Family Business Organizational Structure

By Roger Zimmerman

The family has always been important in God's plans throughout history. The command to "be fruitful and multiply and replenish the earth and subdue it" was his first commandment to Adam and Eve.[1] In the early Biblical narrative God worked through family units such as Noah, Abraham, and Jacob in forming the 12 tribes of Israel. Throughout the Old Testament, the family has an important part in society and the faith community. Joshua 4:6 shows that fathers and children will be together in the coming generations: "That this may be a sign among you, that when your children ask their fathers in time to come, saying, What mean ye by these stones?"

The Bible places the primary responsibility on fathers to pass on the faith to the oncoming generations. Deuteronomy 6:7 shows that this should happen naturally as we go about our daily activities.[2] At one time this was done on family farms here in America, but this is no longer a viable option for all families and communities. As a result, many Anabaptist people work together in family businesses. For our people, the family business isn't just for making a living by making products or providing services; it is a way to teach the principles of faith as lived out in daily life and work[3] and to be a light to society.[4]

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Since family businesses have historically been a part of Anabaptist society, why is organizational structure, and more importantly family business governance, important to discuss now? Why is it even an issue?

Family governance[5] is a topic many families are reluctant to discuss, but it is vital to the health of a growing business. What may have worked early in a family-owned business may no longer work as the business grows. There is a need to discuss things like estate plans, family business leadership transition, and family fairness.[6] Family Business Institute states that "most family businesses, especially in the formative years, take on the characteristics of the founder or founding family. Although this entrepreneurial model works for an early-stage family-owned business, as

[1] Genesis 1:28

[2] Deuteronomy 6:7 "And thou shalt teach them diligently unto thy children, and shalt talk of them when thou sittest in thine house, and when thou walkest by the way, and when thou liest down, and when thou risest up."

[3] Colossians 3:17 "And whatsoever ye do in word or deed, do all in the name of the Lord Jesus, giving thanks to God and the Father by him.

[4] Matthew 5:16 "Let your light so shine before men, that they may see your good works, and glorify your Father which is in heaven.

[5] The main purpose of family governance is to define how a family-owned company is to be run once more generations get involved and/or more family members become active within the family business.

[6] https://www.familybusinessinstitute.com/consulting/family-governance/

the company grows in size it needs gradual evolution to a different model."

In the Zimmerman family,[7] we've come to pay more and more attention to family business governance. You'll have your own unique story as your business grows and changes. Nevertheless, we conservative Anabaptists share the same goals of effective decision making, cohesive teamwork, a God-honoring legacy, and positive succession. As you follow our story, you may find areas that also apply to your family business.

Family business governance isn't a romantic topic, especially when it comes to talking about accountability. We tend to think of accountability as discipline if we fail to do something, and that makes us feel uncomfortable. However, clear accountability does not have to be negative. In fact, it is vital to the future of a family business. This article will address three spheres of influence in organizational structure and how there needs to be clear accountability between each of them—the family, the ownership, and the business. We'll also look at how a family business tends to grow and how accountability can be easy to resist, especially early in the growth.

But first, let's answer the question of why family business governance matters.

Why Does Family Business Governance Matter?

One of the main reasons family business governance matters is that the energy and vision of a founder or leader will only last so long. The business can falter when there is no plan in place for how the business will continue after the initial driver has passed off the scene.

I've talked with quite a few people in family business. For many of them, things didn't work out well when a founder tried to hang on too long to the business. The leader may have had the underlying feeling of, "I'm going to live forever." From my experience, most people who try to live forever die trying.

A few years ago, I talked with the former chief financial officer of a large family business whose founder wouldn't let go. He made no effort to plan for his succession. After the founder passed away, issues arose and the business ceased to exist in just a few short years. It was devastating to the family and employees. This is why it's important to look at family business governance.

