



THE  
NORTHERN TRUST  
INSTITUTE

# KEEPING THE FAMILY BUSINESS IN THE FAMILY

FIVE STRATEGIES TO PRESERVE THE LEGACY OF YOUR  
FAMILY BUSINESS FOR FUTURE GENERATIONS



Many successful business owners face a common problem — how to ensure your business remains family-owned from one generation to the next. Laying the groundwork for sustaining a multigenerational family business involves making critical decisions around ownership, management and family communication in the form of a governance structure.

By establishing an objective governance structure well in advance of the next leadership change, you can reduce the chances of future family conflicts, and improve the likelihood that decisions about the business will be made in a way that aligns with your family's long-term vision.

### What Can Go Wrong?

Consider the case of a client, the owner of a large technology business who passed away, leaving equal shares of his business to his three sons. One son succeeded his father as president of the company, while the other two were not involved in the business. Aside from basic estate planning, before his death, their father did not outline his long-term vision for the business, nor did he create a formal governance structure for how information about the business would be communicated to shareholders or establish guidelines for voting the shares. As a result, within a few years after his death, the sons who did not work in the business voiced concern over the lack of information they were receiving about the company from their brother. They complained that with no “seat at the table,” they lacked the ability to offer their input and ideas on the strategic direction of the business. Concern soon turned into animosity, with accusations that the brother running the company was mismanaging it and intentionally withholding information. Although the brothers eventually agreed on a path forward, the family dynamics were irreparably harmed.

To avoid similar conflicts within your family and lay the foundation for your own governance structure, here are considerations to help you preserve the legacy of your family business for future generations.

## CREATING A GOVERNANCE STRUCTURE

Before you begin building a governance structure for your business, consider the following questions:



### Family

What is your vision for the business over the long term?

Have you communicated your vision to your family members?

Are there any current or anticipated tensions in your family relating to the business?

How do family members get involved with the business, formally and informally?



### Ownership

Who will own shares of the business (voting, non-voting) during and after your lifetime?

What rules will dictate how shareholders vote on corporate matters and transfer their shares?

How will shareholders receive sufficient information on the business to allow them to make informed decisions when they vote their shares?

Have you identified any long-term, trusted advisors or friends who, in some capacity, can help provide guidance to family members who own shares of the business?



### Management

How does the business identify and groom individuals to succeed the current management team?

Are there next-gen family members willing to assume leadership roles within the business?

Are these family members prepared for the roles that they will be stepping into?

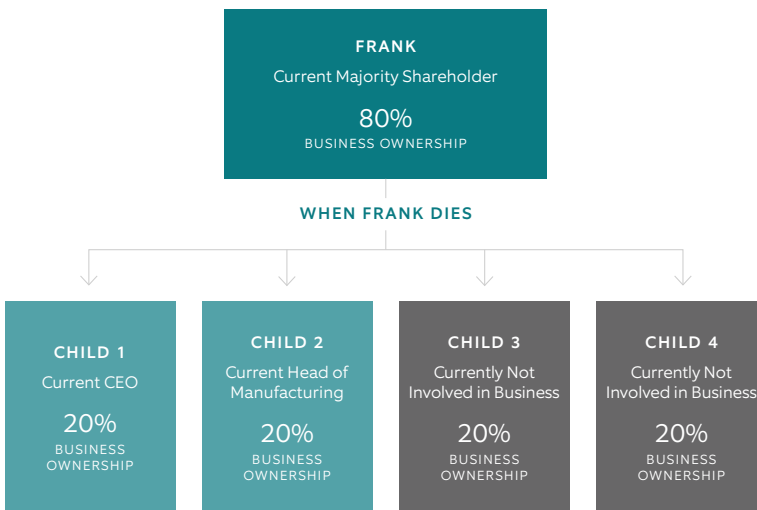
Does the business have a functional governance structure in place (e.g., a board of directors)?



# STRATEGIES FOR BUILDING A FAMILY AND CORPORATE GOVERNANCE FRAMEWORK

Our client, Frank, owns 80% of a packaged food company generating approximately \$35 million in annual revenue. Two of Frank's four children actively work in the business — one recently became the chief executive officer, and one oversees the company's manufacturing operations. The other two children are not involved in the business. Previously, 20% of the business was transferred to the family.

In his estate plan, Frank plans to give equal ownership of the business to all four children. Although he would like the business to remain family-owned and operated, he is concerned about how his children and future generations will handle major corporate decisions (for example, hiring senior executives) when he is no longer around.



We advised Frank, as we do with other clients experiencing similar concerns, to consider implementing the following five strategies to build a more robust family and corporate governance framework for his business.

