Stages and Transitions: Managing Change in the Family Business

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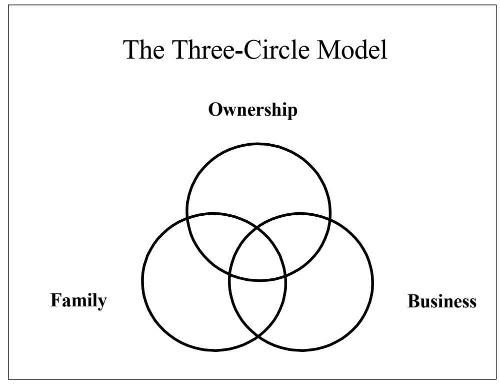
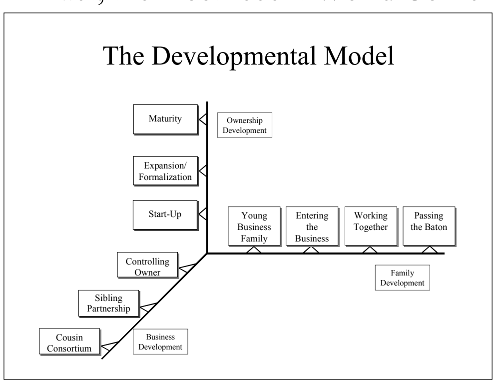
For the past decade and a half, the primary conceptual model of family business has been the three-circle model, which views family enterprise as a complex system made up of three overlapping sub-systems (ownership, business, and family). The three-circle model is an excellent tool for understanding the dynamics at work in any family company at a particular point in time. In our more recent work, we have found it even more useful to transform this three-circle concept into a developmental model, in which each of the three sub-systems moves through a sequence of stages over time.[1] In our developmental theory, for example, family business ownership moves from a Controlling Owner stage to Sibling Partnerships, and then to Cousin Consortiums, or the company itself changes from a Start-up through other stages to Maturity. Many of our colleagues have offered similar elaborations. In fact, the most recent World Conference of the Family Business Network was organized around three stages in the development of family business ownership. There is no doubt that specifying the stages of family, ownership, and business development enhances our understanding of any family business.





However, while we continue to learn more about the special nature of each stage, we have now become particularly interested in the periods of change between stages: the transitions. Every stage theory must describe some mechanism, which takes a system from one stage to the next. Why focus on the transition periods? Because they are the most critical and challenging moments in the development of family enterprises. Transitions are often periods of uncertainty when the decision-makers feel most anxious and vulnerable -- understandably so, because that is when the organization makes fundamental choices that will profoundly shape its future.

By calling attention to the transitions, we do not mean to imply that periods of "stability" within each stage should be taken for granted. The transitions are opportunities for reassessment of the course the business is following, and *fundamental change*; the periods in the middle of a stage, when the firm is committed to a particular ownership structure or organizational design, are the major opportunity for *focus and growth*. Both change (transition) and growth (stability) are essential for success and continuity, although they require different kinds of work. The tasks of transition periods are exploratory and strategic; the tasks during periods of "stability" are operational and tactical in nature. Put another way, during the transition we may consider all options and decide which mountain to climb – often while the army cools its heels in the valley and waits. Then, during the stable period which follows, all our efforts are focused on climbing the chosen peak, without a moment's wasted thought about the other mountains not chosen. Understanding these differences, and the essential alternation of change and stability, is critical for the effective management of a family enterprise over time.

