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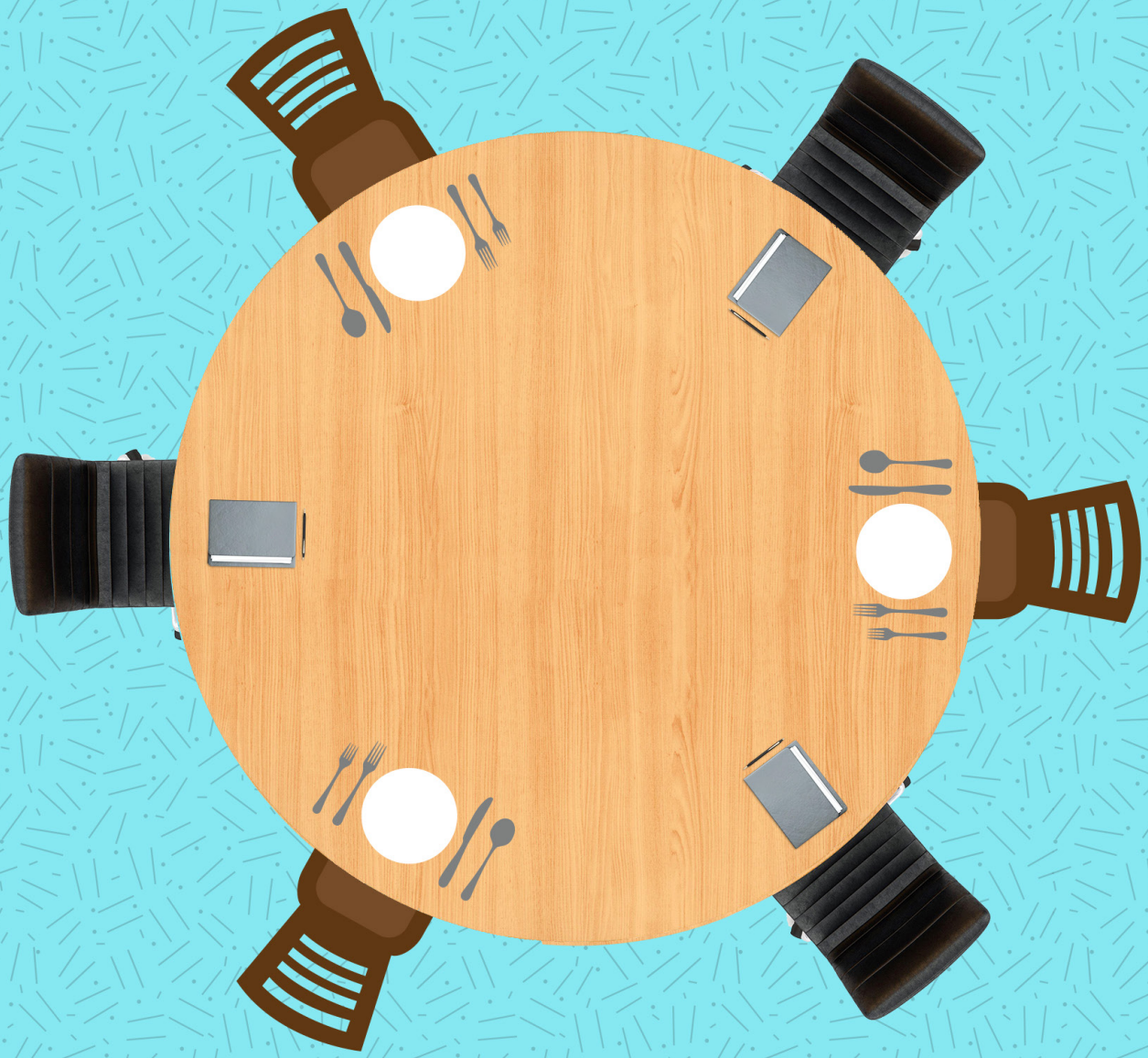

Private company issues and opportunities 2020

Family business edition

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Executive summary

Family is one of the most evocative words in any language. It conjures up thoughts of love, strength, support, and special bonds, but also of conflict, tension, and drama. Nurturing the positive side of this equation takes effort and dedication. While this can be challenging for any family, those in businesses together must work doubly hard to achieve long-lasting harmony. Few family businesses survive into the third and fourth generations, and oftentimes the culprit is misalignment between the goals, wants, and needs of the business and individual family members.

Carl Allegretti

In this report, we examine the common traits of family businesses around the globe that have solved this puzzle. Articles from Deloitte practitioners who work with family businesses provide actionable insights on topics ranging from succession to social responsibility, preserving family capital to assessing the health of family businesses, and from innovation to the future of work.

What we found is that successful family businesses tend to have one quality in common: a sense of purpose beyond being profitable. Of course, making enough money to sustain a business is as important to family-owned concerns as it is to any other commercial enterprise. But they are also driven by unique pursuits that, for many, will define their legacies for years to come. Whether it's a commitment to giving back to their community, becoming environmentally sustainable, or producing a perfectly crafted product, purpose informs everything they do. Our opening chapter covers this theme, examining some of the cultural and regional differences between family businesses young and old when it comes to finding and fulfilling their purpose.

William Chou

We often talk about how important family businesses are to the economies in which they operate and prosper; however, delivering against these non-economic aims may be the most influential impact they have on society. As globalization and the pace of technological change disrupt business as usual, how family businesses retain and project their sense of purpose could make the difference—not only in how they sustain themselves and prosper, but also in the way their contributions will be recognized and remembered.

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Family business and purpose

William Chou
Deloitte Private global family business leader

Off the northwest coast of Japan, there is a family business that's been around longer than nearly every part of the landscape that surrounds it, except the ancient cedar trees and a Buddhist temple built in 717. The Hoshi Ryokan is a small inn that is one of the world's oldest independent family businesses, created just one year after the temple and currently closing in on 50 generations of ownership.

For the Hoshi family, its identity and that of the hotel are inseparable, connected by a longstanding commitment to nurturing a business and legacy of 1,302 years—and counting.[1]

For many family businesses operating in Asia, the Hoshi Ryokan represents the ideal—a successful business perpetuated by each generation, with no end in sight. Family is the key element in Asian culture. Everyone wants their legacy to pass on from the first generation to the second and third generations and on down. Therefore, the number one purpose for most family businesses here is the continuity of the family.

No matter where a family business resides and operates, it likely has a purpose that extends beyond profit-making. Culture, heritage, tradition, community, innovation—these are some of the words you hear when you ask family business owners what really drives them. Yes, profits are needed to sustain family businesses, but they derive at least in part by a sense of purpose that resonates with stakeholders across the spectrum, from customers to employees to people in the places where they operate.

It's a concept that is finally getting its due among some of the largest public companies in the world. In August 2019, chief executive officers from 181 of the biggest US multinationals issued an open letter titled "Statement on the Purpose of a Corporation." In it, they recognized that each of their stakeholders is essential, not just the shareholders in their companies. "We commit to deliver value to all of them, for the future success of our companies, our communities and our country," they wrote.[2]

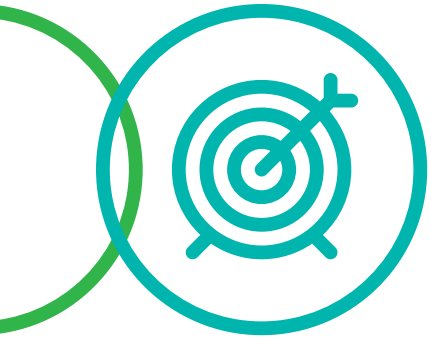
The letter represented a major break from the longstanding economic principle that the sole focus of a business is to maximize profits for the benefit of shareholders. But for family business leaders, this change in thinking may have felt overdue. For them, purpose has always meant building something greater than themselves.

The third-generation problem

Around the world, it's rare to find a family business that has survived three generations. In the United States, fewer than 30 percent of family- and founder-owned businesses endure past the second generation as family-owned businesses.[3] On its face, the problem is one of succession. But there are many underlying symptoms that can create succession issues, and one of the most influential is a lack of purpose that unifies different generations within a family.

Every family business, when it's established, must have a purpose, and it must live this purpose from the first generation to many generations to come. When that doesn't happen, it's typically because family members have different intentions or ideas about their individual purpose.

This dynamic used to be mainly confined to large, developed economies in the West, where younger family members traditionally have gone off to college and then formed their own households and built their own careers. This separation gave rise to independent thinking and new ideas, not just about the family business, but about other potential career paths.



Purpose for a family business is not just about the purpose of the business; it is also about the purpose of the family.

By contrast, families in the East traditionally live together for much longer periods, with multiple generations commonly living under one roof; however, that is beginning to change now that globalization and technology are contributing to a world that is becoming smaller and smaller.

In many ways, mainland China is at the epicenter of this culture shift. Although the country is thousands of years old, many of its family businesses were started only a generation ago after the end of the Cultural Revolution. The wealth they have created has allowed them to send their children to be educated overseas, and they are returning home with different perspectives and priorities.

In one case, a business owner I know in China sent his only son to study abroad in Australia, where he ended up living for 20 years. The father wants his son to succeed him in the business, but the son doesn't feel like that's an attractive opportunity for him. It's become a conflict between Eastern culture and Western culture.

Bridging the divide

A clear purpose is fundamental to any family business, and those with the strongest sense of purpose are often the most successful. Purpose for a family business is not just about the purpose of the business; it is also about the purpose of the family and defining how it fits in with the enterprise and establishing why family members are in business together in the first place.

For some, that purpose is serving as a role model for others by generating a positive social impact. In Deloitte's *2019 Global Human Capital Trends* report, 44 percent of business and human resources leaders surveyed said social enterprise issues are more important to their organizations than they were three years ago, and 56 percent said they expect them to be even more important three years from now.[4] Societal impact and ethics are the most common reasons why millennials—not just customers, but employees too—are changing their relationship with businesses.

For their part, family businesses have an opportunity to deliver social impact not just through their business, but through the family foundations made possible by their financial success.

Of course, purpose doesn't have to be so high-minded. It can be about maintaining a tradition or a core set of values. It can be about identifying with a place: There are countless scores of family businesses that wouldn't think of leaving their communities; their identities are intertwined with the towns where they were created and found success. Purpose can also be about something as straightforward as superior customer service or craftsmanship.

