FAMILY OFFICE REVIEW
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Losing the Family Office: A Study in Family Dynamics

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Preventing Family Dynamics from Destroying Your Multi-Generational Family Enterprise

You're a tremendous business success. You create a successful enterprise and establish a family office to provide financial support and investment counsel for future generations. Everything seems to have worked out - except, the family part of the Family Office disintegrates over time and in the end, often destroys family relationships.

Holding together a multi-generation Family Office is difficult since the core legacy and natural focal point, the original "family business" may no longer be present, providing easier options for family members to branch off on their own.

What makes this scenario tragic is that many of the family dynamics that can threaten the longevity of the Family Office easily could have been solved by addressing the "softer issues" associated with family stakeholders. Unfortunately, these considerations are often overlooked by senior family members, then deferred by succeeding generations and finally ignored by Family Office boards.

Needs-Based Differences

Any approach to managing family dynamics must recognize that the needs of family members are not only diverse, but their priorities and interests will understandably change over time based on factors such as age, marital status, lifestyle, income, and risk tolerances. Any area where interests do not align is a potential flashpoint for family conflict that can affect enterprise longevity.

With each succeeding generation, the challenges are magnified as extended families come into play. Instead of dealing with siblings, you might be dealing with first-, second-, or third-generation cousins. With each succeeding generation, the fundamental reason for being a part of a family enterprise can be lost. The experience then transitions to one that is impersonal. In a short time, some members may view the Family Office as a constraint on access to inherited assets or an obstacle to liquidity. This can lead to adversarial relationships.

We have consulted with families that do not speak to each other because of perceived or real slights. They skip holidays, weddings and other milestones because of family business-related tensions. Underlying frictions most commonly rise to the surface when the prior generation becomes disengaged from the family enterprise and personal agendas are pursued by the next generation.

Avoiding these unhappy and potentially costly events requires facing and resolving certain issues while the prior generation is still actively engaged in family affairs. We recently helped a client work with all of her children and their spouses to define and secure each family member's needs and desires. We facilitated the thoughtful communication necessary to resolve family members' emotional and financial needs while preserving the family enterprise's future viability.

The result was an agreed-upon written plan addressing current needs and desires with a methodology and governance structure that plans for future issues as circumstances undoubtedly change. We find it is critically important to understand and respect the needs of each stakeholder at an individual level so that an overall structure can be developed that meets individual as well as enterprise needs.

We have found the key areas most frequently at the core of family dynamic difficulties are centered around:

- Mutual Respect
- Family Inclusiveness
- Power/Control
- Perceived Fairness
- Compensation

Our approach helps our clients deal with these issues by concentrating on the "Four C's for Success."

The Four C's for Success: Consideration, Communication, Connectivity and Cash

Consideration of family members' emotional and financial needs sounds obvious, but is often not addressed in any measurable way. This, above all other elements, provides the framework for positive family business dynamics. The first step is defining the family's collective values regarding the Family Office; understanding family history can be a powerful starting point for establishing a sense of commonality of interest. Begin with a few basic questions:

- What are the values we all share and trust?
- Why was the original business started?
- Why do we have a family office?
- How do we balance "family needs" versus the enterprise's needs?

As you can imagine, reconciling the needs and desires of various passive family members can be a thorny issue. This requires clear identification and agreement of roles and responsibilities as a family member, a beneficiary, a Family Council or Board member, or employee.

Communication is similarly critical. Two widely accepted governance organizations, the Family Council and a Board of Directors, are extremely helpful in creating a strategy for clear and consistent communications as they provide participative governance of a family enterprise. As a former fourth-generation family business CEO, I advise my clients to regularly communicate individualized updates to all key stakeholders.

Verbal communications from the Family Office CEO or head of the family with supporting written reports is much more effective than exclusively issuing quarterly or annual reports. Some family members may not read or understand the content of a report. Part of the value of the communication is recognizing and respecting a family stakeholder as someone important enough that you are willing to take your time to discuss family affairs. Good communication and open access to information by family members flush out concerns before they become magnified and help keep the family unified in pursuing common and individual goals.

Connectivity among all family constituents is essential to creating both a sense of purpose and family member personal identity with the family and the Family Office. Educational, philanthropic, financial/investment and social agendas are critical to keeping the family together for multiple generations. Annual family gatherings where personal relationships either develop or are maintained, where future generations meet each other, where training about the purpose of the Family Office and sharing of the family history all contribute to a sense of connectedness.

Managed correctly, you will significantly increase the odds that future generation family members will see the purpose and benefits of maintaining the Family Office.

Cash for family stakeholders is the fourth issue that must be addressed...and, thoughtfully. Cash and other benefits are often a hidden problem affecting family dynamics that speak to issues of fairness and equity among family members. Fairness is actually based on individual perspectives. Some family members will have differing needs than others. Care in attempting to adjust Family Office practices to meet individual stakeholder needs is key.

Of course, discussions must include overall Family Office financial resources and capital needs, compensation and perks for family employees, and individual shareholder distributions and needs. Bringing sensitivity and objectivity to these discussions is necessary. That way, a family operating agreement to legally memorialize these and other important stakeholder issues can be more easily negotiated.

Specific Passive Stakeholder Strategies

Passive stakeholders frequently have a minimal voice in the management of a family enterprise. They often feel "trapped," with no control and no meaningful options to get out. This dangerous situation can lead to lawsuits, disruption of operations, embarrassing PR, and overall poor family dynamics. Such circumstances often set enterprise interests against personal ones. Some best-practice passive stakeholder strategies that we developed for our clients include:

- Developing a legal shareholder agreement addressing policy issues such as individual shareholder rights, key decision-making authorities, shareholder distribution policies, governance issues, etc.
- Electing passive stakeholder(s) to the Board of Directors (in addition to the Family Council);
- Naming a passive stakeholder as the Board Chair to provide more balance and communications between active and passive shareholders in decision-making processes;
- Providing board meeting attendance rights for non-board members (apart from executive sessions);
- Inviting passive stakeholders to enterprise outings, special events, award ceremonies, retirement parties and extended family social events and perks;
- Providing regular financial reports, business plans, and other stakeholder communications to passive stakeholders;
- Avoiding the discussion of business matters or issues at family outings; or if this occurs, including passive family members in the discussion;
- Avoiding any action that makes family members feel like a "second class" participant in the business or the family.

By understanding and addressing the differing needs of all family stakeholders; clearly delineating duties and responsibilities; promoting transparent and regular communication policies; developing and executing an agreed-upon shareholder agreement for all stakeholders; and creating a vehicle for long-term conflict resolution, your family dynamics will support and foster a long and successful family enterprise for generations.

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