The oldest known family business was a Japanese construction business called Kongo Gumi, which specialized in building Buddhist temples. They were in business as a family for 40 generations. The business was operated by the family from 578 A.D. to 2006 when it fell on hard times and was purchased by Takamatsu Construction Group. That's a total of 1,428 years of transitions! Did they focus on family business governance? Yes, they did. That was very important to them. Through the years, the line continued through either a son or a daughter. Its last president was the fiftieth Kongo to lead the firm.[8]

Sadly, this story is rare. Family-controlled businesses make up about 62 percent of the U.S. workforce and contribute about 64 percent of the U.S. gross domestic product. However, statistics show that only 30 percent of these family businesses successfully move into the second generation. Only 12 percent move into the third generation and only 3 percent move into the fourth generation. Why do 70 percent of family businesses not even make it into the second generation?

Most times there are issues within the family dynamics and how the family relates to one another. A lack of clarity in family relationships carries over into how the business should be run when thinking of transitioning between generations.

One of my earliest memories of hearing about family business conflicts was when I was working in our hardware store after school. One evening a customer whom I was helping said, "I don't understand how you guys can get along working in the family business. A few years ago, I hired my sons in my business, and I soon came to realize that I was going to have to kill them or fire them."

Being fairly shy, I simply replied, "So what did you do?"

"Well, I fired them," he replied. That stuck in my mind, and I haven't forgotten this gentleman's frustration with trying to bring his sons into his business.

Many families I have met over the years have transitioned into the fourth, fifth, and sixth generations in the family

[7] Roger Zimmerman is the third generation of the Zimmerman family at Paul B. Zimmerman, Inc.

[8] Wikipedia contributors. (September 27, 2018). Kongō Gumi. In *Wikipedia, The Free Encyclopedia*. Retrieved 14:44, November 9, 2018, from https://en.wikipedia.org/w/index.php?title=Kong%C5%8D_Gumi&oldid=861420465

business. Invariably they spent time developing the three spheres of family business governance that we will look at later in this article. Looking first at how a family business grows will help us see why these spheres matter.

Stages of Family Business Growth

The first stage, sometimes called the founder stage, is characterized by a founder who has tremendous commitment and passion for the work. He spends a considerable amount of time in survival mode; that is, he survives with some financial hardships and a very simple governance structure.

In our family's history, Paul B. was this type of founder. He moved into manufacturing after not being a very good farmer. He loved to serve the community by fixing and making equipment. As he worked in this early stage, he knew what survival mode was all about and how to stretch to make ends meet. He lived that way for a long time.

The second stage in family business growth is the sibling stage in which the children of the founder are entering the business. They often bring new energy and ideas but are still pretty close to the founder and know what the business is all about. Children can become involved in the life of the business as early as the first decade.

The third stage is what I call the "cousin stage" or what some have called the "cousin catastrophe." Things start getting complex at this stage—cousins are working with cousins, and in-laws are becoming involved. The parents of the cousins were siblings and children of the founder. Each may have had a different way of explaining the family business to their children, because each child experienced the family business a little differently, depending when he or she was introduced into the business. Not only that, but now there could be various church fellowships involved that may place different restrictions on the size and operation of the business.

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The fourth stage is the collaborative stage in which you have a complex mixture of generations. There may now be more nonfamily leaders and owners that don't have operational roles.

So, at which stage is a good time to work on family business governance? Before answering this question, consider the spheres of influence we've been referencing.

What is a Sphere of Influence?

A sphere of influence is a field or area in which an individual or organization has power to affect events and developments. These encompass three areas of focus: the business management sphere, the business ownership sphere, and the family membership (relationship) sphere.

Each sphere demands unique attention, and each is accountable to another. Each has its own role and rewards. Each has its benefits and pitfalls; for example, if the family is unclear about the business's purpose, the ownership is going to be uncertain what success looks like. The business could underperform, and nobody knows what to do about it.

