CHAPTER 2

Family-Owned Businesses

CHAPTER CONTENTS

LEARNING OBJECTIVES

After studying the material in this chapter, the student will be able to:

1. Discuss some problems involved in organizing and operating small family-owned businesses.
2. Explain how family relationships can affect the business.
3. Describe the activities needed to prepare the next generation to enter the firm.
4. Discuss the importance and method of preparing for management succession.
5. Discuss the need for tax and estate planning in small companies.

CHAPTER OVERVIEW

This second chapter develops three ideas: the family in business; the problems of management succession, preparation for sudden and planned departure of key personnel, and hints on selling a business. It explores factors that affect the firm's future, including problems of hierarchy, interaction, limitations, resources, and preparation. An introduction to estate planning is included.

BRIEF CHAPTER OUTLINE

I. **ROLE OF THE FAMILY-OWNED BUSINESS**
   - A. The Family and the Business
   - B. Family Interactions
   - C. Family Limitations
   - D. Culture and the Family Business
   - E. Family Resources
   - F. Preparing the Next Generation

II. **PREPARING FOR MANAGEMENT SUCCESSION**
   - A. Why Succession Is a Problem
   - B. An Overlooked Problem

III. **PLAN AHEAD!**
   - A. Sudden Departure
   - B. Planned Departure
   - C. Selling to Family Members
   - D. Selling to Outsiders
   - E. Making the Transition Easier

IV. **TAX AND ESTATE PLANNING**

A. Tax Planning

B. Estate Planning

V. **ESTATE PLANNING TO MINIMIZE TAXES**

A. Estate Planning Issues

B. Estate Planning Techniques

CHAPTER OUTLINE AND TEACHING NOTES

CHAPTER OPENING PROFILE:

Farris-Feuerborn Memorial Chapel

The opening profile features the Farris-Feuerborn Memorial Chapel, a good example of a successful family business that has survived several generations. 35-40% of the Chapel's business has been prefunded burial policies. The owners have planned, trained, and developed family members for succession.

I. ROLE OF FAMILY-OWNED BUSINESS

Learning Objective 1.

Discuss some problems involved in organizing and operating small family-owned businesses.

A. The Conway Center for Family Business

Estimates that between 80 to 90% of all U.S. companies are family owned.

1. The majority of small companies have fewer than 30 employees.
2. The Institute estimates that only about 30% of these firms survive to the second generation of family members.
3. More than 46 million Americans work in home-based businesses.

B. Family businesses can be their own obstacle to success.

1. When close relatives work together, emotions can interfere with business decisions.
2. Families often have differing value systems and challenges.
3. If a family member is involved in something that evokes unfavorable publicity, it affects the business.

C. **The Family and the Business**

CHAPTER OUTLINE AND TEACHING NOTES

1. Family businesses need a *family mission statement* to cope with the business' demands.
    a. The younger generations should be involved in the decision-making process.
    b. Family members should be given clear descriptions of their responsibilities and job in the business.

Real World Example 2.1

The Levy brothers who run the Levy Organization in Chicago, believe their mother is the heart of their organization. They named a Deli after their mother and use her recipes.

2. R*ecent trends that involve careful planning and co-operation:*
    a. Spouses going into business together.
    b. Young people, setting up business by getting funding from their families.
    c. Retirees want to work part-time for the children's business without assuming a lot of responsibility.

REAL WORLD EXAMPLE 2.2

Jim and Eva Sisler are examples of this trend. They combined their desire to travel with a truck-driving business venture.

3. In any business, especially where families are involved; one person should be clearly in charge. A clearly defined chain of command is needed.

CHAPTER OUTLINE AND TEACHING NOTES

D. **Family Interactions**

Learning Objective 2.

Explain how family relationships can affect the business.

1. Usually the founder is the head of the business.
   a. The next head of the firm may be a family member who will move up through the ranks.

REAL WORLD EXAMPLE 2.3

Asplundh Tree Company is a family-held business with no desire to go public. Members of the fourth generation help carry on the family business.

   b. Family members' sense of ownership can be a strong motivator.
   c. Conflicts occur because each relative looks at the business from a different perspective.
2. *How to deal with incompetent family members*
   a. The best interests of family members are with a profitable firm with strong leadership.
   b. Members can be guided to jobs where there abilities are best suited.
   c. If members are not people-oriented, they should be assigned jobs allowing minimal contact.

CHAPTER OUTLINE AND TEACHING NOTES

3. *How to compensate family members (Making sure every company position and salary is in writing, agreed upon at funding of company, will save some problems later.)*
    a. Each family member has different perceptions of their contributions.
    b. Compensation should be based on job, and performance, not family position.
    c. Deferred profit-sharing plans, pension plans, and stock purchase programs can be effective in satisfying disgruntled family members.
    d. When a company succeeds into the second generation, titles start to matter to children and younger relatives.