Starting and sustaining the conversation

Whatever a family business's purpose is, open communication is critical. Individual family members need to share their personal aspirations as a starting point for any family conversation about values, vision and purpose. When the business does something that runs counter to the family's priorities, there needs to be a governance process for addressing it.

To be sure, holding a meaningful discussion on the purpose of a family business can be difficult, especially when there are multiple generations involved who have different life experiences and perspectives.

But these conversations might yield insights that can transform a company's legacy, help generations settle conflicts, and find a healthy balance between tradition and innovation. With successful family businesses, older and younger generations are always in a process of alignment and debate about their purpose.

One example is Lee Kum Kee, a more than 130-year-old family business in China's Guangdong Province that invented and built an empire basedc on oyster sauce. The company introduced a comprehensive governance system in the early 2000s after some family disagreements nearly ended its reign. The family's leaders turned certain business units into a training ground for younger family members, who were sent on "innovation trips" around the world to bring back fresh thinking.[5]

In this case, the core business remains the same, but the younger family members helped them introduce new sauces and packaging. They found their purpose and it's one of the main reasons the company is now in its fifth generation.

"Study the water"

With the world changing so much these days—due to the rapid pace of technological change, globalization, and the flow of information across borders—it pays to be nimble. But for family businesses, rooting themselves with a defined purpose can prove to be a stabilizing process. Consider the Hoshi family example from Japan, whose philosophy all along has been, "study the water running down a small current."

In China, we like to say "the strongest surface is not necessarily the hardest." When you have water go over a stone for 1,000 years, it will eventually cut a hole through it. Family business is much the same. If you want to preserve value and be the best of the best, it's not about being the quickest to change. It's about being the most enduring.

Notes

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Assessing the health of family businesses

Larry Keeley
President and co-founder of Doblin, a Deloitte business

You don't have to look too far to find examples of extremely successful family businesses that have stumbled or fallen apart due to conflict or strife within the family. Multibillion-dollar enterprises have been split up and sold off over family quarrels that metastasized and undermined those who remained keenly focused on the company's success.

But even when family businesses find a way to sustain themselves, they can fail to make the most of their potential due to inner conflicts. Family turmoil can stem from differences of opinion about the company's strategy or change in leadership, but it can also arise from behind-the-scenes personal issues that have little to do with running the business.

Whether a family is involved in the day-to-day operations of the family business or simply retains a controlling stake, these family health issues can derail legacies and erode wealth over generations. And, in many cases, they're treatable. We have yet to find dysfunction in a family business that can't be explained by some combination of identifiable factors. Predictive analytics can show families where their weaknesses are likely to lead if they aren't promptly addressed.

Issues

At some point in their history, many family businesses migrate from startups with a single founder to sprawling enterprises managed by a host of family members and/or leadership brought in from outside. As more family members become involved, natural tensions emerge across generations. When a family creates a wildly successful platform business, there's a lot of money at stake and family tensions can become intensified.

That's particularly true of businesses that need to innovate or shift their model to keep growing. Older family members who guided the business through its formative decades and are emotionally attached to it tend to discount the opinions of younger generations when it comes to new, tech-driven business initiatives. For example, the "old guard" might push back based on previous projects that were unsuccessful and wasted money. Interestingly, successful family members tend to have a quality that less successful family members don't: humility. Their experience has taught them to be more careful and not take success for granted. In many cases, it can be difficult to find common ground between these divergent perspectives. It's within those generational divides where the dysfunction can be particularly acute.

When such conflicts can't be remedied internally, it's common for the family to bring in outsiders to take over the company's management. They might find someone with perfect credentials for the job, but they don't have enough information about the family dynamics that led to the trouble in the first place. If they ignore that context, they do so at their own and the company's peril. In those cases, the business tends to cycle through a series of CEOs, consultants, and other leaders in rapid succession and the real issues are never addressed.

Even when family members understand that they have a problem that is inhibiting the business, it can be difficult to address it. In certain regions of the world, such as Asia, younger generations tend to defer to their elders and look to avoid any conflict. In Europe, by contrast, a family's reputation can dominate other considerations, arguing for keeping problematic facts confidential rather than subjecting them to a public airing.

Much like a patient's health record in the hospital, an assessment provides a way to be more objective about the issues a family may be dealing with.

Opportunities

Family businesses don't need to wait for a public dust-up or other failure to obtain a true sense of their strengths and weaknesses. Typically, an objective look at the business from inside and out can point to their reasons for its success and where it can improve.

Many dimensions of running a family business are interrelated, meaning an issue that's impacting the health of the family could explain why a part of the business is suffering, and vice versa. For instance, a lack of confidence in the family's younger generation to contribute to innovation discussions can contribute to performance and succession issues down the road. In another family, a clear lack of boundaries for the roles and responsibilities that family members take on can upset nonfamily members in the business and promote a sense of unfairness.

Family businesses should consider undergoing a diagnostic assessment that pools a variety of perspectives from family and nonfamily members—from 20 to 50 contributors—to get a truer sense of what they're doing right and wrong. For many companies that go through such a process, it's the first time family members share their perceptions—and are exposed to the perceptions of others—about problems long deemed to be holding back the business. Much like a patient's health record in the hospital, an assessment provides a way to be more objective about the issues a family may be dealing with and get it down all in one place. This can be particularly important when a family business is undergoing a leadership succession.

New predictive analytical tools can make these exercises more fruitful. By drawing on the experiences of other companies and how their experiences aligned with their scores, the results from the diagnostic can project likely outcomes for family businesses that rate high or low among certain family and business factors. As patterns start to emerge, family businesses can start to get ahead of potential trouble spots or replicate success.

Questions to consider:

- Are there meaningful differences in opinion at your company about the role of family and nonfamily members in running or overseeing the family business?
- Have internal family conflicts kept your business from pursuing new growth opportunities or contributed to high-profile missteps?
- Does your family business have clear lines of authority that are inclusive and exclusive where necessary to promote the success of the business?
- Do you embrace an environment of openness between family members of different generations when identifying potentially emotional obstacles to communication?
- Have you done anything to objectively assess the strengths and weaknesses of the family, as well as the strengths and weaknesses of the businesses run by the family?

Zoom out to zoom in

John Hagel
Co-chairman, Center for the Edge, Deloitte LLP

Examine the most successful technology companies in Silicon Valley, and you will find that they often have a very different approach to strategy compared to their more traditional counterparts. As part of their regular planning meetings, they constantly ask themselves what their market or industry will look like 10 to 20 years from now and what kind of company they need to be when that time arrives.

The next part is critical: The answers to these questions help set their investment priorities for the next six to 12 months. This "zoom out to zoom in" approach effectively cures company leaders of their development-driven short-term myopia and clears the way for them to think more proactively about the future so their businesses can carve out a meaningful role in it.[1]

Despite having inherent advantages that lend themselves to adopting a similar "zoom out/zoom in" approach, most family businesses remain focused on the here and now. When they do plan for the future, their vision of the horizon is limited. In Deloitte Private's *2019 Global Family Business Survey,* 71 percent report their company plans for only the next two to five years, while another 6 percent don't look past next year.[2] You can't really understand exponential change if you're just focused on what's changing from day to day. By zooming out to zoom in, family businesses have an opportunity to drive disruption rather than being a victim of it.

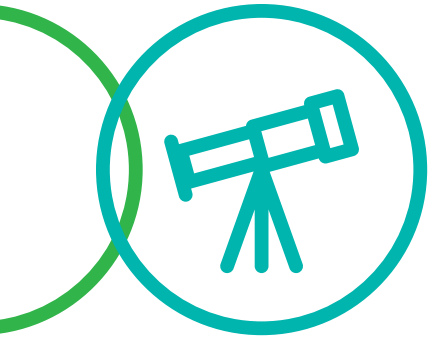
Issues

While family businesses express confidence in their preparedness for the future, many may be overconfident given where they spend the bulk of their time. Deloitte's global family business survey found that more than half of respondents believe they have the right strategy to meet the challenges of the next two decades[3] But when it comes to formal planning processes, they don't think that far ahead and rarely beyond the next five years. They might hold an off-site meeting once a year in which employees are asked to envision the future and what it might look like, but once they return to work those freewheeling discussions often don't translate into concrete action.

Things are changing so rapidly that family businesses often find themselves getting swamped by what's happening today. It can consume all of their attention. They get distracted by what's going on that moment and lose sight of where they're going and what they're trying to accomplish.

As a result, these businesses focus on trying to respond as quickly as possible to events as they occur, increasingly spreading their resources more thinly across an ever-expanding array of initiatives.

In some ways, the same traits that have come to define small businesses can also contribute to short-term myopia and complacency. One such defining characteristic is resilience. Family businesses have been found to enjoy higher survival rates during severe economic downturns as they demonstrate the ability to bounce back more quickly than their nonfamily counterparts.[4] This experience can feed a belief among family leaders that they need to stay on their present heading, since it's served them so well in the past. They may say "failure breeds success," but success can also breed failure. The more successful you are, the more complacent you can become and not recognize that things are changing at a more fundamental level than you think.



The zoom out/zoom in approach can work for any company, but family businesses may be primed to benefit more than most.

Family businesses have also historically benefited from loyal customer bases,[5] which may not be as much of a given now that consumers have 24/7 access to price comparisons, customer reviews, and other information and can just as easily shift to a competing product or service. Those companies included in this year's global family business survey seem well apprised of this issue: Only 21 percent believe that customer loyalty will drive their business's sustainability in the years to come.[6]

Opportunities

Rather than take a one- to five-year view of the competitive landscape, family businesses should consider doing the opposite. Companies pursuing a zoom out/zoom in approach spend almost all of their time concerned with the 10- to 20-year horizon and the six-to-12 month horizon, figuring if they get that right, everything else will take care of itself. The 10- to 20-year timeframe is far long enough that it's difficult to envision an unchanged future, particularly given the current pace of technological change. As they ponder what that future might look like, the leadership team works to build alignment around a shared view of the future, using scenario-planning techniques and outside experts to help challenge their key assumptions.