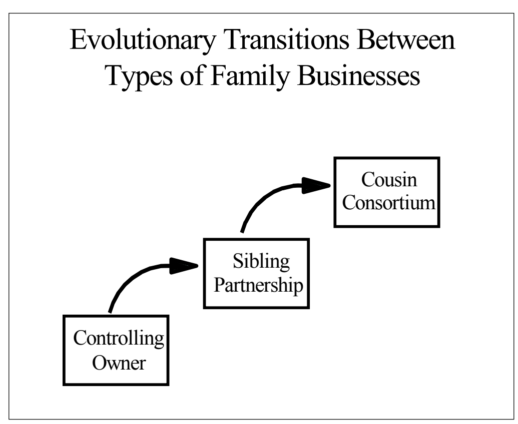
Our current research is focused on exploring transitions along the ownership axis. The stages of family business ownership in our model are Controlling Owner, Sibling Partnership, and Cousin Consortium. In previous work, we have identified three types of ownership transitions between these three stages:

1. **Recycles** (changing individuals, but retaining the *same* basic structure of ownership):
   Controlling Owner → Controlling Owner
   Sibling Partnership → Sibling Partnership
   Cousin Consortium → Cousin Consortium

2. **Devolutionary Transitions** (moving to a *less complex* structure):
   Sibling Partnership → Controlling Owner
   Cousin Consortium → Sibling Partnership
   Cousin Consortium → Controlling Owner

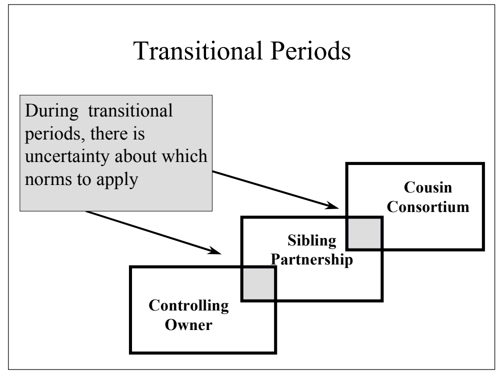
3. **Evolutionary Transitions** (moving to a *more complex* structure):
   Controlling Owner → Sibling Partnership
   Controlling Owner → Cousin Consortium
   Sibling Partnership → Cousin Consortium

In this paper, we will briefly explore evolutionary transitions, as family companies mature through their lives from simple owner/manager control to the more complex later-generation forms. Demographic trends throughout the western world suggest that evolutionary transitions are on the rise. There are many likely reasons for this. The departing WWII entrepreneurs (COs) are leaving behind many more sibling partnerships (SPs) and cousin consortiums (CCs). The changes in communication, transportation, and the vast expansion of effective markets argue in favor of larger, multi-faceted firms. Finally, from the family side, the bias towards single ownership may be diminishing in part because some of the old inheritance practices (such as the unequal treatment of women and strict primogeniture) are no longer the norm in many societies.

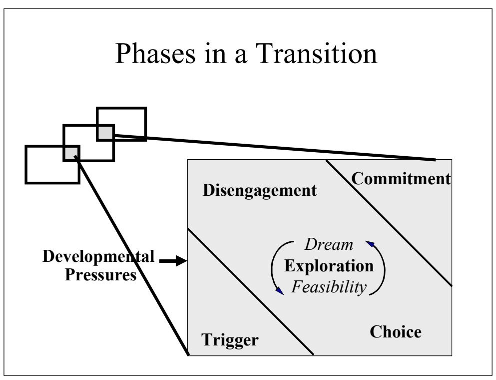


I. Six Components of Transitions

How does ownership in a family company evolve over time? Obviously, the movement between ownership stages does not happen instantly. (In fact, many systems can exist as a hybrid of two stages for an extended period of time.) However, our fundamental message is that periods of transition between stages do occur at predictable times and follow a typical course. More importantly, we believe that understanding the underlying structure of transition periods is probably one of the most useful things we can do as academics, professionals and as business owners. If we learn to manage these periods more effectively, we can dramatically increase the chances of family business continuity.