1. Draft a Family Cornerstone Statement
2. Consider a Delaware Directed Trust
3. Establish a Family Voting Agreement
4. Form a Family Council
5. Develop a Leadership Succession Plan

## DRAFT A FAMILY CORNERSTONE STATEMENT

A cornerstone statement is a document that captures your family's shared past, projects it into a vision for your collective future and identifies action steps to bridge current and future states. The [five-step process](#) Northern Trust has developed to help families draft their cornerstone statement is designed to incorporate both financial and non-financial priorities while promoting healthy communication patterns, developing decision-making skills and building transparency among family members. All are skills we have found to be the hallmarks of successful multigenerational families.

### Components of a Cornerstone Statement

- A motto consisting of a short phrase that encapsulates your family's core beliefs
- A list of three to five core family values
- A vision statement that describes your family's future direction
- An action plan of three to five agreed-upon steps to put your family's shared values into action and begin building toward your vision for the future

### EXAMPLE CORNERSTONE STATEMENT



Our family is a loyal and supportive family, dedicated to compassionate involvement in each other's lives and advocating for one another's well-being. We are a family that values experiences that provide knowledge and awareness of other cultures and perspectives, building our capacity to be empathetic and open-minded. We desire to stay motivated and active intellectually, physically and emotionally, consciously searching for ways to improve both ourselves and the world around us.

## CONSIDER A DELAWARE DIRECTED TRUST

Transferring voting shares of the business into a revocable Delaware directed trust allows for the retention of full discretion over the shares (shareholder votes, distributions, etc.) during your lifetime, while providing for a division into separate trusts, holding equal shares for each child upon your death.

- Children could serve on an investment committee that would allow them to participate in investment decisions along with members of your inner circle of advisors.
- Alternatively, you may want to consider giving shares in trust only to those children who are actively involved in the business, while providing your other children with non-business assets of equivalent value having the potential to generate a similar cash flow (for example, real estate).



## ESTABLISH A FAMILY VOTING AGREEMENT

In addition to creating a trust structure to address family and investment succession, this document should:

- Determine who will vote the shares — family members or a voting group comprised of both family and non-family members with provisions for appointing successors.
- Note that consideration will need to be given to coordinate with the terms of any existing trusts and/or partnerships that may currently hold shares of the business.

### Provisions to Consider Including

Typically, a family voting agreement is put into place so that all shares of the company are voted as a block. This is especially important in situations where some shares are held outside the family or might be at some point in the future. Typical provisions to cover include:

- Subjecting the shares held by all parties to the voting agreement, including all future holders of the covered shares
- Providing a mechanism for voting the shares as a block (e.g., by majority vote of all parties to the voting agreement, by committee or by family branch with tie-breaker provisions)
- Specifying the period covered by the voting agreement (e.g., perpetual, terminates after a period of time or upon supermajority vote, or terminates upon an event such as a sale or IPO)



## FORM A FAMILY COUNCIL

Create a family council comprised of all your children and adult grandchildren. The family council allows your family to bring to life the shared values and vision articulated in your cornerstone statement. The family council's responsibility is to keep family members who directly or indirectly own shares of the business informed about the company — especially those who are not actively involved in the business. Further, the family council will provide input to the board and any outside advisors with voting responsibilities regarding the family's desires with respect to the business.

- If family members are voting the shares, having such a council helps align the way family members vote with the family's long-term vision for the company, as reflected in the cornerstone statement.
- If a voting group is voting the shares, having a council helps promote awareness of the family's vision for the company as well as the perspective of management and outside advisors.

### **Typically the family council bylaws set forth the operational rules for the council, including:**

- Who is considered family (blood relatives, in-laws, both)
- Eligibility to serve on the council (representatives of different family lines, etc.)
- Matters the council will consider
- Connectivity with the company, such as:
  - Information shared with family council (e.g., periodic management updates and reports)
  - How the family council will provide input to the company (e.g., the family council's chair serves as one of the company's board members, or a board member is designated as the liaison with the family council)
- A mechanism for the family council to engage with next-generation family members who may serve as future leaders (management, family council and/or board members), for instance: periodic meetings with the next generation, management presentations, office tours and participating in corporate events and philanthropy

## DEVELOP A LEADERSHIP SUCCESSION PLAN

Having a [leadership succession plan](#) for your company addresses potential senior management vacancies and ensures that the board of directors has the right combination of family, management and outside, independent perspectives. When doing so, it helps to consider forming a Succession/ Management Development subcommittee of the company's board to help draft a succession plan for both the board of directors and the senior management team.



# GETTING STARTED

With decades of experience helping business-owning families navigate succession challenges, our Family Business and Family Education and Governance Groups welcome the opportunity to work with you to develop a governance framework that meets your long-term objectives.

#### ABOUT THE NORTHERN TRUST INSTITUTE

The Northern Trust Institute is a research center dedicated to advising affluent families. More than 175 experts collaborate across 34 areas of expertise to analyze behavioral patterns and identify the strategies that have been most effective for our clients — bringing the breadth and depth of our firm to each unique situation. The resulting insights position you to take action with confidence and achieve optimal outcomes with your wealth.

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