E. **Family Limitations**

1. Entrepreneurs tend to be specialists in a given activity and may not be good general managers.
2. It is hard to say “no” to a family member who wants to enter the business.
3. Family members may feel they have to clear routine matters with the top family member.
4. Lines of authority and responsibility in the company must be clear and separate from those of the family.

CHAPTER OUTLINE AND TEACHING NOTES

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5. When no family members are available to run the business, some families form corporations and hire professional managers.
   a. This has the *advantages* of using professional management, freeing family time, reducing friction, and having employees treated more fairly.
   b. The *disadvantages* are reduced family employment, lower income, concentration of power, difficulties in finding and keeping good management, and loss of the "personal touch."
6. Divorce creates a special problem for many husband-and-wife-run businesses and can be handled by:
   a. Having the business appraised.
   b. Negotiating a buyout agreement.
   c. Deciding what to do with any business stock held.
   d. Consulting with a professional for help with tax issues.

F. **Culture and the Family Business**

1. Some cultures such as those of Utah's Mormons (70% of the state's Population), encourage home-based family businesses.
2. Stay-at-home moms refine craftwork and turn hobbies into profits.

REAL WORLD EXAMPLE 2.5

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When her husband's construction business collapsed, Laura Savage discovered her home business was the key to her family's survival.

2. Many stay-at-home moms turn hobbies into home-based businesses.
3. A recent trend—"Dadpreneurs."
4. Census data shows a recent 20% increase in home-based businesses.

REAL WORLD EXAMPLE 2.6

Two entrepreneurs launch home-based businesses. Diane St. James went into business for herself so she could stay home with her two daughters. Krista Sweeney left a corporate position and launched her own website.

G. **Family Resources**
   1. Available capital available within the family may limit expansion.
   2. Borrowing power is limited by the amount of family assets.

H. **Preparing for the Next Generation**
   1. Apathy on the part of offspring is a growing problem.
      a. Children may not be interested in taking over the family business.
      b. The two primary reasons that children follow in their parent's business are to make money and because they like the business.
      c. A powerful motivator for anyone is being able to do a job they like.
   2. *Start at part-time or full-time jobs?*
      a. In preparation for succession, offspring can begin with simple jobs, or on a part-time basis.

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b. Children can also prepare by working for another company in order to broaden their training.

3. *Start at entry-level or higher-level positions?*

a. It is not a good idea to allow a son or daughter to work in senior management until he or she has worked elsewhere and broadened their knowledge and expertise.

b. Rotate the person in varying positions.

c. Give promotions when earned.

d. Devote at least half an hour each day to face-to-face training.

e. Do not take business matters home.

f. If the newcomer is ready to learn the business, true responsibility must be given.

REAL WORLD EXAMPLE 2.7

Lee Patterson Co. is a good example of a family business that has evolved from a corner store into a major supplier of paint supplies.

II. PREPARING FOR MANAGEMENT SUCCESSION

Learning Objective 4.

Discuss the importance and method of preparing for management succession.

A. Any business must be ready for changes in its top management.

1. The key job requires considerable training and experience.

CHAPTER OUTLINE AND TEACHING NOTES

2. To prevent a disastrous transfer of power, *plan early and carefully, and groom a successor.*

B. **Why Succession Is a Problem**

1. The successor needs the ability to operate the business, plus the education, talent, and desire to do so.
2. In one survey, owners said their main concern was treating all children fairly.
3. Other concerns were the reaction of nonfamily employees, family communication, conflict, and estate taxes.
4. Another trend is to form an "executive committee" of two or more children to run the business.

REAL WORLD EXAMPLE 2.8

Bill Feurerborn chose politics and retail as a career path, instead of the family's funeral business.

5. Ongoing training should begin early for family members in line for succession.

REAL WORLD EXAMPLE 2.9

Susan McManigal joined her family's business, French Hand Laundry, as an accountant and learned the business from the ground up.

6. When the choice of replacements is limited, the owner may reorganize the present assignments and use present managers more effectively.

REAL WORLD EXAMPLE 2.10

There is no fourth generation successor for the Bon Ton Hatters. The only child, a daughter, is training to be a pediatric intensive care nurse.

CHAPTER OUTLINE AND TEACHING NOTES

C. **An Overlooked Problem**

1. Developing managerial personnel and planning for management succession are often neglected, frequently until too late.
2. According to research, most entrepreneurs simply don't want to face the inevitable.
3. Many entrepreneurs develop formal succession plans to avoid disagreements.

III. PLAN AHEAD!

Learning Objective 3.

Describe the activities needed to prepare the next generation to enter the firm.

A. Management succession occurs when the leader dies, becomes incapacitated, leaves the company, or retires.

1. Entrepreneurs should start planning early for their replacements.
2. Planning can help make sure operating authority passes smoothly from one generation to the next.
3. Plans should be flexible enough to include a sudden or planned departure.