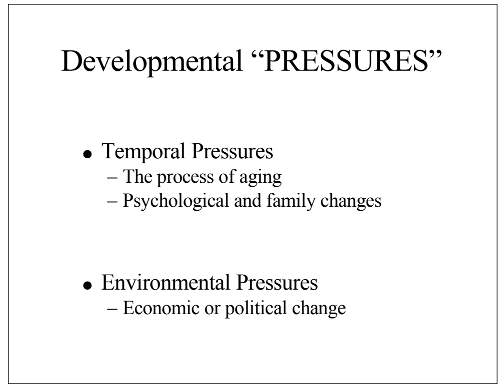
We believe that this is a general model of system change, applicable to a broad range of family companies at every stage. For example, while there are basic differences in the issues that arise in the transition from Controlling Owner to Sibling Partnership (CO → SP) and those that arise in the transition from Sibling Partnerships to Cousin Consortiums (SP → CC), there is a fundamental structure to transition periods that can allow us to understand and predict them. The overall time span of a transition may be a few months or several years, depending on the type of transition and the complexity of the system. But we believe that all transitions from one stage to the next follow the same basic pattern, beginning with the continuous accumulation of developmental pressures, and continuing with three additional components:



Our research suggests that there are six distinct components of transitions. The first is a characteristic of the inter-transitional time that draws the system toward the transition. The remaining five are stages in the transition itself.

- **<u>The continuous accumulation of developmental pressures</u>**

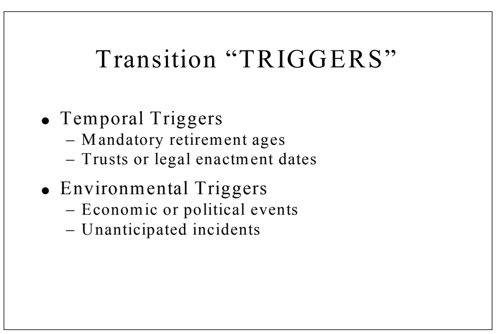
One metaphor that captures the nature of the forces that propel transitions is the glacier. A glacier, like a family enterprise, is a growing, working system -- constantly interacting with its environment, and balancing movement with stability. The forces at work in a glacier as it moves across the landscape are powerful and complex, but they are largely invisible. Over time, as the pressure builds in the river of ice, it is preparing for change. Then suddenly, when it has reached a state of "readiness," it may only require a momentary trigger to initiate the calving of huge sections from the edge of the glacier into the sea, giving the glacier itself a new shape.



In the same way, the developmental pressures that accompany families and their businesses are constantly at work – creating the need for, and a readiness for, change. Individuals age, the family dynamics evolve, and the economic environment is continually in flux. Like the glacier, family enterprises normally resist change for as long as they can, protecting their habits and routines. But sooner or later the pressure to change becomes irresistible. At those moments of "readiness," important changes most often happen in concentrated bursts, initiated by a trigger – one action or event. Once the transition has been triggered, all the accumulated pressure is activated, and the system has an opportunity make the fundamental changes which bring it more in alignment with its resources, environment, and goals. For a moment, immediately after the transition, the new shape of the glacier is in homeostasis. The forces are relieved, and everyone takes a deep breath. And then, the developmental pressures begin again, starting the process over which will ultimately lead to the next transition – perhaps far in the future.

- **<u>The trigger</u>**.

The trigger that sets the transition in motion can be either a temporal "alarm" (such as the approach of a mandatory retirement age), or an event (such as a health crisis or a dramatic conversation). It is surprising that the trigger may seem insignificant in itself. This is because, in Shakespearean terms, "the readiness is all." The energy for the change comes from the accumulated developmental pressures in the system; the trigger is just the spark that starts the action. To return to the metaphor, a glacier can be under such internal pressure that the shout of a tourist from a passing ship can be enough to trigger the splitting off of hundreds of tons of ice. In the family business, it can be an event in the life of one of the key leaders, a meeting of the board, or an occurrence on the shop floor or around the dining room table, that sets the transition in motion.



Once the transition has been "triggered," the actual work begins. Transitions are composed of three sequential tasks.

- **<u>Disengaging.</u>**
  This is the first task, to acknowledge that the era of the old structure is coming to an end, and a new one must be found. In ownership transitions, disengagement is often symbolized by a public commitment to a retirement or share transfer date, or a schedule for the career advancement of leadership candidates in the next generation.

- **<u>Exploring alternatives</u>**.
  This is the most critical work of the transition. It involves considering different forms for the new ownership structure, and then measuring their viability against the dreams, talents, and capabilities of the participants. This is a process of testing, learning, and revision. It may happen quickly, or be prolonged over several years. Managing this exploration phase is the most important leadership challenge of transitions.

