Family Business Succession: Is the Next Generation Ready to Lead?

Avoiding succession strife amid generational transitions

Family businesses face unique and often unanticipated challenges transitioning from one generation to the next. The struggle to maintain and protect both family interests and business interests is intricate and complex. According to PwC's 10th Global Family Business Survey, 58% of family members share similar views about the direction of their family business.[i] However, only 34% of family businesses said they had a robust and documented succession plan.[ii]

Succession planning challenges are made all the more difficult when the next generation of the family does not include a strong candidate to lead the business, or when some members of the next generation are natural leaders and others are "along for the ride."

That disconnect is a significant problem. Finding a solution when the "heir apparent" isn't so apparent magnifies the issue, implicating legal and cultural issues that weave through both family and business.

There are three lessons to bear in mind when family business succession plans are complicated by family members with varying levels of aptitude:

- Be clear about what's "fair"

In a family context, fairness comes down to equal opportunities for siblings and respecting all family members. In a business context, fairness comes down to rewarding those who excel. That rift alone makes conflict difficult to avoid.

A family member interested in participating in a family business typically begins with the goal of leading the business. The assumption is that those who end up in a lesser role or outside of the business are "lost sheep."

Less qualified family members may fight to avoid that stigma and stay within the business. Dissuading them from doing so or ensuring that their compensation is commensurate with their contributions takes time and tact. It is helpful to remember that siblings can be given equal ownership stakes but different compensation for performing different functions. This allows family members to benefit equally as owners while those who play more critical roles are better compensated as employees.

Laying out these terms can be tricky. Nobody wants to hear that they're considered unqualified and their sibling will be taking over the business; families need to create consensus around those moves and the economic implications. Keeping all parties in good graces is a smart move and lays the groundwork to change the structure at a later date.

- Don't shortcut succession planning

Especially when there are egos at stake, succession is a complex process. Creation of an appropriate structure cannot be accomplished in one meeting or around the dinner table: this is a multiyear, evolving process of education and change.

At the outset, families should establish a values-based decision-making process. The family should agree on axiomatic principles or a mission statement, which will then serve as a foundational part of the company's organizational documents. With that in hand, families have a guidepost to decide how management is selected or changed.

Families can also write in their management or budgetary safeguards to limit control of the executive team. A separate group can be responsible for executive compensation, related party transactions, and other potentially thorny situations. In addition, any significant transactions typically require approval by a separate group.

Another consideration is to expand the decision-making group during succession planning. If more family members or independent advisors are part of the process, conversations about roles become less tense. When there are two siblings vying for leadership roles, there is more obvious conflict than when a nine-person team is in play. With more participants, the message is softened and shared as a group.

- Speak with a unified voice

Non-family employees are likely to be curious about conversations and decisions that could impact the future of the company. Family members must resist the urge to comment or clarify, however, unless they are the appointed spokesperson for the family.

The family decision-making process should be kept separate from the non-family executive team and other employees of the business, and the family must speak with one voice to the rest of the team. Messages and statements about the family's positions concerning succession or other business matters should not be delivered until the family has had an opportunity to deliberate and reach consensus.

Succession is an emotional, tense, and legally significant undertaking. Businesses have risen and fallen based on their ability to get it right. The families that work to understand the wishes and qualifications of the next generation, take the planning process seriously, and act as a unified front can preserve the business – and family harmony – through this time of change.

Additional resources

- Business Dealings With the Four D's: Death, Divorce, Disability, and Drug Dependency
- Intra-Family Loans: Options for Friendly Terms in a Rising-Rate Environment
- Context Conflict: Preserving Goals and Values in the Family Enterprise

Endnotes

(i)10th Global Family Business Survey, PwC, 2021

(ii)*2021 Family Business Survey: US Findings,* PwC, 2021

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