B. **Sudden Departure**

1. A successful business must continue to operate even when the owner/manager leaves.
2. An owner's vacation can be an opportunity for on-the-job training for those left in charge.

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3. The sudden death or incapacity of the owner can be very disruptive, unless advanced plans are made.
4. An owner should make a will and keep it current, including instructions about what should be done with and in the business.
5. The firm can take out life insurance on the owner, so that the proceeds will go to the company in case of death.

C. **Planned Departure**

1. What happens when owners plan to leave depends on the type of business ownership.
2. If the company is a *corporation*, the selection is handled by the Board of Directors.
3. The entire family tends to become involved in the replacement decision in *proprietorships* and *partnerships.*

D. **Selling to Family Members**

1. *The advantages:*
    a. The business stays in the family.
    b. It provides a source of employment for family members.
    c. The family's stature is maintained.
    d. The former owner is free to relax or travel.
    e. There is pleasure when the successor is successful.
    f. It can strengthen family bonds.

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REAL WORLD EXAMPLE 2.11

Dudley Feuerborn, the previous owner of the Feuerborn-Farris Memorial Chapel featured in the opening profile, sold the business to son Reuben. He has purchased a motor home and plans to travel extensively.

2. The business can also be sold to outsiders and later repurchased by one or more family member.

REAL WORLD EXAMPLE 2.12

Charles Alfieri sold his hair replacement business to a Japanese company. Nine years later, the family repurchased the business.

E. **Selling to Outsiders**

1. If no relative will assume responsibility, the owner can sell to a partner, an outsider, or close the business.
   a. Many small businesses are sold and moved offshore.
   b. Some companies expand in other countries, and later sell the established spin-offs to locals.
2. *Reasons for selling to outsiders:*
   a. Assured income.
   b. Lack of worry about what subsequently happens.
   c. Possible opportunity to consult.
   d. Release of family tension.
   e. Relief of further responsibility.
3. However, selling to someone outside the family can hurt the family since it marks the loss of something the founder built.

REAL WORLD EXAMPLE 2.13

CHAPTER OUTLINE AND TEACHING NOTES

Sometimes selling to outsiders can have a beneficial effect on family relationships, as happened to one troubled family business.

F. **Making the Transition Easier**

1. Owners need to broaden their focus in preparation for their departure.
2. They should begin to devote more time to hobbies and outside group activities.
3. The transition can be made in phases, slowly turning over parts of the business.

IV. TAXES AND ESTATE PLANNING

Learning Objective 5.

Discuss the need for tax and estate planning in small companies.

A. Planning is needed to minimize estate taxes.

1. When a firm has appreciated in value, inheritance taxes can be devastating.
2. Owners should review estate plans frequently in regard to tax liability.

B. **Tax Planning**

1. The owner must consider the influence taxes will have on profits and the business's capital structure.
2. Owners should probably have an annual planning conference with a CPA.

C. ***ESTATE PLANNING*** is preparing for the orderly transfer of the owner's equity in the business when death occurs.

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1. Usually the major concerns are keeping the business running and maintaining liquidity.
2. The heirs may have to sell assets to pay estate taxes, reducing the firm's equity.
3. *For a small business, estate planning can:*
    a. Reduce the need for beneficiaries to withdraw funds.
    b. Influence heirs to keep funds in the firm.
    c. Provide for a smooth transition.
4. *Estate planning can be in the form of:*
    a. Gifts to children.
    b. Stock sales to family members.
    c. Living trusts.
    d. ***FAMILY LIMITED PARTNERSHIPS***, which allow business owners to pass assets to heirs with a minimum of income and estate tax costs while retaining control of assets during their lifetime.
5. Estate planning activities must comply with IRS regulations.
6. *There are three methods for determining the true value of a business:*
    a. Determine the *value of a comparable business* that is publicly traded.
    b. Ascertain the business's value by *capitalizing its earnings.*

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c. Estimating the business's value by determining its *book value.*

7. A ***BUY/SELL AGREEMENT*** provides for the corporation to buy back a shareholder's stock when he or she leaves the company.
    a. This agreement binds the IRS to accept the existing company valuation.
    b. A properly prepared buy/sell agreement assures a market for the stock and protects the minority stockholder.

REAL WORLD EXAMPLE 2.14

One young woman held 28% of the stock in her employer's corporation. When she lost her job, her employer refused to redeem the stock.

V. ESTATE PLANNING TO MINIMIZE TAXES

A. The owner will want to minimize taxes on the estate so that the benefits of the estate pass to the family.
   1. Owners who lack financial skills can use a Certified Financial Planner.

B. **Estate Planning Issues**
   1. Trying to minimize taxes.
   2. Retaining control of the business.
   3. Maintaining flexibility of operations.

