REFLECTIONS ON LEADERSHIP AND FAMILY BUSINESS CONFLICTS
(& Why It Matters for Family Attorneys)

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"Within every family, every community, and every organization, there are trials, tests, and tribulations. Do these lead to arguments, blame, and recrimination? Or does the group see them providentially, as a route to some future good (a "descent that leads to an ascent" as the Lubavitcher Rebbe always used to say)? Does it work together to meet the challenge? Much, perhaps all, will depend on how the group defines its reality. This, in turn, will depend on the leadership or absence of leadership that it has had until now. Strong families and communities have a clear sense of what their ideals are, and they are not blown off course by the winds of change."

Rabbi Jonathan Sacks, Lessons in Leadership

Attorneys advising wealthy families and their family owned enterprises are frequently asked by these clients what are the characteristics to help them navigate the inevitable tumultuous family conflicts and stay true to their purpose and mission?

One might think that the logical solution to avoiding these conflicts, or at least substantially mitigating them, lies in the process of more structural business planning. That is too narrow a conclusion.

One thoughtful family advisor perceptively (& humorously) articulated the problem:

> *"There is an old estate planning joke (of sorts) where an attorney is being arrested standing over the dead body of a client with a smoking gun on his desk. When questioned as to his motive, the lawyer says -"That plan he just signed was so complex and elegant, with so many moving pieces, I just had to see if it would actually work."* [1]

There is no shortage of real-life cases where the courts have commented on the brilliance of some type of estate planning strategy which resulted in significant estate tax savings for the family but that very same plan seemed to have provided the petrol for the fire for the ensuing acrimonious litigation resulting in the near destruction of the family enterprise.

Families with diverse business interests are like ships at sea. When the weather is fair and the sea calm, the structural integrity of the ship is not under stress. Vulnerabilities, such as deeply rooted family issues or even leadership succession issues, are either not recognized or ignored under the guise of not being imperative. Unfortunately, human nature being what it is, all things change-including the values and perspectives of different family members which in many cases frequently diverge from tax centric "estate planning" strategies ingrained in the operating business. And when these forces collide the family enters a tempest.

The events could be unexpected and internal, such as the untimely death of a family patriarch or matriarch that provided the "glue" of keeping the family bound together, or external business pressures that materially degrade the ability of the family business to generate sufficient cash flows to satiate the needs of diverse stakeholders in the family enterprise. Today, changes come rapidly, sometimes unexpectedly to all industries, the immunities are none. But, when these changes happens to family enterprises, highly technical tax driven family planning that ignores conflicts of interests between different family members can quickly digress into a perfect storm, endangering the fabric of the family and stress to the entire business enterprise.

CAUSES

The relatively new multidisciplinary world of advisory services focusing on family owned enterprises, has populated significant research into the area of the root causes of conflicts and the triggering events that are all too often seen by those attorneys and other professionals focused on this area of work.

It certainly should be noted that even the word "conflict" in family owned enterprises can be a misleading term. Some practitioners have noted the positive outcomes of family conflict. "Conflict provides an opportunity to obtain greater understanding of the opposing parties and how they think, act and feel. It gives individuals a chance to demonstrate an acceptance and respect for the unique ways in which others think, act and feel." [2]

But conflict left unchecked without help from professionals deeply schooled in understanding this area of work is likely to spiral out of control. And as many professionals have noted, families in business have a hard time openly talking about and analyzing these divisive issues-even when they can negatively impact an operating business. But this aversion to deal early on with these issues is depriving the family (and the business) of its needed oxygen.

In a valuable new book entitled Deconstructing Conflicts – Understanding Family Business, Shared Wealth and Power [3], the authors frame for us three core reasons for all conflict in business families. While seemingly self-evident to many practitioners, these reasons are: Opposing goals, Incompatible values and Historical Impasse.

Examples are indeed abundant of opposing goals and have no complete inventory, but for many families who share business enterprises some examples include:

- Paying dividends to help lifestyles of non-working family members vs. reinvesting free cash flow for growth,
- Sell the company to monetize all the years of hard earned work vs. retaining of ownership of the enterprise as a means of perpetuating the legacy of those family member(s) who still work in and control the enterprise.

But all of this begs the question of what triggers these conflicts. As noted earlier, many of these "estate plans" seem fine when conceived. My (non-scientific) observations are that hibernating over long periods of time there is a subtle noxious interplay between leadership that can become compromised and highly structured business planning that has the potential to alienate different family members by creating subtle conflicts of interest.

"Conflict is triggered by the exertion of power by one individual or group over another, in a manner that is perceived as without legitimate authority or moral authority, arbitrarily, undeservedly… or humiliating to the target of the power." [4] Conflicts of interest can certainly devalue legitimate authority.

And when conflicts erupt the differences in the attributes of a leader and a trustee's fiduciary duties become apparent. Compromised fiduciaries, once camouflaged by indifference are now targets of anger.

Examples are abundant but usually involve family values that collide, deep conflicts of interest in one key family member having different roles in overseeing the enterprise, preferred and non-transparent compensation systems and deeply rooted family behavior that predates most advisory services.

So, how does this relate to the practice of law and the delivery of services to these business families? How can attorneys be of value to these families when all too often clients either want quick answers or are too impatient to pay for services that are indeed hard to conceptualize arising in the future?

