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STRATEGIC MANAGEMENT IN FAMILY BUSINESS: AN EXPLORATORY STUDY OF THE DEVELOPMENT AND STRATEGIC EFFECTS OF THE FAMILY-BUSINESS RELATIONSHIP

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By

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Strategic Management in Family Business: An Exploratory Study of the Development and Strategic Effects of the Family-Business Relationship
(Under the direction of WILLIAM R. BOULTON)

The focus of this research is the interaction between the constraints of family members who own and/or manage a family business and the competitive requirements of that business. This interaction provides the major impetus for change in the family-business relationship. The consequences of this interaction has both strategic and operation effects in the business.

Using a clinical research methodology, data were collected from twelve family businesses on several organizational levels in each business. Data collection focused on history and development of strategy, operations and management systems, and the family association with the business. Interviews were also conducted with approximately fifteen individuals who work for or with family firms.

Analysis of the data produced a theoretical framework for the family-business relationship. The family-business relationship passes through four stages of development which are labeled Prefamily, Family, Adaptive Family, and Postfamily. The sequence and timing of the development of the relationship through the stages are related to the process of adjusting discrepancies between family constraints and competitive requirements of the business.

A series of propositions is presented based on the framework which suggests that the management of the family-business relationship requires appraisal of the power bases of management and the rate of change in the environment, as well as recognition of family constraints as a factor in strategic decision-making.

INDEX WORDS: Family Business, Management Constraints, Politics in Management, Owner Control, Evolving Business

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The need to preserve anonymity for the many managers, family members, and observers of family business who participated in the study precludes thanking them by name. The willingness of these individuals to share their time and their experiences made the project possible and their interest and candor made it enjoyable.

Family and friends have lent the emotional support to this project which is as necessary as the intellectual assistance already acknowledged. My parents have always encouraged me in many ways, and I am grateful to them. My husband, Mike, is due special thanks for the many sacrifices he has made during my years of doctoral study. His unfailing

optimism and balanced perspective were resources which I drew on constantly and for which I am very thankful.

TABLE OF CONTENTS

TABLE OF CONTENTS (continued)

LIST OF TABLES

LIST OF TABLES (continued)

LIST OF FIGURES

CHAPTER ONE

INTRODUCTION AND METHODOLOGY

The purpose of this study was to develop a conceptual framework of the family-business relationship with particular attention to the development of the relationship as a process affecting the strategic management of the firm. This focus evolved from an initial interest in placing family business in a business policy/strategy context and was shaped by the realization that the lack of a descriptive theory of how family and business interacted made it impossible to frame meaningful hypotheses. The clinical methodology described in this chapter was chosen to facilitate the process of exploration and description.

Why Study Family Business?

The National Family Business Council estimates that there are about ten million family-owned businesses in the United States. These firms employ about 44 million people and their sales volume reaches the trillion dollar mark (Fowler, 1979). These businesses account for more than 96% of the total number of U.S. businesses according to another estimate but account for only about 43% of the Gross National

Product or 48% of the Gross Business Product (U.S. Small Business Administration, 1978).

While the majority of these family-owned businesses are small with fewer than 100 employees, family business is by no means limited to "mom and pop" operations. In a study published in 1972, Philip Burch reported that 16% of the *Fortune* Top 300 firms of 1962 were family-controlled and another 42.7% were possible family-controlled. Only 41.3% of the firms could be classified as under managerial control, that is, publicly held with no concentration of stock in hands of relatives of the founder and with no family members in top management positions or on the Board (Burch, 1972). Burch's study did not include large privately-held corporations which are not included in the *Fortune* listing because they are not subject to financial reporting requirements.

Family businesses are found in all sizes, and while data are not available on the distribution of family businesses among industries, Burch found family-controlled firms in merchandising, transportation, and commercial banks as well as manufacturing (see Table 1-1, on page 3).

Family businesses are an important economic and social institution, but one which is viewed by many as precarious. The increased choices and opportunities available to young people work against the survival of family businesses, as do tax laws and increasingly concentrated industrial structures. On the other hand, family business is an institution of ancient lineage which has endured social and economic change before. Regardless of its long-term future as an institution, the family business enterprise is a type of organization in which many managers must function and for which top managers must provide strategic leadership. The business press provides many examples of the difficulties of their charge and of the rewards of success.[1]

Table 1-1: Corporate Control in Large Firms

Business Category	Probably Management Control	Possibly Family Control	Probably Family Control
Manufacturing Firms Top 300	41.3%	16.0%	42.7%
Merchandising Firms Top 50	28.0	14.0	58.0
Transportation Companies Top 50	46.0	18.0	36.0
Commercial Banks Top 50	48.0	22.0	30.0

Source: P. H. Burch, Jr. The Managerial Revolution Reassessed. Lexington, Mass.: Heath, 1972, pp. 67 and 96.

[1]Contrast for example the feuding Joyce family ("Seven-Up Made the Joyce's Rich but It Created Fierce Family Rivalry," Wall St. Journal (December 4, 1979), p. 1.) with the Bechtel family in construction and engineering ("For a Family Concern, Bechtel Group Works on Enormous Projects," Wall Street Journal (April 10, 1979), p. 1.

This study was planned to contribute a theoretical foundation for distinguishing between these two outcomes and for directing the enterprise toward the former.

What Is a Family Business?

One book on family business uses the terms "small business," "family business" and "closely held business" interchangeably to mean substantially the same kind of enterprise (Becker & Tillman, 1978). While this convention is a fairly common one, it imposes size and stock ownership criteria, thus eliminating some firms which should be considered family firms (Mars Candy Company is an example)[2] and including small entrepreneurial ventures in which no family connections exist.

Donnelly (1974, p. 94) developed a definition of family business which is oriented to the processes and relationships that exist in a given company.

> . . . A company is considered a family business when it has been closely identified with at least two generations of a family and when this link has had a mutual influence on company policy and on the interests and the objectives of the family. Such a relationship is indicated when one or more of the following conditions exist:
>
> - Family relationship is a factor, among others, in determining management succession.
>
> - Wives or sons of present or former chief executives are on the board of directors.

---

[2]See "Mars: Behind Its Chocolate Curtain Is a Sweet Performer," Business Week (August 14, 1978), pp. 52-57.

- The important institutional values of the firm are identified with a family, either in formal company publications or in the informal traditions of the organization.
- The actions of a family member reflect on or are thought to reflect on the reputation of the enterprise, regardless of his formal connection to management.[3]
- The relatives involved feel obligated to hold the company stock for more than purely financial reasons, especially when losses are involved.
- The position of the family member in the firm influences his standing in the family
- A family member must come to terms with his relationship to the enterprise in determining his own career.

While this definition correctly focuses on important phenomena in a family company rather than one dimensional criterion such as stock ownership, there are at least two problems in using it. The first is the requirement for identification with two generations of management. This would eliminate the family firm which is founded by brothers, sisters, or cousins and also would postpone examination of family processes until after the first transition in management is made. The transition from founder to second generation is very much a family matter. A second problem with this definition is difficulty in operationalizing many of the criteria. The presence or absence of wives or sons on the Board of Directors is fairly easy to determine, but the relationship between the position of the family member in the firm and his standing in the family requires a much more subjective evaluation.

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[3]The masculine pronoun is used throughout the study to refer to males and females.

Dailey, Reushling, and DeMong (1976/77, p. 60) have adapted Donnelley's definition without the two generation requirement as follows:

> We considered the American family-owned corporation to be a company that has been closely identified with at least one generation of family ownership where the relationship between family members and corporate policy making is dynamic and interactive.

They listed five characteristics which would serve to indicate the presence of such a "dynamic and interactive" relationship:

(1) The presence of family members in managerial positions.

(2) The existence of an agreement to preserve family control of corporate policy making in the future.

(3) The common stock of the corporation is held by family members and a few unrelated shareholders and is not publicly traded.

(4) Product and service characteristics or corporate traditions are associated with the family name.

(5) Outside organizations equate family name with social corporate image.

The second criterion, that the company be privately held, would eliminate firms from consideration which would meet the other, more behaviorally-oriented criteria. Barry (1975, p. 42) took another approach:

> The term "family firm" can obviously be used to cover a wide range of organisations and the definition adopted by the writer is that of an enterprise which, in practice, is controlled by the members of a single family. This includes both the private limited

> company in which virtually all the shares are owned by the members of a single family, and the public company in which the distribution of the equity is such that the family has effective control.

This definition raises the question of what constitutes effective control. Reeder (1975) explains the difficulties of trying to produce an unambiguous answer to that question:

> Neither a pre-determined percentage of stock ownership _nor_ family representation on the board _nor_ a combination thereof is enough to determine decisively the actual locus of control in many firms. There are simply too many factors involved. For an additional example, consider the fact that even though the same "family" may own fairly large amounts of stock there is nothing to insure that all members of the family will _agree_ on matters where control could theoretically be exerted. On the other hand, family ownership rights in a number of separate but interacting firms (especially when one or more is a financial institution) can give the family effective control of all the firms without a sizable bloc of stock in any single one of them. . . . It must also be noted that many times it is not only outsiders who don't know the locus of control in a corporation. Sometimes the owners, directors, and managers don't know themselves until the question is put to the test in an actual fight over some issue. (p. 26)

The final approach to consider in connection with defining the family firm is the adoption of the assumption that family firm is a concept which most readers recognize and for which there exists a general understanding of legal and social relationships involved. The practical advantages of this approach are apparent, but added to the variety of definitions found in the literature of family business, it makes comparing findings of research difficult and introduces extraneous variables without identifying them.

The purpose of this discussion has been to give the reader some feel for the problems involved in developing a definition of family business which meets the criteria of (1) reflecting the essential aspects of the institution which tend to be open to ambiguous interpretation and (2) being sufficiently concrete to be operationally useful. These criteria are often in conflict, and this is reflected in the fact that none of the definitions really meets both.

The approach taken in this study is that the real issue is not the development of a definition of family business but the specification of the characteristics of the firms included in the study to provide the reader with the information needed to make comparisons with other research and personal experiences with family firms. The companies included in this study are characterized as follows:

(1) The founder or a member of his family is president and/or executive officer.

(2) Members of the founder's family are employed by the company.

(3) Members of the founder's family can, if they agree, decide issues brought to a stockholder vote.

(4) Managers accept the designation of their firm as a "family business."

While more specific characteristics of the companies studied will be presented in a subsequent section of this chapter, it should be noted here that the sample was not restricted either to small or to privately held firms.

The Literature of Family Business

A number of researchers have used a comparative approach and analyzed family business by describing advantages and disadvantages of family business (Barry, 1975; Calder, 1961; Christensen, 1953; and Donnelly, 1964). The most recent study (Dailey, Reuschling & DeMong, 1976/77) was based on interviews with executives in 25 family firms most of which were moderately small manufacturing firms. Findings of the study are reproduced in Table 1-2. These findings contrast with other such studies in two areas. The first is a question of classification and the second lies in the omission of an area which most other researchers include. Between 80 and 90% of the respondents to this study agreed that "flexibility for meeting changes in competitive activity" is an advantage of family firms. Donnelley (1964) found lack of flexibility a problem in family business and joins Barry (1975), Cohn and Lindberg (1978) and Levinson (1971) in listing failure to meet competitive needs of the business as a disadvantage linked to family ownership and management. The second contrast with other studies is the lack of mention of personnel and succession issues which other researchers consider among the most critical issues and disadvantages of family business.

In relating this research to the purpose of this study, it is important to note that the traditional approach in family business research has been to take a problem by problem approach to the subject. Because of the definition

Table 1-2: Advantages and Disadvantages of Family Business

Response	% of Respondents Labeling Response	
	Strength	Weakness
Advantages and Disadvantages Associated with the Social Interest Group Sector		
Community relations	70	
Association with local business groups	70	
Resources to make social responsibility known		50
Views on corporate philanthropy		70
Demands on executives' time		90
Advantages and Disadvantages Associated with Competitive and Buyer Sectors		
Independence and secrecy of operations	85	
Customer security in buying from family companies	85	
Improved customer service and less red tape	85	
Flexibility for meeting changes in competitive activity	80	
Family name associated with high product quality	80	
Credit and financing arrangements for customers		45
Willingness to expand into new markets		55
Lack of regional and national markets		62
Pricing of goods and services		75
Management attitudes towards product and marketing development		75
Advantages and Disadvantages Associated with the Regulatory Sector		
Avoidance of financial disclosure regulations	80	
Simplicity of accounting procedures for tax purposes	60	
Degree of internal specialization		80
Occupational and Safety Health Act Regulations		70
Dealing with Affirmative Action, Equal Opportunity of Employment Regulations		45

Table 1-2 (continued)

Response	% of Respondents Labeling Response: Strength	Weakness
Estate Taxes		90
Advantages and Disadvantages Associated with the Supply Sector		
Informal and long relationships with suppliers	80	
Less red tape for suppliers dealing with a family business	75	
Time necessary to meet changes in the supply sector	90	
Knowledge of production and raw materials	70	
Suppliers' view of family's tradition in business	80	
Acquisition of credit for needed raw materials and supplies		95

Source: From R. C. Dailey, T. E. Reushling, and R. F. DeMong. Uncertainty and the Family Corporation. Journal of General Management, 1966/67, 4, p. 60.

of family business by some researchers as small business, most problems have been operational and immediate. Among those who have taken a topical approach to family business, succession has generally been the subject of research. While succession is a process which begins before and continues after the acquisition of a new title and office by an individual (Longnecker & Schoen, 1978), it is also a process which is dormant at many times in the history of the business.