C. **Estate Planning Techniques**
   1. Making gifts to family, as soon as possible, is one way to reduce taxes on your estate.
      a. Gifts must be of "present interest" rather than a "future interest."

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b. The first $13,000 in gifts made by each spouse to each person during the year is tax free.

c. Lifetime tax-free gifts are limited to $3.5 million.

d. The gifts can be cash, bonds, real estate, the family business, interest in a partnership, and so forth.

2. *Establish a limited family partnership*

   a. Forming a family partnership allows the owner to take money out of the company at lower tax rates.

   b. This type of tax shelter is quite complex and requires professional help.

3. *Sell stock to children*

   a. You can also sell all or a part of your business to your children.

   b. Like establishing a family partnership, this form of transfer is complicated.

   c. This method can also be combined with gifts to the family.

4. *Establish a living trust*

   a. A ***LIVING TRUST*** resembles a will but, in addition to providing for distributing personal assets on the maker's death, it also contains instructions for managing those assets should the person become disabled.

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b. The owner can put property into a living trust while they are still alive. c. Then when the owner dies the firm's assets can be automatically distributed to the beneficiaries, and can save estate taxes. d. A living trust changes the ownership of all real estate and other assets. e. As with the limited family partnership featured earlier, it is important to talk with experienced financial managers in preparing a living trust.	

LEARNING OBJECTIVES REVISITED

1. *Discuss some problems involved in organizing and operating small family-owned businesses.*
   - Family members may not have the desire, talents, or experience to lead the business.
   - Objective evaluation of family members' skills is often difficult.
   - When close relates work together, emotions can interfere with business decision making.
   - Conflicts can occur when each relative looks at the business from a different perspective.
   - Family managers may feel it necessary to clear routine matters with the top family member.
   - Compensation decisions are difficult.

2. *Explain how family relationships can affect the business.*
   - To the extent feasible, ownership and management should be separated from family affairs.
   - Upward movement of family in the business can generate positive motivation, but evaluation of family members' skills is difficult.
   - Disruptive members should be isolated.
   - Compensation should be based on job performance, not on personal or family relationships.
   - The family can form a corporation and hire professional managers.

3. *Describe the activities needed to prepare the next generation to enter the firm.*
   - Start planning for succession early to smooth any sudden transition.
   - If family members are going to run the business, training should begin early.

     Take them to work with you, taking time to show them what you do and what your business is about. Talk about who your customers are and what your business provides for them. Speak in positives.
   - The owner needs to prepare a will including instructions for dealing with the business.
   - The owner's vacation can create an opportunity for on-the-job training for family members.
   - When the choice of replacements is limited, the owner can reorganize the present assignments and use present managers more effectively.
   - The firm can take out life insurance on the owner.

4. Discuss the importance and method of preparing for management succession.
   - Children may not automatically want to enter the family business, having become bored with the business.
   - Children can begin in part-time, simple jobs, or they can work for another company to gain experience.
   - Successors need to get to know the business before being placed in leadership positions.
   - Plan early and carefully, and groom a successor.
   - Two or more children can form an "executive committee." Include the children in family conferences. Discuss what is best for the business and what is best for each of them.
   - On-going training should begin early.
   - Most owners have trouble facing the inevitable. In the end, do what is best for all.

5. *Discuss the need for tax and estate planning in small companies.*
   - Estate planning can minimize the tax burden on the owner's heirs.
   - Strategies should be developed to reduce the beneficiaries' need to withdraw funds and provide for a smooth transition.
   - Gifts to children, selling stock to family members, starting up a living trust, and setting up a family limited partnership can help.
   - Owners should consult professions to assure that IRS regulations are met.

KEY TERMS USED IN THIS CHAPTER

A ***buy-sell agreement*** provides for the corporation to buy back a shareholder's stock when he or she leaves the company.

Estate planning is preparing for the orderly transfer of the owner's equity in the business when death occurs.

A ***family limited partnership*** allows business owners to pass assets to heirs with a minimum of income and estate tax costs while retaining control of assets during their lifetime.

A ***living trust*** resembles a will but, in addition to providing for distributing personal assets on the maker's death, it also contains instructions for managing those assets should the person become disabled.

NOTES FOR DISCUSSION QUESTIONS

1. *Why is management succession an important issue for any small firm? For a family firm?*

Management succession is important in any small firm because, if it is not handled properly, there will be a lapse in the quality of management. This might result in a loss of customers that would ultimately force the company out of business.

The successor must be as willing as the founder to make the business work. If all the family members involved in the business do not agree on who should take over, the resulting tension among the family members could lead to a split in the family. If an agreement cannot be reached, it may be in the best interests of both family and business to sell the business to someone outside the family.

