CPA Australia Podcast

Transcript – Episode 64

Michelle: As this podcast was recorded on Skype you may experience some audio interference.

Hello and welcome to the CPA Australia podcast, your weekly source for business leadership and public practice accounting information.

Hello everyone and welcome to another episode of CPA Australia podcasts. I'm your host Michelle Webb and I'm part of the team which manages public practice content here at CPA Australia.

In today's episode David and Kim Harland discuss the changes they are noting in the family business sector and what proactive family businesses and their advisers are doing to benefit from those changes. Family businesses are the oldest and most frequent business ownership model in the world. By nature, they have to be both nimble and dynamic to survive. David Harland, who is a Fellow of CPA Australia, is the executive chairman of FINH and he's a leader in the family business advisory field. He provides family business clients with expert advice on such challenges as succession and transition planning, family governance strategies, raising liquidity and sourcing capital.

Kim is the managing director of Insights, a provider of customised online resources for family businesses. The Insights team understand that specialist tools and information play a vital role in managing family business risks and improving the longevity, growth, and most importantly, the sustainability of each and every family business.

Thank you both for joining us today. Kim, I'll hand over to you to get it started.

Kim: Thanks Michelle. As you've said, my name is Kim Harland, I'm the managing director of Insights and we provide online resources tools and education for family businesses.

David: Thanks Kim. David Harland's my name and I'm the executive chairman of FINH and I play two roles I suppose with that title. One's leading a strategic board that is establishing an operation globally, and the second one is as an executive. I manage a number of family business clients in terms of handling their succession through to the next generation.

Kim: That's great. So, David the first thing that I thought we should clarify for all of the listeners is - what is a family business?

I think the whole sector of family businesses really flies under the radar. But if you look at the statistics, family businesses create around 80 per cent of GDP globally and 65 per cent of all employment around the world.

I guess if you look up the definitions - there's plenty out there - but probably at its most simple family business is considered to be business actively owned and/or managed by more than one member of the same family.

But for our listeners David how do you define a family business, how do we define it when we're working together. And I think it'll probably be good for the listeners to get some examples of family businesses that might surprise them.

David: Yeah, it's a really important point, Kim, is the understanding of what is a family business because you know traditionally in the marketplace I hear a lot that someone will say, "Oh you're just a family business," and the implication is that family business is small and problematic.

Now I suppose whilst some family businesses or any business can be problematic, determining a family business based on its size is the problem. And I pick up on what you said. It really is about who owns the family business and I place a lot of attention on the issue of a family business or, I like to say, a family in business, which puts more emphasis on who owns the business.

So I would argue that a family business is a business that's controlled by a family group and therefore it bypasses that notion of size because a family business in fact can be a large publicly listed company.

Kim: Yeah, I think that's fairly reasonable and certainly equates with the way that we deal with the businesses and families that we're talking to.

Some examples I guess of family businesses globally include Wal-Mart, Samsung, Mars and Lego. And from a local perspective here in Australia, Akubra Hats, Linfox is listed as a family owned and operated business, Visy, and Coopers Brewery. Did you have any others that you thought were probably worth bringing to the attention of the people that are listening?

David: Oh, look I think we always jump to the high profile family businesses because they're probably the easiest and it resonates with most people, but I wouldn't like to think that, after saying that, I think Kim you said the statistic is about 80 percent of GDP is generated by family businesses.

So, to talk only about the big large ones probably doesn't give credit to a lot of the small private companies or mid-sized companies that contribute to that GDP.

But if we want to capture and attract attention to the space, I think the larger ones in Australia, you've mentioned very well but I see Visy is clearly an Australian family business. Westfield is a family business and they're the ones that seem to be in the media a lot but people see them as a big institution when in fact it's a family who sit behind those businesses.

The other one that's probably been in the media for the wrong reasons over the last few years with the tensions or disputes between the current generation and the next generation of course is the Rinehart group in terms of the iron ore mining operation and there are some good examples I think but I want to make the point and leave the point with the fact that they're the big ones, are the high profile ones, that are the tip of the iceberg of a lot of very private and confidential family groups that operate under the radar in the market.