The status of current research is that we know that family business is different from professionally-managed businesses in that certain advantages and disadvantages accompany the family relationship. Furthermore, these advantages and disadvantages are a function of the relationship. Donnelley reminds us that

> The success of many family companies indicates that ignorance of the relationships involved <u>and not family participation per se</u> is a key factor in the success or failure of such firms. Understanding the contribution a family may make to the firm's long-term strengths, analyzing the weaknesses involved, and implementing organizational restraints to control such problems, all are aspects of the manager's problem in a family firm. (p. 105)

The process by which the family and business interact has received some attention in connection with succession, but the family-business relationship has not been examined. The changes that occur in the relationship as the business and the family grow have not been described nor has the relationship been analyzed in relation to the policy and strategy of the firm. By focusing on the relationship between the family and the business, the results of this study provide insights into the problem of complying with the common prescriptions given to family business: capitalize on the advantages and minimize the disadvantages of the family-business relationship.

Research Methodology and Procedures

The lack of research on the family-business relationship and the lack of a theoretical base for hypothesizing the nature of that relationship dictated a multiphase, iterative approach to the research. The first step was to develop a conceptual framework which could be used to generate research questions. The nature of the research questions suggested the use of clinical research methodology. The phases of field work and analysis are described in the remainder of this chapter. Phase one, the preliminary inquiry included both literature review and field work. The findings were incorporated into the second phase of the research, the development of a research framework and the generation of research questions. The third phase was the selection of methodology and research sites. More field work followed using documentary and interview data. The final phase was that of analysis and theory building. While these phases are best described as discrete steps in the research process, it should be noted that this research was iterative and there was interaction between the phases. Of particular importance is the fact that the analysis phase was begun before all the data were collected and before all the research sites were finalized. This forces the researcher to reassess the meaning and relationship of the material several times from different perspectives. The phases of the research are described in detail below.

Phase One: Preliminary Inquiry

While the contraditions in some of the literature of family business first suggested the need for a conceptual framework that would incorporate the diversity found among family firms, a series of interviews conducted in the summer of 1979 effectively drove the point home. In an effort to incorporate as broad as possible a spectrum of roles in family businesses, both family and nonfamily managers in family businesses were included, as well as family stockholders, bank officers, and consultants. Dimensions of diversity which appeared included legal organizing and stockholding patterns, personal contact among family members, goals and objectives of family management, formal management systems and degree of interest in business by nonmanagerial family owners. Other dimensions such as size, age of business, industry, and financial success are not related directly to the family-business relationship but also present wide variety, and this list suggests, rather than exhausts, the differences.

Another line of preliminary inquiry which proved useful was an examination of a number of histories of family businesses, as well as case studies and articles appearing in the popular business press. The quality of such pieces varied greatly from public relations works published at company expense to serious and careful research, but taken as a whole and placed with academic research and the preliminary interviews, they contributed to a conceptualization of the development of the family-business relationship.

Phase Two: Research Framework

A firm needs resources, both human and financial, to fund and manage growth. While all firms do not grow at equal rates or to similar sizes, the phenomenon of the firm outgrowing the capability of one family, however large and talented, to provide the technical skills, capital, and management expertise necessary is a common one. Figure 1-1 represents this stereotype of the growth of a family firm.

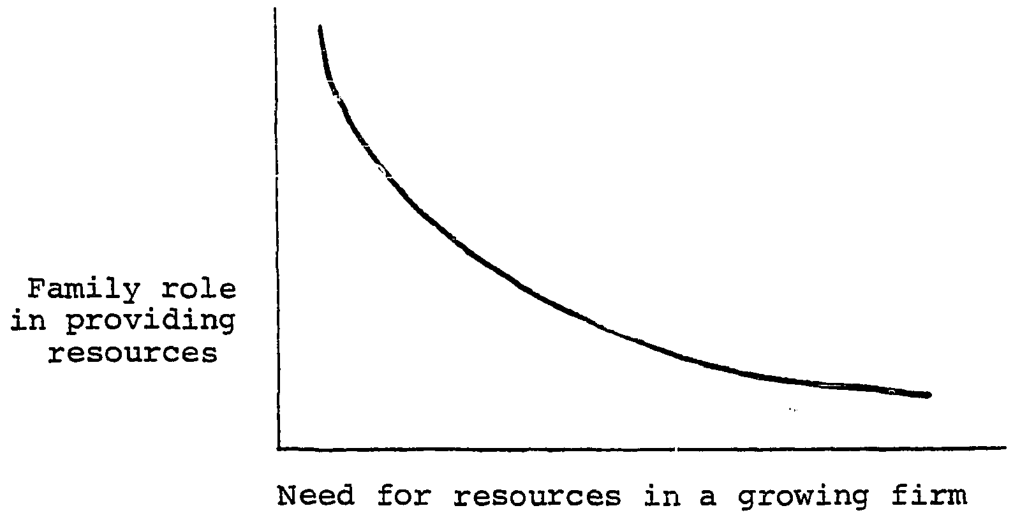
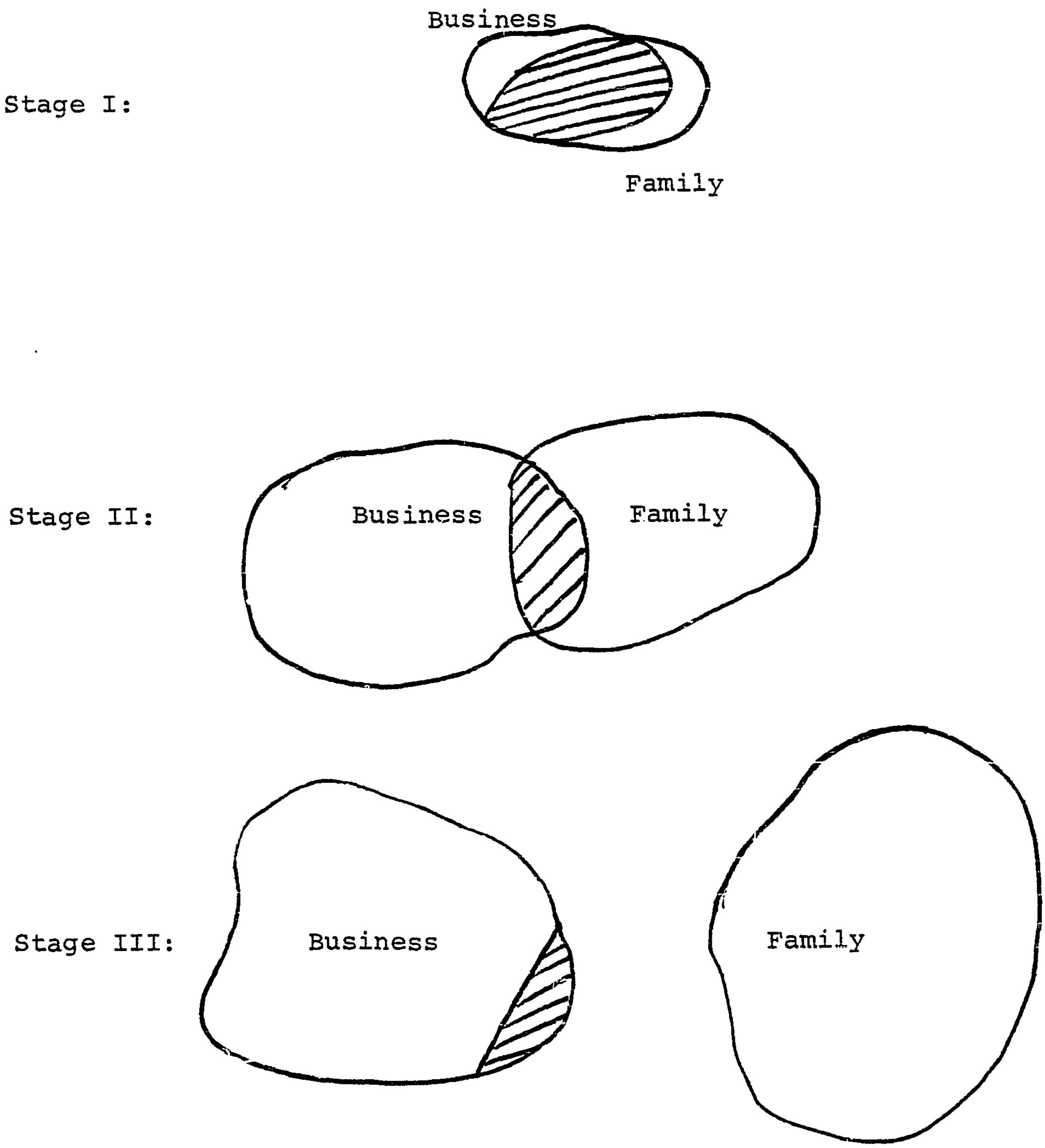


Figure 1-1. Role of Family in Growing Firm

While some firms may move from the close family ties of some entrepreneurial firms to complete disassociation of the founder's family with the enterprise very rapidly, in other cases, the process spans several generations of management. In still other firms, the growth process is arrested at some point, and the family connection can be considered, for all practical purposes, permanent. From the founding to the point of disassociation, the presence of family members in management and/or ownership positions constitutes a relationship between the business and the family.

If this relationship is "dynamic and interactive," it is reasonable to assume that the changes which occur over time are subject to description and analysis and also exhibit patterns which would help explain the similarity as well as the diversity found among family-business relationships. Based on the preliminary research, a stage concept of the family-business relationship was adopted as a way of thinking about the interaction of the two institutions and the changes which occur over time in the relationship. A representation of this way of thinking is presented in Figure 1-2.

It should be emphasized that neither the firm nor the family is the focus of this research, but rather the interaction between the two and the effect of this interaction on the strategic decisions and options of the firm. The stages concept has been widely applied to the development of



Shaded areas represent resource demands met by family.

Figure 1-2: Development of Family-Business Relationship the firm as a whole[4] and has been applied to the succession issue in family firms.[5] Neither the general models nor the applications to the succession process address the dynamic and interactive aspects of the family role in the business. The succession applications identify family stages with the generation of family management; that is, first stage was first generation, second stage was second generation, etc. The preliminary research in the field indicated that a change in generation did not automatically change the family relationships so it was decided to postpone further assessment of previously developed stages models until the findings of the research were available.

The conceptual framework represented in Figure 1-2 and used to generate the research questions is described below.

The Family-Business Relationship

Families grow by biological processes and the general trend is for each successive generation to be larger than the last. Thus the business and the family both start

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[4]For a review of stage theories of organizational development see William F. Glueck, "An Evaluation of Stages of Corporate Development in Business Policy." Paper presented at the Midwest Academy of Management Annual Meeting, Kent, Ohio, 1974.

[5]For an application of the stage concept to management succession see Ram Charan and Charles W. Hofer, "The Transition to Professional Management: Mission Impossible?" Paper presented at the National Academy of Management Annual Meeting, Kansas City, Missouri, 1976.

relatively small. While the founder is himself a member of an extended family, for the most part, only the nuclear family of which he is head will be directly involved in the business, and only his direct descendants and their spouses are likely to inherit ownership in the business. Based on preliminary interviews, working descriptions were developed as follows:

Years of Founding and Establishment - The relationship is characterized by personal involvement of family members and decision-making based on established family patterns. The head of the business is head of the household as well, and there is typically much overlapping of role and function between the two.

Expansion of Business and Family - As businesses grow, formal or informal management systems replace one-man control and families grow through marriage and reproduction. Some families divide ownership in the business among all heirs while others restrict ownership by some criteria, usually to family managers. In either case there is more opportunity for divergence of family members' objectives for the business in this stage.

Business Outgrows Family - Many family businesses outgrow the ability of the family and other sources to provide capital, and for financial or estate reasons choose to offer their stock for public sale or for acquisition by another firm. With loss of family ownership, the family firm becomes less and less distinguishable from other publicly-held firms. Family management may remain, but managers will more and more be judged on purely professional standards and family members with managerial talent will more and more assess the career opportunities in the family firm against those in other firms without sentiment.

