelines for the roles individuals will play in the leadership of each circle: the family/personal circle, the ownership circle and the management circle.

The purpose is to not only ensure that the objectives of each circle are met, but that each person has the opportunity to excel in the roles they play. The approach is the same for each circle – clarify the **roles** required to meet the objectives of that circle, identify the MO for each candidate and then see where you have a match. Identifying the core strengths

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Core Strengths

Can an apple help you, your family and your entire team feel truly fulfilled in life? On the outside, an apple can look close to perfect. But eventually, the skin of the apple will dry and shrivel up. The true strength of the apple however lies deep inside – in its core. Note the seeds that provided the nourishment as the apple matured. These seeds represent the natural strengths and abilities that are at our core and can ultimately lead us to find real fulfillment.

We all have different natural abilities, or what we call **core strengths**. They are the things you love to do and do extremely well. Think about it for a moment. How many people do you think truly experience a sense of fulfillment from their careers? Incredibly, only 12% of the population.

The rest are spending time in activities that are outside their core strengths. They will eventually become one of what we call the walking wounded – people who might be very good at what they do, but don't enjoy that sense of achievement that the 12% experience. They don't have a passion for the tasks they have to do and often portray diminished interest or even cynicism. They watch the clock. They become jaded and bored.

As much as 50% of what we do in our daily lives could be considered boring. However, we need to beware of the onset of critical boredom – that is, being tired of the whole scene, day in and day out. Boredom at this level manifests itself as stress.

Biologically, stress results from a real or imagined threat to our physical or emotional well-being. When we frequently work at tasks that we don't do very well, whether from a lack of skill or a lack of interest, we induce stress. It's a fact that as work satisfaction drops, stress increases. While dis-engaged, the vast majority of people suffer in silence but you will likely see absenteeism, low morale, or hostility at home and on the job. Some leave to find greener pastures or take early retirement. Others might be fired for their lack of commitment to the job.

When we try to exist in a role that is *consistently* outside our core strengths, the stress leads to more serious issues. Although our bodies try to adapt to the strains, they cannot keep it up indefinitely. More and more, our resources become depleted. If the situation is not addressed, we can burn out.

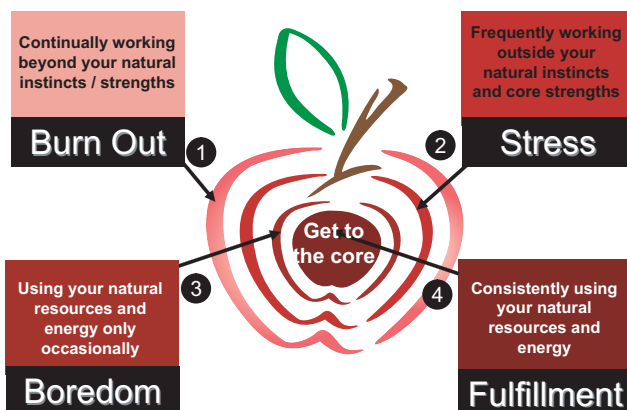
Burnout is defined as moving from resistance to emotional exhaustion. The toxic cocktail of too much stress plus too little satisfaction can lead to increased health problems and situations that involve drug or alcohol abuse. This chronic exhaustion more often than not leads to long-term disability.

Hans Selye, a doctor who devoted much of his life to researching the issue of stress noted that people have a **natural urge and need to work for their own benefit**. In other words, our physical and mental health depends on our inner satisfaction.

So whether it's your family or your management team who are just scratching the surface of their potential, it's important to go deeper than the skin to identify the core strengths. Look for:

- Roles where the work they do actually gives them energy that they can put right back into enjoying their lives and achieving success.
- Careers that feel perfectly aligned with who they are, as comfortable and perfect as a tailor-made suit.
- Ways to feel as inspired by the internal rewards of the work they do as the external ones.

We can help you find the right tools for identifying core strengths so you can put the most effective team together – a team that is qualified to take the business into the next generation. Finding their passion is the best investment you can make! ■



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1388-C Cornwall Rd.
Oakville, Ontario
L6J 7W5

905-566-7333
www.loftusallen.com