Kim: That's an interesting segue into our next question David because the next question is: what are five common characteristics of a family business? Five things that you think every family business has in common.

For me from my experience I think one of the first things it always comes to mind when I think of the family businesses that we're working with is they are always incredibly private and incredibly confidential. So you're right there are many, many family businesses that really fly under the radar of public opinion, the media and every other channel.

So, yeah, on that note, what would you say? Probably four or five, if you've got them, common characteristics of a family business.

David: Yes well, I think overarching all of that question Kim is, on one hand we say there's a lot of common characteristics among family business but the paradox is that every family business is different as well and that's the hurdle that we must get around and when you're working in this industry is to understand that very point.

But if we go back to the point, what's some commonality among family businesses, let's see how we go. But the first one I would put at the forefront is that they are patient and they're long term, and I think when we go to the heart of business in Australia, what we're hearing a lot of now in the marketplace, there's a Royal Commission in the banking sector, there's a lot of focus on the short term nature of institutions and it's really coming home to roost that short term focus doesn't necessarily serve the community and the country best interests.

And underlying all of this is the family business sector and the number one characteristic is that they're patient, they don't make short term decisions that distract them from their long term vision for the business, and when I say long term vision they're not thinking in the current generation even, they're thinking across generations when they're making their decisions. And of course we all know that when you look at the long term and you're patient, you make much better decisions that are much more grounded and sustainable for the future.

I reckon that, that's the number one characteristic of families in business.

If I was to stretch my thinking somewhat further and maybe I won't get the five, Kim. The other one is that they manage their systems very well and if you think of family business you think of the business or the financial system and you also have to think of the family system and one's very clearly made up of hard financial decisions and the other ones made up of softer, I hear that term a lot in the industry, softer human issues. And family businesses, the strong characteristic they have, is that they have the capacity to manage these two systems together extremely well.

And this goes to the very heart of the long term nature that without the management of the human element integrated with the financial element then it's very difficult to stay for the long term.

So, I'd say that would be more in number two characteristic of families in business.

Now if I could probably turn my mind to some of the challenges that ordinarily occur in family businesses is of course when you're managing these two systems ordinarily tensions arise and one of the common downfalls of families in business, or family business - is the time we're using in this context - is that they leave matters unresolved when it comes to the human interaction with the financial capital, and these unresolved tensions in families, if it goes unchecked for a long time, can cause the dismantling of a family in business.

And it's a big component of our work in fact, is how to put in place structures and processes to ensure that the communication is transparent and is understood. So there's this financial literacy around the family and we overcome some of those tensions by being proactive in the management of that.

So Kim, I think there's three characteristics that I've given you, two that are the strength of family business and one that if unchecked is the dismantling of family business. So hopefully that gives you some sense. There's only three there but three might be sufficient I think for your question.

Kim: I think so. The other thing that I think we see a lot and hear a lot about family businesses is that they have the ability to be able to make quick decisions, fast decisions. They don't have to deal with bureaucracies. And yes decisions can be made very quickly.

So based on that, knowing that family businesses and the family business model is the oldest and still the most prevalent business model in the world, and that we know that this is an era of change and disruption, how are you seeing family businesses change and maybe if you can nominate two or three things that you've seen change in family businesses within the last decade.

David: Yeah thanks Kim it's a complex question. Let me just think about how to structure an answer that will help the listeners go away with something.

And the first thing that comes to mind that's different in family business - and as you said, family business is the oldest model of business that exists - but the one thing it's just the one thing that's so different today than has ever existed before, is the issue, and I call it the royal factor because it's a lot like the royal family, in that if we talk about succession and sustainability and moving from one generation to the next, the biggest change is that everyone is living longer.

And the fact is that when everyone lives longer you have much more human capacity to help grow the business or businesses of a family group. But at the same time if you don't understand the dynamic of having potentially four generations well, capable and interested in business, and how you manage the interaction of four generations being involved in business is one of the key areas of change, and how we manage that change is so important. And particularly if you think about family business being patient and long term, then bringing the next generation while the current generation is still capable and happy to stay into the family business is one of the major challenges.