An additional consideration in thinking about the family-business relationship is that it always operates in a specific competitive setting. The structure of the industry(s) in which a firm operates is likely to limit and shape the relationship and the effect of this and other moderating variables should be considered.

Research Questions

Assuming that the family-business relationship is a dynamic and interactive one which passes through stages of development, the following research questions were developed:

(1) How does the relationship between a family and a business change over time?

(2) What are the factors which promote change or stability in the family-business relationship?

(3) How does the family-business relationship affect the stragetic management processes in the firm? How can this effect be managed?

(4) Does the family-business relationship affect the responses of the firm to competitive changes within its industry segment?

The first question was intended to provide a descriptive background for the research by tracing the history of the family and business from the founding to its current situation. While the relationship in a given firm may be stable over a period of time, an historical approach was expected to facilitate the recognition of dynamic aspects of the relationship.

The second question sought to identify stimuli which had produced changes in the relationship while the third question was an attempt to determine the effects of the changing relationship on strategic processes within the firm. The question of whether the family-business relationship affects the competitive responses of the firm was introduced to provide some point of reference external to the firm with which to evaluate the relationship.

The objective of the study was to develop a descriptive framework of the development of the family-business relationship. Such a framework was deemed necessary to provide a theoretical base for developing propositions about the interaction of the family and the business and for delineating the managerial implications of the relationship.

Phase Three: Selection of Methodology and Firms

An exploratory methodology was chosen for this study after an abortive attempt to test hypotheses about the family-business relationship demonstrated two problems which arise when there is little research dealing with a topic.

The first problem is that theories which are generated before field work is done may turn out to be inappropriate to the actual behavior or processes of interest. The second problem is that the narrowing of the scope of the inquiry to a particular hypothesized behavior could prevent the researcher from perceiving more relevant aspects of the phenomena.

With very little information available on the developmental aspects of the family-business relationship prior to the beginning of the field work, a clinical approach was selected as the best way to obtain descriptive data about the family-business relationship without imposing preconceptions which would ultimately frustrate the objectives and purpose of the study. The essence of the clinical methodology is the attempt to gather information from multiple sources on many aspects of the firm's operations and management including the family relationship. As the data collection process proceeds, the researcher analyzes the data and relates findings to previous research or generates theories to bridge gaps between the findings and the state of knowledge on the subject.

Selection of Research Firms

The framework described earlier suggested that it would be possible to answer the research questions by a thorough study of one firm which had passed through family ownership into public ownership. Characteristics of the firm at each stage of the development of the family-business relationship should be a matter of company record and/or management memory and the firm would have fully experienced the dynamics of the process as well. A one-firm sample would not be desirable, however because it would yield no comparative data, and company record as well as management memory are likely to be focused on the current stage. To facilitate comparison and to assure data about the earlier stages, it was necessary to study firms at each stage of the relationship. To make comparisons more meaningful and to provide a setting in which to observe the dynamics of the development of family-business relationships preference was given to firms in similar industry settings.

Twelve research firms were included in the study. Characteristics of these firms are summarized in Table 1-3 and described below. The sites represented several segments of the food processing industry. All were involved in fairly simple processing of agricultural commodities. Two were vertically integrated (dairy products and eggs), while the others buy commodities and differentiate their products through processing, distribution, and/or advertising. Each operates in segments which have experienced a change in the competitive environment which required a strategic response. In most cases this change has involved a decrease in the number of competitors and the concentration of resources in the hands of larger companies. In meat,

Table 1-3: General Characteristics of Sample Firms

Industry or Company	Number of Employees	1979 Sales	Generation of Family	Market Scope
Snack Products	7,000+	$250 mil	2nd & 3rd	Southern and Eastern U.S.
$Meat_1$	450	n.a.	4th	Southern Miss. Valley
Sauce/Canning	350-600 (seasonal)	$20 mil	3rd & 4th	Southeast, Tx, NY, Calif.
$Meat_2$		n.a.	2nd & 3rd	Local
Sauce	150	n.a.	4th	International, U.S.
$Meat_3$	50	$4 mil	2nd & 3rd	Local
Dairy Products	100	n.a.	2nd & 3rd	Local
$Meat_4$	50	$3.5 mil	2nd & 3rd	parts of Tenn., Ga. and Va.
Eggs	250	$40 mil	1st	Regional and Northeast
$Meat_5$	50	$3 mil	2nd	Local
$Meat_6$	50	$3 mil	2nd & 3rd	Local
$Meat_7$	4	$.25 mil	1st	Local

government regulation has changed the economics of the industry in favor of larger firms.

While most of the firms are in the second and third generation of family management, two first generation firms and two fourth generation firms are represented in the sample. No claims can be made for the degree of accuracy to which this sample reflects the population of family firms, but it does, at least, represent several generations and this approach provides a broader range of experiences than focusing on, say, the second generation.

The family companies studied range in size from three employees with annual sales of half a million dollars to over seven thousand employees and annual sales of over $350 million. All the other firms fell into a range of from 50 to 500 employees with sales of from 3 million to about 30 million dollars annually. In view of the preponderance of small businesses in the family business category, it seems likely that this distribution is fairly representative.

Phase Four: Field Work

Access to the research sites was gained in a variety of ways, and obviously the willingness of management to cooperate was the most important criterion in choosing the sample firms. Several were contacted directly by the researcher and agreed to participate. The remainder were contacted through individuals who were personally acquainted with or in a position to influence top management. While all managers were helpful, those in the latter category were most cooperative and this strategy for gaining access is recommended.

Published Documents

Once arrangements had been made for an initial site visit, an examination of published documents relating to the firm was begun. The research sites varied greatly in size as well as whether or not they are subject to government disclosure regulations because of publicly-traded stock and whether there was anything unique about them that made "good copy." Within these constraints, available publications were reviewed to identify key changes and issues in the firm's history to use in the clinical phase of the study. Knowledge about key issues made it possible to provide a focus for interviews. In several cases, publications were made available on the site and these were used to supplement other data.

Interviews

In order to describe the family-business relationship and its development, interviews were conducted with individuals in each firm who were in a position to observe or participate in the relationship. Since the strategic impact of the relationship was of primary interest in this research, interviews were also sought with those who participate in or observe the strategic decision-making process. Interviews were conducted on three levels in the firm:

(1) The individual who has primary decision-making responsibility for the whole firm. In the larger firms, this individual will be called president or chief executive officer (CEO); in smaller firms, the individual will be the president or the owner-manager.

(2) The individuals who are directly responsible to the CEO in staff capacities. In larger firms, these will be financial officers, planning officers, corporate secretaries, etc. In smaller firms, these individuals may be people with staff or line responsibilities.

(3) An individual who has had opportunity to advise as an outsider. An outside director should provide this perspective in a larger firm while a banker, legal advisor, or consultant may do this for the smaller firm.

In addition to the individuals on the three levels of the firm described above, an effort was made to include a family member who was somewhat knowledgeable about the firm's history and activities. Such a family member was not available in most of the firms.

The interviews with the chief executives focused on the firm's strategy and the changes made in it over the years, the firm's competitive environment and changes in it, and his perception of critical events in the history of the firm. Questions were also included which dealt with the family's role in the business and how it had changed, the contributions made by the family and the impact of the family relationship on decision-making.

With the individuals who had first-hand knowledge of family-business relationship and its impact from the inside of the company, questions dealt with the development and impact of that relationship. The questions about the firm's strategy and environment were also included.

Discussions with the outsider who had an opportunity to observe the development of the firm were aimed at identifying key events and issues and the role the family plays in the business. Questions for family members dealt with their personal association with and interest in the business.

Table 1-4 represents the questions asked of these individuals. Interviews were tape-recorded and transcriptions were returned to interviewees to insure accuracy. These typescripts together with information gleaned from documentary sources provided the raw material for the analysis phase.

Phase Five: Analysis

The process of analysis involved two steps: the examination of the history, strategic thrust, management systems and techniques, and family-business interaction in each firm and a comparison of these areas among the firms. The aim was first to describe and then to compare to produce a more general description of the phenomena of interest.

Table 1-4: Representative Questions for Levels in Family Business

Board Level

1. What events and issues have been most important in shaping the firm as it is today? Which individuals have had key roles in this process?

2. What was the firm like when you first became associated with it? How has it changed over the years? What was the family like? What changes have you observed in it?

3. What role does the family play (collectively or as individuals) in the management and decision-making in the firm? Would changes in this role be beneficial to the firm in your opinion?

CEO Level

1. What was the firm's strategy when you first became involved? How has it changed over the years?

2. How would you describe the competitive situation in the industry? How has it changed? What are your expectations for the future of the industry?

3. What events stand out in your mind as particularly critical in the history of the firm? What times have been particularly difficult? Why?

4. What is the family's role in the business? How has it changed over the years? What changes do you see in the future?

5. How would you evaluate the contributions of the family association with the business? What difficulties does it create? What impact do family factors have on the process of decision-making? On the decisions that are made?

Staff Level

1. What events and issues have been particularly important in the firm's growth over the years?

2. What is the family's role in the business? How has it changed over the years?

3. How has the industry changed over the years? How does the firm deal with changes?

4. Who has been most instrumental in making the business what it is today?

Table 1-4 (continued)

5. What are the most important criteria for strategic decision-making in the firm? Does the family or its interests enter into this process?

<u>Family</u>

1. What was the business like when you first became acquainted with it? How has it changed?

2. How are you associated with the firm? Which of its activities do you keep up with? Are other family members more or less interested in the firm than you are?

3. What events or issues over the years have aroused family concern or interest in the firm?

4. Do you see any changes in the association of the family and the business in the future?

As each case was examined, an attempt was made to produce a generalized description of the relationship between the family and business in that firm. As more data became available, the generalized description was adjusted and this iterative rethinking of the relationship was an important element in the analysis process. All findings are reported with cognizance of the limitations inherent in such a process.

Limitations of the Research

The research was descriptive due to the lack of a testable theory about the relationship of business and family in a family firm. The desire to understand the process of development of the relationship has been controlling and requires that detailed data be collected from several perspectives concerning events of interest. The limited generalizability of such research is acknowledged.

In this exploratory research, no attempt will be made to determine how the sampled firms represent the total population of family firms nor to relate effectiveness measures to particular patterns of development.

The interview techniques used in this research are dependent on the ability of the interviewee to remember events in the past and in some cases to accurately report events which he did not observe. The use of duplicate sources of data provides some relief for the first problem but not the second. Because the nature of the process is episodic and erratic it is not amenable to observation or participation by the researcher so that interviews with their problems is the best alternative.

Most of the data were collected from individuals inside the business organization rather than from family members who were involved primarily as stockholders. This may introduce some bias into the results but the extent of such bias cannot be estimated.

Organization of Dissertation

The findings of the research are summarized in Chapter Two. This general summary is followed by four case studies in Chapter Three which illustrate the processes by which families and businesses interact. Chapter Four contains a more detailed description of all 12 firms in the sample and a comparative analysis of the nature and consequences of family-business interaction in these firms. Chapter Five draws some managerial implications and implications for family owners based on the findings. The final chapter raises questions for future research and presents a series of propositions describing the interaction processes in a family business.

CHAPTER TWO

FINDINGS

The purpose of this chapter is to provide the reader with an overview of the research findings as an aid in considering the cases presented in Chapter Three and the comparative analysis of the data in Chapter Four. The findings are discussed in this chapter in a generalized way without reference to specific cases. In Chapter Four the reader will find the analysis which links the data to the findings.

The Need for a Descriptive Framework

The review of the literature of family business in Chapter One pointed to the lack of a descriptive framework from which to generate hypotheses about the family-business relationship. An attempt by this researcher to generate and test hypotheses without such a framework further illustrated its importance.

This lack may be due in part to the tendency of researchers either to focus on one issue in the relationship or to focus on outcomes of the interaction of family and business rather than on the interaction itself. The succession issue, for example, has received a great deal of attention. This is warranted because it is a key issue for many firms, but the succession process is only part of the continuous interaction between family and business, and to focus on it exclusively is to overlook other areas of the relationship. Some researchers have looked at broader aspects of family business, but this research tells us more about the outcomes of the interaction than about the processes which produce these outcomes. Works which examine the advantages and disadvantages of family business fall in this category.

While this study is process-oriented in its intent to examine the dynamics of the family-business relationship, it is also concerned with the structural features of the relationship as determined by the process and the effects of both structure and process on the strategic management of the firm.

