HOW SUCCESSFUL FAMILY-OWNED BUSINESSES

Marge O'Connor

A better idea, skillful expertise, and sheer ambition are all typical traits of an entrepreneur. When the business succeeds and the founder eventually thinks about retiring, what are the best options for transitioning leadership of the family business so that it stays on course? What are the key elements and timing of a transition plan?

According to Drew Mendoza, Managing Principal of Chicago-based Family Business Consulting Group, Inc., key considerations in a transition plan are the financial and capital needs of the business as well as the capital and financial needs for the senior generation.

"The owner needs to address key points such as: What is the vision for this company and what strategy do we need in order to meet that vision? Do we have the right successors in place? Have they developed skills and qualities that will be demanded of leadership and owners 10 years from now? If not, how do we create opportunities for them to develop those skills and qualities? After that, they need to think about taxes, trusts, and stock bifurcations."

The Family Business Consulting Group works with family-owned businesses all over the world and Mendoza specializes in working with adult sibling and cousin teams of family business owners and managers and larger shareholder groups.

As for timing, he says sooner is better than never thinking about it. "At a minimum, you need 5 to 10 years to successfully transfer an operating company to the next generation. The organization needs to get ready and so do family members. If you're thinking of selling the company, you really don't have to look for ways to get the kids interested or trained. If a company is sold, the advisors will teach them how to manage the business," he says.

It also helps to consider any transition an ongoing process. "We increasingly find ourselves using the term continuity. Succession implies an event. In a family business it is continuity, or the transfer of responsibility and authority, that matters," Mendoza says.

Having a business continuity plan also communicates to employees and customers that the owner is committed to the long-term continuity and integrity of the business, which also can affect borrowing ratings. "In its simplest form, a good plan can help manage a company that the owner or leader continues to run for at least another generation. This is different from a company that the owner plans to sell," he says.

Mendoza says that in a majority of the cases where a family exits ownership, several years later the operating company is outperforming the assets given to the previous owner.

"I can understand the attractiveness of selling a business—the owner receives cash and gets rid of headaches. The fact is that, over the long run, multigenerational family businesses outperform nonfamily businesses. They take great interest and care in their community, and to my way of thinking, a family business is a precious vehicle in which to raise children and to teach them about the responsibilities as well as the rewards that come with being in business," Mendoza says.

He also notes the importance of the mindset of the next generation. "When the senior generation wants to pass the business to the offspring, we spend enough time with them to assess the readiness of the offspring and what they need to learn to make the company work. If there are siblings and cousins in the business we ask why they are in business together. We need to be sure of their intent, and their answer should actually help move a family through a succession process more efficaciously."

It's also crucial for the founders of the company to prepare future shareholders about ownership and teach them how to manage the paradox of family and business. "Frequently, children who own stock don't work in the business. Those working in it may think similarly to their dad—sort of a "dad, part two." We don't think it's wise to choose business first or family first. Neither approach will work and will alienate one or the other. The owners need to know how to manage inactive shareholders and how the business influences who they are as a family."

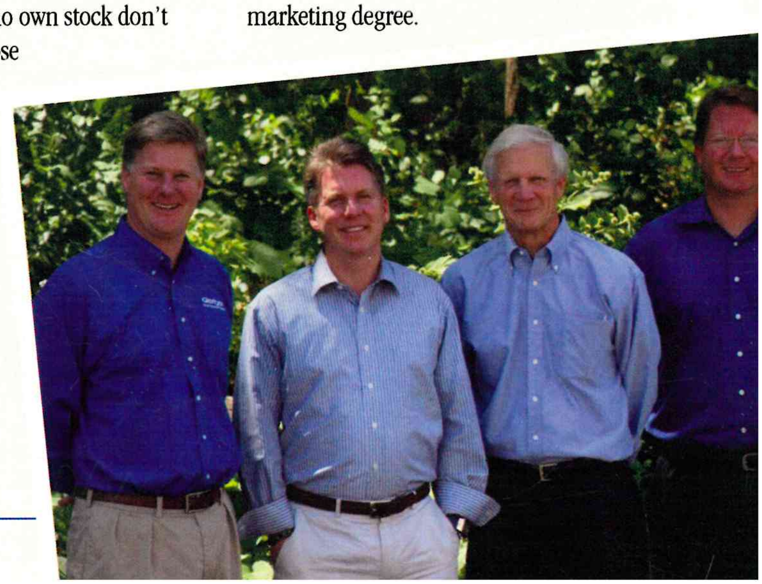
For companies with second, third, and fourth generations in the business, the pride is evident and so is attention to transition—whether via a formal plan or a simple concept. Following are two examples:

In 1978 Jim Peterson, Sr., started a one-man roofing company out of his garage in suburban Chicago. Now located in Mt. Prospect, IL, Peterson Roofing, Inc., is close to ten times bigger than it was at the beginning. And after 33 years, Jim is not ready to retire, but he's begun preparing the next generation to run the company.