- **<u>Choosing</u>**.
  At some point, one alternative must be selected and the rest put aside. While this task is often given the most attention, it is actually only one step in the process, and can only be successful if it follows an adequate preparation.

These three tasks may happen in a direct sequence, and the time span may be relatively short or long. Alternatively, some families move back and forth among tasks. They may announce an impending change, but delay exploring alternatives. In those cases the "developmental pressures" continue to build, and since the transition has already been triggered, the force of the pressure is enhanced and the system usually experiences uncomfortable and disruptive stress. Other families begin to explore a limited set of alternatives, and may even make a preliminary choice, but then become aware of important flaws in the chosen path. This may send them back to the exploration task, casting the net more broadly this time. Whatever the sequence, a successful transition ends with some clear choice, when competing alternatives are put aside, and the system moves to the final transitional stage.

- **<u>Commitment to the new structure</u>**.
  The choice does not mark the end of the transition, but instead must be solidified with a closing phase of commitment. At this time, the family enterprise formally declares itself ready to operate differently. It involves actually implementing the changes in the structure, and helping (or requiring) the environment to deal with the new system. These tasks often include the withdrawal of the prior leaders from critical roles in operations, important changes in support systems and individuals, and the implementation of new policies and routines.

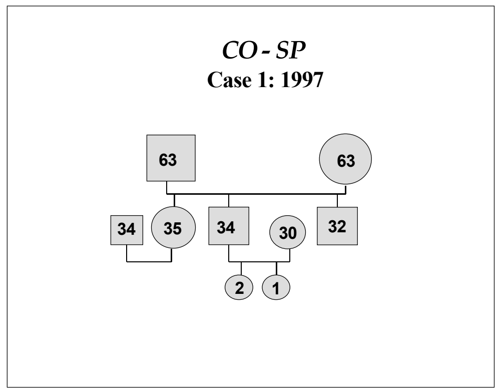
II. Case Examples

The following series of case vignettes, taken from our experience with actual family companies undergoing evolutionary transitions, are designed to illustrate the concept of transitions described above. Each case highlights two or three of the transition stages.

Case #1

In the first case, the family had been casually discussing but avoiding action on an impending transition from Controlling Owner to Sibling Partnership.

⇒ ***Developmental pressure***: The three siblings all vehemently opposed the non-family successor chosen by their father a year before. The father brought in the non-family successor because he believed his son was not capable of succeeding in the job. The father had spent a lot of money to find and recruit the person about whom the siblings now had so much concern. All the offspring felt he was eroding the distinctiveness of their products and image, and was offensive to family members. Their complaints and criticism had been steady, but without any observable impact on their father.



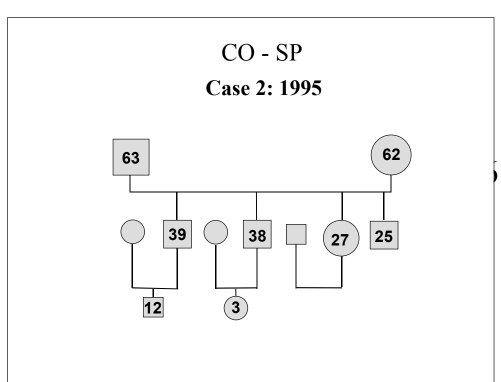
⇒ ***The trigger***: The middle son declared to his parents that he was at the end of his tether, meaning he just could not cope anymore - he'd been stretched far enough. He announced that he was now making plans to take his wife and children (both under two years old) away. The father made no response, which was his typical way of dealing with his offspring's demands. This time, however, the mother then said to her husband: "If he is leaving the area, then so am I. I am not losing my grandchildren over this. This man you have brought in is splitting our family and ruining what we've created." This was the first time the son could recall that his mother had ever backed him against her husband.

