Harvard Business Review
Family Business Handbook

How to Build and Sustain a Successful, Enduring Enterprise

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Dear Reader,

Are you involved with a family business – as an owner, a future owner, a trusted adviser, or an employee – that you love, but don't fully comprehend? That's not surprising. As your own experience will surely tell you, family businesses don't follow conventional business rules. And perhaps more importantly, they define their own version of success.

But we have good news. It's possible to better understand your own family business once you understand how family businesses work and evolve. We have written the *Harvard Business Review Family Business Handbook* to help anyone whose life is shaped by being part of a family business. The advice, frameworks, and practices in this book are based on our decades of experience working with family businesses in a wide variety of sizes, industries, countries, and cultures. The book deals with the full breadth of issues most family businesses face, such as how to establish good governance, build trusted relationships, manage conflict, transfer the business to the next generation, set family employment policies, and much more. The approaches we will describe have worked for hundreds of business families, and we hope you find ways that they can work for you, too.

One of the best benefits of our job is learning from great family businesses. We hope that this book offers an opportunity to continue that learning process. If you have comments, questions, even disagreements, about what you read, we would love to hear them.

From all of us at BanyanGlobal Family Business Advisors
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PART ONE

Cracking the Code of Your Family Business

Decode Your Family Business

Who cut down Mom's rosebushes? Rosebushes! This fight nearly derailed a successful second-generation family business. We had scheduled a meeting with the company's owners to discuss whether to retain their underperforming nonfamily CEO. Instead they spent almost the entire time arguing over whether one of the brothers had the right to "prune" or "kill" (depending on whose version you believed) their mother's prized rosebushes at the family cottage. Despite our efforts to change the subject, they couldn't move past the rosebush incident. The meeting ended in a deadlock, the group unable to make any decisions together.

It's hard to imagine a public company's board coming to a standstill over landscaping. Outsiders often scratch their head at how family businesses seem to defy conventional business rules. That's because family businesses are different. If you're part of such a business or working for one, the business's uniqueness will be no surprise to you. But that doesn't mean you always understand how and why the business operates the way

it does. You just know that conventional business wisdom doesn't always apply. But what are the rules?

We have good news. Family businesses can be understood if you stop scrutinizing them like conventional businesses and instead use these three levels of analysis:

- Individuals, especially owners, have a huge impact.
- Relationships are multidimensional and interlocking.
- System dynamics shape everyone's behavior in ways you might not realize.

In this chapter, we will help you identify and understand the influence of critical individuals in your family business, decipher and map key relationships, and recognize the often-unseen system dynamics at play that will shape your future.

The impact of individuals

For all the talk of "imperial CEOs" of public companies, these executives can't touch the influence of a family business leader backed by ownership power. The owners, a relatively small number of people (most family businesses are owned by far fewer than a hundred people), have ultimate authority over every decision in the business. They can fire the CEO, add or remove board members, change the strategy, sell the company, decide who can be an owner, and even cut the rosebushes, to name just a few things in their control. Family ownership keeps power in the hands of a few individuals. Who these individuals are and what they want will have a profound impact on their family business. And that impact will vary, of course, from business to business and family to family.

One US entertainment company has been quietly owned by one family for generations and has managed to grow and thrive with just one global brand, a rarity in the fickle, consumer-driven entertainment business, which is dominated by multibrand conglomerates such as Disney.

While the family CEO has had numerous opportunities over the years to buy competitors and diversify his portfolio, he held firm in his stance. This CEO—we'll call him Frederick—is clear: he just wants to own and run one company. Frederick is a man of routine. His calendar is set a year in advance, lunch is always served at 12:45 p.m., and he leaves the office on time to see his family and read books. "Owning many brands would be a pain in the ass," he told us. "Someone would need to run the businesses. And that someone would be me." Not one for surprises, he structures his life and his business in predictable ways. He likes to perfect his family business incrementally, prudently, and meticulously. And as long as he's in charge, that strategy will never change. Frederick would not have chosen to run his company any differently. His approach is fundamental to who he is.

By contrast, a European family business has a CEO we'll call Ian. During his thirty-year reign as CEO, Ian's family business acquired more than twenty-five companies in industries as diverse as automotive parts, insurance, information technology, and furniture manufacturing. The industry did not matter. Ian would buy low, upgrade management, find where price could be raised, and be off to the next acquisition. He would check in on the previously acquired companies only twice a year in day-long reviews of the firms' balance sheets and profit-and-loss statements—fancy strategy documents were left untouched. "Our strategy is to make money!" Ian would declare. He loved the thrill of the hunt and knew what he needed to be successful. After "retiring" at seventy-five, Ian purchased several businesses in Africa to keep himself busy.