The family includes three sons and a daughter. Jim, Jr. is the oldest child and has been in the business full time for 6 years, previously working part-time through high school and college; Joe currently works in the field as a repair technician; and John is learning the business to become the office manager. Their sister, Jaclyn, enjoys a successful teaching career and has no plans to be active in the business.

Although Peterson does not have a formal transition plan, he has been in the process for at least 5 years and believes it will take another 10 to make the full transition. "I wanted to start early to prevent a situation where the owner turns the business over quickly and in 2 years the business is gone. I consider a good transition period to be 10 to 15 years."

So far, says Jim, Sr., the informal plan is working well. "Jimmy, Jim, Jr., is a fantastic asset. He's got good field experience and a marketing degree.



He's doubled the business since he started full time about 6 years ago. We just made a major move to a huge facility and he managed that process. Joe is working as a repair tech and he will eventually take over the commercial roofing portion and Jim Jr. will run the residential roofing in addition to heading up our marketing."

Like many people who leave paperwork aside to take care of the task at hand, Peterson just hasn't had time to formalize a plan. "Business is booming and we recently added some divisions, so my mind has not been on putting our informal schedule into a formal document. In the meantime, we have insurance in place so that my kids will inherit the company in a way that prevents tax difficulties. So if I die, everything's okay; it's when I'm alive that there's a chance for trouble," he adds.

The company now has eight field crews; five estimators; four office personnel; and eight divisions, including commercial, residential, siding, gutters, tuck pointing, insulation, repair, and clean and seal.

The other major reason for a slower transition is customer retention. "A lot of our customers still want to deal with me. I'm 52 years old and may get out of it altogether when I'm 65," says Jim, Sr.

According to Jim, Jr., the challenge is changing over all the contact people. "Even to this day I can help our long-term customers, but they really want to talk with my dad. That can definitely be an issue in any transition."

But, as his dad points out, Jim, Jr., is creating his own niche. "It's interesting, though, because Jim has been very successful at creating new business. He has a lot of his own contacts and is working with them. He's actually building the next generation of customers. Jimmy is training me. He keeps saying that we need to be more computerized and he's right. We see more estimates coming through the Internet. Even though the majority still arrive by phone, I can tell the computer is a becoming more of a factor."

Both men agree that the most important aspects of making a plan work are training, trust, and having the employees aware of the plan. "Without proper training you'll never completely hand over anything. My dad had me on the roof in high school and college, so it helped me earn the respect from the field crews. They know I put in my time," Jim, Jr., says.

His dad adds, "In making a turnover, the people in each position have to know what they're doing and have experience. Most of our administrative staff has been here for a long time and they may all retire in the next 5 or so years. Their replacements will probably be younger and work under Jimmy's wing. Right now, it's sometimes hard for older staff to see him as an authority figure."

The Giertsen Company, headquartered in Minneapolis, is an example of multiple transitions with a more formal plan. The company has been family owned and operated for more than 90 years. Although it has grown tremendously to include several divisions and services, it remains focused on providing restoration services, which include roofing, from its operations in Minneapolis, Milwaukee, Chicago, and Naples, FL.

Rick I. Giertsen is the third generation to run the company and his sons will be the fourth. Rick's grandfather, Walter, began the business in 1918. His only son, Richard W., took over the helm in the 1950s and Richard I. began managing the company in the 1980s. According to him, the interest in running the business has passed down with each generation. And success has definitely followed.

Rick's sons are midway through the 4-year program that will allow them to take over in 2 years when Rick, who is 66 years old, plans to retire. He worked with attorneys and accountants to set up the plan for his sons to take over and says it was rewarding but difficult.

"Transitioning from one person running the company to setting it up to be managed by three people has been a bit challenging. I had to honestly and objectively look at each person's skills and determine who could do what. The way it worked out, one son will handling marketing, another operations, and the third finances. Each one will bring their skills to each of our company sites and help balance each other. They will each visit other sites on a monthly basis to be sure all our locations are operating well. We put some structure in place but I'm leaving a bit of the details on how they want to run things up to them. I will also have some checks and balances set up for that."

He notes that the challenges are in both financial and operational areas. "We did some long-term planning fairly early to resolve financial problems, but the major part is dealing with the different layers of ages as the next generation takes over. Some of our staff and subcontractors have been with me for 30 or 40 years and now they'll be asked to take direction from the next generation who are in their 30s or 40s. The other challenge is passing along all the expertise you've acquired from being in this business for so many years."

As for customer retention through the transition, Giersten says, "You win them over by quality and effort. For example, most of the property management companies we've dealt with for so many years have themselves changed management during that time. In those cases, we've maintained the business by providing good performance."

Marge O'Connor is a Chicago-based freelance journalist, who has specialized in the construction industry for more than 20 years.

Photo (left): From left to right, Rick Giertsen Jr., Kevin Giertsen, Rick Giertsen Sr., and Andrew Giertsen.

Photo (right): The Petersons: Jim Jr. (left) and Jim Sr. (right).