What do these spheres of influence look like through the stages of growth? In the early stage, you might think, "Well, I'm the founder, and it just doesn't seem that complicated. I run my business the way I want. I'm the family. I'm the ownership. And I'm the management."

True, these three spheres do overlap, especially when a business is just starting. But in the second (sibling) stage, as the business and family grows, these spheres of thought tend to grow apart. In the business management sphere, you likely have more employees and possibly a leader that's not a family member. Inside of the family sphere, you may have a new spouse married to one of the siblings. With these changes you have some additional influences you need to recognize.

In the third (cousin) stage, these spheres separate even more. Now the founder's grandchildren could be involved, and each of the spheres start battling for prominence and influence. It is in this stage that the purpose of the business needs to be well defined and understood by all involved.

Although there may be different perspectives about what the business is and what it should be in the future, the vision and mission statements need to be clear to bring everyone to common ground. There may be competing priorities, especially if the

cousins are a part of different church fellowships, but for the business to continue, a consensus needs to be reached to avoid conflicts and infighting. If differences are not dealt with up front, the transition to the cousin sphere can be devasting to the organization and potentially fatal to the company.

In the fourth stage, the spheres become very distinct. This is one of the areas which we've started working on in the Zimmerman family.

Throughout all the stages, the spheres won't always have perfect symmetry. When you're actually working through these areas of thought, it's going to be a little lumpy, as you may be working in one sphere but find that it also effects one of the other spheres. So, let's take a closer look at each of these spheres.

The Business Management Sphere

This is the sphere that people tend to spend the most time on. It's about production! It's where things happen, and the rubber meets the road. You're out serving people, doing what you set out to do in business. You are working *in* the business as opposed to just working *on* the business.

In the business management sphere, you need to think about ***mission, culture,*** *and* ***strategy.***

In the business management sphere, you need to think about mission, culture, and strategy. Consider the organizational and leadership structure. Consider decision-making systems—how do you do meetings? Human resource systems—how do you take care of your people? Business metric systems—how do you know if your business is doing well? These are all interconnected.

Also inside the business management sphere of influence are the daily operations. How does the business run? How does it care for its customers and employees? What about vendor relationships, payroll, and finances?

As your business grows and adds more employees, how do you organize departments so that everyone gets along and decisions can be made to serve customers effectively? Organizational charts need to be made to ensure everyone knows who reports to whom. Leadership roles and employee roles need to be clearly defined. There will also be meetings, agendas, and minutes. These areas are all inside of the business management sphere of influence.

The Business Ownership Sphere

Although people tend to spend the most time in the business management sphere, the business ownership and family membership spheres actually deserve more of our time and attention. We need to step outside the business management sphere and think about the business simply from an ownership perspective.

What are our values and vision? How do we expect the business to perform? What is expected for the way that we lead in the business? What is the legal structure of the business and the plan for succession? Documents, bylaws, and legal structure all need to be taken care of under the business ownership sphere of influence. As a business grows, this becomes even more important. We'll see later in the article that this sphere is built on a foundation that the family needs to form.

There are other things to consider inside of the business ownership sphere. Is your business ready for an advisory board? (This is someone who can advise you on the larger-scale changes and shifts in strategy.) Do you need a board of directors? How do you form a board? Do you have independent directors on the board for outside counsel? How do you clearly define the role of the board?

Two other important things that relate to the business ownership sphere are the buy-sell agreement and the shareholder agreement. Sometimes these two agreements are in the same document. One of the documents we have spent a good bit of time on in our family is the shareholder agreement. It's basically language governing the relationship between shareholders, such as determining who's eligible for ownership and when. It addresses conflicts of interest and conflict resolution and describes how each individual's ownership is valued.

The buy-sell agreement is the terms for shareholders buying and selling stock—how a shareholder sells and at what rate. It also decides what happens in the case of a shareholder death. All of these issues and other restrictions are defined inside of the business ownership sphere, although the decisions are also influenced by the family.