Then the focus shifts back to the immediate term, and what tangible steps the business can take to effectuate the future they envision. It's vital that senior leaders agree on two to three highest-impact initiatives that can be pursued within the next year and dedicate appropriate resources toward them. That makes a theoretical exercise become real. Clear marching orders emerge for what the company will be doing differently in the short term to build the capabilities they will need in the future.

The zoom out/zoom in approach can work for any company, but family businesses may be primed to benefit more than most. One reason is that at many family businesses, the leadership remains intact for many years. At the average public company, the median tenure of a chief executive officer has shrunk to just five years. That means any major investment initiatives they approve could be easily upended as soon as someone else is in charge. In contrast, family business leaders and their family successors can see those spending priorities through to their conclusion.

The question for them is, "How do I prepare something really big for the next generation?" This approach lets them focus on what really matters—and that's the big legacy-creating opportunities.

Our team studied one longstanding Chinese family-run company that engaged in a similar, less formal exercise back in the 1970s. Li & Fung had succeeded for 70 years by serving as a deal-making broker for apparel manufacturers and other export companies looking to sell their goods to

the United States and Europe. After two brothers took over the company in the mid-1970s, they noticed the business's commissions were shrinking. They studied the global apparel industry and considered how it might continue to evolve over the next 10 years.

What they saw was increasing complexity and competition, as well as an opportunity to become a trusted adviser who could help their clients orchestrate their resources up and down their supply chains. They fundamentally transformed their organization as a result, starting in a focused way with a new business unit targeting one apparel designer, before scaling up dramatically. Today, Li & Fung has over 250 offices in 40 markets worldwide, working with 15,000 suppliers and servicing 8,000 customers.[7]

Family businesses have another opportunity in applying the zoom out/zoom in framework and that's engaging in the process younger generations who will be called on one day to assume leadership responsibilities. Typically, younger family members have risen through the organization's hierarchy under a prescribed set of practices and career paths, without much input on strategic direction. The younger generation can serve as a challenging force to at least bring in a different set of experiences and perspectives. They're the ones who are going to ask, "Wait a minute, is this really going to work as well in the future as it has in the past?"

Questions to consider:

- Do we have a formal process for envisioning the future?
- How far ahead are we willing to look as an organization to get ahead of meaningful shifts in our business?
- What will our relevant market or industry look like 10 to 20 years from now?
- What kind of business family will we need to be 10 to 20 years from now to be successful in our market or industry?
- What are the two to three initiatives that we could pursue in the next six to 12 months that would have the greatest impact in accelerating our movement toward that destination?
- Which voices, both within and outside the organization, do we need to incorporate in this kind of scenario planning to ensure we are getting a mix of perspectives?

Notes

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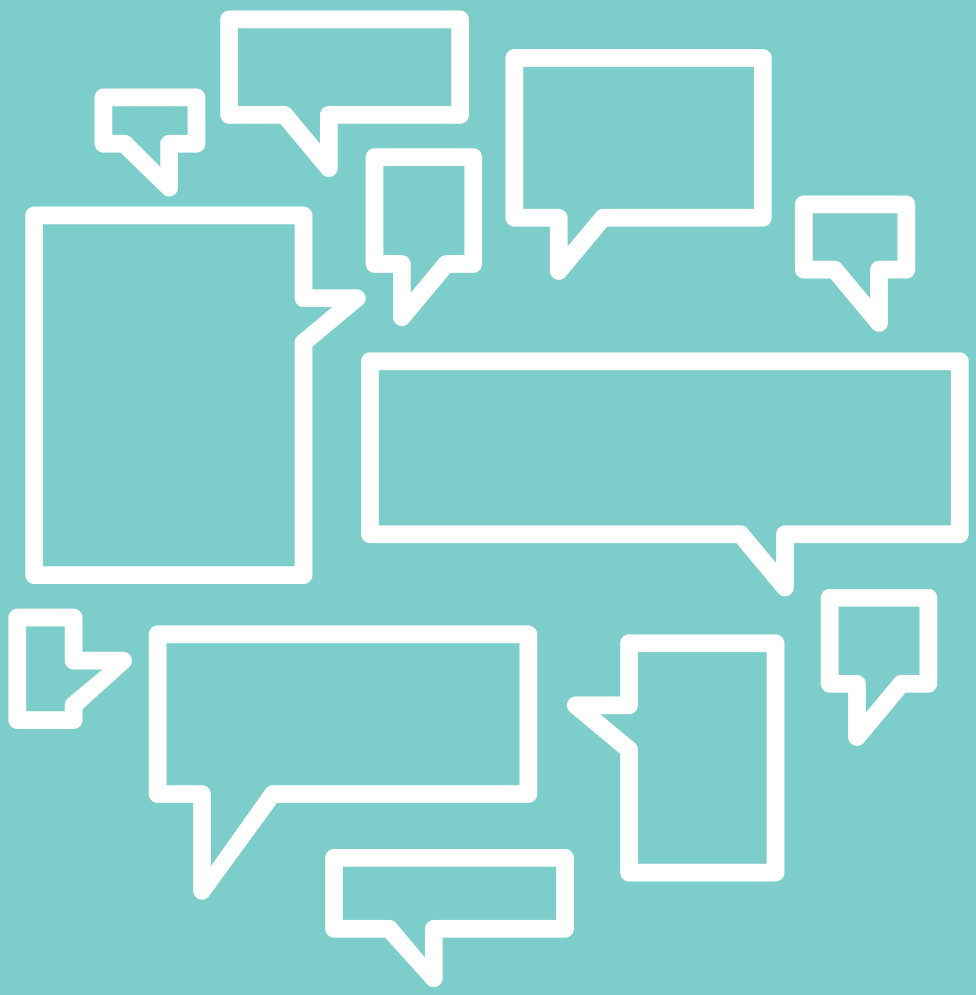

Good family governance: Driven by good family communication

Michelle Osry
Partner and family enterprise consulting practice leader, Deloitte Canada

Communication is probably the single most important ingredient in building and managing a successful family enterprise, but often proves to be the most difficult part. Open, honest, and productive communication can be a challenge for any organization, but for a family enterprise it can be particularly difficult.

By their nature, family enterprises are complex, and as they evolve past the first-generation founder-manager, business and family issues become intertwined, especially as the enterprise transitions from the generation of sibling owners and managers, to the generation after that, cousins.

In our family enterprise practice, we consistently see that good family governance relies on open and transparent family communication, but that business families quite often lack the skills and capability to navigate tough discussions together, particularly those involving both business and family matters. Rather than risk family disagreement, business families often default to avoiding difficult or sensitive conversations. But we know that allowing management, succession, and ownership discussions to slide can place not only the business but the owning family at risk. Indeed, research and practice show time and again that breakdown in communication is largely the cause of transition failures in family-owned enterprises.

Fortuitously, effective family communication can be learned, and today we see more and more families committing time and budget to facilitate and improve their family communication skills and capabilities.

Issues

Communication across a family enterprise can be difficult for a number of reasons:

- Family members will have different interests, different aspirations, and sometimes different values. Overlapping familial roles and responsibilities, combined with management, ownership, and economic interests, provide fertile ground for misunderstandings and conflict. Lacking methods to navigate complex and tough discussions, families become vulnerable to the business, and vice versa.
- A lack of transparency in family matters is quite normal, and it is easy for family members, especially those not involved in management of the business, to misinterpret information received informally. It can be difficult to speak truth to power in hierarchical family business cultures. Differing levels of knowledge, authority, ownership, and responsibility, plus tensions and biases between generations have real impact.
- Unlike nonfamily businesses, emotions and personal feelings aren't left at the boardroom or office door, and personal and private values, beliefs and personalities matter. Not being able to discuss and resolve an issue with a parent, spouse, sibling or cousin who may or may not also be an executive or shareholder of the business, can leave a family feeling stuck and confounded. As a consequence, business decisions may seize up, opportunities may be squandered, and blame can set in, dividing the family and the business, unfortunately sometimes to the extent of family estrangement and failure of the business.
- As the business and family grow, more and more family members expect a say or voice in the family enterprise. Apportioning questions and decisions between the family, the business, and the shareholders sometimes requires difficult discussions. Trustees, enterprise executives, board members, and beneficiaries are often the same people. We see too often that when processes and structures are forced on family recipients, dispute is inevitable.

We find it useful to visualize family enterprise governance as a process of building out different rooms in a house, each fit for a distinct purpose.

Building a family's communication skills takes time and effort. But we consistently see that good communication is ultimately what sets successful business families apart.

Opportunities

Despite their complexities, family enterprises have significant advantages over their nonfamily counterparts. Through being brought up in the business, family owners have a unique and superior ability to adapt and pivot, particularly when guided and sustained by the family's vision and values.

To capitalize on this strategic advantage, we encourage business families to invest in building their communication skills as an integral part of their overall practice of governance. Meaningful, sustainable communication takes patience to set out, and a commitment by all family members to engage with open minds and open hearts. Working with a neutral family enterprise adviser may help to level the power-playing field, so that all family members feel they can have a voice at the table. Importantly, a structured approach allows difficult issues to be worked through in a sensitive and productive way, allowing a family to heal and reset past behavior patterns.

Working through the mandate and decision-making authorities of a family board or council, as contrasted to the business board or shareholders' council, is another facet of the work required. Successful multigenerational family enterprises are then able to direct conversations and decisions to the appropriate governance forum. We find it useful to visualize family enterprise governance as a process of building out different rooms in a house, each fit for a distinct purpose.[1] Different conversations and decisions are made in each room. For example, the family council is the forum for discussing ownership and family matters, as well as family education and philanthropy. The business board meets to oversee the performance of management, and to review, approve, and monitor the business's strategic plan. These governance bodies are not just checkboxes or rubber-stamp exchanges. Each forum requires a unique set of skills to deal with a unique set of issues.

Understanding, defining, and attending to family dynamics are vital for the good functioning of a family enterprise's governing bodies, and underlying everything is the recognition that good communication is both an art and a science. The fields of neuro-cognition, how the brain works, and systems thinking—the notion that everything is inter-connected—offer much for family enterprises:

- Identifying and addressing generational, cultural, and gender biases and emotional triggers.
- Listening empathically, asking genuinely open-ended questions, and accepting that we all come to any conversation with our own story and assumptions, are learned skills.
- Practicalities are important, such as scheduling family meetings in a neutral location, having ground rules that differentiate them from family gatherings, and ensuring that participants are pre-prepared by a facilitator to attend briefed and present.
- We find that family leaders often need to invest time one on one with family members, especially those more withdrawn or less likely to speak up during group gatherings, to build trust and understanding of the value of a family program to them. Those leaders may also need to recognize that as they open lines of communications, they may be challenged in ways they aren't used to.