Stages of Development

The first finding concerns the pattern of development which was observed. The interaction of family and business can be described as a family-business relationship which exhibits four stages of development. The first stage is one of domination by the founder-owner and is followed by a stage of expanded family participation, a stage of broadened ownership which admits nonfamily members and emphasizes professional management, and a final stage in which the family connection is severed. These stages do not necessarily correspond to generations of family management nor should they be identified with stages of organizational development in the traditional sense. Instead, they represent four variations in structure in the family-business relationship.

While the transition from one stage to the next may correspond to management succession from one generation to the next, it is possible for a relationship to remain in a given stage for more than one generation or to pass into another stage during the tenure of one generation. It should be understood that these stages refer to the development of the family-business relationship not to the development of the organization itself.

Overview of Stages of Development

The four stages of development have been labeled Prefamily, Family, Adaptive Family, and Postfamily. The stages differ along dimensions of organization and distribution of power, reward and incentive systems, information dissemination, and the role of the family. In general, power becomes more widely distributed, rewards more uniformly determined, information flow more important to managing the relationship, and family members less central to the business as the relationship moves through the successive stages.

Table 2-1 portrays the development of the family-business relationship through the four stages. A more detailed description of the stages follows.

Table 2-1: Stages of Development of the Family-Business Relationship

Stage	Stage initiated by	Relationship characterized by	Focus of relationship
Prefamily	Founding of business	Concentration of power in single individual	Survival, succession
Family	Entry of relative of founder or sole owner/manager into management and/or ownership	Power dispersed among several individuals based on family connection	Resource acquisition
Adaptive Family	Sale of stock to nonfamily members	Power based on management position and stock ownership	Performance
Postfamily	Liquidation of family stock holdings	Power based on ability to function in new organization	Adjustments

Stage I: Prefamily

Stability in the Prefamily Stage of the family-business relationship is achieved through the literal unity of family and business. A single individual is the founder of the business and the head of the family and as such is able to adjust family constraints to the requirements of the business by virtue of his position at the apex of both institutions.

The business requirement that is first to intrude on this stability is likely to be internal. The business may grow beyond the ability of the entrepreneur to manage it or it may simply outlive the entrepreneur. In some cases the need for new management can be reconciled with the entrepreneurial penchant for one-man management by hiring "yes" men or arranging the inheritance process so that only one heir acquires the business. If such an adjustment can be made, the relationship will remain stable.

More common is the transition of the relationship to a new stage. As the family grows and matures, expectations increase for participation in the business and the entrepreneur is less committed to unitary management and more concerned with building for the future of the business and the family. As several have pointed out, the act of taking family members into the business does not instantly divide the power (Barnes & Herschon, 1976; Longnecker & Schoen, 1978), but it is the beginning of a changed relationship because of the potential for the creation of multiple bases of power in the business and the creation of new family units as branches of the original nuclear family.

The management problem in the Prefamily Stage lies in the recognition of changing business requirements and family constraints as much as in the response. In the Prefamily Stage, all the eggs are in one basket, and if the intuitive grasp of the competitive situation which the entrepreneur brought to the business in the first place does not remain sensitive to changes in the situation, the stable relationship will not be of much benefit to the company.

Stage II: Family

As more family members enter the management of the firm and as stock ownership becomes more dispersed, the maintenance of stability in the family-business relationship becomes more a matter of negotiation and consensus. Expectations of family members in management for each other's performance must be well understood, and generally that understanding includes who is really in charge although the organization chart is not likely to reflect this understanding. In some businesses, family members depend on nonfamily managers to maintain smooth relations and see that expectations are met. Not only must family constraints be considered in internal division of labor in the firm, but also the expectations of family stock holders who have no management positions are more likely to be important at this stage of the relationship. While official input is usually limited to meetings of Board of Directors and Annual Stockholders' Meetings, there is ample opportunity for informal input in some families. Whether this is positive or negative depends on the degree to which it is informed input and how much of it is redundant and consumes valuable management time.

Changing business requirements in both financial and managerial resources can have a direct impact on the relationship and may be harder to explain to family members with little direct involvement in the business. It is also difficult to withdraw family "perks" which may have become institutionalized from a time when they were a substitute for the compensation the company was not able to provide.

The managerial problems in this stage of the relationship include not only recognizing changes in business requirements and family constraints but also evaluating the relative merits of adjusting the requirements or constraints as opposed to changing the relationship. In either situation, the problems of "freezing, changing, and refreezing" (Lewin, 1947) are also present.

Stage III: Adaptive Family

The family is joined in the Adaptive Family Stage by new resource providers. Stock is sold to nonfamily members, and family managers must meet professional criteria just as their nonfamily counterparts must. While family constraints must still be considered by management, another set of constraints is added. The performance criteria by which capital markets judge firms become a factor. The extent to which those criteria match the constraints of the family determines the task management will have in meeting these criteria.

Family members may still have considerable power both as stockholders and holders of positions on the Board or in management, but there is a narrower range of activities in which the family can exercise this power. The narrowness of the range does not mean that the issues are unimportant, however. Family constraints in this stage are likely to be exercised in connection with succession and with offers to buy the business.

Adjustment of family constraints to the requirements of the business becomes an educational process in this stage. It is not as critical as in other stages because family members have a more liquid asset in this stage than in the others, and while selling their stock might be a least preferred option, it is an option that provides something of a safety valve for the relationship.

Stage IV: Postfamily

When the family chooses to sever completely its connection with the business, the relationship ends. The transition from an adaptive family relationship to a publicly owned and professionally managed firm or to the status of subsidiary or unit of some other firm is fraught with difficulties which have been outlined elsewhere. People are involved in addition to the physical assets, and when these people have been employed and socialized in an organization which has institutionalized the family constraints, the new relationship will also have family-related problems.

Management problems at this stage relate to distinguishing and preserving those family constraints that have operational or motivational utility. At the same time employees must be weaned away from family practices which are contrary to those of the new unit.

Factors Which Shape Development of the Family-Business Relationship

The foregoing discussion suggests that the family-business relationship evolves similarly in family businesses with certain characteristics such as distribution of power and reward and information systems distinguishing one stage of evolution from the next. The second major finding of the study deals with the process of development. The factors which determine the evolution of the family-business relationship arises in the competitive environment of the business, the internal pressures of operations, and from the growth of the family and its changing fortunes. An event which creates a discrepancy between the competitive requirements of the business and the expectations of the family in the form of the constraints they hold for the business provides an impetus for change. This discrepancy is often resolved by an adjustment in either the business or the family. An adjustment in the business usually involves a change of policy, plans, or strategy while an adjustment on the family side usually involves a change of constraints. When such a resolution is not attempted or not desired, the structure of the relationship becomes the focus of change. The concepts of business requirements and family constraints as sources of discrepancies in the family-business relationship are discussed below.

Impetus for Change: Discrepancies in the Family-Business Relationship

A distinction is frequently made in the literature of family business between "business interests" and "family interests." Cohen and Lindberg assert, for example, "If family ownership is to be effective it must display more self-discipline (placing the needs of the firm above all other needs) than is commonly found in business" (p. 201). Dailey, Reuschling, and DeMong refer to a danger in family business of "consistently plac[ing] family interests above long run corporate interests" (p. 66). A final example is Donnelley's reference to the ability of the family "to pursue its own objectives and aspirations, even when they are at variance with the best interests of the enterprise" (p. 94).

In practice, it may be difficult to distinguish "family interests" from "business interests." A policy of employing all family members who request jobs seems to be clearly a matter of family interest. Such a policy may be a means of assuring the support of important family stockholders for the chief executive and be seen by him as being in the best interests of the business. It can be difficult to assess the implications of policies completely enough to categorize them with confidence. Another difficulty is the time dimension. Several managers and observers of family business argued that family and business interests converge in the long run though there could be differences that are quite pronounced in the short run. Many of the managers interviewed felt that business and family interests overlapped more often than not. The assertion was made that "what's best for the business is best for the family."

While maintaining the association of family and business interests, managers did make distinctions between actions taken because of business pressures and those taken because "the family preferred it that way." The former have been labeled "competitive requirements of the business" while the latter will be referred to as "family constraints." Table 2-2 lists events and developments which can require action from either the family or the business side. This categorization is based on the origin of the developments and events and does not require a determination as to whether business interests or family interests are being catered to.

Table 2-2: Sources of Change in the Family-Business Relationship

Business Requirements Causing Changes

1. Growth of the business
    - A. Pressure on managerial resources
    - B. Pressure on financial resources
2. Changes in industry structure
    - A. Increased rivalry in the industry
        1. Increase in number of competitors
        2. Changing size distribution in favor of larger firms
        3. Slowing of overall industry growth
        4. Increase in fixed costs, excess capacity
        5. Products become less differentiated
        6. Firms in industry become more diverse in personality
    - B. Increase in relative power of buying or supplying industry
    - C. Changes in entry barriers
        1. Changing economies of scale
        2. Change in absolute costs
        3. Change in financial requirements
        4. Change in availability of access to distribution channels

Family Constraints Causing Changes

1. Growth of the family
    - A. Changing need for jobs
    - B. Changing interest in business activities
    - C. Changing identification with business
2. Changing family fortunes
    - A. Changing dependence on the business
    - B. Changing role in providing resources

Business requirements. The term "business requirements" is used to refer to those imperatives which arise as a consequence of and as a requirement for staying in business. These requirements may stem from the structure of the industry, the regulatory and legal environment, the state of the economy, and other factors which determine the environmental threats and opportunities which a particular business faces. Business requirements also refer to factors which are internal to the business and determine its strategic competencies and weaknesses. Requirements in this category would include managerial resources, financial resources, and suitable organization structure and management systems.

Generally, management is dealing with a range of potential responses to business requirements which is determined largely by the nature of the requirements. When the requirements arise in the regulatory or legal environment, the choice may be between compliance and going out of business. In the case of requirements arising from internal changes, the option of simply ignoring the requirement may be available.

Family constraints. The term "family constraints" is used to refer to the set of goals, expectations, and objectives which family members have for the business. Generally, these constitute a range of achievement and behavior rather than precise targets. The set of constraints which is of particular concern to managers is those of family members who have the power to enforce them. This power may arise from stock ownership, personal influence, or the position of the family member in the business. Family constraints typically include financial expectations about the return on invested assets, expectations about who is to be selected for management positions, and perceptions about the noneconomic responsibilities of the business.

Family constraints change as a function of the growth of the family and the loss of interest in operations by family members who have no direct involvement, from changes in the financial fortunes of individual family members, and from inadequate or incorrect information about the business. The range of responses to changing family constraints depends on the power of the family to force compliance and on the effect of compliance on the business. Providing summer employment for the grandchildren of the Chairman of the Board is not likely to have strategic consequences, while increasing dividend payout could.

<u>How discrepancies arise</u>. Both business requirements and family constraints are products of situations which are subject to change. Many, perhaps most, changes in one do not affect the other; that is, it is possible for managers to make decisions to fulfill business requirements which do not conflict with any of the constraints the family has for the business. Conversely, family constraints can be met without jeopardizing the competitive stance of the business.

When a situation does arise which puts business requirements and family constraints in conflict, several outcomes are possible. The family constraint may go unrealized while the business requirement is met; the requirement may be unmet but the constraint is maintained; or some compromise may be attempted. In each case there is a discrepancy between what the family expects and what the business produces. This gap can be felt in a number of ways including a decline in the performance of the business, an increase in the involvement of nonmanagerial family members in the business, and increase in interpersonal conflict in the business and/or the family. Such a discrepancy is essentially a dysfunctional situation and must be resolved. The discrepancy creates an impetus for change in the relationship which is comparable to the first step of Lewin's process of change, the step of "unfreezing" the current behavior. The change itself may take the form of an adjustment of the element of the relationship which appears to be out of step or the changes may be a transformation of the family-business relationship.