2. *Why is it often difficult to make reasonable decisions in a family business? What problems are caused by a family organization structure?*

Reasonable decisions are sometimes difficult to make because personal emotions and conflicts interfere with professional judgment. Emotions and differing value systems can cause conflicts between members.

To the extent feasible, ownership and management should be separated from family affairs in order to be fair to nonfamily employees and to reduce friction. Family members may be promoted through the ranks, but evaluation of family members' skills is often difficult. Disruptive members should be isolated, delegation should be practiced, and compensation should be based on job performance—not personal or family relationships—if possible.

3. *What problems face a company when a key officer leaves suddenly?*

When a key officer leaves suddenly, questions such as the following can bring about many problems. Will the officer return? Who will replace him temporarily or permanently as the case may be? How will the business be run?

All of these questions should be asked by the owner soon after the business is opened so they can be planned for and operations can continue to run smoothly when the key officer leaves suddenly.

4. *If you start a business when you are in your twenties and thirties, should you do anything about your replacement? Explain.*

You should give some thought to your replacement, because doing so will avoid succession problems in the future. In the case of your sudden death or disability, the business will have someone who understands how it is run.

5. *Suppose you have a successful business now, but decide you want to leave it. What might be some reasons for leaving it? What alternatives do you have for the business?*

An owner might decide to retire, because he or she has reached the perceived retirement age, because of health problems, or simply because they are tired of the business. They may also want to give the next generation a chance to run the company.

The founder could sell the business to a family member, to an outsider, or to someone in the business or close it down entirely. If someone in the business is able to buy it, an inside buyer would be preferable to an outsider, because that person would have more experience in the operation of the business and first-hand knowledge of how it works.

6. *How important is estate planning? How can you do it?*

Estate planning minimizes estate taxes and prepares for the transfer of the equity of an owner at his or her death. Estate planning reduces the need for beneficiaries to withdraw funds, helps maintain beneficiary's interest in keeping funds in the firm, and provides for a smooth transition. Estate planning can be in the form of gifts to children, stock sales to family members, living trusts, and family limited partnerships.

NOTES FOR CASE QUESTIONS

CASE 2.1: Tire Rack

This is an example of a family-run business that works. They want the company to "feel like a family" to all employees. Such an atmosphere is hard to achieve.

1. *Why is management succession so important in a family firm?*

Owners often neglect succession planning, sometimes refusing to face the reality of their eventual death. If no successor is named, the owner loses the opportunity to train and educate the next generation of leadership. Every transfer of ownership and power is an invitation to disaster. To lessen the chance of failure, the owner should do two things: plan early and carefully, and groom a successor.

2. Why is it often difficult to make decisions in a family-run business?

Family businesses can be a source of unresolved family tensions and conflicts, which can create obstacles to achieving even the most basic business goals. When close relatives work together, emotions often interfere with business decisions. The interaction of family values and business reality can create conflict.

3. What qualities have contributed to the success of Tire Rack?

Mike Joines and his father-in law, Peter Veldman, created Tire Rack to sell name-brand tires to consumers and to other retailers. Customer service is the company's priority. Employees are treated like family. Joines was also astute enough to jump into online commerce when the idea was new.

BONUS EXERCISE

2.1 Managing a Family Business

*This exercise gives students a chance to "manage" a family business. Use **Handout 2-A: Managing a Family Business** on the following page. This can be an individual assignment or a small group project.*

HANDOUT 2-A

Managing a Family Business

Nicholas Stavros opened his first restaurant in Cedar City twenty-five years ago. Stavros's family-style Greek food and atmosphere proved popular, and three additional restaurants were opened in outlying suburbs. One of Papa Nick's children now runs each: Maria's Stavros, Peter's Stavros, and Eric's Stavros. Nick Junior runs the original Nick's Stavros.

The menu is consistent across all four restaurants, but each restaurant features a daily special prepared by the local chef. Customer comment cards consistently rank the quality of food as very high.