The Family Membership Sphere

I want to focus mainly on the family membership sphere, because this is the sphere in which underlying issues can surface. A situation similar to Jacob and Esau could arise if tensions already exist between family members.[9] In the Zimmerman family, we started on this sphere a little later than we should have. You might find yourself in that situation, as well.

In the family membership sphere, relationships and generational complexity are at the top of the list. Families become more diverse and complex as they grow, and with more family members around, there are more people that could have influence. Roles of the family tend to change; you'd be amazed how roles can be influenced simply by who is the oldest or youngest. There's significance in understanding what family roles mean.

In this sphere we also look what values we have in the family business and specifically in the family. Are there values we hold important but have never stated? These values could have to do with how and why we own the business and how we want the business to be managed. Are there traditions we want to recognize and carry on? Perhaps there are traditions we want to let go. What about conflict? How do we deal with conflict inside the family so it doesn't affect ownership and business management?

***Family businesses** can have a significant influence on kingdom work.*

Another aspect of the family membership sphere is what roles and expectations we have for the family to be financially involved in the community. Two things that come to mind are philanthropy and stewardship.[10] This is something we've been talking about in the Zimmerman family. Philanthropy and stewardship are two items that have torn family businesses apart if they aren't defined well.

As we are profitable in business, we want to be able to give, moving kingdom work forward. But how we do that needs to be defined—and defined well—along with the concept of stewardship. We need to spell out the family's view on profit and prosperity. The founder held a certain view, his children probably held a similar view, but now we may have cousins that hold slightly different views.

Family businesses can have a significant influence on kingdom work. We have a huge opportunity. What we do to help define the company values related to giving and stewardship will help set the stage of influence for the family. Family has the potential to influence the ownership, which can influence business management which, in turn, can represent the values the family set out to represent.

Using a Family Charter

One way the family has potential to influence the family ownership and management is by doing a family charter. Some have called this a *family constitution* or *family protocol*. In their book, *The Family Constitution,*[11] authors Daniela Montemerlo and John L. Ward say that "a family agreement is any kind of written principles and/or rules that regulate the relationship of the family with its business." So many times, we tend not to document these principles or rules when the business is founded. But when it's time to start an LLC, we need that family charter. Now there are two owners and a family that the business is representing. We need to know who we are as a business, so we can come together as a family. The family charter is a way to set that stage and build that foundation as you move forward.

In the Zimmerman family, we had the necessary legal documents. We worked extensively on the management and our business units. However, questions began to come up concerning who we are and what is our purpose. These questions were answered differently depending on the generation, family lineage, or views held by different churches. It wasn't necessarily that we had disagreements,

[9] Genesis 25:28-34, and Genesis 27—Although this situation was not a business situation, the same kind of feelings can arise during a family business transition if it is not handled correctly.

[10] Philanthropy is the desire to promote the welfare of others, expressed especially by the generous donation of money to a good cause. Stewardship is the job of supervising or taking care of something, such as an organization or property that is owned by someone else. For the Christian it is recognizing that God owns everything we possess.

[11] Montemerlo, Daniela, and John L. Ward. *The Family Constitution: Agreements to Secure and Perpetuate Your Family and Your Business.* Palgrave Macmillan, 2011.

but differing answers have the potential to cause issues in the family, depending on how strongly the views are held.

As we looked at how other family businesses successfully navigated through succession, we discovered that invariably the successful ones worked on some kind of family clarity. Having this family clarity influenced the ownership positively and influenced the business and its management, as well.

The family charter seeks to answer a number of questions, including:

1. Who are we as a business? Who is the family? What is the main family line? How did the extended family come together?
2. Why are we in business? Was this some lucky thing that we started, or is there more of a purpose or calling?
3. What is our story? There's a lot of rich history in our families and businesses. We don't want to miss the story.