Once a family begins to communicate effectively, it begins to lay a foundation for transparency, fairness, accountability, and participation. Getting it right might take years of evolution and requires courage and commitment. Missteps and miscommunication are part of the process, so it also requires love, practice, and patience.

Questions to consider:

- How well does our family communicate about family and business matters? Can it be improved?
- How effective are our governance structures in meeting the family's needs for what really matters? Do we have the right governance bodies in place for the current stage of our family enterprise, or must they evolve?

Note

1 Josh Baron, Rob Lachenauer, and Sebastian Ehrensberger, "Making better decisions in your family business," *Harvard Business Review,* September 8, 2015, https://hbr.org/2015/09/making-better-decisions-in-your-family-business.

Aligning family and business strategy

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Psychologists define attitude alignment as the concept of modifying one's opinion to agree with others. This is especially true in close relationships, when parties have different views, but are motivated to change their opinions to match their counterparts.[1]

In family-owned businesses, shared values, vision, and culture are among the traits we attribute to entrepreneurial success. But as our research suggests, there appears to be little alignment between personal preferences and overall business strategy in many of these firms. In Deloitte's *2019 Global Family Business Survey,* only 35 percent of respondents say company objectives align with family goals.[2] A lack of harmony can lead to disagreements in any organization. But in family-owned businesses, the absence of alignment between individuals and the business can become a threat to performance, growth, and longevity.

Issues

Decision making in family businesses often depends on factors beyond immediate results and financial success. These businesses make decisions based on the family legacy, and that influence can endure for generations to come.[3] One key issue that can prevent the alignment of family and business strategy is communication avoidance; many family companies aren't prepared for difficult conversations or avoid such discussions altogether.

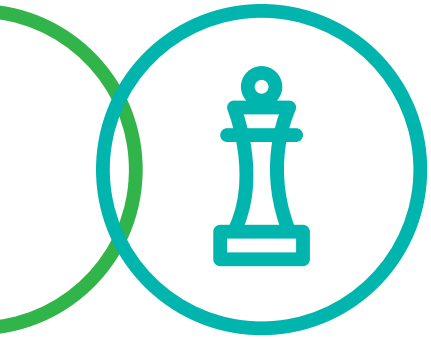
One frequent discussion for families involves risk tolerance. Our global family business survey indicates that some firms are inclined to be risk-averse. As a result, they are unwilling to innovate for fear of potential negative outcomes such as a reduction in family wealth.[4] Regarding specific risks, family-owned companies sometimes view partnerships or joint-venture opportunities with skepticism. Family-owned companies are by nature entrepreneurial, innovative, and risk-taking. But they're careful to protect the things that made them successful.

Another area where family goals may not align with company objectives is around the value of third-party advice. Many family businesses have been operating for decades without the benefit of advisory boards; however, the perspective these external boards provide can not only help bridge interpersonal differences about the direction of the business, but also help the company plan for transitions that will inevitably come with a change in leadership.

Third-party perspectives can help bring founders and owners into alignment with successors on the future of the firm. Next-generation leaders have a tough job, and advisory boards can help them with issues the founder never had to deal with when they started the company. It's a different world. The competitive landscape, multinational customers, multinational supply chains, and speed of technological disruption—younger generations are inheriting these businesses and they need a different type of support to make them successful.

Opportunities

One opportunity for firms to align family and business strategy is through meaningful conversations about their values. In this year's family business survey, just 11 percent of respondents cite shared values and ethos of the family as one of the key characteristics that will drive the sustainability of their firms over the next 10 to 20 years. In addition, fewer than one-third of respondents say there's full agreement within the family about the future development of the company over the next one to two decades.[5]



It doesn't matter if the company is 30, 50, or 80 years old; being in business for decades is not a strategy.

If family-owned companies want to make sure that business strategy aligns with family objectives, they should first work collaboratively to define their values and communicate those principles to the organization. It doesn't matter if the company is 30, 50, or 80 years old. Being in business for decades is not a strategy. Businesses need a process to see where they want to be in in the next 10 to 20 years.

Another consideration for family businesses is to seek alignment around a wealth strategy, specifically determining how wealth preservation will be managed. For example, a company that goes from $100,000 in revenue to $200 million will need a chief financial officer who can handle more complex transactions, and a chief operating officer who can manage a growing business and the wealth it generates.

There are some basic questions for family businesses to ask, including: How are we going to preserve family wealth for three or four generations? What's the strategy in terms of investment, in terms of distribution? How are we going to educate the next generation to be entrepreneurial?

Another opportunity for family-owned businesses is to bring their teams into alignment around agile business practices that allow the company to respond quickly to changes in their industry. In the global family business survey, 61 percent of respondents say agility is the most crucial attribute of a family business. Respondents perceive agility, along with other distinctive features—such as innovation capabilities (39 percent) and financial position (32 percent)—as essential to sustaining their business.[6]

Ideally, discussions around innovation should involve all generations in the company. Ultimately, it's up to owners to communicate to the family how these capabilities fit into the direction and goals of the business. Family-owned businesses have a unique opportunity in this respect—acquiring new skills that help the company operate like a larger firm without the bureaucracy that could leave the organization feeling impersonal.

For people who innovated, created a business, and grew it to something that's much larger, the perseverance that they use to build it got them to where they are today. But now, business is so much more complicated. It's a different economic environment. It means that family businesses need to have more structure, governance, and discipline to perpetuate that growth.

Questions to consider:

- Have you defined and communicated your family's values?
- How can you customize your governance model to address your ever-changing business and family issues?
- Are you and the generations immediately following you prepared for the rapidly increasing disruption cycles that will define the future?
- Can you define a common vision for the future? Does it align with the interests of the family and the business?
- What are the roles and responsibilities of each member of the family, particularly those who will serve in leadership roles?
- How will you educate successive generations on business management?

Notes

1 Jody L. Davis and Caryl E. Rusbult, "Attitude Alignment in Close Relationships," *Journal of Personality and Social Psychology,* 2001, Vol. 81, No. 1, 65-84, https://pdfs.semanticscholar.org/ca87/d69bc99ee5707332b5b232fa86f642a20938.pdf.

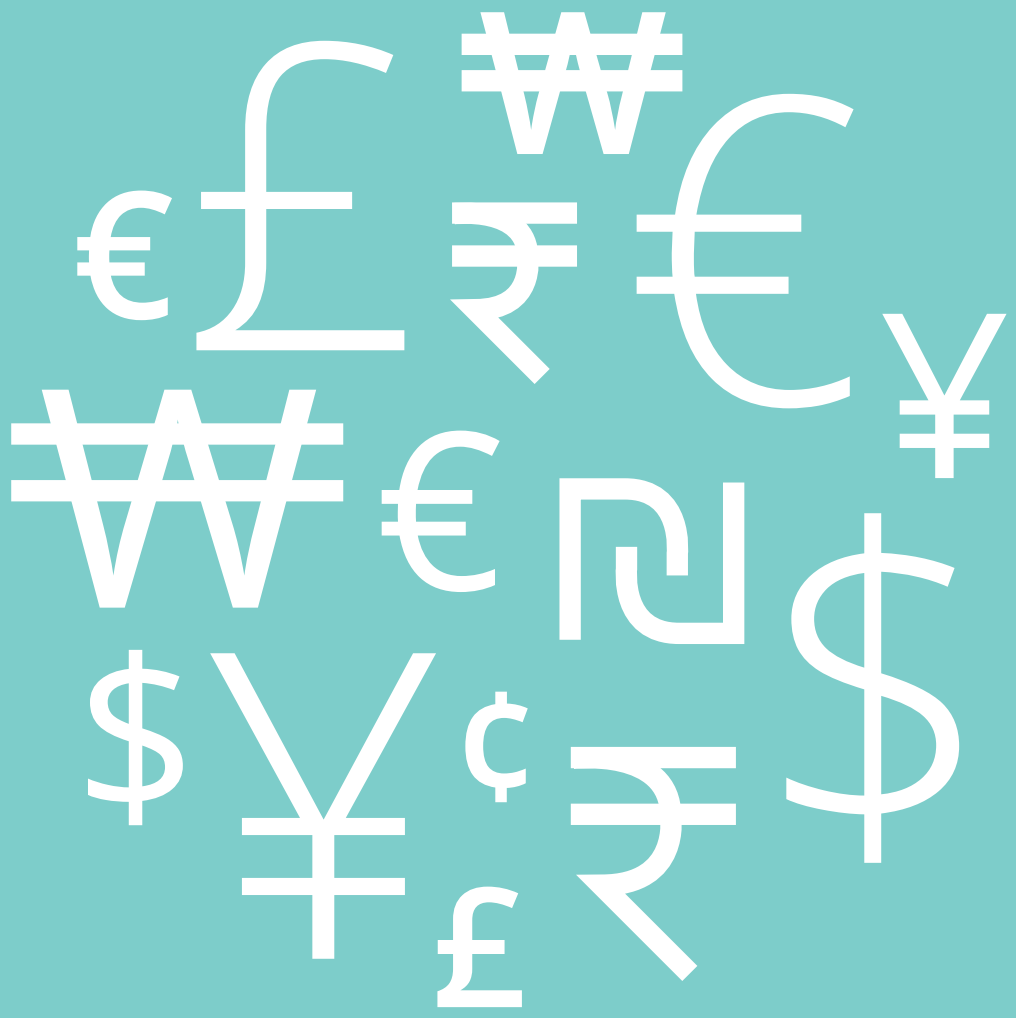
2 *Global family business survey 2019: Long-term goals, meet short-term drive,* Deloitte, June 2019, https://www2.deloitte.com/content/dam/insights/us/articles/r7-12011_long-term-goals-meet-short-term-drive-family-business-survey2019/DI_Long-term-goals-meet-short-term-drive.pdf

3 Pietro Gottardo and Anna Maria Moisello, "The impact of socioemotional wealth on family firms' financial performance," *Problems and Perspectives in Management,* 13(1), 67-77 2015, https://businessperspectives.org/images/pdf/applications/publishing/templates/article/assets/6331/PPM_2015_01_Gottardo.pdf.

