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Ownership Succession

The family-owned business is more than just a business. It's a dynamic flow of family relationships, based on both love and resentment. It's a combination of entitlement and opportunity—hidden by the more apparent ingredients of products, money, jobs, markets, and benefits. Family restaurant owners are often too busy fighting suppliers, offering promotions, cutting costs, and beating Uncle Sam's regulations to think about ownership succession.

Of all the dynamic ingredients in a family restaurant business, the issue of succession is foremost. Three questions most commonly asked are:

1. How will I know when my heir is ready to take over?

2. How do I teach my heir to take over for me?

3. Should I give or sell my company to my heir?

While a full discussion of each of these can be the subject of many articles, it might be fruitful to outline some of the factors that have provided guidance for family business owners contemplating an heir succession to management.

THE RIGHT TIME. When is an heir ready to take over? The correct answer is sometime after he thinks he is ready and sometime before the father thinks he is ready. There is no set formula to determine when a person, let alone a close family member, is ready to step into the founder's shoes. Observation, communication, and discussion will assist both parties in determining the correct time. The following considerations may be helpful in making the right choice at an appropriate time:

- Choose a time when the organization needs the assistance, not just when the heir feels he is ready.

- Prepare the business for the heir to assume a position. Meet with key supervisors to discuss the change.

- Choose for ability, not age or gender. The eldest son doesn't necessarily make the best manager.

- Match the talents of the heir to a specific position. If the successor has financial interests and education, slot a position in the financial or real estate division. It wouldn't make sense to place an aspiring chef into the accounting department.

Most managers assume that their children will want to operate their business. Even before the age of reason, children of entrepreneurs know that there is something that keeps a parent, or both parents, from spending time with them. They hear about the business, visit the business, and even have to make sacrifices because of the business. Why then, do most parents assume that their offspring will be interested in the family business?

Experts in the behavioral sciences feel that ownership succession in family businesses is often not chosen by a child but rather inflicted upon the heir by years of tradition. This implanted desire can lead to rebellion, unfulfilled lives, and destroyed family businesses.

The early years of a child's exposure to a family business are often thought to be years of learning, and therefore, preparation for a future ownership role. The early years do provide some exposure to aspects of the business. However, the father must recognize that to have continuity of family management, he must take time to teach. Unfortunately, most children have to learn the same way their fathers did— through luck, perseverance, and mistakes. Teaching is perhaps the most important step that a founder can take in preparing for succession.

Some techniques that have worked well for others include:

- Never allow a child to work in a senior management position in the family business until he has worked at least 2 years for someone else. This provides the heir with a frame of reference to compare management styles, methods of operation, and even his own options. Further, it allows him to develop new talents, and permits him to test the learning process (make mistakes and take risks) before entering the family business. Among co-workers, this experience increases the heir's credibility and gives him qualifications for other jobs if the family business does not work out.

- In the early years, ages 13 to 18, allow the child to work to earn extra money. The need for money should be the motivator, thereby linking the family business and work to earnings. Forcing a child to work without pay brings on resentment, which remains a part of the child's association with the business throughout life.

- Rotate positions. Allow managers to provide on-the-job training without parental influence. Make it clear to both the manager and the child that the child is to be treated like any other employee. Allow his initiative and ingenuity to guide his success.

- Give him promotions as they are earned.

- Devote at least one half-hour each day to face-to-face teaching. Learn while teaching. Listen. Encourage ideas and be prepared for a challenge.

- Don't bring business matters home. It can destroy rather than build unity.

Because of the unusual business environment created in the family business and a closely held company, careful consideration must be given to the best approach to ownership succession. It should be noted that management succession is not necessarily the same as ownership succession. However, when they are the same there are several reasons why the company should be sold to an heir rather than given.

1. Creates liquidity for the retiring owner. Without a salary or the availability of dividends, the former owner will need a source of income.

2. Removes the ability to take back the company. With a gift comes the Derceived right to take it back or at least the feeling that it can be rescinded. This is difficult for both the child and the father. Likewise, a child who purchases the business becomes more committed to making the endeavor a success.

3. Provides strong motivation to succeed. Paying a monetary price for the right to operate a business generates an immense amount of self-esteem— one of the strongest motivators in human nature.

4. Removes the caretaker syndrome. Unless the owner truly believes that he can improve established practices, experiment with new concepts, or change personnel, he will never take the risks necessary to grow the family business. The father may give the authority to make these changes, but if the right to make the decision is not followed by the responsibility for the success or failure, the business may become stagnant in a changing market.

5. Allows the income from operations to pay for the business over time. Most children have not accumulated the wealth necessary to purchase a family business. Earnings generated from the operation can be paid over a period of time to the former owner.

6. Establishes the value of the business. The value established in a sale to one child sets the price of equality with the other children. Sibling rivalry is often carried into adulthood. Unequal treatment can cause problems that can lead to the forced sale of the business.

7. Allows for estate planning. Most tax experts advise that gifts of closely held stock should be made over a period of time, thereby minimizing the taxability of the transaction. Should a death occur during the gift process, the company's direction might be compromised by unclear directions from the new owners. Through the sale process, even though payments may be made over a period of time, total ownership passes on the sale date.

COMPLEX RELATIONSHIP. The family business is a complex relationship of many people. The skills required in a family business arise from the interaction of these ingredients. Too often, family members grow up unprepared for their intended management and ownership roles.

If the owner plans carefully, the ownership transition can be a positive and non-disruptive process. Working for a successful family business can be more rewarding and have more advantages than working for a less personal, more bureaucratic non-family company.