We should also ask, what are our special business objectives? Are we expecting to sell only ice cream or only cars, or do we want to be diverse in the things we offer? Is our objective to be the best or biggest at something?

Too often we overlook what success is, because ***we haven't defined what it looks like.***

Also, what does success look like? Some may define success as creating jobs for the family, which draws the family closer. Others may focus their success on the business aspect only. Still others might measure success in whether we are an outreach to the community. The healthiest balance is in the middle—providing jobs, profits, and outreach; that's where it's best for the family, for the business, and for our faith community. Too often we overlook what success is, because we haven't defined what it looks like.

Define specific family values and link these values back to the founder. The Rechabites in the Bible were an example of this. They followed the values that their father Jonadab taught, regardless of what others were doing.[12] So many times, the principles with which the founder started his business are principles that still stand today and need to be continued.

Although we have values we want to preserve, sometimes we're just not very good at documenting them. We need to ask why the founder was called to this business in the first place. What was driving him? How does that apply today, now that there are many more people involved? Again, documenting the answers to these questions and getting agreement among the various families involved will help prevent many issues when the business moves into the cousin sphere.

Set Expectations in the Family Charter

Defining guidelines for governance is an important piece of the foundation for business ownership and management. One example is deciding whether or not the lead person, the CEO, has to be a family member. Also ask how you view investment in the family business. Is it long-term or short-term investment? Is it a "'til death do us part" kind of thing or not? If the commitment is long-term, that will create a measure of influence that obviously will push into the business ownership sphere of influence.

The family charter also defines expectations for shareholders. What does governance look like for a family member shareholder who works in the business versus one who does not work in the business? Sometimes shareholders who don't work in the business still want to be part of the family decisions and ownership of the business. Consider which shareholders

[12] Jeremiah 35: 6-10 "But they said, We will drink no wine: for Jonadab the son of Rechab our father commanded us, saying, Ye shall drink no wine, neither ye, nor your sons for ever: Neither shall ye build house, nor sow seed, nor plant vineyard, nor have any: but all your days ye shall dwell in tents; that ye may live many days in the land where ye be strangers. Thus have we obeyed the voice of Jonadab the son of Rechab our father in all that he hath charged us, to drink no wine all our days, we, our wives, our sons, nor our daughters; Nor to build houses for us to dwell in: neither have we vineyard, nor field, nor seed: But we have dwelt in tents, and have obeyed, and done according to all that Jonadab our father commanded us."

are going to be involved in meetings, committees, and other details that go along with making decisions.

Another big aspect to consider in the family charter is compensation. Many times, compensation gets mixed into the business management side, the ownership side, and the family side as the business grows and family members are active parts of all three spheres. We must be very clear about how and why we're compensating and for what and when—specifically in business management and ownership. In the parable of the laborers, the householder told the workers what they would be paid upfront, but there was still a misunderstanding when they were paid.[13] There needs to be clarity so that everyone's expectations are the same. The family also needs to be okay with how these decisions are made.

The family charter should also include a liquidity policy. How do we capitalize the business? Is the cash that's invested in the business locked in permanently or not? If someone wants to sell or partially sell, how does that happen? The family charter doesn't describe all the details that would go into a buy-sell agreement, but it does include some general philosophy about liquidity.

Conflict is another thing to address in the family charter. We don't like to think that there may be conflicts in our families, but the reality is they do happen. As the business moves into the stages after the sibling stage, how conflict will be resolved becomes even more critical. We have a significant section in our Zimmerman family charter for how we go about resolving conflict in the family; that section even ended up in our shareholder agreement. We wanted to be able to resolve conflict in an effective, God-honoring way and not let that conflict go untamed into the business management sphere. The instructions Jesus gave in Matthew 18 are a good basis for resolving conflict in family and business settings, although the final step may be an outside mediator instead of the church.[14]

As we compiled the family charter in the Zimmerman family, we wished we would have done it earlier. Doing a charter became a good educational experience for upcoming generations. We could begin to define many things, even with our young teenagers. It's also a great educational piece for leaders or employees in the business to understand the reasons behind what we do. And for owners not employed by the business—what is portrayed in the charter can be a significant part of what they understand about the family business. Much can be communicated through the family charter.