Nature of Change: Adjustments and Transitions

Figures 2-1 and 2-2 portray the two kinds of changes which are considered in this section. In Figure 2-1, a discrepancy is produced in the family-business relationship by a change in the requirements of the business. This discrepancy is alleviated by a corresponding change in the family

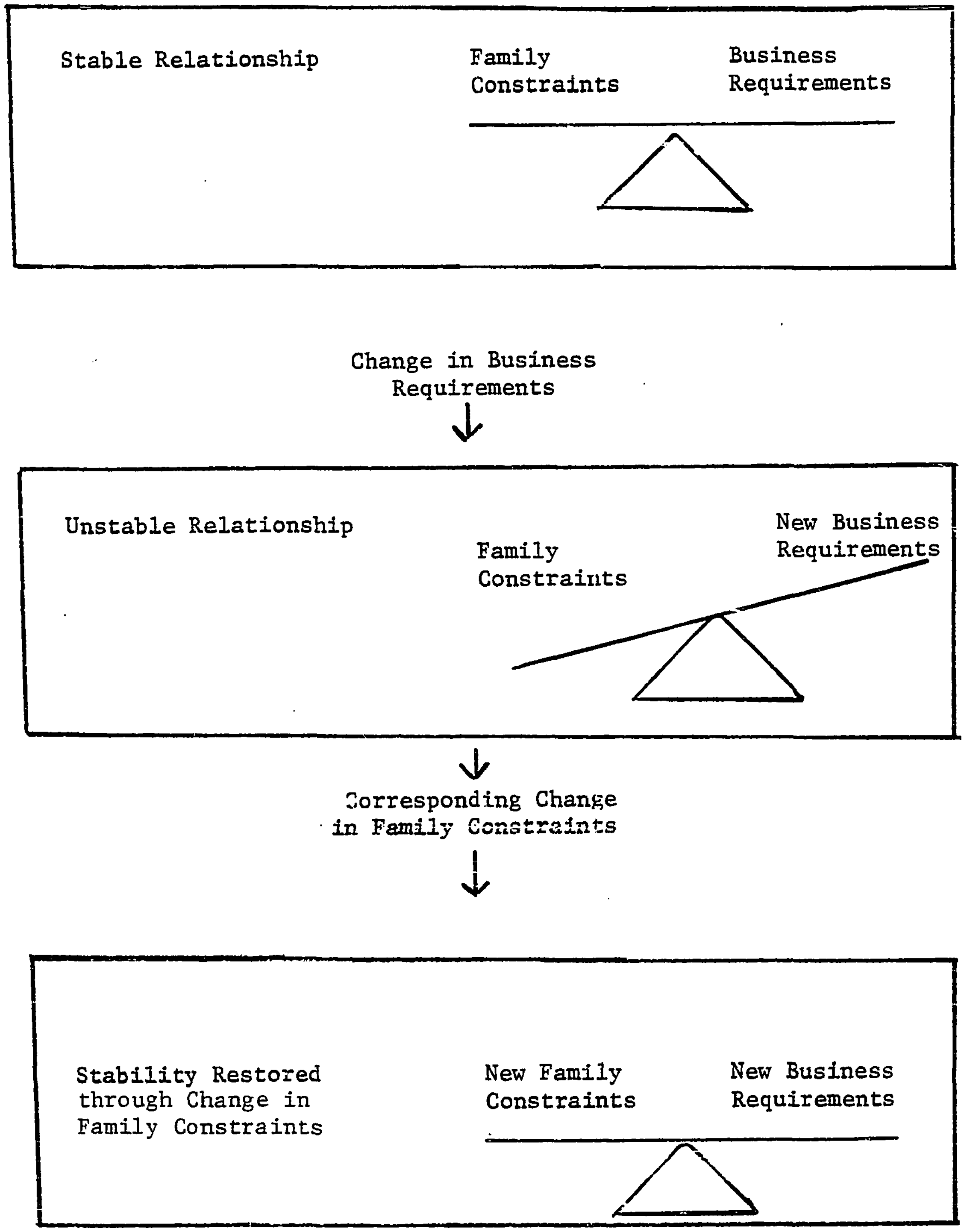


Figure 2-1: Effects of a Change in Requirements of Business and Corresponding Change in Family Constraints

constraints and the relationship is restored to its former stability.

In Figure 2-2, the discrepancy is not resolved by a corresponding change and it becomes an impetus for a structural change in the family-business relationship. In the process of making the transition from one set of structural arrangements to the next, the discrepancy is resolved. Family members may no longer have the power to enforce their constraints or the constraints may no longer be meaningful. The new structure may result in a change in family constraints or may enable the management to meet constraints and business requirements in a way that was not possible under the previous structure.

Adjustment of the Family-Business Relationship

The manager who persuades his cousins to accept lower dividends in order to generate more funds for capital spending, the manager who decides against a proposed building site because of the family's objections, and the brothers who discontinue part of their operation because they cannot meet capital requirements without acquiring debt which the family has never approved are all involved in adjusting the family-business relationship to remove discrepancies. In the first situation, family constraints about the provision of income to the family came into conflict with the needs of the business for expansion of facilities. In the third case, a similar discrepancy was

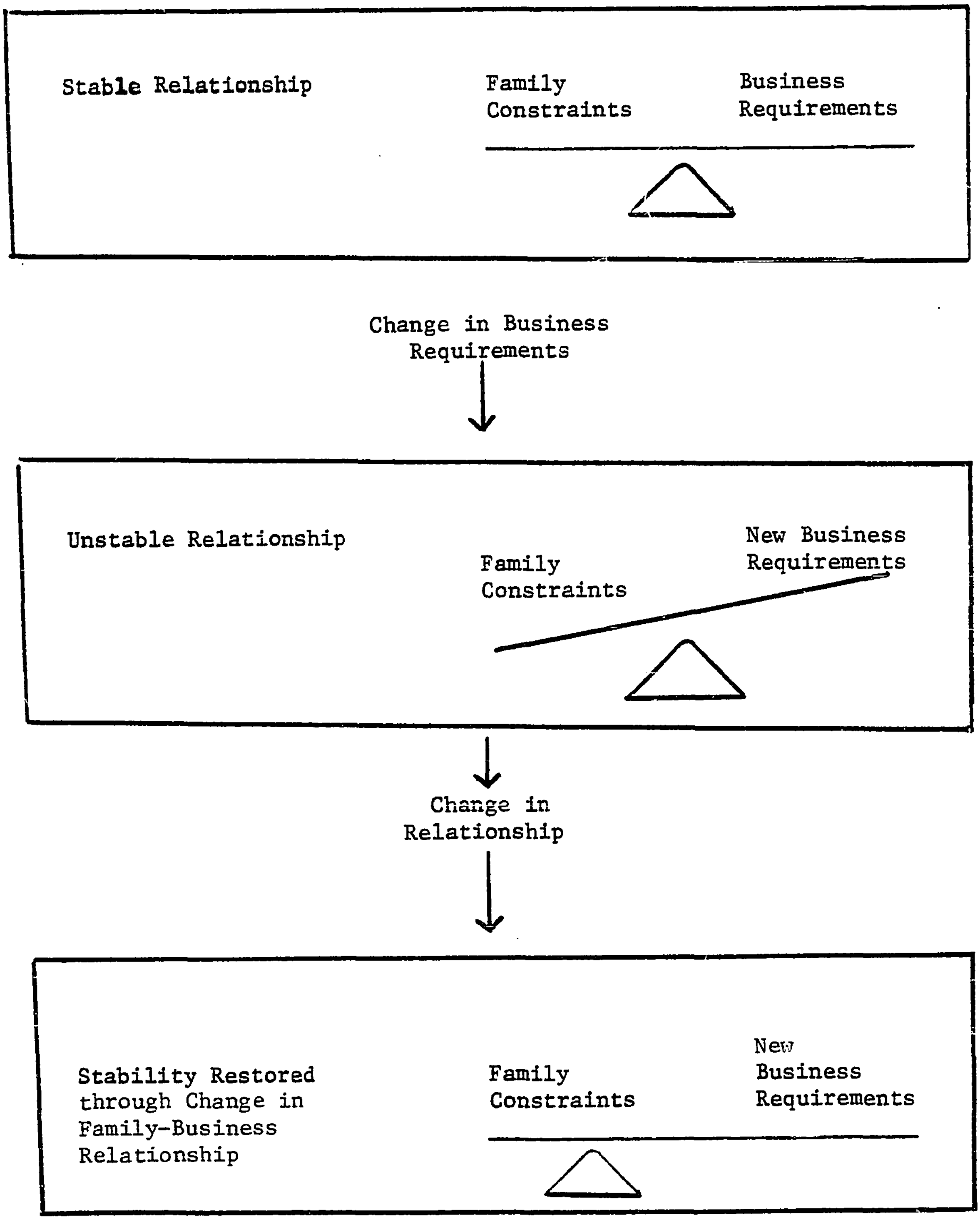


Figure 2-2: Change in Requirements of Business Produces a Change in Family-Business Relationship

resolved by abandoning the activity which required the capital spending. In the second case also, a business decision was shaped by family constraints.

The adjustment process depends on the skills of the managers at persuasion and their perceptions of when family constraints are fixed and the business requirements are more easily changed. The number of adjustments possible within the family-business relationship appears to be limited only by the flexibility of the family and the ability of the manager to generate satisfactory alternatives as discrepancies arise.

Transitions in the Family-Business Relationship

While the relationship may undergo any number of adjustments (within limits of family flexibility and business options), transitions represent more fundamental realignments of the family-business relationship and do not occur as frequently. The study has identified three transitions which occur in family-business relationships and these transitions are the bridges between the four stages of the family-business relationship. Just as the stages have characteristics, the transitions between them have particular attributes as well. Some of these attributes are described below.

Transition 1. As the relationship moves from the Prefamily to the Family stage, the involvement of family members increases. Succession and inheritance processes are often present in this transition and individuals who are accustomed to relating to each other based on family roles must work out new relationships based on business functions.

Transition 2. The opening of ownership in the business to nonfamily members is the hallmark of the transition between the Family and Adaptive Family stages of the relationship. The introduction of outsiders who have important roles in providing both financial and managerial resources necessitates a formalization of organization processes and may include conflicts between "professional" systems and family traditions.

Transition 3. When a family chooses to end its association with the business, it moves from the Adaptive Family to the Postfamily stage of the relationship. Legally, this transition is a rapid one, but for the organization the transition is likely to be protracted as employees and remaining family managers adjust to their new status.

Paths of Development

Transitions from Stage I to Stage IV in the sequence described above are not the only possible sequence. At any stage of the relationship, sale of family interest in the ownership of the business is possible so a relationship may go from Stages I and II into Stage IV as well as from Stage III. Also repurchase of stock by one or more family members could reverse the sequence although this was not observed in the firms studied and, because of that, not included in Figure 2-5. Not only does the sequence of transition provide a means of distinguishing among family businesses but the number of transitions also varies. Some firms avoid transitions and remain in the same stage for generations while others evolve rather quickly out of family ownership and management.

Family business-relationships exhibit three distinct paths of development or evolution of the relationship (see Table 2-3). The first path moves through the stages in order beginning with Prefamily and ultimately ending the relationship in the Postfamily Stage. Changes in the structure of the relationship are foreseen and planned for and the disruption is minimal. This path may be described as the evolutionary path of development.

A second pattern can be best described as sporadic. The relationship skips stages, and transitions may or may not be foreseen. Transitions tend to be a reaction to some emergency or crisis and thus the lead time for planning the change is relatively short.

The final pattern is distinguished more by the absence of change than by how transitions are sequenced. Relationships change very little in this pattern and several generations of management operate under the same structural arrangements.

Table 2-3: Paths of Development of the Family-Business Relationship

Path:	Sequence:	Timing:
Evolutionary	I-II-III-IV. Relationship moves through stages in order.	Transitions are made rapidly enough so that a given generation of management is likely to have experienced more than one stage of the relationship.
Sporadic	I-II-IV; I-III; I-IV. Stages are skipped as the relationship undergoes transitions.	Transitions tend to be sudden and opportunistic.
Arrested	I-II. After initial transition into family stage of the relationship, no more transitions occur. Maintaining the relationship at this stage becomes goal of both family and management.	Transitions are made so rarely that several generations of management have experienced the same stage.

The consequences of change in the relationship depend in part on the path of the development which has been experienced by the relationship. While any transition raises issues of managerial decontrol, conflict resolution, information dissemination, and employee adjustment, a relationship which has had a sporadic path of development responds differently from one which has developed in a traditional manner.

Managers in a firm which has followed a traditional path of development have had more experience with change and anticipating and planning for transitions. Managers in firms which have experienced sporadic development are less likely to be prepared for changes in the relationship. Not only are they less likely to have experience in transition but are more likely to see transition as an out rather than a means of orderly development. Managers in firms with arrested family-business relationships are least prepared of all for making transitions and tend to focus their efforts on making the adjustments in the family-business relationship which enable them to maintain the current structure of the relationship and thus avoid transitions.

Summary

The interaction of a family with the business it owns and/or manages can be described as a relationship which develops in stages. In the earliest stage, the family and business are united in the person of the owner/founder, and in subsequent stages, the family and business become increasingly separate until finally in the fourth stage the association is terminated. The impetus for change in the relationship arises in subsequent stages, the family and business become increasingly separate until it is terminated in the process of transition into the fourth stage. The impetus for change in the relationship arises when discrepancies or conflicts arise between the competitive requirements of the business and the family constraints for the business. If these discrepancies are not adjusted by changes in the business or in the family constraints, the continuing discrepancy provides an impetus for changing the structure of the family-business relationship. A structural change refers to an alteration in the requirements for participation in the organization and the roles of the participants and usually affects both ownership and management roles.

