Insight for family enterprises presented by the Sauder School of Business

Selling the family business not a panacea for solving problems, say experts

In Canada, family enterprises are unparalleled engines of our economy. Sadly, challenges ranging from interpersonal conflicts to insufficient succession plans too often result in many family-run operations failing to transition to future generations.

This sorry reality has prompted business family experts to urge business-minded clans to consider their options before selling the family enterprise and potentially facing a lifetime of regret.

"Family enterprises grapple with family dynamics and communication issues," says Diane Friedman, a Vancouver-based business family advisor. "The traditional family as we imagine it is not reality for most (business) families. There are a host of issues – 'fair versus equal,' competency, competitiveness, divorce and mental illness – that no one really wants to talk about, but they become critical to the succession process."

Noel Golden, a partner at legal firm Borden Ladner Gervais, says common problems and conflicts often stem from the blurred lines between the family, the business and ownership. "In addition, the leader may be resistant to formalizing structures and systems necessary for the business to flourish in a transition. It can be a barrier to building the abilities and independence of the next generation that enable them to take over."

Often, an inability to communicate about difficult issues leads to entrenched conflict. That conflict may lead to the conclusion that selling the business is the only alternative – but a sale may only transfer the conflict into the distribution of assets and beyond, leaving the family mired in regret and recrimination, he says.

To achieve a successful transition, a framework is required for communication, decision-making and accountability within the three realms of family enterprise: the family, the business and the owners, says Mr. Golden. "These decisions affect not only those people directly involved in the transaction – owners or workers – but everyone within the family system. Understanding everyone's goals and objectives is essential to success and harmony in the family."

The habit among business owners to overestimate the value of the business is another common pitfall. "Sellers are emotionally attached to their business because it's been their life's work," says Mr. Golden. "But the sweat-equity a vendor puts into a company is only relevant to a buyer if it shows up in the company's numbers, financial strength or prospects for growth."

He suggests a professional evaluation of the business, but warns that even a thorough economic analysis doesn't provide all the necessary data for decision-making. "You have to assess the family dynamic. Might there be a missed opportunity for the children to continue the life-work of the founder? Do family members involved in the business have replacement activities planned?"

Professional advisers can play an important role, helping families transform conflict into a positive mechanism for change, says Ms. Friedman. "Start early, and be prepared to invest the time. It can take three to five years to prepare a business for sale, and 10 years or more may be more appropriate for a family transition."

When considering the sale of a family business, owners are encouraged to consider not only the economic and workplace ramifications, but also the potential impacts on the family and its members.

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about

The Business Families Centre at UBC's Sauder School of Business is a one-of-a-kind resource for business families, their advisors and other professionals. The BFC provides services that touch on every issue relevant to the business family, including governance, relationships, advisors, wealth preservation and succession.

SAUDER School of Business

Business Families Centre

For more information, call **1-877-764-1232** or visit **www.FamilyEnterprise.ca**

EXPERT OPINION

When determining your business's worth, see the big picture

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For owners of family firms, it is not solely material value that counts when they assess what their company is worth to them.

While this idea may not be new, our research demonstrates – for the first time – that when owners reflect on an acceptable sale price for their ownership stake, they tend to value socio-emotional aspects next to financial aspects, creating a gap between their perceived value and the price they might objectively expect to achieve in a sale. On average, our findings suggest that owners tend to overvalue their ownership stakes at about 30 per cent above market value.

The strongest driver of what we call "emotional value," the gap between the owner-perceived value and market value, are the intentions of the owners to pass on the firm to the next generation. In the presence of strong transgenerational sustainability intentions, owners had a stronger inclination to overvalue their firms.

Owners also differentiated between types of buyers: comparing acceptable sale prices between family and non-family buyers, we found owners were willing to sell at a 20 per cent discount to family members in comparison to a sale to a non-family buyer.

We also found evidence that, with increasing duration of family control, the owned firm developed an "heirloom meaning," inducing owners to further heighten emotional value and acceptable sale prices.

Just as importantly, our research shows that physical and mental stress may induce owners to withdraw and reduce sale prices. We also found that, in cases of overt conflicts among family owners, the owners priced the efforts put into the conflict and sought compensation for conflict-related 'sunk costs.'

When they think about selling, the values that owners assign to the emotional and social aspects of controlling a firm have a strong impact on their offering prices. In our research, we were able to correlate monetary figures with these emotions – findings that have significant implications for the likelihood of actual sales, as well as for the choice of acquisition targets for potential buyers seeking to acquire privately held firms.

CASE STUDY: REFRIGERATIVE SUPPLY

Family gained financially, but still feels loss of selling business

When the Strand family realized that significant investment would be required to upgrade the equipment within their company – a manufacturer and installer of insulated panels for cold storage warehouses and food processing plants – they focused on the financial risks.

Regrettably, they didn't consider the risks of an optional sale as thoroughly. "My father started the business in 1969; in September 2006 we sold it to the largest company in the world in our business (sector)," says Larry Strand, the company's former president.

While he says it was probably a good decision to sell, Mr. Strand notes that he and his sisters still ask themselves if it would have been wiser to keep the business in the family. "Could we have made it work? Probably. And if we had taken that next step, it would have been a far bigger business had we decided to sell it later."

The variables the family didn't consider, he says, were the loss of identity and pride associated with owning a respected business. "When we sold the business, we believed the new company would keep our family culture. We stayed on as employees, but we've all now left with the exception of my father, who provides some consulting."

The Strand family continues to feel the loss. "We had dinner every Sunday night and talked about the business. Sometimes the discussions got heated, but we enjoyed the business and the prestige associated with it."

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