4 *Global family business survey 2019,* Deloitte.

5 Ibid.

6 Ibid.



Access to capital

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Like all businesses, family-held concerns often find themselves in need of capital. For many, an influx of funds can help their business development plans, both in the short and long term. That might mean deploying capital to organic growth in existing markets—adding staff and building new facilities. It also might be funding more ambitious plans like acquiring a competitor or entering into new markets or product lines.

In the *2018 Deloitte Global Family Business Survey* of 400 family businesses, more than four in 10 said they expected to acquire another company in the year ahead; about half said they would boost staff.[1]

External developments are heightening the urgency for companies to raise capital. Changes in business dynamics are occurring rapidly, meaning that companies are recognizing and feeling the need to move fast to acquire technology or enter into new regions and service lines. Business uncertainty is a factor—from Brexit to trade issues to regulation and government instability—to the low interest rate environment. These outside trends have a lot of family businesses focused on securing capital now to make sure the business has the funds to address changing dynamics—not only within their own families but also on a macro level.

Issues

While those drivers are similar to the needs of private companies, there are some unique reasons why family companies may need cash. Some need capital to respond to family dynamics such as cashing out relatives who are retiring or simply to provide money to family members who may need it.

There's a commonly-held belief that family-owned businesses are self-financing. Yet, less than one-third (30 percent) of family-held firms we surveyed expect to tap internal resources when then they need capital, as opposed to 35 percent of private concerns.[2] As a result, many look outside, to private investors, public markets, and banks. While these are traditional sources of capital, there are issues that emerge with each funding source that are distinct to many family-controlled enterprises.

The stakes are high for family-held enterprises to raise capital and do so in the right manner. In the absence of doing it right, a lack of capital could lead the company into irrelevance or bankruptcy—and put an end to the institution the family has created.

There are a handful of unique factors that define many family businesses and shape the decisions they make in securing capital. For starters, maintaining family control—or at least influence—is a leading priority. Another key: discretion and privacy. For example, one Japanese family business balked at getting a bank loan when the banks started asking for documents that the family had kept confidential and considered personal.

The twin factors of maintaining control and preserving privacy might lead some families to shy away from public markets and initial public offerings. While the absence of stock exchange pressures gives them greater freedom to operate, limited access to public markets when funds are needed can turn the positives of independence from the market into a problem if others sources of capital become more scarce.

Families that plan ahead can mitigate many of the issues that might hinder their ability to raise capital.

Another factor common among many family businesses is a focus on long-term capital appreciation. Sheltered from the demands of appeasing public shareholders on a quarterly or semi-annual basis, many businesses focus on creating generational wealth and have a longer timeframe than other companies. That may shut out IPOs as a source of capital.

In some parts of the world, particularly in Asia, there's one additional complication in raising capital. Many family-owned businesses have been in existence for decades (in Japan, some are centuries old) and have complex business structures. That can make them difficult to value. As a result, there have been instances when companies throughout Asia try to liquidate their shares and raise capital but run into valuation problems and difficulties with tax authorities or regulators.

Opportunities

Families that plan ahead can mitigate many of the issues that might hinder their ability to raise capital. For example, through carefully designed shareholder agreements that could last for decades and regulate how shares can be traded inside and outside the family, families can ease ownership concerns and open up capital-raising opportunities.

While only a minority of family businesses express interest these days in an IPO, they might want to reconsider. In Asia, families often turn to the public markets to help with complex valuation issues. The public markets can solve a lot of the valuation issues that families encounter when they try to assign value to large, sprawling family businesses. For companies with such aspirations, that might mean they need to reorient their strategic focus—and align their finance and other reporting functions—toward quarterly performance measures.

Traditionally, bank finance was the favored route of raising funds for most family businesses if they couldn't generate the cash internally. While still a popular route for many, more family businesses are turning to outside investors (including private equity, alternative debt investors, large family offices, and high net worth individuals), especially when these investors can offer additional expertise within a particular industry.

There are a growing number of non-traditional sources of capital that are willing to provide capital on favorable terms with investment criteria that are better aligned with the needs of family businesses. Though family businesses are keen to maintain control, they also recognize that outside experience and knowledge can bring significant benefits to their company.

Overall, there's a rising pool of capital from a variety of providers coinciding with heightened needs for families to secure cash to fund their future growth, particularly amid uncertainty about the near-term outlook. Family businesses want capital today because the marketplace could be very different in the near future. In the event of an economic downturn, for example, access to capital might not be as strong as it is today with many providers and historically good borrowing terms. This can be a great time to begin to assess what a family business will need for the road ahead.

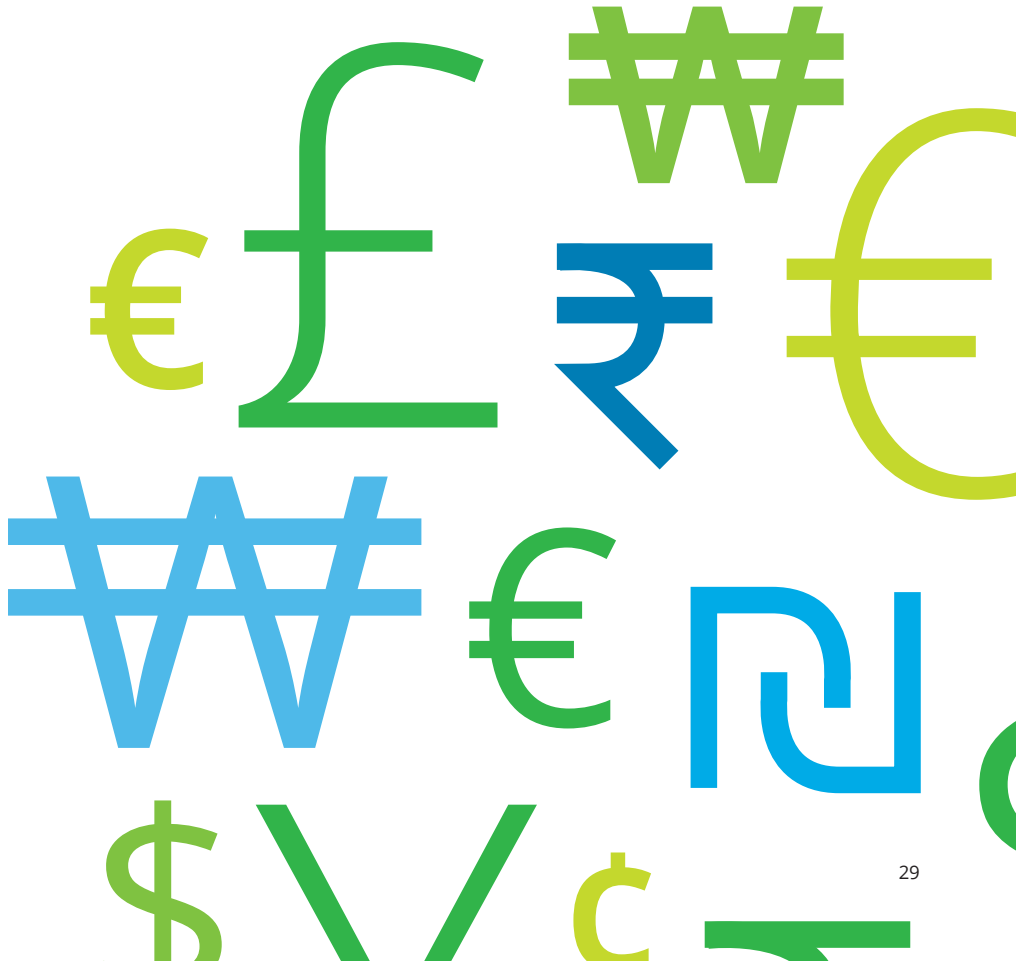
Questions to consider:

- What capital needs will my family business face in the near and long term?
- What are my options for securing capital? What non-traditional sources have we considered?
- What tradeoffs (if any) is my family business willing to make to secure capital?
- Is it important to find a lender who can bring more to the table than capital, in terms of advice and guidance about my business?
- Do we have enough financial flexibility and access to capital to weather a significant economic downturn?

Notes

1 *Global perspectives for family businesses: Plans, priorities, and expectations,* Deloitte, March 2018, https://www2.deloitte.com/global/en/pages/strategy/articles/global-perspectives-for-family-businesses.html.

2 *Global perspectives for family businesses,* Deloitte, March 2018.



Social responsibility: Why family businesses give back

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At a certain point in the lifecycle of family businesses, many owners ask themselves how they can support their communities—the places where they have historical, economic, and social ties. While some family-run businesses traditionally make contributions directly to charity, others set up foundations that support the values of the company to achieve their philanthropic goals.

Times and traditions are now changing. Increasingly, family-owned businesses and family offices are giving back through impact investing—identifying causes that include social objectives and financial returns, with specific performance measurements of both areas.[1] Social impact investing is a relatively new phenomenon: According to the nonprofit Global Impact Investing Network, more than half of impact investments have been made in the past decade. The current global impact investing market stands at $502 billion.[2]

In Deloitte's *2019 Global Family Business Survey,* 19 percent of respondents report that making a social impact with the business is among their family's priorities over the next 10 to 20 years.[3] But as family business leaders discuss how to effectively invest their wealth, there are multiple paths to ensure their contributions produce lasting impact.

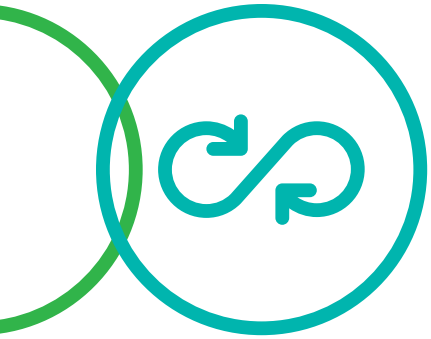
Issues

Social impact investing includes a number of different models, from upfront payments, to debt-based funding where providers split the risk with borrowers, to investments where payments come with the achievement of specific outcomes.[4] That compares to traditional social responsibility activities sponsored by many family-run businesses and family offices, where founders and owners set up a foundation to support a number of charities. Successive generations are challenging that model in favor of ways to embed social impact into projects.