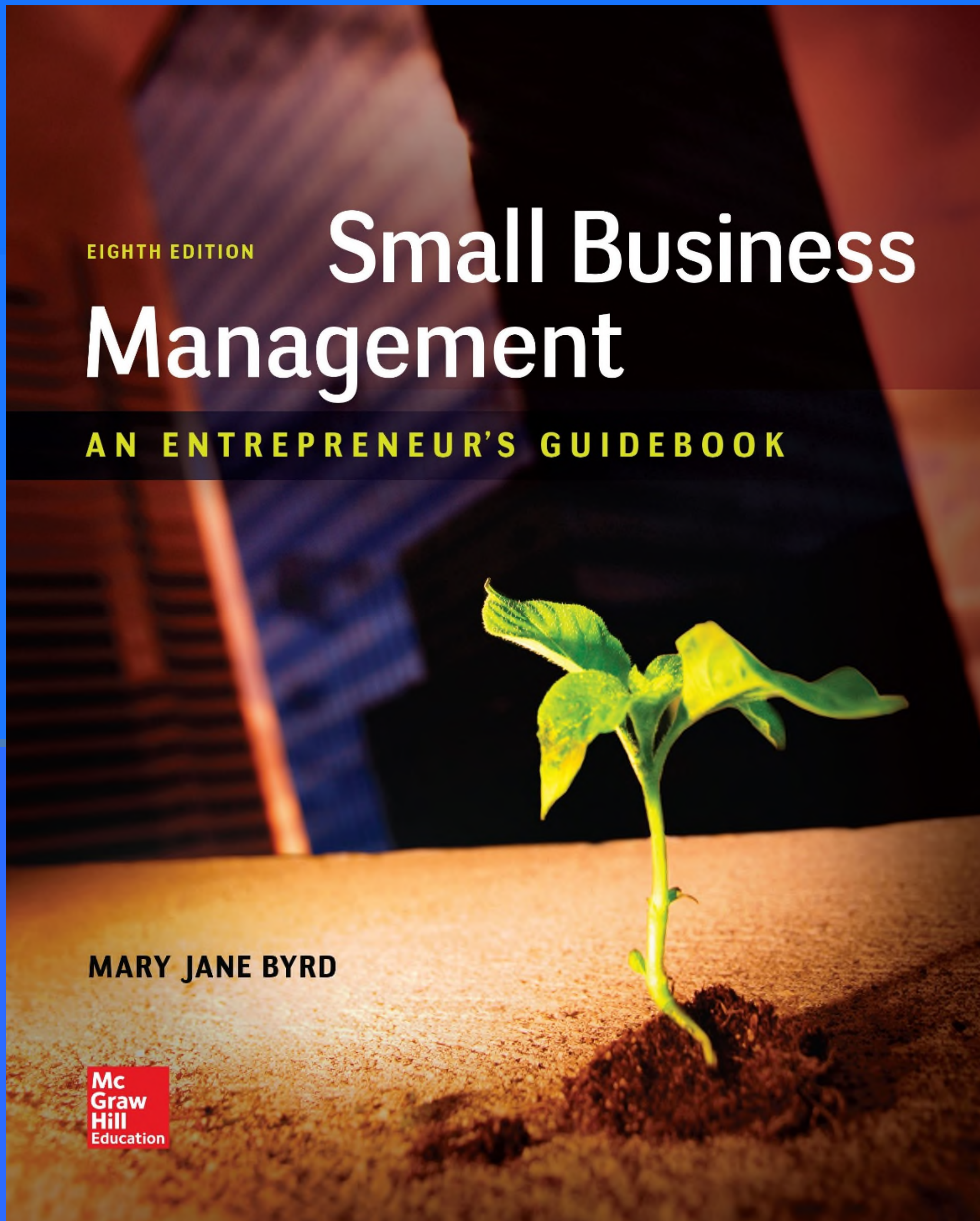
Papa Nick now divides his time between the restaurants and the family's real estate holdings. Major decisions are made by Papa Nick. All employees at each restaurant report to the restaurant's Stavros manager, providing some degree of decentralization.

Customer comment cards have begun to show some problem areas at Peter's Stavros Restaurant. Service ratings have fallen to "fair," and many customers have written specific comments about slow service and poor wait service attitude.

Because it is the newest restaurant, Eric's Stavros has received more resources for advertising and promotion. The equipment is also significantly newer than that at the other three restaurants. Over time Maria, Peter, and Nick Junior have come to resent the attention Eric has received. The tension has become so high that the staff at Peter's Stavros does not speak to the staff at Peter's Stavros.

Papa Nick is reviewing two pieces of information. One, the profit margin from restaurant operations has declined over the past year. And, finally, several employees have mentioned their desire to join a union.

Papa Nick has asked your advice for improving the performance of his restaurants. What advice would you give him? Outline a plan of action, with goals and timelines.



Family-Owned Businesses

Chapter Two

Learning Objectives

1. Discuss some problems involved in organizing and operating small family-owned businesses.
2. Explain how family relationships can affect the business.
3. Describe the activities needed to prepare the next generation to enter the firm.
4. Discuss the importance and method of preparing for management succession.
5. Discuss the need for tax and estate planning in small companies.

The Family-Owned Business

- Conway Center for Family Business estimates that *between 80-90% of all U.S. companies are family owned.*
- The Institute estimates that *only about 30% of those survive* to the second generation.
- More than *46 Million Americans work in family-related businesses.*
- Family businesses bring challenges resulting from clash of business necessities with family needs.

The Family and the Business

- Family businesses *need a family mission statement* to cope with business/family demands.
- It is important that the children be included in making decisions and setting goals. *When the entire family is included, they become a family again.*
- Business owners tend to *get caught up in business activities and delay attention to families* while concentrating on the financial needs.