You will find Fredericks and Ians in the story of every successful family business—leaders whose strategies deeply reflect their personalities. Without that person, without their "singular genius," the family business would probably be dramatically different. Put Ian into the entertainment company or Frederick into the conglomerate, and you would probably get radically different outcomes. The average CEO tenure in a family firm is at least thirteen years, compared with five years in publicly traded firms. With both more time in the seat and more decision power as an owner, these family CEOs put their personal stamp on their companies.

Despite the pervasive myth that only founders can have supersized influence on a business (think Sam Walton at Walmart), subsequent generations can also have a profound impact. For example, Rupert Murdoch took the modest foundation of his father's Australian media assets and built a global, multibillion-dollar empire. People such as Frederick (G3, third generation) and Ian (G4) play a role we call *creators*; they sit at the power center of their family companies.[1] As we'll discuss, other owners can play significant roles, too, even if they're not the CEO of the business.

But owners are far from the only people who, as individuals, make and shape important decisions in family businesses. Though they may not show up on the company's organizational chart or the ownership documents, spouses, children, cousins, in-laws, nonfamily executives, and board members can all influence a family business's direction. In a public company, it matters little who the CEO's spouse, parents, siblings, or friends are, but in a family business, these people can matter greatly. A nonfamily CEO who has the full support of the company's owners, even if those owners are relatively uninvolved, can also play a significant role in shaping a family business because of that support. (Think of the power and influence of *Vogue*'s longtime editor in chief, Anna Wintour, who had the enduring support of the legendary S. I. Newhouse, co-owner of Advance Publications, for decades.)

People's personal character plays a key role in directing the fate of a family business. For example, we met a family that is one of the largest landowners in Colombia. The father loved the game of business and passionately pursued creating more family wealth. Because his wife grew up in another, but conflict-ridden, family business, she was determined to give away their family fortune before she died. She urged that the profits from their family business be distributed, instead of reinvested, and then given to charity. Their son was indifferent to both the business and the family's wealth, happily pursuing a career as a ranch-hand on one of the family's cattle ranches. He is probably one of the world's richest cowboys. Their daughter, feeling profoundly guilty about her family's wealth, married a minister, and together they moved to the slums of Bogotá. None of these family members are on the same page about what the family should

do with the wealth their business creates—but they all have a say in what happens to it.

To anticipate what will happen to this company in the next generation, we have to understand what the daughter and son want for their family business. Will they divide it so that each of them can make a personal decision about what to do with their wealth? Will they move out of their current professions and take an active role in leading their business? Will one sibling want to sell to the other? The only thing that is certain is that their choices will be driven at least in part by their personal priorities, which have little to do with the business itself.

The seemingly irrational decisions of family businesses often reflect rational choices of thoughtful people who value things beyond higher profits. And since they own the company or influence those who do they can "want what they want"—be it growing through a personality-fitting strategy such as those that Frederick and Ian applied, or focusing on distributing money out of the firm, or directing the firm to combat climate change or poverty. As individuals with unique goals and desires, they get to chart their own course.

Make-or-break relationships

You can also decode your family business by examining the **relationships** inside it. Unlike in a nonfamily business, where clear boundaries usually separate professional and personal relationships, a family business involves multidimensional relationships that influence each other in profound, often unexpected, ways. In fact, three distinct types of relationships are simultaneously at play.

Family relationships are at their best when they are inclusive, forgiving, protective, and supportively challenging. They "trade" in emotions—love and some more negative emotions at times. Families are emotionally connected. And family relationships are the longest relationships of most people's lives.

Business relationships, on the other hand, are hierarchical; there's a boss and a reporting structure. They are usually meritocratic. If you

don't make the cut, you are fired or you leave. The average tenure of US employees is now less than five years. Businesses "trade" in competencies. You hire a vice president of manufacturing for the executive's knowledge and experience in the business issues you face. And the person is in the role only as long as the mutual investment makes sense for both parties.

Owner relationships come down to who has the voting control of the firm and who has influence through their voice, even without a vote. Owners "trade" in power and are part of an exclusive club: you are either an owner or not. In family businesses, unlike, say, at Apple, ownership is sticky. Most companies have limits on whom you can sell your shares to, and how. Exit and entry are not simple, quick options.