There are scenarios in which emerging generations within family businesses attempt to influence founders about new approaches to social responsibility. The children haven't got the power, but they want to support social impact. So how do they convince the previous generation that still controls the money to decide to invest in these areas?

Approaches to social impact among family companies and family offices vary greatly across regions, largely due to historical business trends. For instance, some US or European family-owned companies have been operating for many decades or centuries and therefore have a long history of social responsibility activities.[5] That compares to Australia, where the legacy of postwar European immigration policies means that family-owned companies and family offices are generally newer and have begun to develop their social impact policies more recently.[6]

As family-run businesses across the globe shift their giving priorities to social impact investments, the changes are placing benefactors in the spotlight. For instance, some family members might not support investments with connections to potentially controversial causes, products, or services that run counter to the mission of the company. There's lot more pressure now to ask, "Are we doing the right thing? Are we supporting the right companies? Are we investing in the right companies?"



Companies should have a clear idea of the social responsibility policies of the organizations they intend to support.

Opportunities

One of the first things family business leaders should consider when they're setting up a social impact program is establishing guidelines around transparency. Some of the details businesses might consider when investing in social impact projects include the development of contracts, project design, and the evaluation of program outcomes. Companies should also have a clear idea of the social responsibility policies of the organizations they intend to support and ask for evidence of what they're doing in those areas before they start to invest.

In other cases, families aren't considering such projects at all, and it's common to hear younger generations question why founders aren't supporting social impact projects. One way to introduce the concept is by including younger or newer family members in decision-making roles around investments in corporate giving.

In this year's global family business survey, two-thirds of respondents say they expect to hand down their company within the family.[7] One of the key ways these companies can help their social impact program endure over time is getting family members across generations aligned around investment goals to avoid conflicts.

Questions to consider:

- What is my family's commitment to social responsibility?
- Am I open to new approaches to philanthropy?
- How do I determine whether my company and family are investing in the right causes?
- Have I set up a mechanism to ensure accountability from the organizations I intend to support?
- How can I attribute financial value to social impact?
- How should I continually evaluate my investments?
- What mechanism have I put in place to decide how to end an investment/engagement?

Notes

1 Natasha Doherty and Simone Cheung, "The role of evaluators in social impact investing," Australasian Evaluation Society Conference presentation, Sept. 20, 2016, https://aes.asn.au/images/stories/files/conferences/2016/Presentations/27NatashaDoherty.pdf.

2 Abhilash Mudaliar and Hannah Dithrich, "Sizing the Impact Investing Market," Global Impact Investing Network, April 1, 2019, https://thegiin.org/research/publication/impinv-market-size.

3 *Deloitte Global Family Business Survey 2019,* Deloitte, June 2019, https://www2.deloitte.com/content/dam/insights/us/articles/r7-12011_long-term-goals-meet-short-term-drive-family-business-survey2019/DI_Long-term-goals-meet-short-term-drive.pdf

4 Natasha Doherty and Simone Cheung.

5 "World Pasta Day 3 million spaghettate to charity," italiaatavola.net, Oct. 18, 2017, https://www.barillagroup.com/en/media-coverage/italiaatavolanet-world-pasta-day-3-million-spaghettate-charity.

6 "Postwar immigration drive," National Museum Australia, 2019, https://www.nma.gov.au/defining-moments/resources/postwar-immigration-drive.

7 *Deloitte Global Family Business Survey 2019.*

Family businesses and the future of work

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Every family business is unique and has its own distinguishing culture. But every family business faces certain core challenges, including attracting, developing, and retaining talented workers and adapting to changing workplace environments. In the *2019 Deloitte Global Family Business Survey,* talent/human resources emerged as one of the top five priorities for boards of directors over the coming 12 months.[1]

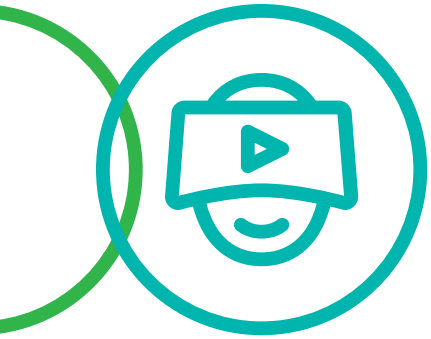
As their companies grow and the workforce evolves, many family businesses may need to eschew the hierarchical, entrepreneur-driven structures that created their foundational success. Both family and nonfamily employees require investment in them, and younger generations in particular will likely reward these efforts by bringing new perspectives to strategy setting.

Issues

The typical founder of a family business is a self-made matriarch or patriarch with entrepreneurial dreams and a bold business vision. But realizing those dreams takes a team, which often means hiring a manager from outside the family, a step that can be met with reluctance by founders. The first generation often doesn't understand that the presence of an external manager and the development of modern management culture creates value for the company.

When outside leadership is brought in, their role needs to be clearly defined, as a lack of clarification around their responsibilities can and often does lead to conflict. There is already the potential for tension since a third-party director who challenges a colleague who is also a member of the family may simultaneously be challenging a member of the board of directors or a shareholder. When the family foments a culture of interference, it can drive outside talent away from the company. Even an experienced CEO with years of multinational leadership may face new pressures in a family-led environment. In these instances, companies need a governance structure put in place to stop the family from interfering with what they hire these people to do.

More broadly speaking, it can also be difficult for founders to accept the different demands of workers from younger generations. For instance, they often have firm ideas about how hard employees should work in the early part of their careers and can bridle at the notion that they deserve a more equitable work/life balance, among other things. First generation leaders may need to adjust to changes in the workplace desired by younger talent who have different ideas about the hours that they work. They want flexibility and parental leave and social impact. According to the *2018 Deloitte Millennial Survey,* there were "strong correlations between those who plan to stay in their current jobs and those who said their companies deliver best on financial performance, community impact, talent development, and diversity and inclusion."[2] It's of little surprise that changing demographics of the labor force was cited by nearly a quarter of the respondents in Deloitte's *2019 Global Family Business Survey,* when they were asked to list the issues likely to have the most significant impact on the market in which they operate.[3]



As younger workers join the organization, it often leads to the introduction of new technologies, innovation and sources of growth.

Opportunities

When family businesses recruit external talent, it's important to take into consideration cultural compatibility. Family businesses tend to have strong values and cultures that reflect the family and the company, and it is important to hire people who understand the purpose and character of the business and will fit in. But many family businesses may also need to reinvent themselves by building a culture that supports continuous learning, incentives that motivate people to take advantage of learning opportunities, and a focus on helping individuals identify and develop needed skills.[4] Investing in talent development programs can help strengthen employees' attachment to the company while expanding their capabilities.

These kinds of investments tend to happen more often after the founders have made way for new leaders. Once the second or third generation take the helm, they often start to consider programs for education and retaining external managers. The second generation of the family is often very well educated and more oriented towards management than entrepreneurship.

Even when employee development is a priority, though, tension between family and nonfamily members is still inevitable. Families can work to reduce this tension by putting into place firm rules and regulations that anticipate conflict and help families manage internal politics as well as the business. Family governance structures can prevent interference by making family members aware of exactly how and to what extent they can be involved in the operation of the family company. Role clarification is really important. There should be role definition, key performance indicators, and annual performance reviews so that if there is any conflict between family and those working in the business, the solutions are clear.

As younger workers join the organization and begin working their way up, it often leads to the introduction of new technologies, innovation, and sources of growth.[5] In one company, for example, a second-generation leader recognized his son's technological savvy and awareness of how the industry was changing. Although he didn't originally understand it, the older leader allowed his son to add an online market to their business and test it for three months. The son put everything behind the digital platform to set it up for success during the trial period, and it became an integral part of their business that now accounts for 60 percent of company revenue.

As family businesses become more digital, they face a growing imperative to redesign themselves to move faster and adapt more quickly. For some, human resource issues may require organizational restructuring. This can be a particularly difficult task for family businesses to undertake, but the way high-performing organizations operate today is radically different from how they operated just 10 years ago. One important part of designing for adaptability is a shift away from hierarchical organizational structures toward models where work is accomplished by teams, the smaller and more flexible the better in many cases.

Questions to consider:

- How much of a priority is your board of directors placing on talent and human resources issues?
- Does your family business have a strategy in place for meeting future workforce requirements?
- When was the last time you revisited your incentive program to reflect changing demands of new workers?
- Does your firm have protocols and structures in place stipulating the roles and responsibilities of family members and nonfamily professionals?
- Has your company invested in suitable educational and development paths to nurture the talent of family and nonfamily, next-generation talent?

Notes

1 *Global family business survey 2019: Long-term goals, meet short-term drive,* Deloitte, June 2019, https://www2.deloitte.com/us/en/insights/topics/strategy/next-generation-family-owned-businesses-emea.html.

2 *2018 Deloitte Millennial Survey,* Deloitte, March 2018, https://www2.deloitte.com/us/en/insights/topics/talent/deloitte-millennial-survey-2018.html.

3 *Global family business survey 2019,* Deloitte.

4 *2019 Deloitte Global Human Capital Trends,* Deloitte, March 2019, https://www2.deloitte.com/content/dam/Deloitte/cz/Documents/human-capital/cz-hc-trends-reinvent-with-human-focus.pdf.

5 *2017 Human Capital Trends,* Deloitte, February 2017, https://trendsapp.deloitte.com/reports/2017/global-human-capital-trends/the-organization-of-the-future.html.

Ecosystems and innovation

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A lot of the talk about access to assets versus outright ownership in today's marketplace is around trends like carsharing or coworking. Companies that operate under these collaborative models have dramatically disrupted their industries. Family-owned companies are also debating the value of owning assets versus sharing them with partners in their ecosystems.

In a recent global Deloitte survey of next-generation family leaders, 56 percent of respondents see opportunity to tap into business ecosystems to grow their firms. A bigger share of executives in the survey (65 percent) said they've increased their interactions with third parties in recent years. Yet only a quarter of respondents report having a digital transformation strategy in place.[1]

Joining and thriving in an ecosystem can be a challenging yet rewarding endeavor for family businesses. Turning to external partners to collectively launch a new product or service can create conflict—especially when business interests have been closely guarded within family circles. But in contrast, the opportunity to grow a business as part of an ecosystem of disruptive innovators can take family business as far as their imagination will allow.