Trends in Family Businesses

- **First**, many young people are going into business for themselves—and tapping their parents for funds to finance their ventures, in return for giving one or both parents a seat on the board.
- **Second**, a large number of spouses are going into business together.
  - Referred to as *copreneurs.*

What Copreneurs Should Consider

- *Jot down what each hopes to accomplish and see if their goals are compatible.*
- *Find trusted employees or advisors to help settle disputes.*
- *Consider talking to a marriage counselor about how this will affect their relationship.*
- *Let each spouse take the role he or she fills best.*
- *Schedule personal time.*

What Copreneurs Should Consider

- **Don’t** hold grudges.
- **Don’t** have one spouse work for another as an employee.
- **Don’t** let business arguments get personal.
- **Don’t** make major decisions without consulting your spouse.
- **Don’t** start a business in the first place unless the relationship is strong.

Making It in Business with Your Spouse

FIGURE 2.1 | Making It in Business with Your Spouse

Following are some tips for spouses to follow in running a jointly owned business:

- Don't be blinded by romance; follow all the rules.
- Define each person's role and accentuate each other's talents.
- Don't ignore business conflicts in an attempt to spare a personal relationship.
- Agree to disagree—set the ground rules.
- Be clear and specific about your expectations of each other.
- Set aside family time, and stick to it.
- Set up a system for recognizing and rewarding hard work done by family members.

The Family and the Business

- In family firms *strong family ties* can improve the chances of consensus and support, while dissension can lead to disagreement and/or disruption of activities.
- Family members' "sense of "ownership" can be a strong, positive motivator in building the business and leading to greater cooperation.
- Historically, leadership passed from father to son, but that is changing.
- Reuben Feuerborn says, *"It's the talent and interest in people that is important, if Peyton (His daughter and oldest child), wants to do it, we'll have no problem including her in our family business."*

Women Who Want To Lead Should:

- ✓ Express Interest.
- ✓ Gain experience outside the family business.
- ✓ Learn from the senior generation.
- ✓ Be sensitive to the parent.
- ✓ Get involved and ask questions.
- ✓ Meet with women who lead family businesses.
- ✓ Define yourself.
- ✓ Develop a company vision.
- ✓ It is estimated that women own 40% of all U.S. businesses.

How to Deal with Incompetent Family Members

- Some family members are unable to make objective decisions about one another's skills and abilities.
- One possible solution is to convince family members, as well as nonfamily employees, that their interests are best served by a profitable firm with strong leadership.
- Another is to set up a rotating board to handle HR decisions.
- Family members with little ability to contribute to the firm can be placed in jobs in which they do not disturb other employees

How to Compensate Family Members

1. *Compensation should be based on job performance, not family position.*
2. *Fringe benefits, such as stock, pensions plans, or insurance programs, can be useful as financial rewards, but they must conform to those given to nonfamily employees.*
3. *A title is perceived as a confirmation of a job well done and also tends to serve as a motivator.*

Family Limitations

- Personality conflicts and emotional reactions can cause bottlenecks in production.
- It is important that family as well as other employees **maintain the chain of command.** Lines of authority and responsibility in the company must be clear and separated from those within the family circle.

Family Limitations

A. Some families organize their businesses into corporations and hire professional managers to run them when no family members are in a position to manage.