There are three major transitions which occur in the evolution of the family-business relationship. The first involves the broadening of the family participation in the business and is accomplished through succession and inheritance. The second transition is the introduction of outsiders into the ownership ranks of the business by the sale of stock. The third transition is the sale of all family interest in the business and often results in the incorporation of the operation into a larger unit.

While the four stages and the three transitions represent the range of possibilities for the development of the family-business relationship, the findings of the research indicate that there are differences in the patterns of development which families and businesses exhibit. These differences relate to the sequencing and timing of the transitions.

The overview of the findings of the research presented in this chapter and summarized here provide the reader with an introduction to the four cases which are presented in Part Two.

CHAPTER THREE

CASE STUDIES: THE FAMILY-BUSINESS RELATIONSHIP

The findings of the research were presented in Chapter Two and provide the rationale for the choice of which of the 12 firms in the sample are included in Chapter Three. Because of limitations of space and the similarity of the development processes among some of the firms, cases which would allow the reader to judge the findings and analysis were chosen. Chapter Four includes summary data for all the case studies.

As indicated by the findings, the family-business relationship is one which can be described in terms of the current stage of the relationship, the adaptations which serve to preserve the relationship in that stage, and the transitions which have been experienced. In addition, the path of development which the relationship has followed serves to differentiate it. The cases were selected for inclusion in this chapter to illustrate these differences.

While four stages of the family-business relationship were identified, two of the stages, Family and Adaptive Family, exhibited more significant and intense family-business interaction than the other two. The first stage, Prefamily, sees less interaction because of the central position of the owner-founder in both the family and the business. The last stage, Postfamily, recognizes the fact that family interaction with a business does not end at the moment ownership ends, but there is much less interaction in this stage than in the previous two stages. The cases included in this chapter are, for these reasons, currently in the second (Family) and the third (Adaptive Family) stages of the relationship.

Three transitions occur in family-business relationships. These transitions are the broadening of family participation, the extension of ownership participation to outsiders, and the dissolution of the relationship. The cases included in this chapter provide information on the elements of each transition. The cases also illustrate the process of adjustment which occur within stages as managers work to preserve the current structure of the relationship.

Of the three paths of development identified in the findings, the traditional path and the arrested path are represented by cases in this chapter. These paths were more representative of the sample firms' development than the third path, sporadic development.

The order in which the cases are presented takes the reader from the smaller firms with single product or single product line businesses and fairly simple organization structures and operations to the most complex organization in the sample. The presentation also begins with relationships which have experienced mostly adjustments and closes with relationships which are in the process of undergoing or have undergone significant transitions.

Piedmont Meat Company

In 1948, a retired meat packer used the proceeds from the sale of his business to provide capital for a new meat business. The business, incorporated as a family business, was headed by his oldest sone who was soon joined in the business by his two brothers. The father and three sisters were the other stockholders in the enterprise.

Piedmont Meat Company (PMC) slaughtered and butchered animals and provided fresh beef and pork as well as some processed meats such as ham and sausage to its customers. The business grew slowly until employees totaled 100 in 1970. The plant was closed that year for renovations to comply with new federal regulations concerning facilities. When the business reopened on a reduced scale, it was as a processor of meats with no slaughtering activities.

Currently, the company employs approximately 50 people. It has established itself as a supplier of processed meats and related food items to independent grocers within about a 100 mile radius of the plant. Annual sales are approximately $4 million.

History

1948-1968: Slaughtering and Processing

Piedmont Meat Company was actually the second family meat business. The original business was a meat-packing operation in which the founder of PMC and his partner had been involved for twenty-seven years. The death of the partner without any buy-sell agreement had created problems and the business was sold in 1946. The daughter of the founder described her father's reaction to the death of his partner:

> Daddy was in his first business with somebody that was not related and, as far as I was concerned, there were no problems between he and his partner. But after he died, his whole half of the business went to the widow. She was not a participator and there was no clause in there for her either to sell out or have anybody involved in it. I don't know the financial arrangements, but I know that it caused a lot of conflict and Daddy made the statement that whenever he got in a business, he would have a clause to take care of that eventuality.

Both the founder and the oldest son had been very involved in the first business and, as the son related, could not find satisfactory alternatives after the sale:

> I was the oldest boy and the only one in the dressed beef industry. My brothers were in school. After we sold the dressed beef company, our father was going to raise cattle and I went into the advertising business. Dad wasn't particularly happy with just raising livestock. It wasn't fast enough after being exposed to the day-to-day management of a business that employed some 120 people. He was the president and general manager.
>
> We decided to go to a small abatoir and have cattle custom killed. He would do the buying and I would

> do the selling and deliver them. After a few months we got a truck. We started out delivering just a very limited number and I had a car I could load one or two quarters of beef into.

This limited venture was a success and the facilities soon became inadequate. The son explained:

> In about six months' time, we had outgrown the facility that we were operating out of and about that time, the city and county-owned abatoir became available and someone on the Chamber of Commerce was aware of the fact that we had sold out our business, and they contacted us. We came and looked at this one and we liked the location. A good agricultural section for raising livestock and market potential--over two-thirds of the population of the state within some ninety miles. So from a marketing standpoint, it was a good opportunity. Livestock was a little limited but still, based on the premise that if you can bring your livestock from within a one hundred to one hundred and fifty mile radius, it's still feasible. So the livestock looked like it would be feasible for some time to come.

The move produced one surprise:

> We found when we came here that other than the abatoir function--that is, killing for the public as opposed to buying and selling and processing--there was no business here. I think they were selling about two hundred pounds of beef among a couple of butchers.

The scale of the operation was also a great change for the father:

> When we left our previous location, we were killing about a thousand hogs a week and three hundred cattle a week and when we came up here we didn't need but two cattle a week and about ten hogs a week. He wasn't used to going to a sale to get a little handful. It was a tremendous comedown from an operation with some twelve to fifteen salesmen and a fleet of trucks to one part-time salesman and two people.

Both father and son sold to new accounts. The father continued buying cattle while the son supervised the plant and kept the books while the operation was getting underway. As the oldest son recalled:

> To start with Daddy did some part-time selling and I did some selling. I had two butchers who did the killing. I had had some experience in slaughtering operation. My wife and I did the bookkeeping on Sunday afternoon.
>
> We started off about three men, my dad doing the buying one day a week. He could go to a sale and get in two hours all we'd need for a week. We had one kill floor and one little cooler and we bought one truck.

The father's solution to the lack of business in the new area was to force his son and himself to create it:

> My father worked on the principle that if you needed five cattle, he would buy seven and say "I bought them now you sell them." It would keep the pressure on you. It was perishable merchandise. He would force you to extend, to go on and move this out. If you sold seven this week he would buy eight the next week, so it was a force feed proposition.

The growth of the company over the years was symbolized for the managers by the additions to plant capacity and processing ability:

> We actually leased the plant the first six months to see if it would go and determined it had potential. The original kill floor was built in the early Thirties but it was well built. It was very substantial even though it wouldn't pass current day slaughter standards for poured, reinforced concrete construction. It had a tin roof and metal sides and all, and it couldn't be built in this manner and meet today's standards of sanitation.

> Through the years we would add a cooler, add a route, add another room on to the plant. I think we've built in all eleven different times. The first big building project was about 1952. We began to utilize all of the available facilities--just outgrew them in about three years. The first major project we added was two coolers and a shipping department and also the smokehouses.
>
> Most recently we put in air-conditioned smoke houses year before last. Not a major item but with the new addition we can smoke eight cages at a time, a 25% increase in capacity. Where the others were brick houses, built in 1952, these are stainless steel. Humidity as well as temperature is controlled. We've got $40,000 in two smokehouses where the original smokehouses were about $3,000 a piece.
>
> It's part of the growth process and in order to keep up, we have pursued for the entire thirty-two years a policy of plowing back into the business every year some new equipment.

By the late Sixties, the company had 100 employees and provided customers with fresh dressed beef and pork as well as processed items including sausage and ham. Several challenges in the competitive enviornment of the firm had been building during those years. The passage of the Wholesale Meat Act had the most immediate effect on the operations of the company but the decline of the independent supermarket may have the more protracted and ultimately more significant effect.

<u>1967-1970: The Wholesome Meat Act</u>

The Federal Meat Inspection Act, commonly known as the Wholesome Meat Act, was passed in December of 1967. The Act stated that by December 1, 1969,

> each state was to have in operation, inspection standards and procedures for red meat at least equal to those of federal requirements, or submit to federal inspection of meat and plants in which meat was slaughtered for sale within that state's borders. (McCoy, 1972, p. 158)

The compliance date was later extended until December 1, 1970. The President of PMC described the background of the event from his perspective as a small meat-packer:

> What was behind that was basically a power struggle between the small packers and the big packers. The small packers had taken a larger percentage than the big packers because they knew the local people and could season for local taste. The big unions had come in and to a large degree done the same thing to the big meatpackers that the unions have done to the American automobiles--literally priced them out with shoddy work and higher pay. Small hometown business still had a personal relationship and they could just out compete them. Consequently, with the growth of that segment of the industry, big unions and big government got together and they passed this so-called wholesome meat act. And being opposed to the wholesome meat act was like being opposed to motherhood.

A long time observer of the industry described the years following the passage of the Act as a time of troubles for small, independent meat packers and the direct cause of many closings. While all had been inspected by state meat inspectors, many exceptions had been made over the years based on the inspectors' knowledge of local conditions. The passage of a uniform meat inspection system meant an end to these variances and the necessity of making costly and sometimes arbitrary changes:

> We were killing baby beeves here which are small cattle--four to six hundred pounds. A lot of the major packers, the majority of the big packers were killing heavy beef weighing 1,100 pounds. Well, these regulations said that all plants had to have a 10'2" rail from the top to the floor. It so happened that we had a 10'2" rail in most of the plant. One of the factors was width of the doors and the size cattle that we processed, four foot doors were more than adequate and most of our doors were four foot doors. The government said "You've got to have five foot doors." Cattle might sway and hit the edge of the door and bruise the meat, and if you've got a big thousand pound cattle, that's true. But if you're killing five to six hundred pound cattle, you've got plenty of room on each side. As I said the first three years, they said "We'll use the rule of reason." So they'd look at your operations--of course the state inspectors who had been here for some time knew what the situation was, there was no problem. But when it came under federal, you had to change and there was no market for your doors. All the other processors had to put the same thing in. At twelve hundred dollars per door, it was serious. I think we had eleven doors.

PMC's managers were determined to survive and embarked on a program of retrenchment and renovation which changed the nature of the business:

> I think that in two years, we spent something like one hundred thousand dollars doing things that when we had finished, our plant wasn't appreciably more valuable. It was just that we had to do this to conform to regulations. And human beings interpret the regulations. You get a certain inspector out of Atlanta and a district supervisor over here and they come by and want you to do this. They're promoted or transfered and someone else comes in and their emphasis is on something else. It reached the point that we finally decided the potential rewards were just not there so we closed the kill floor. We operated it from 1948 until, I believe, 1971. That's twenty-three years that we killed here in this plant, and in '71 we modified our operation to just strictly processing. Also we added some jobbing feature. We took on turkeys and turkey parts and frozen meats. We expanded our cheese that moves through the meat markets. We adjusted operations and it was a right

> cruel adjustment because it took us two or three years to adjust our sources of raw materials, some shift in machinery, and some retraining for personnel. We cut the organization from one hundred to thirty. We closed for two months for major renovation. To lose $28-30,000 a month--it hurt. We lost close to a quarter of a million.

The brothers called on employees, family, and bankers for support, and it was provided:

> There were people who had been with us a long time, and they were very loyal to stay when we couldn't raise them when everybody else in the neighborhood was getting raises. We took our sisters' debentures and made stock out of them in order to eliminate any debt structure. Then we personally bought the stock and issued them personal notes. Temporarily they joined forces with us too. We had dealt with a banker for twenty-five years or so and we had established a reputation.

Another source of support was the state meat packers' association which the brothers had been instrumental in founding. The sales manager, a younger brother, explained:

> The state association helped us while we were closed. I'm not positive how much it helped us but some of our competitors made our sausage. Of course they didn't give it to us, but it helped us to keep contacts. We never did get out of the market, but we got out of the profit end.

The test of the success of all these efforts for the brothers was the survival of the firm:

> We still haven't paid all those debts yet. For a family business, it was a grave necessity. I suppose the thing that was accomplished as we look back now is that the government closed up over three hundred independent meat packers across the nation and so much of it was a struggle between big business and

> the big labor unions aided and assisted by big government and their regulation.