⇒ ***The transitional tasks***: Within one month, a number of major moves had taken place. 1) the non family manager was gone; 2) the father went to his lawyer, bank and accountant to find a way of passing the entire ownership of the business equally to his children; and 3) the eldest daughter was appointed managing director. When asked by outsiders what led to such a sudden retirement, the father said that with a change of government now becoming inevitable, he had been advised to save tax by handing over the business before the election.

Case #2

The second case illustrates how the transition tasks can be approached in a style that follows the company and the family culture.

⇒ ***Developmental pressures***: The Controlling Owner father was



anticipating his retirement and the concurrent retirement of a key manager. Both departures required significant financial planning for the company. His wife was making plans for their retirement "life structure" which meant a new home, exploring outside interests, and travelling. There were four adult children working in the business. The eldest has a muscle-wasting disease, and the family was increasingly aware of deterioration in his condition. Three of the four siblings (excluding the one who was ill) were having fights that were becoming more serious.

⇒ ***The trigger***: The glacier cracked when the father suddenly stated his wish to be completely out in 15 months.

⇒ ***Disengagement*** was accomplished when the father made a public commitment to his decision, and the family set a timetable for all the things that needed to be attended to in the forthcoming year and a half.

⇒ ***Exploring Alternatives*** involved an intense period of education about family business, and facilitated family meetings. They were interested in governance, and explored options for dealing with issues of ownership, business and family matters. This led them to work as a sibling team on a process for choosing a non-executive adviser to re-design their boards and instruct them in how to professionally run their growing business. Through some exercises, it became obvious that despite their differences, they all shared a common Dream: that the business should be preserved and protected so that their family could benefit from it as their parents had wished.

a) The *Choice* for this family was a sibling partnership, although they have not yet resolved all the issues of equity and leadership. United in ownership, and controlled through good business practice in the boardroom, they started to see how they could make things work for themselves, rather than struggle against each other.

⇒ ***Commitment***: At this time, the system is still moving back and forth between acknowledging and consolidating these new structures, and reverting back to the earlier phase of *exploration.* In the past, when unresolved issues came up, the siblings would normally not "take hold" for fear of making mistakes, and would defer to their father. However, the system is moving in the direction of commitment and exit from the transition. On a recent occasion when the father and mother were away on holiday (this vacation itself was evidence of "letting go"), a crisis emerged. With the support of their adviser, the siblings took hold of the problem, held an emergency meeting and sorted it out. Their father was not aware of the problem - and its solution - until he got back from holiday. He had mixed feelings; he missed being involved but was pleased they had proven themselves.

A further sign that they are moving towards exit came when the siblings asked their father not to chair the board meetings (his meetings went on too long and did not focus on the agendas). Later they asked if, since he was no longer officially a board member, it would be OK if he did not attend and they just shared the minutes with him. They acknowledged that this was their way of defending the new stage, and moving past the transition.

The third and fourth case examples concern the transition from the Sibling Partnership stage to a Cousin Consortium. While the structure of the transition remains the same, each phase plays out differently at this stage in the development of the family business. Returning to the glacier analogy, there are older, more mature glaciers which are not a single river of ice, but rather a network of many streams, which approach the sea as fingers extending from the glacier's arm. The developmental pressure that has built up in the glacier is not distributed equally to all of the fingers. As a result, a trigger, like the tourist's shout, may have an impact on some fingers, and no impact on others.

In the same way, Sibling Partnership to Cousin Consortium transitions are more complex, involving many more individuals and organizational components. With a large number of in-laws and cousins who often are strangers to each other, and with some shareholders who might be far removed from the company, the critical work of the transition involves being aware of the wide range of views and uneven readiness for change. In particular, triggers work differently in these transitions. As we saw in the first two case examples, in the Controlling Owner to Sibling Partnership transition, the energy that is required to initiate the transition has to make only one person move: the controlling owner. In these Sibling Partnership to Cousin Consortium transitions, the triggers have to energize a sibling group, who may be at very different stages of personal development. The challenge as the transition begins, particularly for those individuals in leadership roles, is to generate and channel the energy of the system (coordinating the pressure in all fingers of the glacier) to bring all constituencies to a degree of readiness that will allow them to begin and sustain the transition process.

