When a Family Business Needs Outside Talent

KEY TAKEAWAYS

- A family may not have a deep enough bench of members to maintain the success of a family business.
- Non-family executives should understand, appreciate, and share a family's values and vision.
- A combination of compensation methods may be needed to attract top talent.

In many ways, family businesses are the foundation of the economy. Their ongoing success has a pronounced ripple effect, benefiting other businesses and society at large.

But many family businesses—especially those involving multiple generations of family members—often face a big challenge: finding the executive-level talent they need to survive and thrive for the long term.

Family businesses are well served when they develop younger family members to join the company. These people have often grown up in the family business and, consequently, share the value and norms of the family.

Unfortunately, it's rare for a family to be the sole source of high-quality talent that can continue to lead the business.

As a result, families often have to go to outsiders to ensure they have the range of expertise and capabilities to perpetuate the family business. This need to go outside the family can become especially critical when younger family members pursue different career choices rather than join the family business.

Finding and nurturing top non-family talent can be complicated. The family business must be an environment in which capable, determined executives can succeed and are rewarded for their accomplishments.

Family businesses have used numerous approaches over time as they seek to have their businesses managed by exceptional and dedicated people. There are often three aspects to having the best talent (see Exhibit 5):

- Selecting executives with demonstrated competence
- Focusing on the family's values and culture
- Providing motivational compensation arrangements

EXHIBIT 5
Ensuring the Family Business Secures the Best Talent

Selecting executives with demonstrated competence

When bringing outside talent into the family business, there are many criteria the family can use to evaluate quality and competence. Some of the biggest factors are the person's track record of accomplishments and temperament. These help the family see what the professionals have done in the past and how well their previous successes relate to what the family is looking for.

This assessment tends to be somewhat harder when it comes to family members. When family members start at or near the bottom of the company and move up, their abilities can be assessed. Another approach is to have family members demonstrate their competence by working for other companies before joining the family business. This ensures these family members are committed to the family business. They are also likely to bring new ideas to the family business.

Focusing on the family's values and culture

Unlike family members, non-family talent doesn't automatically know the values and culture that underlie and support the family company. They need to be formally trained in this area.

Educational programs as well as meetings that concentrate on family history and values are often useful in getting new non-family members up to speed. These are also good ways to clarify what is important to the family. In these sessions, it is often useful to discuss strategic decisions that were shaped by the culture within the family.

Another approach sometimes used by family businesses is to have non-family members become immersed in the values and perspectives of the family business. This might mean hiring non-family executives in the lower ranks of the company and having them "work their way up"—which can be an effective way to ensure the non-family professionals develop the same values as the rest of the family.

We find that many family businesses are strong believers in lifelong learning. Specifically, to keep the company competitive and successful, family business executives—both family and non-family members—need to always be expanding their knowledge and improving their skills.

Such lifelong learning takes a number of forms (see Exhibit 6):

- Coaching services, whereby executives work on developing and refining their managerial and decision-making skills
- Executive education programs offered by universities, consulting firms and a variety of training facilities
- Peer-to-peer support groups, often referred to as mastermind groups, in which executive members share experiences and solutions to business challenges they've faced

EXHIBIT 6

Lifelong Learning

When these learning resources are aligned with the perspectives of the family business, the attendees are likely to better understand the values and culture of the family business.

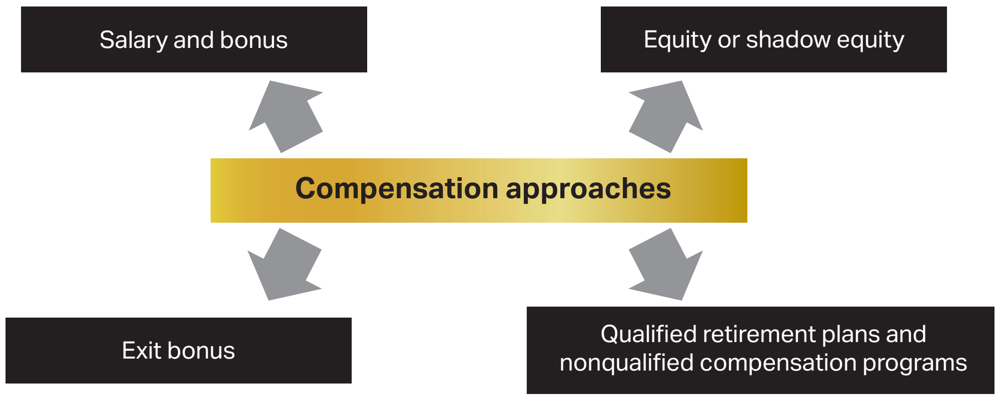
Providing motivational compensation arrangements

Not surprisingly, non-family executives care about how (and how much) they are being compensated for their expertise and commitment to the family business. In any scenario, the more that compensation is results-based, the more it is perceived as equitable—and the more motivational it becomes.

A number of approaches can be used to construct a compensation package (see Exhibit 7). They include:

- **Salary and bonus.** The more closely the bonus is tied to performance, the better for all involved.
- **Shadow equity.** Whereas family members might have equity in the family business, the tendency is not to offer equity to non-family executives. Instead, shadow equity (also known as phantom stock) can sometimes be used. With shadow equity, the aim is to mirror the performance of the equity in the family business.
- **Exit bonuses.** These are usually put in place to compensate executives if the family business is sold. This approach is commonly seen as a safety net for non-family executives, who often don't have much of a say in the sale of the company.
- **Qualified retirement plans and nonqualified compensation programs.** These plans enable senior management to build up funds in retirement. Very often, when non-family executives are not given any form of equity, nonqualified compensation programs are effective in helping lock them in and motivate them.

EXHIBIT 7
Compensation Approaches



Often, a combination of these approaches (and some others) is needed to keep non-family business executives highly engaged and committed to the success of a family business.

Conclusion

Ultimately, family businesses may need to look beyond their circle of family members for leadership that can help them excel. Outside executives must be highly capable, of course—but they should also fit in well with the family business's culture. For

VFO Inner Circle Special Report
By Russ Alan Prince and John J. Bowen Jr.

Unless otherwise noted, the source for all data cited regarding financial advisors in this report is CEG Worldwide, LLC. The source for all data cited regarding business owners and other professionals is AES Nation, LLC.