Issues

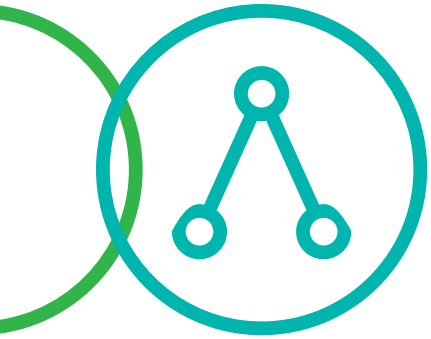
One way to view ecosystems is by describing them as communities that create and capture new value both through collaboration and competition.[2] As family businesses explore these networks, one of the first hurdles they encounter is often their own reluctance to trust third parties with sensitive company matters. Consequently, it may take years and a great deal of convincing before some family businesses are willing to even consider potential alliances. Add in the complexities of potential partners that are located in a different region or on a different continent, and it can be even more difficult to persuade business owners that collaboration with external partners is a good idea.

Many family businesses work with their instincts, and their appetite for risk is usually low. They are concerned about privacy, and about the environment in which the partners live. They take their time, and they wait for what they perceive to be the right opportunity.

A related issue for family-run businesses that are considering alliances is whether to build, buy, or own particular assets in the first place. Cost, technical complexity, or the availability of talent to build solutions internally are among the factors family-run businesses encounter in these scenarios.

Instinctively, people will start by saying "we'll build this on our own." Once they start digging into it, doing the research and the analysis, they often realize that there are components that they cannot master themselves, and that they are better off working with a specialist so they can achieve their targets faster and more efficiently.

There's also an emotional element to alliances. Before signing an alliance agreement, the parties tend to consider the underlying principles of the legal framework—that agreements be built upon mutual respect, and that partnerships include transparency both in deeds and words. That's especially true in global scenarios where a business partner is out of immediate reach.



Research reveals that organizations experience success when they access trusted external networks to help them develop new business ideas.

Business partners have to accept the fact that they may no longer own 100 percent of the parameters of their chain of production. They also need to identify how they are going to get their product at the best price possible, and with the best relationship possible. The world today is built on relationships: "Fail me once, you don't have a second chance to do business with me anymore."

Opportunities

There's power in collaboration when it comes to family-owned firms—which also happen to be among the most innovative companies in their sectors. A meta-analysis of 108 studies over three decades shows that although family firms tend to have smaller R&D budgets, their output per dollar invested in research is higher than other companies of similar size. The research revealed that these organizations experience success when they access trusted external networks to help them develop new business ideas.[3]

The existence of borderless supply chains is one way family businesses can achieve scale without having to make major operational adjustments. Reaching an agreement with a foreign supplier is far less complex than it used to be. It's easy for a family business to identify a potential partner in India or Zimbabwe, source raw materials, intelligence, and know-how—all without having to leave their home location.

Another phenomenon that may encourage global alliances is the generational shift that's taking place in family companies—especially in developing markets. As noted in the 2019 UBS Campden Wealth Global Family Office Report, past generations favored ownership, the current generation values experiences, while the next generation will regard transformation as a core value.[4] The next generation has less apprehension about the unknown, making alliances, and partnering with people they don't know on the other side of the continent or the world.

To thrive in today's dynamic, complex business ecosystems, many family-owned businesses will need to shift their mindset to take a more expansive view of the kinds of business relationships they can use to drive value. Family businesses that set high standards around accountability and measurement may have a better chance of success through strategic alliances.

Questions to consider:

- What can you accomplish by joining an alliance that you wouldn't be able to achieve on your own?
- How much are you willing to share with your innovation partners?
- Have you clearly defined the questions to be addressed during the due diligence phase?
- How would you assess existing ecosystems within your industry? Are there successful examples of alliances you can point to?
- What are your non-negotiable values in an alliance?

Notes

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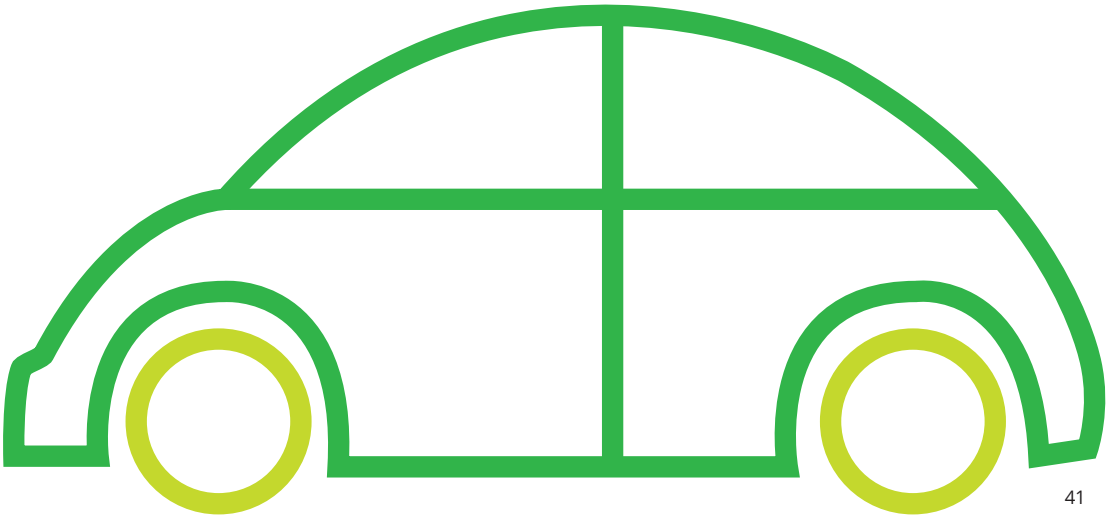

Cyber risk

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Today's family businesses operate in a highly connected environment in which the increasing volume of data has also intensified the risk of online attacks. Though many family businesses may consider themselves out of harm's way because they operate out of the spotlight, they still may be large enough to make attractive targets for hackers and criminals.

Despite the warnings and constant media coverage of information security threats, many family businesses have comparatively weak cyber defenses. Consider a recent report by Campden Research in which 32 percent of family offices reported losses from cyber attacks, yet fewer than half (48 percent) had cyber security plans in place.[1]

If family businesses intend to overcome cyber threats, everyone from the founders down to the most recently hired employees need to understand the risks—and recognize that the bad actors can launch attacks that hit close to home.

Issues

One of the most common tactics for cyber criminals is gaining the confidence of employees through realistic-looking communications. The offenders exploit that trust, convincing workers to release sensitive information, approve a financial transaction, or take other action that can have damaging consequences for the company. So-called "phishing" attacks are a global phenomenon, and a frequent problem in areas such as the Middle East. In this region alone, organizations reported the highest average number of breached records per incident—40,000 compared to the global average of around 25,500 per incident—according to a recent annual study on the financial impact of data breaches.[2]

Awareness and potential responses to these threats among family businesses generally varies by the size, industry, and visibility of the organization. For instance, a manufacturing firm might be focused on keeping its intellectual property secure throughout a supply chain. A consumer products company might be more concerned about customer data. In terms of governance, cybersecurity is now an agenda topic for many boards of directors.

Regardless of company size, sector, or prominence, the potential damage to family members' reputation is a worrying consequence of information security breaches. For example, fake social media posts from a hacked account can potentially harm a company's standing. Family businesses also should be concerned about exposure to attacks that arise from the use of connected devices—which could even expose homes and cars to cyber intrusion.[3]

Everything around families is sensitive information—their privacy, information about their assets, privacy around the non-business initiatives they have. As potential targets for cyber criminals, families have to work to protect their information, their privacy, and their honor.

Some leading family businesses address information security risks by embedding cyber readiness into their business strategy.

Complying with national and international information security regulations is another issue family-owned companies have to manage. In Turkey, for instance, the KVKK Personal Data Protection Law went into effect in 2016 in an attempt to bring the country's data protection laws into harmony with the European Union, and applies to entities processing personal data in Turkey.[4] The EU's 2018 General Data Protection Regulation (GDPR)—which sets guidelines for companies that collect and process EU customer data—joins a small but growing number of privacy-focused laws family businesses will have to keep in mind.[5]

Opportunities

Some leading family businesses are addressing information security risks by embedding cyber readiness into their business strategy.[6] In addition to third-party monitoring tools that can detect anomalies and enable a quick response, many families are taking advantage of education and awareness training, not just for employees, but for the founders and their successors. Some companies conduct full-day training sessions, while others simulate phishing attacks on their own employees to help them recognize the signs of a breaching attempt.

In addition to taking preventive, detective, and response measures, some companies and business families are also acquiring cyber insurance against breaches to protect the family business. The global cyber insurance market was estimated at about $4.5 billion in 2017, according to the most recent report from the EU-U.S. Insurance Dialogue Project.[7]

In the event of a cyber attack, the extra emotional element within families can present additional challenges. But for families that are prepared, the response can be quick and effective.

Questions to consider:

- Do you know your company's cybersecurity maturity level?
- Do you have a defined strategy in order to identify, protect, detect, and respond to potential cyber threats that may affect your business and/or your family?
- Understanding that many cybersecurity breaches are caused by human error, does your company train employees to keep vulnerabilities low?
- How can you start or improve internal training for staff on ways to avoid and detect threats?
- Are your data storage policies sufficient/up to date? How do you know?
- Do you have a clear idea of the digital assets that are most critical to your family and your wealth?
- Do you have a single point of contact who is responsible for information security matters? If not, are you willing to assign this responsibility to someone on your team?
- What is your organization's social media policy?
- How effective is your organization's policy on the use of personal devices for work purposes?
- Are you and your family members aware of your level of exposure to cyber, IT or social media risks? What measures are you taking to minimize exposure?

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Preserving family capital

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Family-owned businesses have a lot of demands on the wealth they create. There's the ever-present need to keep the business growing, but that requires investment—often in areas that represent new risks in order to stay competitive. There are also the demands of family members who want to increase their standard of living and enjoy their success.