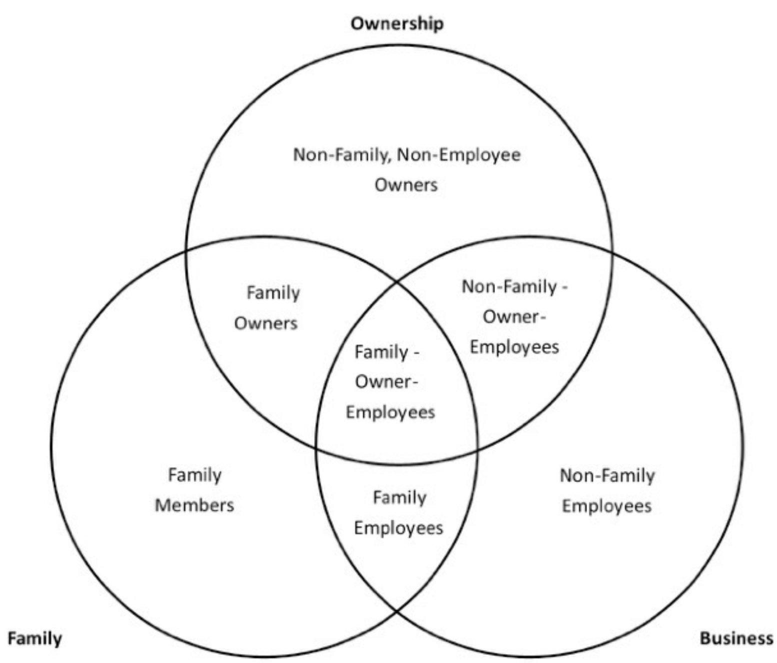
THOUGHTS ABOUT LEADERSHIP

A few short comments about family business leaders. Being a leader is not (or should not) be something anyone inherits-it needs to be earned and not just by hard work-a leader needs to exercise a high level of moral authority, be a keen listener and have humility for their office. Today, leadership based upon primogeniture is rarely of long term benefit to a family.

As Rabbi Sacks has noted: “It is the vision that matters, not the office, the power, the status, or the authority. Leaders are led by their vision of the future, and this is what inspires others.” Like a sieve, compromising this office, this moral human compass with conflicted duties, only dilutes one’s authority and vision no matter how well intended.

Being a trustee and being a leader of a family enterprise should never be confused as simultaneous duties. There is indeed a fundamental difference between a family choosing the right leader (which is certainly hard enough and which can fill a library with literature) and a non-conflicted fiduciary acting as Trustee for other family members who are stakeholders in the family’s enterprise. A family member assuming the twin duties of these two offices (leader & trustee), even under the best of intentions, will likely not work.

Even a quick glance at the famous three circle model below [5] details the complexity of most family enterprises – making it clear to any casual viewer the complexities of managing family enterprises. So, why complicate offices?



Tagiuri and Darvis, 1982 [5]

IN THE CONTEXT OF PLANNING

It is not unusual for the parents of a family enterprise to leave their discounted and non-voting business interests in trusts centrally managed by trustees who all too often lack a deep understanding of the family, business and fiduciary duties. This type of legal planning only exacerbates deeply rooted family behaviors.   Unfortunately, all too often this planning fails to account for the fact that some family members are getting disenfranchised and have no voice in the vision of the company, and have few, if any, clearly defined exit strategies to monetize the value of a gift or inheritance.

But in this author's opinion not carefully thinking this through, not building into the family business a set of checks and balances is like walking on thin ice in an April thaw-go too far out in time and there will likely be severe fractures in values and expectations of different family members ultimately culminating in the family falling into the great morass of frigid water.   One just never knows when these fractures occur, but poor governance systems deeply rooted concentric only tax planning are one of these fracture points.

Without a system of checks and balances, the appointment of a director or other key officer as trustee of a trust that owns a family business can easily compromise the general fiduciary duties of loyalty and impartiality that any trustee owes to its beneficiaries.   Officers and directors often have very different viewpoints about what is best for the family enterprise. Thus, it is not hard to imagine a situation arising where some family members might feel alienated and estranged when they are disenfranchised from the decision-making process. They inherited their status due to, in this example, estate planning ideas that were good for tax mitigation- i.e. creating business interests that have no voice or control in the business. While it is often noted that not all conflicts are conflicts of interests in the legal sense, preventing the interested family member or board member from serving as a trustee, diligence must remain high to carefully plan with key professional advisors the structures of governance that remain transparent and elastic over extended periods of time. These are systems where values are aligned in the family and where the checks and balances of governance are ingrained in the family's ethos.

Navigation through family conflict usually requires a leader with a keen and sincere sense of listening to other family members and who has no ingrained conflicts of interest.

Some might say that there is even a simple example to emulate-In the United States our three branches of government, Executive, judiciary and legislature, are there for a reason.

Footnotes

1. The Problem with Planning, Matthew Wesley, The Wesley Group.

2. The Legacy Family, Lee Hausner & Douglas Freeman, 2009, Pg. 140

3. Deconstructing Conflict, Understanding Family Business, Shared Wealth and Power, By Doug Baumoel and Blair Tripp, 2016

4. Id, page 57

5. The Three-Circle Model of the Family Business System was developed at Harvard Business School by Renato Tagiuri and John Davis in the 1970s. It continues to be, the central organizing framework for understanding family business systems, used by families, consultants and academics worldwide. This framework clarifies, in simple graphic terms, the three interdependent and overlapping groups that comprise the family business system: family, business and ownership. As a result of this overlap, there are seven interest groups present, each with its own legitimate perspectives, goals and dynamics. The long-term success of family business systems depends on the functioning and mutual support of each of these groups.