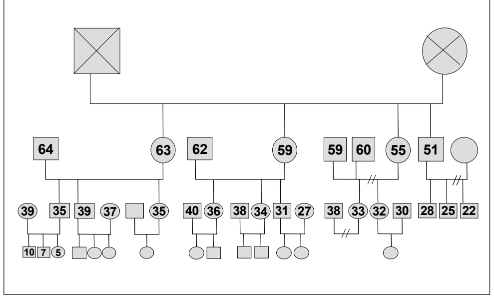
Case #3

In our third case example, the senior group was composed of four siblings with an age spread of 12 years, three sisters and a younger brother. The CEO was the husband of the older sister.

⇒ ***Developmental pressures***: The CEO was approaching the mandatory retirement age (a looming temporal trigger) and his outside directors were forcing him to plan his succession. But the younger siblings were not ready to consider retirement for themselves. The cousin group was eager for their place under the sun, and were asking the seniors questions about transfer of ownership and career opportunities in the business at the very senior levels. They also felt that the siblings' informal arrangements were not sufficient for them and were asking for more structure and policies. In addition, the environment was offering the company new opportunities for

SP to CC

Case 3: 1997



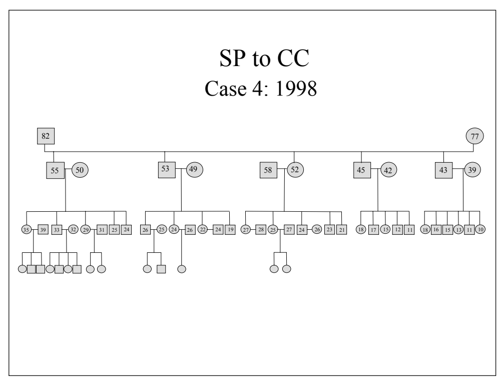
growth.

⇒ ***Triggers***: Different triggers initiated the transition for different "fingers" of the system. The senior branch was triggered by the impending birthday, signifying retirement. The trigger for some of the other branches, however, came from a completely unanticipated event. A family member in one of the branches that was not involved in the business, was a victim of a violent crime and was in a coma for many months. The victim's branch of the family expected that he would receive financial support from the business, and they were infuriated when he was denied access to it. This caused a power struggle amongst the branches, triggering the younger siblings to start talking about transition.

Case #4

Similarly, in our fourth case example, the senior group was composed of five siblings with an age spread of 12 years. They had taken over the leadership of the company in a very orderly fashion when their father was still alive. The oldest brother was the CEO/Chairman. Although he had been very dominant and his siblings frequently had to reign him in, the mix of complementary skills and a relatively healthy sibling bond had allowed the Sibling Partnership to maintain a very workable relationship.

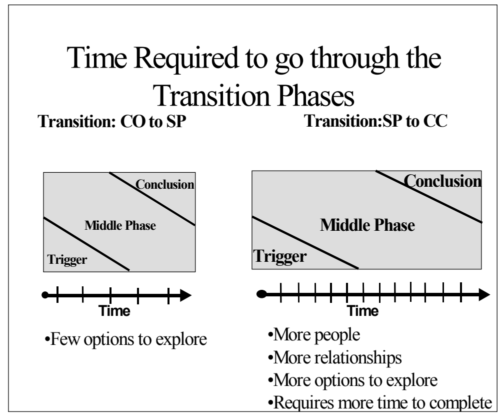
⇒ ***Developmental pressures***: The entry of the cousins into the business raised concerns over how the transition was to be handled. Health concerns were also a major factor. The older brother had hypertension and had a history of heart problems. In fact all three older siblings had weight problems and had serious brushes with death.



⇒ ***Triggers***: The transition was set in motion by two triggers. The company was ripe for a strategic repositioning and had hired a consulting firm to help them with a strategic plan. The plan, calling for an elaborate investment of money and time, caused the oldest brother to complain that if he was to spearhead the effort, he was interested in receiving a handsome retirement package. A second trigger was the death of the founder. These two stimuli confronted the siblings with the fact that they needed to take responsibility for charting the future of the system, and the transition began.