What a Family Charter is Not

Let's take a brief look at what the family charter is not. The family charter is not meant to be a legal document. It is not the same thing as a shareholder agreement or buy-sell agreement. Some people think the family charter or constitution needs to have teeth and be enforced, but it's not meant to solve a problem quickly. Instead, a family charter is similar to the power of common consent.

Think back to how our country was founded in the early 1600s when the Pilgrims on the Mayflower came to this new land. One of the first things they did was to put together some common documents, some common understanding of how they were going to live together here in America. Those documents set the stage for effective governance.

What they did can apply to us today. Having common consent around the family charter can take us much further than any legal document will. The power of common consent is something that needs to be grown inside of the family.

When to Start

To conclude, when is a good time to work on governance? The answer is simple; begin early. You might wonder why it matters, especially if your business is small and only started 10 or 20 years ago. But the early stage is the perfect time to

[13] Matthew 20:9-15 "So when even was come, the lord of the vineyard saith unto his steward, Call the labourers, and give them their hire, beginning from the last unto the first. And when they came that were hired about the eleventh hour, they received every man a penny. But when the first came, they supposed that they should have received more; and they likewise received every man a penny. And when they had received it, they murmured against the goodman of the house, Saying, These last have wrought but one hour, and thou hast made them equal unto us, which have borne the burden and heat of the day. But he answered one of them, and said, Friend, I do thee no wrong: didst not thou agree with me for a penny? Take that thine is, and go thy way: I will give unto this last, even as unto thee. Is it not lawful for me to do what I will with mine own? Is thine eye evil, because I am good?"

[14] Matthew 18: 15-17 "Moreover if thy brother shall trespass against thee, go and tell him his fault between thee and him alone: if he shall hear thee, thou hast gained thy brother. But if he will not hear thee, then take with thee one or two more, that in the mouth of two or three witnesses every word may be established. And if he shall neglect to hear them, tell it unto the church: but if he neglect to hear the church, let him be unto thee as an heathen man and a publican."

start documenting your thoughts and the values important to you. Working on governance doesn't mean just *talking* to your children about it, but reviewing it with them and having them help you compile the necessary documents. Then, as another generation comes in, you have a healthy foundation.

And certainly, don't hesitate to reach out for counsel. Proverbs 15:22 says, "Without counsel, purposes are disappointed, but in the multitude of counselors they are established." It's okay to reach out for help. As our journey unfolded in the Zimmerman family, we sought guidance from a consulting group called the North Group. We also spent a lot of time reading; it's amazing how many resources are available about governance, specifically family business governance.[15] I encourage you to read stories about other family businesses and learn from them what worked and what didn't work.

When we think of counsel, we often think of looking for an accountant or attorney for legal help. But there are also people out there who work with families to seek common consent on business decisions and direction.

Many Anabaptist businessmen have been richly blessed in their generation. To continue the family business, founders must transition it to the following generation, continuing an environment where faith is lived out in daily work. "As every man hath received the gift, even so minister the same one to another, as good stewards of the manifold grace of God" (1 Peter 4:10). A kingdom-focused family governance can be a blessing to the family, the church, and society as a whole.

[15] Craig E. Aronoff and John L. Ward. *Family Business Governance: Maximizing Family and Business Potential* (New York: Palgrave Macmillan, 2011). Daniel Montemerlo and John L. Ward. *The Family Constitution: Agreements to Secure and Perpetuate Your Family Business* (New York: Palgrave Macmillan, 2011). The Family Business Consulting Group, www.thefbcg.com (accessed on April 9, 2018).

AF Stewardship Resources

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