Operations and Management Systems

Since the closing of the kill floor, the company has become primarily a processor and distributor of pork, beef, poultry, cheese, and other meat-related items. Sausage and ham are manufactured at the plant while other products are obtained from jobbers to complete the product line. According to the sales manager, processed items are most profitable:

> It's really so difficult to keep the volume level up. Of course, we want to sell enough branded. All small packers like to push their processed items because that's basically where the best profit margin is. We sell some neck bones, pigs' feet, things like that to have something to go on the truck with you. And if you can make $3 on this box and $2 on this one and make a good profit on the sausage that you take along with it, theoretically it will all work out. But it's increasingly more difficult to make your break-even.

Products are sold by route salesmen who call on customers weekly as described by the president:

> I don't think you can work effectively unless you have a very dense population. The criteria that I like to think in terms of is "Can I send a salesman out and have him back the same day? Can I send out a truck in the morning and have him work his way out?" I don't like to send him out and have him deadhead back in. But if he can go out 50 or 75 miles and work across 25 miles and come back in from this small town to this one and this one. Now when you go into a large city, you send two salesmen up there one day and send a truck the next day. Of course one of the problems is that you can't distribute because of the traffic congestion. You can't serve as many customers as you did a few years ago.

Customers are given a week's credit:

> Since we give seven day terms, we try to have the salesman call on the merchant at least once a week. He gets the order and he gets the money from last week. This is part of a successful operation. If they can't pay you for one week, how can they pay you for two? You're understanding and the customer knows that you expect to get paid.

The limited capital with which the firm operates has placed an emphasis on careful spending for plant and equipment. The sales manager described a recent purchase:

> The trucks that we used to buy a chassis for $3,000 and equip it are an example. I buy a good many used trucks. The big packers can afford to pay these prices. We do have a small leasing company of our own which handles financing of most of our equipment. But we bought a diesel truck the other day at around $9,000. If the truck were new it would have been $25,000 and yet it has 120,000 miles on it. We think it will serve our purposes.

The president reported similar practices for equipment:

> The big majority of the time in the last thirty-two years, we've searched out good used equipment. Not always, but many times. In the last twelve months, we bought a stainless steel blending machine and the new cost of it was about $16,000. We happened to locate a place that was going out of business and we bought it for $8,000. It had very little wear on it and we'll get as much use as if we'd bought a brand new one for twice as much. We just won't get to charge off quite as much depreciation.

Organization

The oldest brother has served as president of the company since its founding. He was joined by his two brothers in the business after they completed college. All of the brothers got experience in operations while developing functional specialties. The sales manager felt this base of experience was important:

> I think another thing that's been helpful as far as our organization is concerned is that all three of us before my younger brother died have come through the organization. In other words, I made sausage for ten years. Now I'm in charge of sales. If you know the production end, it helps you with your sales. One brother bought livestock and my older brother has done it all.

The brothers divided the responsibilities of running the business so that the one was in charge of operations and finance, another was in charge of sales, and the other bought livestock. With the death of the one brother and the nearing retirement of the president, there is increasing delegation according to the president:

> I'm leaving more of the business to my thirty-year-old son. He's been working with it since he got out of the Coast Guard about seven or eight years ago. Increasingly my deceased brother's duties and part of mine and the other brother's have gone to people who are nonfamily members. The office manager has been with us twenty-five years; our shipping man has been with us twenty years; the maintenance man has been with us twenty years, I recokon; the smoke house man has been here thirty-two years. When you retain good people and they know their jobs, you can go off and leave them.

While the company has no formal long range planning, the brothers are very conscious of the need to monitor the environment. The president uses conventions for this purpose:

> I like to attend at least one or two conventions a year to keep up with the industry, to keep up with

> what's going on with the government, to keep up with the latest techniques and what's happening. I think it helps you compete. If you don't keep up, you get left behind and little by little, you lose your business.

Both brothers participated in the formation of a state association for independent packers and they feel this allows them to have some influence on the environment:

> There are a lot of mutual problems we've found. Small packers, even though they may be competing, a lot of times, have a common problem. You and I can go talk to the regulatory authorities and maybe they will listen. If you go as one small business, they will be courteous but that is all.

Competitive Challenges: Independent Packers and Chains

The distribution of retail food, including fresh and processed meats, has been radically affected by the development of chain supermarkets and their buying practices. Chains buy in quantities which small independent meat packers cannot provide and they require central delivery to warehouses for distribution to local stores. Both of these practices make it difficult for the small meat packer to enter the chain markets. The president told of a venture into the chain buyer's office:

> A few years ago, two of us went together and went to see a chain buyer. He wanted to talk about smoked ham. He thought both our hams were good and he liked them both and he would be willing to accept them in the store--either ours of theirs. He said "How many hams are you talking about selling me a week?" Harry said 10-15,000 pounds a week and I said 5-10,000 pounds. He said, "In other words, you're talking

> about a maximum of 25,000 pounds out of the two plants every week." I thought to myself, I don't know about Harry, but if he were to want 25,000 pounds a week, I sure would have to step up production. That would strain us. He said, "Well, it takes about 60,000 pounds the average week and when I have a sale, I've got 124 stores I'm serving out of this warehouse." With 124 stores, you can see that's only a couple of thousand pounds per store on the average week.
>
> We wound up and thanked him, and we agreed that we'd both sell him on a fill in basis if he ran short. We still quote them every week and they still use us as a fill-in. We just couldn't handle the kind of quantities that the mass merchandisers were selling. Some of these individual stores will do as much business as the whole packing house. Weekly sales on some of these big store units is bigger than our total output.

Selling to supermarket chains is left to the national packers who have the capacity to supply their needs. The sales manager stated:

> One thing works in our favor. Oscar Meyer will be in the chain warehouses but he's not going to spend a lot of time beating the bushes out in these small stores. He may sell to the co-op but really, competitive wise, the small packers compete against each other.

While the company does sell to the grocery chains most of their business is with the independent grocer. Independents are also exploiting the advantages of bulk buying and the use of warehouses through cooperatives. The president explained the advantages of warehousing:

> Another problem you've got to face is that because of the high cost of the so-called back rooms of the supermarkets, they want you to deliver to the warehouse enough for fifty or a hundred stores and they

> will assemble it into loads with canned goods and everything else and send it down to the individual store. He'll back up there at eight-thirty in the morning and unload that truck and it will be on the way in an hour's time and in that way will serve several stores with one truck. Now they don't have to have somebody back in the back room when PMC comes by and he gets a hundred pounds of this and another one comes by with that and to get thirty thousand pounds of merchandise may take ten or twelve hours. The warehouse system allows them to work so much more efficiently.

The warehousing concept has hurt the business according to the sales manager:

> Our customers are predominantly independent grocers. We have some chains. I imagine chains in the true sense of the word make up probably 5%. That may be a little high. Of course there are a great many independents who are members of these grocery co-ops which unfortunately a lot of them have gone to meat warehouses. But because of the independent being as independent as they are, we still get some business from these big independents but not as much as we used to.

The brothers admit that their future is tied to the independent grocer's future but feel that they can maintain business by adjusting their product line. They believe there is a trade-off between volume and profit and that relatively lower volume is more profitable for them:

> It's a philosophy of business whether you push the volume concept and try to do big volume or whether you push the quality and lesser volume. Generally your margins may be a little bit better than a high volume dealer.

Even without the direct competition of the large packers, the industry is highly competitive:

> You don't stay in business twenty years or thirty years and see the same customers week after week after week. If they don't like what you brought them last week they won't take some more. We counted here in town and there were twenty-four different meat packers calling on merchants here. If you get just a small percentage of it, it's more than your share.

While the demand for meat has remained fairly stable over the history of PMC, the access to the market has been curtailed and is likely to continue to become increasingly difficult. The independent packer who cannot produce enough to supply the order of the large chains has the alternative of selling to meat warehouses which in turn sell to the chains in the quantities they desire. The difficulty with this is that it adds another middleman and squeezes the already tight profit margins of the small packer.

Another alternative is to produce private label goods. The president explained why PMC rejected this alternative:

> Some of our friends have gone to private label where they set up their operation pretty much on manufacturing and put it out on some chain's label and then the chain decided they wanted to do something else. Suddenly they have a plant and equipment to do 200,000 pounds a week and the business is gone in three months' time and they don't have time to develop any substitute. I've seen them fold. We don't have any customer that buys as much as 10%. We have intentionally diversified.

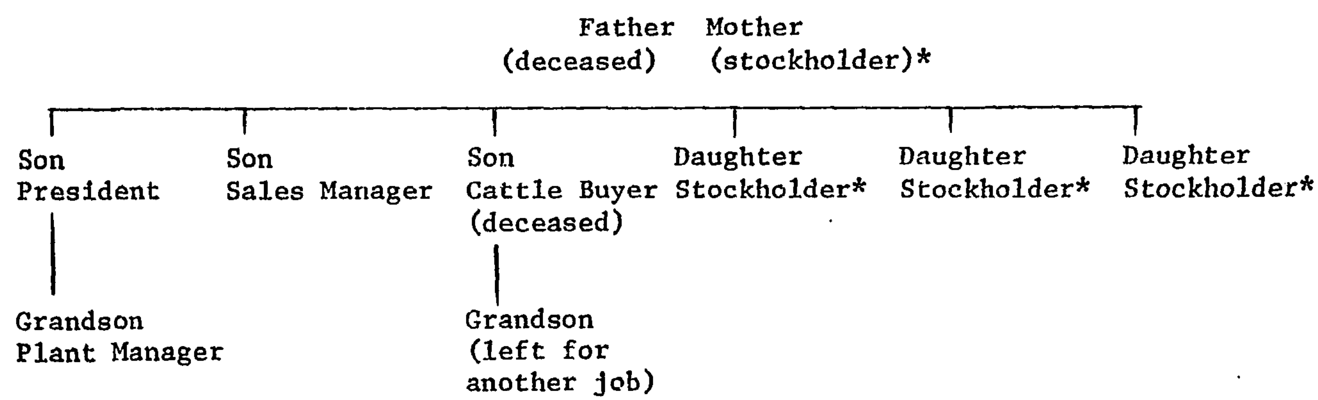
The spread of chain supermarkets to all but the most isolated locations has reduced the market for the independent meat packers product, and the extension of federal meat inspection regulations to cover locally produced and marketed meat has forced the company to reexamine its business definition. The potential profits from the continued production of fresh meat did not justify the investments required so the company stopped slaughtering operations and specialized in processing and distribution. The changing competitive environment has forced the company to segment its market and to specialize its operations. These strategic adjustments have been made within a family-business relationship that was carefully planned and is periodically adjusted.

Family-Business Relationship

Figure 3-1 depicts the association of the founder and his children with the business. The founder himself died four years after the business was established. His three sons provided the management for the business while his wife and three daughters were stockholders. The president described this aspect of the association:

> Prior to the time that we left the other location, one brother left school temporarily and came into the dressed beef business there and the other brother had not quite finished school at the time, but still when we set up the organization, we set it up as the three brothers. My father and the three girls were involved initially by common stock. At a later date, after an examination of the tax laws, we made an exchange with the three sisters and with Mother and substituted debenture bonds, a fixed obligation, as opposed to common stock. The theory being that if the boys put their time and their talent into it, they would first have to pay the fixed obligation to the girls. We set the rate of return to them a little higher than savings programs or low risk investment programs would have

Figure 3-1: Family Managers and Stockholders, Piedmont Meat Company



* Stock is being purchased by the two brothers in management.

> shown. And the fact that they had priority meant that we would only draw, other than just a salary, after we had paid that obligation.
>
> It was a method of organizing the company so that it would accomplish what you wanted to do without suffering undue tax burdens. It also served a very useful business purpose by those individuals who invested their time and their talent and taking risk as opposed to the girls who were primarily teachers and other vocations and this was an investment. The return of their investment was to come ahead of anything the boys would get and so it seemed like a fair division of risk-taking.

The youngest sister said that she was satisfied with the arrangement: "This gave them some capital plus it gave us some income. I think it has served them pretty well."

The oldest son of the president is plant manager and it is generally accepted among family members that he will succeed his father and uncle in the business. One of the sales manager's sons who is still in college has expressed some interest in entering the business while a son of the third brother had recently left the business for other employment. The only other family member who has been involved with the business was the husband of the youngest daughter who worked as a night bookkeeper for eight years in addition to his regular job.

The brothers are in the process of buying out their mother's and sisters' interest in the business and have set up the corporate charter so that the survivors buy out any brother's interest should one die.

Family-Business Interaction

PMC was founded as a family business to provide employment for the sons in the family and income for the parents and daughters. Although the oldest brother was, for a time, the only family member involved with the business on a daily basis, his father's periodic presence and participation as well as the fact that the business was established with all three brothers and the father involved from the beginning required a consensus mode of decision-making from the beginning. Each brother developed a different area of expertise, and the older brother headed the organization, but decisions were made by consultation among the brothers. The process of reaching agreement was not always smooth according to a sister:

> Two of the boys are very compatible. The other one, I don't think he differed that much, but any time there are three, it's a little hard to get them all to agree.