Both of these cases have just initiated their transitions, but they already illustrate some distinctive features of the "task" phase of Sibling Partnership to Cousin Consortium transitions. First, *disengagement* will be more prolonged and complex in these transitions. The siblings are faced with the decision of whether to all retire at the same time or in steps. If they retire together, the younger siblings may feel they have been cheated of their opportunity to lead. On the other hand, if they leave in a staggered pattern, the older siblings must ask themselves: Do I trust my siblings to protect my interests and to take care of my children? Often, the Sibling Partners' difficulty with disengagement will be evidenced by prolonged negotiation concerning their retirement packages, as they struggle with their personal status and their unfinished personal aspirations.

The *exploring alternatives* task is also more complicated. In the Controlling Owner to Sibling Partnership transition, the system had few options to explore and a small number of people to mobilize. In the Sibling Partnership to Cousin Consortium transition, there are often more options to consider. Choosing a structure for the Cousin Consortium is more complicated because of the broader age spread, the blurring of generations (often cousins in one branch will be older than uncles and aunts in another), politics and hierarchies among family branches, and the gradual sequence of departures among the siblings. There are so many possible steps, often involving hybrids of possible models. And, because the process takes longer, the system is more vulnerable to environmental change and crises during the transition.



Finally, once the *choice* is made, the *commitment* phase of the transition is often prolonged. Many new structures and policies need to be formulated. Often the cousins start realizing that the resources will be stretched thin when they are divided among the expanding cousin generation. With a wide range of interests, ages, competence, and commitment, they feel the need to come to a formal agreement on who gets what and when. A big part of the work in these transitions is the design and the implementation of a governance structure, often much more developed than previous stages.

III. Lessons From Experience

How can leaders of family enterprise apply these concepts to guide them through transition stages? People who find themselves in these transitions often feel like they are in a middle of a circus. This is not far from reality. Things are very complex. But they can be understood and managed in such a way as to make the most of the opportunity for change that is inherent in transitions, and to emerge stronger at the transition's close.

The first suggestion for leaders is to recognize the transition for what it is, and to reassure the family and the company that what follows will be planned change, not destructive chaos. The leader can help the key stakeholders focus on the long-term developmental forces that made change inevitable, rather than on the often-dramatic trigger (the "shout") that put the change in motion. The leader's delicate task here is to bring all parts of the system – all the fingers of the glacier – to a position of readiness for change, so that they will be willing to do the real work necessary to achieve continuity.

Second, transitions are opportunities for change, not guarantees of improvement. Transitions raise anxiety. Many family members and business executives may wish for a premature decision. They would like to move directly to "commitment" without spending enough time exploring alternatives and evaluating experience. Leaders need to avoid the pressures to choose a new structure too early. More than anything, transitions are rare opportunities when it is acceptable to ask difficult questions and to challenge routines. Leaders can increase the chances of long-term success if they open the process to a range of possibilities, test the feasibility of each option, and make decisions based on adequate, reliable data. If a choice is made prematurely, it may not stand the pressure of implementation, and in the end the organization will pay dearly if it has to undo a poor choice and start again to find a better one.

Finally, there is the other side to the "premature closure" issue. Exploration of options is essential, but so is choice. Businesses and families do not operate effectively in an environment of unending provisional status – particularly regarding such fundamental issues as the structure of ownership. Leaders need to recognize when it is time to bring the transition to a close, and commit the system fully to the chosen future. The exit from the transition – initiated by the new leadership structure -- is a perfect opportunity to signify the implications of the change. This signals to the family, the company, and the environment that the torch has been passed, and the new era has begun.

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[1] See Gersick, Davis, Hampton, and Lansberg, *Generation to Generation: Life Cycles of the Family Business*, Cambridge, Massachusetts, USA, Harvard Business School Press, 1997. (Also available in Spanish, Dutch, Japanese, Thai, and Chinese.)