B. Frees family time for other purposes, reducing friction, and having employees treated more fairly.

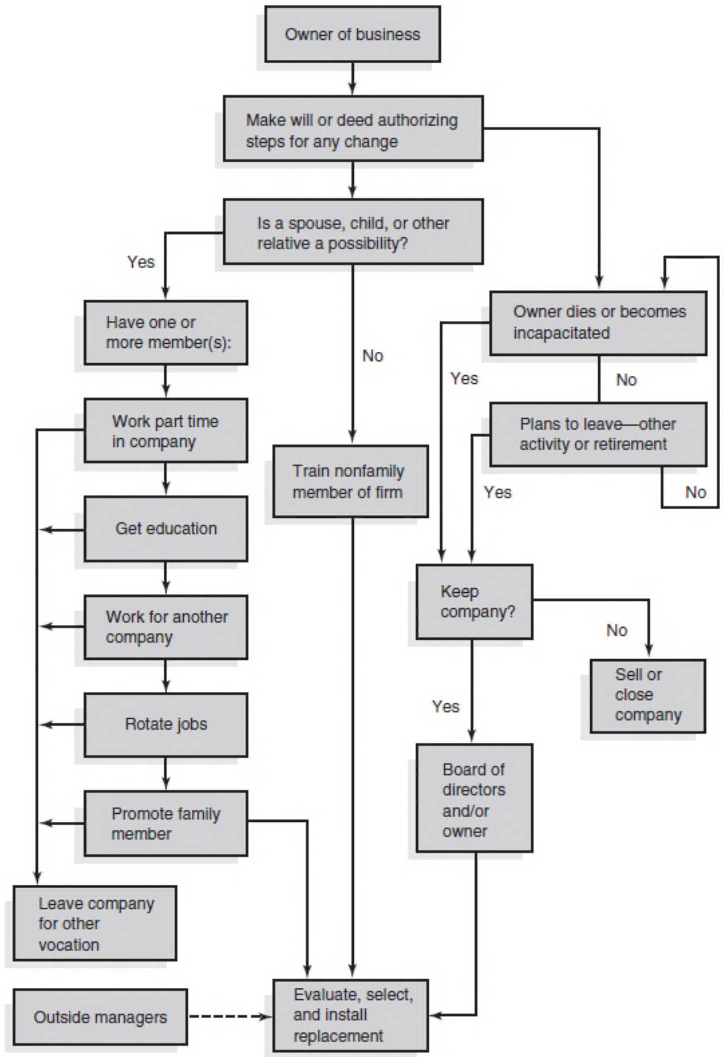
Family Limitations

- **Disadvantages**:
  - Reduced family employment.
  - Lower income.
  - Concentration of power in small cliques.
  - Difficulties in finding and keeping a good management team.
  - Loss of the “personal touch.”

Start at Entry-Level or Higher-Level Positions?

- Never allow a child to work in senior management until he or she has worked for someone else for at least two years.
- Rotate the person in varying positions within your business.
- Give promotions only as they are earned.
- Devote at least half an hour each day to face-to-face teaching and training.
- ***Do not take business matters home.***
- If the newcomer is ready to learn the business, true responsibility must be given. Otherwise, the person cannot lean to manage the business.

Preparing for Management Succession



- To avoid family succession problems, entrepreneurs should start planning early for their replacements.

Advantages of Selling to Family Members

- The business stays in the family.
- It provides a source of employment for family members.
- The family's stature is maintained.
- The former owner is free to relax or travel.
- There is pleasure when the successor is successful.
- It can strengthen family bonds rather than produce additional family friction.

Estate Planning

- **Estate planning**
  - Preparing for the orderly transfer of the owner's equity when death occurs.
  - Needed to maintain liquidity and perpetuate the business.

Estate Planning

Estate planning can:

1. Reduce the need for beneficiaries to withdraw funds.
2. Help maintain beneficiaries’ interest in keeping funds in the firm.
3. *Provide for a smooth transition.*

Estate Planning

- **Estate planning can be in the form of:**
  - **Gifts to children.**
  - **Stock sales to family members.**
  - **Family limited partnerships,** allow business owners to pass assets to heirs with a minimum of income and estate tax costs—while retaining control of the assets during their lifetime.

Estate Planning

- **Buy-sell agreement**
  - Provides for the corporation to buy back a shareholder’s stock when he or she leaves the company.
  - Binding on the IRS written agreement.
  - Assures a market for stock.
  - Provides protection for the minority stockholder.

Buy/Sell Effectiveness

TABLE 2.1 | Buy/Sell Effectiveness

Internal Revenue Code Section 2803 regulations concerning buy-sell agreements:

- It must be a bona fide business arrangement.
- It must not be a device to transfer property to members of the decedent's family for less than full and adequate consideration.
- It is similar to comparable arm's-length transactions.

In addition, applicable case law has established several rules that must be followed:

- The estate must be obligated to sell at death.
- The agreement must have a fixed and determined sale price or a method for determining the price.

The owner cannot sell the property during his or her lifetime without first offering it to the other owners.

- The price must be fair and adequate when the agreement is made.

A buy-sell agreement benefits both heirs and surviving owners.

Benefits to heirs

- Freedom from business worries.
- Guarantee of a fair purchase price.
- Possibility of avoiding probate delays.

Benefits to surviving owners

- Relief from concern about new and possibly unwanted partners.
- Advance knowledge of the purchase price.
- Retention of good relations with creditors and clients through a smooth transition of ownership.

Estate Planning Issues

- Minimizing taxes.
- Retaining control of the business.
- Maintaining flexibility of operations.

Estate Planning Techniques

- Family gifts
- Family partnerships
- Stock sales to family members
- Living trusts

Living Trust

Resembles a will, but, in addition to providing for distributing personal assets on the maker's death, it also contains instructions for managing those assets should the person become disabled.

- You can put property in a trust while you are alive; then when you die, the property automatically goes to the designated heirs without having to go through probate court, saving time and expense.
- Disadvantages are you no longer own property; Setting up a trust can be expensive; beneficiaries still pay must pay taxes; If you need to refinance your house, some lenders may refuse if it is in a trust.
- Hire an experienced trust attorney,and select a capable and trustworthy trustee.