So I think longevity of life is one of the key changes for family businesses.

But let me give you one other that I think is fundamental. And I think it goes to the very heart of when you asked me the question upfront as to the characteristics of family business, I actually questioned the issue of being a family business or being a family in business. And this point goes to the heart of that.

How often have you heard someone saying, "Well Dad was a," let's just say for example, "a soft drink maker and we've been making soft drinks for two generations and we're going to make soft drinks for the next generation." Well that doesn't cut it today because for a start, is that industry sustainable and how do you make it sustainable and profitable when we have so many people wanting to live and be part of the family business? And you have the next generation who somewhat say, "We don't want to be soft drink makers in the future. We actually want to do something else, something that's more aligned with what's going on in the world at the moment," this huge technological change, Artificial Intelligence, we all hear about these changes going on in the market.

So my point is, if you're a family in business and think you have to stick to the one business and the one industry to go forward, then that can be a challenge for businesses and families if the next generation don't actually believe that this is a business that they ought to be in.

So I think the real challenge there is really critically looking at: are we a family business in this business or are we a family in business? And what business should we be in now ready for the future, and it starts making some really challenging and interesting conversations because people once they start talking about these things can make some significant decisions to reset their family capital ready for the future and sustainability for the next generation.

Kim: I think another point to note in terms of what we're seeing change in the sector is really the fact that research into family businesses really only commenced 30 years ago so they were only considered an entity unto themselves about 30 years ago, and therefore research started into them and from that has evolved specialist family business advisers such as ourselves.

I think traditionally family businesses went to their lawyer, banker for advice but we are seeing more and more people such as ourselves coming through -people who purely specialise in the family business arena and really focus strongly on the family and the business as a whole and how they each impact each other.

So David, what do you think smart businesses are doing to plan for the future? What are your clients doing, the clients that you have at FINH doing to plan for their future in the face of these changes that -that we've just discussed…And give us some anecdotes.

David: Starting off with where you were there's a new industry, this family business advisory area. And I think one way to differentiate it is that typically we have a society that is built around in the professional services industries, whether you're ... I call it the siloed approach and someone's either a tax expert, they're a wealth management expert, an accountant, and you get the picture that they have their silos of expertise, and typically that focuses on the business or the financial side of a family and business systems.

And as I've spent a lot of time answering some of your questions the focus in families and businesses, it's almost a motherhood statement to talk about the financial capital and the expertise required to run a business. But it's more and more ... The more time I spend in this industry, those traditional professional services need to work with a family business adviser whose core strength is understanding the human relationships and in particular how those relationships impact on the financial capital of the family business.

So I'll give you some examples of this. You know we're working in Singapore at the moment with a large Indian family. They're five branches in that Indian family. And when you lift the lid and understand what's going on in the business and in the family you can see that everything has been focused with advisers who talk about how to sell a business, how to maximise their tax, and sort of minimise their tax efficiently and legally, how to acquire a new business. And everything related to the business, and the business has grown to a size where they actually stopped and there was a lot of issues going on in the family. And when you went back behind and looked at the family it was clear we did a lot of work, and we set up some structures around the family we put in place some family governance, which means the family actually formally sitting down and saying, "What do we believe in? What's our purpose for doing this? What are our policies around things like investment? Do we buy this business or sell this business?"

And when it really came down to it, when it when it came down to the purpose of why they were doing this together, they're a very wealthy family. The purpose was that they were happy and they were adding value to the wealth that was given to them by their previous generation.

And when they summarised everything they did into those couple of words, they looked at each other, and it was clear relationships were tense, there was a lot of challenges, and they answered the question and they said, "We are not happy working together like we're working together."

So what we've done now is we've set up a family office for that group and helped them manage that process and in fact we've been able to give them an exit pathway where emotionally they can get away and sort of take some of the capital out of this what we call a shared economy, and are able to go and manage that themselves. But what we're finding is at the same time it's giving them the sense of freedom, and a more of a willingness to want to work together in different ventures, and they are looking at different opportunities together.