In your family business, each big decision you make—to curtail a dividend payment to your mom to protect your balance sheet, to buy out your cousin, to skip your family reunion, or to fire your brother—is within a complex expression of family emotion, business hierarchy, and owner power. Your decisions are never just straightforward business or family calls.

This complexity plays out in a staggering number of important relationships, each with a distinct tenor. For example, Ian, the conglomerate creator, is a son, a brother with two siblings, a husband, a father, an uncle, a cousin, a father-in-law, and a grandfather. In the business, he was the CEO, with twelve direct reports, and was chair of the board. As an owner, he has been a trustee, a beneficiary of the trust, an investment partner with his siblings, an investor who bought additional shares from his other family members, and a board member of their foundation. When you add it up, Ian has more than fifty important relationships.

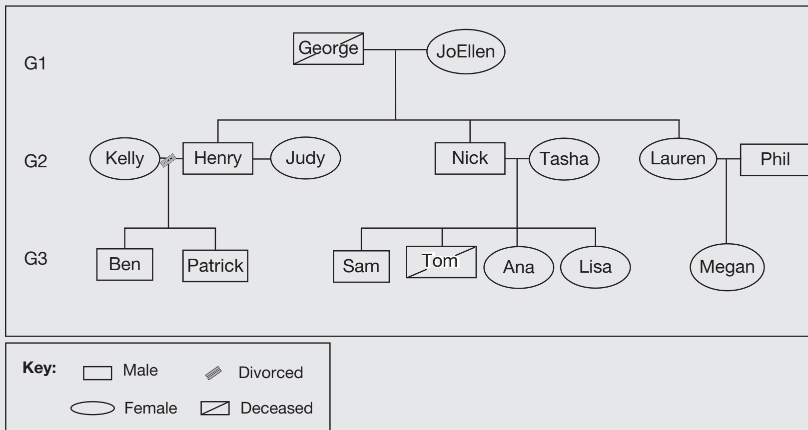
And each family member plays multiple roles with each other. Look at Ian's relationships with his sister, Alison. With Alison, he manages seven relationship roles: (1) her older brother, (2) a fellow board member, (3) the brother-in-law of Alison's husband (who served as CEO of their firm for two years and reported to Ian as board chairman), (4) a fellow trustee, (5) a fellow beneficiary, (6) a fellow foundation board member, and (7) uncle to Alison's son who is a board member. Such multifaceted relationships often lead to role confusion. Famously in the family lore, in a pique of frustration

Family business genograms

To begin to understand the complexity in your family business, identify the individuals in your family system and their relationships with each other. The system is probably more complicated than you think. Start by sketching a genogram (a family tree) with all your family members, including spouses, and going back to the generation that founded your business. A genogram helps you map a business family at a glance—and identify potential issues in the future (see "Further Reading"). In figure 1-1, we map the Dillons, a typical third-generation family business in the pet care industry.[a]

FIGURE 1-1

Sample genogram for the Dillon family



Note: G1, first generation; G2, second generation; G3, third generation.

a. The name and the nature of the business are fictionalized.

at Ian's domineering stance during a discussion, Alison once told him, "Ian, I'm your sister, not your employee. I don't report to you."

Two years after retiring as CEO, Ian, as chairman of the company board, was dissatisfied with the performance of his brother-in-law CEO, who was also Alison's husband. If Ian ousted his brother-in-law, a move that Ian felt was best for the business, how would the change affect his relationship with Alison? Relationships often involve triangles among three people (see "Further Reading" at the back of this book for more on this topic). With his brother-in-law in the hot seat, would Ian, Alison, and her husband still share holiday traditions at their family estate? Would the family fracture into branches? If the demotion were not handled well, would Alison's branch want to sell its shares? Would it trigger conflict among their children?

A single decision can reverberate for years—or even generations. Only family businesses face such relationship challenges.

System dynamics

A family business is a *system*, meaning that the people who are part of it exist within an interconnected environment that affects everything that happens. Yes, individuals and relationships drive much of the behavior in a family business, but each business faces legal, cultural, geographical, and other circumstances that also affect it in fundamental ways. System dynamics shape what happens in a family business, how people act, and even what they want. Four main system dynamics are at play: sameness, mutuality, competing interests, and unintended consequences. Let's examine them.