Finally, many families want to create a legacy outside of the business, through philanthropic efforts that cement their name as multigenerational benefactors.

Unfortunately, many families are not particularly adept at managing these sometimes competing aims. Research has found that only 30 percent of wealthy families see their wealth survive past the second generation, and that figure drops to only 10 percent after the third generation.[1] Wealthy families are recognizing that to sustain themselves through the third generation they need to get a lot smarter about how they manage and preserve their wealth, and how they involve the next generation.

Issues

In Deloitte's *2019 Global Family Business Survey,* more than a third (36 percent) of respondents cited preserving family capital as one of their top long-term priorities for their businesses, second only to continuing their legacy and tradition (49 percent).[2] Both objectives often face stiff competition from individual family members with their own expectations for how wealth should be put to use.

A typical problem occurs when you have the wealth creator focused on preserving the wealth, while the next generation is more interested in spending it. In their eyes the family business is seen as a piggy bank. But business founders also aren't immune to constant calls on capital for personal reasons. It is not unusual for a family office to receive ad hoc demands for funds from a founder or family member to pay for properties or other lifestyle assets on short notice. Very often funds are already committed or tied up in illiquid investments, leaving the family office to call upon other sources, such as the company's operating businesses to provide the cash. This inevitably leads to issues with management, who typically would have earmarked surplus funds for investment in the business.

With newer family businesses in emerging markets, these types of conflicts are often replaced by an urge to use newfound wealth as a means of securing a more stable future—typically somewhere else. Political instability and wealth disparity in developing markets can see wealth dry up, virtually overnight.

In South Africa, where wealth redistribution in the post-Apartheid era is producing new millionaires from previously disadvantaged groups, younger generations from some wealthy families are seeking to leave the country amid political uncertainty and a sluggish economy.[3] One of the challenges family businesses face is that future generations might not be there to continue the family legacy.

These challenges are exacerbated by a lack of organization and structure in family offices representing families that have recently acquired wealth. Without a dedicated third party to help manage their wealth, conflicts can break down into legal squabbles. For many wealthy families in emerging markets, this is new wealth, so it's almost like starting from scratch. They have no structures for managing and preserving their wealth.

When things go wrong, family members may point fingers at the family office by default.

In developed markets, the problem is often the opposite—longstanding family offices that have failed to keep up with the times. Many families have relied on the same team for decades when it comes to providing wealth management advice and services, and some haven't stayed abreast of changes; in particular, exposure from new threats such as cyberattacks. Today, there is the prospect of real reputational harm for families who are the targets pf cyberattacks.

Opportunities

Many family businesses are looking to professionalize their wealth management, either by creating a new family office or ensuring they have the right people staffing it and appropriate systems and controls. For example, experts with advanced investing strategies such as private equity can be aligned with tax advisers capable of reviewing existing tax structures to make sure they're fully compliant with any jurisdiction in which the family invests or has a presence.

There's an education that needs to take place about what the family office is supposed to do and the benefits the family members are supposed to receive. When things go wrong, family members may point fingers at the family office by default; however, some issues may stem from a simple lack of alignment between the family and the family office around vision and values.

One recommendation is that family offices sit down at agreed intervals with individual family members to understand everyone's individual needs. Often, these conversations can yield insights that help set the course for the family business, including decisions to sell the business and cash out or take some of the capital out of the business and reinvest it in another venture. This can help establish the right expectations through transparency and engagement.

In many instances, appropriate diversification of family wealth can ease concerns about preserving it. In addition to alleviating the need for individual family members to take money out of the business to diversify their assets themselves, this strategy can also reduce the dependence on the home market and its exposure to negative economic or political developments.

In South Africa, for example, diversification is a huge part of wealth preservation. A lot of the population there is generally globalizing their exposure with a view to preserving their wealth. As those efforts expand, it will be critically important that they are done right, with due attention paid to compliance with tax and other regulations across the globe, and appropriate governance to ensure risk controls remain up to date.

Emerging markets such as South Africa are also creating fresh opportunities for family businesses to create legacies through a greater sense of purpose. Many are working to set up philanthropic foundations in order to contribute to the region's redistribution of wealth. There's a growing sense of social responsibility on the part of businesses here to give back to their communities. It's now a big part of the mindset for wealthy families, both new and established ones.

Questions to consider:

- What kind of formal organization do we have in place for managing the wealth created by our family/family business? Do we have an appropriate governance structure in place?
- If a family office has been established:
  - When was the last time our family members sat down with the family office to share our expectations about its purpose and the use of family funds?
  - What kinds of capabilities do we need to add to our family office to meet our vision for it?
- Do we have an appropriately defined investment strategy?
- Are we confident that we are fully in compliance with the tax and other reporting requirements of every country in which we reside, invest or own property?
- Could our family's philanthropic mission benefit from being more formalized?

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Succession planning: Regional perspectives

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Around the world, many families are not fully prepared to transfer their business to the next generation. In Deloitte's 2019 Global Family Business Survey, just 41 percent of respondents said their business was ready for the future in terms of succession planning. By contrast, more than half said they were fit for the future when it comes to issues surrounding ownership, governance, or strategy.[1] As the survey results show, succession is the challenge many families find most daunting.

Our findings on more specific planning details show the extent of the work to be done: Just 26 percent of respondents said they had a succession plan in place for the chief executive position, and even fewer had plans for other C-suite roles. It's not for lack of wanting. Almost two thirds (65 percent) said they wanted to pass ownership to the next generation, and within that group, 30 percent said they wanted to keep both ownership and management in the family.[2]

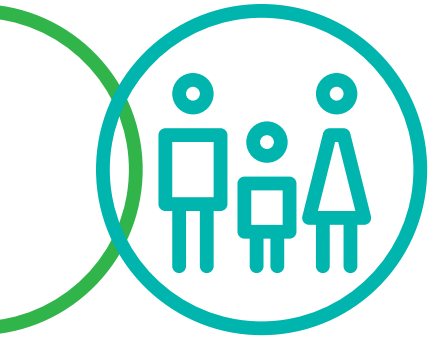
Much of what goes into planning for business succession depends on the cultural traditions and attitudes in a particular society—even if the broad preference for maintaining family control is something seen in every locale. Succession, understandably, is influenced by culture. As a result, the process for a family business in China can be very different than the process for a family business in Germany, for example.

Issues

In China, most of the wealth in today's family companies is quite new. The first opening of the Chinese economy only began in the late 1970s under Deng Xiaoping, and the extraordinary growth in the country's private sector has mostly occurred in the past two decades. This means that many Chinese family businesses are grappling with succession for the first time. Readiness in China is 15 percent, compared to the global average of 42 percent among respondents in our 2019 family business survey.[3]

What's more, the second generation in many wealthy mainland China families mostly has been educated overseas and even may have begun careers outside of China. These younger individuals may want to go into a different business than their parents, or possibly start new ventures rather than fully take the reins of the existing enterprise. Another common feature of family business succession planning in China relates to the government's one-child policy, in place until recently. As a result, many families in business there only have one child.

Japan is in some ways China's opposite, with a very well established tradition of family companies passing from generation to generation. Some of the oldest family companies in the world are Japanese.[4] Adherence in Japan to primogeniture, the tradition that the entire family business or fortune passes to the firstborn son, helps keep control concentrated through multiple generations. This cultural feature has affected the succession of family businesses in Japan for a very long time.



Once the family tree is expanding or enlarging through five or six or seven generations, issues become much more complex to deal with.

Germany is another place where multigenerational family businesses are well established, and most of these are doing a good job planning for succession. While some first-generation entrepreneurs in Germany may not have adequate plans established yet, businesses that have already passed at least to a second generation are likely to have a family charter in place and to have worked through key issues.

Opportunities

In China, members of the second generation of a family business may be better positioned to get the succession planning effort moving—and may be incented to do so based on their own unique needs. Their parents have spent decades immersed in the operational and strategic matters that go into building a business, and they may have a difficult time shifting focus to the task of handing the company off to heirs.

Because there's often just one child in the next generation, families in China should be paying attention early to the question of whether that child wants to take over the running of the business. If not, the family will need to consider members of the extended family—cousins perhaps—who might be groomed for the task. Alternately, the first generation may want to think about developing managers and executives who can be trusted with the future leadership of the organization.

Wherever the family is located, that first handoff, from the founders to their children, should include clear instructions for how the enterprise will be run and governed for the generations that follow. Especially in countries such as the United States where primogeniture is not the norm, each member of successive generations may get a share of family assets. Once the family tree is expanding or enlarging through five or six or seven generations, issues become much more complex to deal with.

Well documented instructions also are important when more than one child will be inheriting. There's potential for conflict should it be left unclear who will have responsibility for particular aspects of the business when succession occurs. Related to that, family businesses also should strive to be certain that individuals in the next generation are properly prepared for the handover, with a full understanding of the business, the right set of skills, and an established timeline.

In Germany, it's sometimes possible to lose sight of key issues that could help ensure the long-term operational success of a family company because complicated inheritance tax issues become dominant in succession planning. While efficient tax management is necessary, too often taxation issues come first and the tax adviser may dominate the process. Family business may want to reverse the order, focusing first on preparing the successors who will run the company and positioning the business to thrive—and then consider the tax aspects.

Indeed, keeping a focus on business strategy throughout the succession planning process is becoming more important than ever. As industries are disrupted by radical technological changes—ranging from robotic process automation to artificial intelligence—business models need to be rethought ever more frequently.

A succession plan cannot be set and then put on the shelf. It should be a priority to make regular updates as a family company's focus and strategy change. Globalization makes this an issue that crosses all borders and affects succession planning in any culture.

Questions to consider:

- Will control of our company remain concentrated in a single individual in the next generation, and is that person fully aligned with existing plans for the business?
- Is there be a process under way to identify members of the extended family or professional managers who can be groomed to lead the enterprise?
- Even if current leadership expects to run the company for many more years, would existing succession plans be sufficient for a smooth transition if something unexpected happened?
- Does our company's succession plan address a proper balance among family members, shareholders, professional executives, and other stakeholders?
- Are tax considerations taking precedent in succession planning over operational and strategy matters that might better prepare our company for the transition?
- Is our family's succession planning process dynamic enough to keep up with changes in business strategy in response to faster paced economic, market, and technology trends?

Notes

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