So I think to summarise that little story is that understand what your purpose is, why you're doing what you're doing, and then once you understand that, put in place the structures and the processes, what we call governance structures, whether it's at the family level or at the business level so that you're actually communicating and talking about these things and growing and developing together. It's a much healthier way, and a much better pathway to sustainability.

Kim: David I think something else that we hear and see really often is of course planning for succession, which is probably the biggest issue that we hear and see. We have very regular calls and emails from family business members, people working within the business, saying, "I'm absolutely stuck, my father," sometimes even unfortunately, "my grandfather is in his role and he will not move on. How can you help me to move that person on?"

For me I think the smart family businesses considering succession planning as a journey. And they are having ongoing conversations about succession and transition. There is no stop start conversation about that. It really just constantly rolls along.

So even if you have just gone through a succession there should be a fairly clear plan in place or a very open conversation that continues about the next transition.

So I think smart family businesses having continuous conversations about transition and as you say they're using formal structures around the family and the business to maintain those conversations and to have them in a really positive way.

David I'm going to make ... This is our last question. I'm going to make a bit of a twist on a on a commonly asked question that I hear that I actually really like and instead of ... Well let me just launch into it, if there was one thing that you could tell every family - 50th year anniversary that have survived fifty years from your experience, what would that one thing be that you would tell every family business to do?

David: Well Kim, the first thing…can I tell you two things?

Kim: Go ahead, make it two.

David: I think the first thing I would tell them to do is to arrange the family to get together-and to look at the history and the legacy of the family history and actually celebrate and-have a bit of a party, that would be the very first thing because they need to pat themselves on the back and congratulate them and say what a great job we've done to make it to 50 years.

But let's get to the heart of your question and if someone's made it to 50 years they've got to be doing something right. And typically what can happen in those situations is that one generation will look at the previous generation and say, "Gee we've been so successful, let's replicate going forward what we've done in the past."

And I think the one thing that families that have come to 50 years need to do is to say, "Whilst we've achieved what we've achieved and we've done it so well, that doesn't mean the way we've done it will apply for the future because the world we live in is a very different place." And if you'll recall one of the very things is this age issue where people are living longer and there's more generations alive, they need to start thinking about what do they do differently to go for another 50 years.

I mean we've got a company here in Queensland in our home state Hutchinsons and they celebrated I think three or four years ago, they 100 years together and they said to themselves at the hundredth year party, put emphasis on their acknowledging their history. They said, "What are we going to do for the next hundred years?" And they acknowledged that they're going to have to do things differently to what they've done in the first hundred years.

So one of the things that I think is really important in that context is that the families need to see themselves not as a family in any particular business but a family in business. And I think to do that what they need to do is establish the notion or the structure of a family office. And what a family office does is it stands a family group, instead of looking at themselves and the world that they are used to through the prism of one business, they start to see the family in business looking at a bunch of capital that they have and how to be good stewards of that capital going forward and are they in the right business or what should they be doing about the management of that capital going forward.

So Kim in summary, have a party. Secondly, set up the structure to separate the view of the family in one business to being a family in business and through the structure of a family office.

Kim: That's interesting you say that, I agree entirely with both of your points, David. It reminds me of a one of the case studies on the Insights platform, Mitchel Taylor of Taylor wines and that's one of his recommendations that every family business should do. Stop and celebrate. And I've always thought that, yes you may have a vested interest in getting people to stop and celebrate as the owner of a winery. But I do think that's really, really important advice for family businesses to really stop and reflect on what they've achieved, they've achieved something that not too many other families have been able to succeed with.

So on that note I hope the listeners have really enjoyed listening about the changing face of family businesses and how they can prepare for that. For anyone who wants to know more or chat further to David or myself our websites are FINH.com, that's F-I-N-H.com, and Insights.org.au. Insights is also on Facebook. Thank you very much for listening and I look forward to chatting soon.

David: Thank you, Kim.

Michelle: Thank you David and Kim for your insights.

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