Sameness

Though your family business is unique, it will behave in predictable ways that are similar to some businesses and different from others, no matter your industry or the size of your business. For example, the stage of development of your family business will shape how it operates. In the seminal family business book *Generation to Generation*, Marion McCollom Hampton and coauthors describe three main configurations of these stages: con-

trolling owners, sibling partners, and cousin consortiums. The distinct patterns of behavior for each configuration are similar the world over. If you meet a family business owned by siblings in Australia or Austria, they will be facing some of the same challenges, no matter the industry or the size of the business.

The laws and taxes of your country and the culture your business operates in will create important similarities with other family businesses in your area. For example, if you live in a country that, like the United States, has high estate taxes, then you are likely to make decisions similar to those made by US businesses to minimize this tax impact. If you live in a country with minimal estate taxes, your choices will be different. Because of differences in these taxes, many large American family businesses are owned through trusts, while most of those in Brazil are not.

Cultural influences also affect the structure of family businesses. In some family businesses, for example, the eldest male in a generation is generally the preferred leader and the other males will usually be owners. The females in these families are seldom the owners but will be cared for by the family. Gender still plays a significant role around ownership in many cultures, with many family businesses bypassing women heirs in favor of men. All of these factors can mean that businesses in a wide variety of industries and sizes have much in common with one another in particular contexts.

Your situation probably has more in common with some other family businesses than you think. You can learn from their experiences.

Mutuality

Family business is a team sport. You win together, and you can lose together. The interconnected nature of a family business means that people can achieve some outcomes, arguably the most important ones, only by working together. Many family businesses want to pass the business on to the next generation. A common interest like this cannot be realized through mandate. Founders may want their children to take over for them, but if the next generation doesn't want to take on the endeavor, there is no family business. You can't simply will it to happen. Even the most powerful people in a family business must learn to compromise if they want to accomplish

goals that depend on the actions of others. In the long run, family businesses succeed by mutuality—making decisions that are of mutual benefit to family members. Common interests can only be achieved through collaboration.

For example, spouses can play a significant role in how the next generation sees the family legacy and business. If they are not treated well, they can find ways to keep their children less involved with the family. Unhappy in-laws can discourage their children from attending family gatherings or accepting internships in the family business. They could also advise their children against seeking a career in the business. Your family business will struggle without their support.

Competing interests

System dynamics create competition inside a family business. *Fundamental attribution error* is what social psychologists call the human tendency to attribute people's actions to their personalities rather than any other causes, such as their situation. You might be quick to dismiss the objections of a family member who is the odd one out and you think this person is always just trying to be a contrarian. But in reality, they might be looking at a business decision through a different lens and are just expressing an objection in a clumsy manner. The family member might have a worthwhile point that you will never consider, because you assume they're just being stubborn. Perhaps a better way to understand behavior comes from the expression "Where you stand depends on where you sit." People's wants depend significantly on their position in the family business. Since those positions will differ—consider, for example, the controlling owner versus someone uninvolved in the business but dependent on its dividends for financial security—individuals will have competing interests.

Competing interests typically emerge over time. In the founding generation, one person, or a married couple, often owns all the shares and heads both the business and the family. No competing interests seem to matter, since the founder is viewed as having the power to make all the trade-offs between the business, ownership, and family decisions. The founder's reason behind a rule is often simply "Because I said so!"

But as your business expands to new generations, with many more people involved, multiple competing interests arise. Well-intended people can want plenty of things—dividends, company growth or its sale, status, love, recognition, and jobs for themselves and the next generation, to name a few. Competing demands are put on the business, the owners, and the family.

In the 1980s, two professors at Harvard Business School—Renato Tagiuri and John Davis—created what's known as the *three-circle model*, which shows three overlapping circles—family, business, and ownership—in a Venn diagram. People can occupy multiple sections of the Venn diagram. For example, a family member can also be an owner and an employee of the company, wearing three different hats at any given time.

This simple depiction highlights the likely interests and roles of the people in a complex family business system. The seven roles have distinct, often conflicting, and largely predictable interests (table 1-1).

As families and businesses expand, people inevitably compete for what they want in predictable ways. With this perspective, you won't wrongly attribute behavior to personalities: "Seth is lazy," "Aunt Laureen is a control freak," "Dad never wants us to enjoy our family's wealth; he only cares about the business," and so on. When you consider how each person's role in the family business system influences their interests, you'll better understand the influences on their behavior and decisions—and you can avoid the fundamental attribution error.

Before going any further, fill out your own version of the table (you may not have someone in each role). You'll see that your point of view—and that of others in your family business—may not always be the same.

Think of a recent difficult decision in your family business, such as how to fire a family executive, buy a family member out of the business, create a board, or transfer ownership to the next generation. See if your new knowledge of the connection between people's roles and their primary interests can help you appreciate where people stand, given where they sit. Note their common interests and their conflicting interests. By looking at each person's interests, you will get useful insights on why things are happening at your family firm. The reasons will be varied, of course, but not so perplexing.

TABLE 1-1

The seven possible roles in a family business

Role	Example of the role	Examples of primary interests
1. Family owners who are employees	Creators such as Frederick and Ian	Invest to grow the value of their company, perform meaningful work, steward the company
2. Nonfamily employees	A nonfamily chief financial officer (CFO)	Progress career, protect their job, be fairly compensated
3. Nonfamily owners	An outside investor in the company	Increase the economic value of the company and the financial distributions from the company
4. Family members who are not employed and are not owners	Spouse of an owner	Protect their nuclear family, especially their spouse and children, from harm; have employment and financial opportunities for their spouse and children
5. Family members who are employed by the business but not (yet) owners	A daughter who recently joined the family business at an entry-level job	Build a career, aspire to be an owner of a thriving firm
6. Family owners who are not employed at company	Stay-at-home parent who is an owner	Steward the company well, increase the value of the company and the financial distributions from the company
7. Nonfamily employees who are also owners	A CFO who has been granted equity but is not related to the family	Build their career, protect their job, be fairly compensated, and grow the value of their equity

Unintended consequences

You can never do just one thing.[2] Does this saying sound familiar? You try to fix one problem but, in the process, create a bigger problem elsewhere. We worked with one family business run by three brothers who wanted to avoid a situation where any two of them could gang up on the other. So, they set a rule that any major decision required unanimity. This approach worked out fine when it was just the three of them in the business and their interests were more or less aligned. But it broke down when the next generation entered the company and each brother became more narrowly focused on what was best for his children. Since any of the three brothers could block a decision, they often ended up in a deadlock.

In a complex system, actions have ripple effects. A well-known example is the butterfly effect, where a hypothetical butterfly flaps its wings and sets off a series of events that cause a typhoon on the other side of the world. This hypothetical property of chaotic or complex systems suggests that when actions are interconnected, small things can have major impacts that are nearly impossible to see until much later. You can never really just change one thing in a family business; a single change almost always triggers other consequences as well. When you take a stand or make a major change, you will often create an outcome that is different from, or even the opposite of, what you originally intended.

Family businesses are deceptively complicated. Consider the family arguing over rosebushes at the beginning of this chapter. As we worked with the family, we quickly came to realize that the fight wasn't really about the roses. It was about years of slights, power plays, and lingering wounds, but also about everyone's deep desire to preserve their parents' legacy. The battle over the rosebushes was merely a proxy for their difficulty making decisions together as a group. The family members were eventually able to see this problem for themselves.

Once you grasp how family businesses work, you can see how an apparently irrational decision might make perfect sense in your family business. More importantly, you will come to understand your family and your business better. Focusing on the right problems can help you maintain both a great business and a great business family. And hopefully, you will then avoid wasting precious time arguing over roses.

Summing up

- There are three "levels of analysis" to decode the unique dynamics of a family business: individuals, relationships, and the system. As you read through this book, you'll find many examples of where these three levels are key to understanding what's really going on.

- Relatively few **individuals** shape what happens in a family business. Figure out who those key people are. Then try to understand their personal history and how it influences how they act today, as well as what matters most to them (i.e., their interests) in their various roles.
- Within your family business are complex, multidimensional **relationships** that cut across the different cultures of families, businesses, and ownership. Assess where relationships are strongest in the family (e.g., generations or branches). Look for particular relationships that have significant tension and try to understand why. Consider the potential reverberations across relationships as you make decisions. And look for those with broad relationships that cross boundaries that can help make change happen.
- A family business is a **system** that is shaped by the environment around it. Be on the lookout for the explicit or implicit rules that shape behavior in your family business. As you navigate your system, remember these points:
    - Your situation probably has more in common with some other family businesses than you think. You can learn from their experiences.
    - The most important outcomes require collaboration. No one has absolute power.
    - Competing interests are inevitable. And where each person stands on an issue has as much to do with their position in the system as it has to do with their personality.
    - Actions often have unintended consequences. Try to think through the second- and third-order effects before you make major changes.
- Keep an eye out for changes within your family business that affect dynamics at the individual, relationship, or system levels. When those changes happen, expect that the previous rules may no longer apply.