While agreement among the brothers was not always a foregone conclusion, the mother and daughters always deferred to the brothers in business matters:

> Really, the three girls and Mother don't know enough about the business. As a matter of fact, sometimes when my brother would talk about what was going on, I really didn't understand. I'm not a business person. I have complete trust in them.
>
> I can't actually speak for my two sisters, but I know as far as Mother's concerned there is complete trust, and I can almost say that there has been on my sisters' part. We trust both of the boys. We know that they

have always done the best they could. I don't know if I knew any more I'd have any more questions. I'm sure it wouldn't change the way I feel.

The older brother has made an effort to keep his mother and sisters informed about the business according to his sister:

We talk together every once in a while. My oldest brother felt that he should report to us at least once a year on the status of the business and whether things were going bad or good. He used to do it around Christmas time, and when things were really bad he talked to us. They were really afraid of going under. I don't know how they managed. Now I haven't talked to him about the business in a long time.

The daughter offered to invest money in the business but was advised against it:

I did mention to my brother that I didn't have much, but if he wanted some of the money to go back into the business, that I would invest it that way. But he advised me to go into money market certificates and that's what I did so I have not actually put any money into the business. I would be willing to. I didn't expect what I've gotten out of it so far. My brother sees it as part of the inheritance from Daddy and I appreciate that but I've never put anything into it personally so I never expect to receive anything out of it.

The older brother views the business as a trust as well as an economic enterprise, according to his sister:

My daddy was the only boy in his family that survived. He had a brother that died. Daddy felt like he was the one that looked after the rest of the family and he had two spinster sisters and he felt like since they didn't get married he was responsible for them. I don't mean responsible; they taught school and they were independent financially to a certain extent but he just made sure everything was alright. He had a very strong family sense of

> duty and I think my brother really assumed the role when Daddy died of caretaker for the whole family.
>
> I felt like (and I told my brother) they had lost so much during the period of time that they had this recession. They had put in so many improvements on the plant. I said "I don't feel like it's fair for you all to lose so much of your money and for us to get exactly what was in there." My brother feels very strongly that he was made the guardian of Daddy's inheritance and that we will get whatever we're supposed to.

The management of PMC has had the challenge of dealing with a changing industry structure while maintaining the family constraint of providing income to their sisters and mother. Several adjustments have been required to accomplish this.

Adjustments in Constraints and Business Requirements

The initial arrangements for the structure of the relationship were planned to prevent the kinds of problems which the father had experienced with the death of his partner. While all the family members participated as stockholders, the stock would be bought back by the company at the death of any of the members except for the father whose stock was inherited by his wife. The brothers have had the complete cooperation of their sisters and mother in making changes to preserve business and this arrangement.

The role of the family women has been changed at least twice with the changing fortunes of the business. Originally, they were stockholders, but the stock was converted into debentures because of tax implications. When the business needed financing to make the necessary capital investment to comply with the meat inspection changes, the debentures were converted to stock to eliminate long term debt. The business was in no position to pay dividends, however, so in order to assure the continued income, the brothers made arrangements to buy the stock themselves over a 20-year period. The requirements of the business were met and the constraints of the family were also fulfilled.

The concerns the sisters have had from time to time about the liquidity of their inheritance have been alleviated by the practice of the brothers of advancing larger payments to the women in times of personal financial stress. This practice seems to have helped prevent changes in the expectations of the family members outside the business concerning the performance of the firm. Changes in family fortunes have been dealt with in a prescribed way so that they do not lead to a discrepancy between family constraints and business requirements.

Stage Characteristics: Stage II

The adjustments which the brother and sisters have made in their financial relationship have probably contributed to the survival of the business and have certainly contributed to the survival of the family-business relationship as it was originally structured. Founded in Stage II and remaining in Stage II, the relationship has experienced no transitions and none appear on the horizon at this time. The characteristics of the relationship are discussed in this section.

Organization and distribution of authority. While the organization is set up according to functional specialties, responsibilities overlap, and the brothers tended to share top decisions rather than delegate them upward to the president. Consensus was apparently more difficult to achieve among the three brothers than it is between the two.

Rewards. Because of the restriction of stock ownership to family members and the understanding that a family member will succeed the top managers, rewards are of necessity different for family and nonfamily members. Financial incentives are the only ones available to nonfamily members.

Information. The judgments of nonmanagerial family members about the business are based on their assessment of the brothers as men of integrity and responsibility rather than on what the performance of the business is or should be. This has occurred because their return from the business is not dependent on its performance. The older brother has attempted to relay information about the business but it has not been presented in a way that those not involved in the business could understand. Because of the separation of the performance of the business from the meeting of constraints, the information was somewhat irrelevant.

Path of Development

PMC is likely to remain in Stage II into the foreseeable future in view of the fact that the next generation of family management is in place. Since the stock of the sisters will not be inherited by their children because of the buy-back arrangements which were made, the number of family members with ownership interest will decrease rather than increase. The brothers are interested in finding a way to distribute their assets equally among their children without hampering the actions of those of the family who succeed them in the business.

Table 3-1 summarizes the characteristics of the family-business relationship and Table 3-2 summarizes the adjustments in the relationship.

While Piedmont Meat Company has operated on the edge of survival for the last decade, Specialty Sauce Company has enjoyed a much different situation. Both companies are in Stage II of the family-business relationship and neither shows any signs of making the transition to another stage. Piedmont Meat is an example of adjustment from a position of weaknesses while Specialty Sauce exhibits the same process from a position of strength.

Table 3-1: Family-Business Relationship at Piedmont Meat Company

	Management Characteristics by Stage			
	Organization/ Power	Decision Process	Rewards	Family Role
Stage I (Prefamily)	----------	----------	----------	----------
Stage II (Family)	Hierarchical, functional structure	Emphasis on con- sensus	Differentiates between family and nonfamily	Central in providing resources
Stage III (Adaptive Family)	----------	----------	----------	----------
Stage IV (Postfamily)	----------	----------	----------	----------

Table 3-2: Process of Change at Piedmont Meat Company

Impetus for change	Actual Change	Consequences
Discrepancy between need for capital in business and desire to insure income to nonmanagement family	Adjustment of equity	Increased risk for family managers

Specialty Sauce Company

Specialty Sauce Company (SSC) was founded in the aftermath of the Civil War to salvage the economic fortunes of a Southern family by making, bottling, and selling seasoning sauce made from a spice grown on the family property. Within four years of the first commercial production of the sauce, an overseas sales office was opened and sales have grown steadily both in the United States and internationally. The company now employs 150 in their domestic operations and have recently increased their production capacity with their first new plant since 1905. The production line has varied over the years but the only product which has been in continuous production is the sauce and it has been the primary source of revenue and focus of activity.

History

Early History of the Company

The founder of SSC married into a family of land owners whose prosperity had been built on agriculture and the mining of a mineral deposit on their land. The family had been forced to abandon their holdings during the last days of the Civil War, and the combination of neglect and military activity in the area had destroyed both the crops and the mine. One of the few surviving crops was spice plants growing in the kitchen garden, and these plants provided the principle ingredient for a sauce which the founder perfected after some experimentation.

Using the spice from the plants in the kitchen gardens, two readily available ingredients and an aging process, the founder produced a sauce which was distinctive in flavor. In the first year of commercial production of the sauce, 350 bottles were distributed to wholesalers as samples. Orders came in the thousands for the next year and in the following year (1807) a patent for the product was secured. An office was opened in London in 1872 to handle overseas sales which were also growing.

In 1890, the founder died and was succeeded by his son. Not only had the successful venture into manufacturing restored the family's fortunes but the mines were reopened on a lease basis. The family now had two independent sources of income.

1890-1964: Protecting the Trademark

One of the son's first actions as president of the company was to make a tour of important customers to discuss the business and its future. He solicited the customers' opinions about what the goals of the company should be, how it should be managed, and what the competitive situation was. The consensus that emerged from these consultations was that the business needed to pay more attention to its markets and selling techniques. Exactly what was done to implement this new strategic emphasis is not recorded, but by the time the son stepped down from the presidency he had built sales to an annual level of $100,000.

He had also incorporated the business with himself and his brothers and sisters as the major stockholders. All but one of the four brothers worked in the business. The two sisters were involved only as stockholders. The other event of significance during his tenure was the opening of a new plant in 1905 which had housed the company's first bottling machine.

The son stepped down from the presidency of the family company to enter government service. While his duties in Washington kept him well-occupied, it seems likely that he kept an eye on the business during trips home and was available to advise his brothers.

The second brother became president of the company and held the position for forty years. The third brother was in charge of production during those years. As the company continued to increase the amount of sales and the scope of its markets, imitators began to appear and a series of legal battles occupied the company. These battles spanned almost the complete term of office of the third family president.

The imitators fell into two general categories. One group used the trade name of the company as the generic name of the product. The other group used the colors and shape of the company's label and the name of their own product. In both cases the customer was led to believe that they were buying the company's product if they did not read closely. Imitators were dealt with individually in a series of trademark fights from 1918 to 1928. In 1931, the name of the sauce, the bottle, carton, and label were all registered as trademarks and in 1946, the company was granted its trade-name as its forever "uncontestable" property by the authorities.

The president's time was not always occupied with company business and he is typical of previous and following family executives in his pursuit of outside interests. He was a naturalist as well as businessman and created a bird sanctuary on the family land. He also wrote several books about birds and collected trophies on hunts around the world. His successor, his nephew, served in World War II and was active in the Marine Reserves, rising to the rank of colonel. Also an avid sportsman, he was a breeder of champion hunting dogs.

1946-present: Recent Activities

The grandson of the founder became president of the company in 1949. He had worked in the company under his uncle before World War II. Under his leadership, the company has increased sales approximately 10-15% annually. Most of the growth is in foreign sales which currently accounts for about 40% of total sales. Changes in the labor supply have increased the proportion of the spice which is grown by foreign contractors while legal advisors have pressed for additions to the product line. The sauce market has caught the attention of larger companies and the company is beginning to experience the kind of competition which lawyers cannot prevent.

Operations and Management Systems

Agricultural Activities

A family executive described the shift in growing regions which the company has made:

> In the last ten years there has been a shift in agricultural operations to South and Central America. Planting and harvesting the spice not only requires hand labor but what is called "stoop labor." This kind of labor is no longer available in America. We have worked off and on on developing a mechanical picker and have produced a prototype, but it hasn't been satisfactory. And then of course the climate is very suitable in those countries so we moved agricultural operations to where labor was more readily available. Production is now at an all time high and most of it has been shifted overseas.

Another executive explained the agricultural operations further:

> There are really two phases to our operations. The growing of the spices is the first phase and the production of the sauce is the second. We have worked to improve the plants but they are basically the same as the founder put into the original sauce. We don't use any other variety although our competitors mix varieties. We still grow plants here but we rely on our suppliers in Central and South America for most of our supply. We find every year that it's harder and harder to get workers for the fields and always they get older. We can't get young people to do stoop labor so gradually our labor market supply is disappearing as the people who have worked in the fields for years are getting too old and there's no one to replace them.

Overseas growing sites are chosen according to several criteria:

> We have developed contacts in these areas over the years as we have been producing on a limited basis

> and bottling in some of these countries for a long time. We look at the availability of labor, the climate, and the political stability of the area. We have an agricultural specialist who spends much of his time out of the country working with our growers. We have been able to maintain the quality as well as the supply.

Both executives felt that availability of stoop labor in overseas growing regions would continue for the foreseeable future.

Product Line: Search for New Products

The original sauce bottled by the founder has been the mainstay of the company throughout its history. Other products have appeared from time to time according to an executive:

> Many products have been tried and eventually dropped over the years. We got into canning for awhile but that didn't work out. The only product which has been in continuous production since the beginning is the sauce. A few years ago, the patent attorneys got worried about the trade-mark becoming the generic name for the product. They suggested that we introduce some new products with the trade name to protect it. The original plan was to introduce a new product every two years but so far only one has been introduced.

The lag in new product development was attributed to the fact that the president was not fully committed to the plan and to the difficulty of developing products that complied with the family's quality standards and could be competitively priced at the same time. The executive explained:

> The most recent product that we considered was a bar-be-que sauce. I really liked that idea, and we came up with a tasty product. The problem was that the family insisted in only the best ingredients with no preservatives and this would mean the price for the consumer would be considerably higher than the competition. Of course, this is true of our other two products too. If you look at the ingredients on the label you can see that where other people list water first; ours isn't watered down at all. In that sense people don't pay more at all. They can take our product; dilute it with their own water and have the same thing at about the same cost. Anyway, to introduce the barbecue sauce to the public at the price that would be needed, would require a tremendous amount of promotion and we just couldn't justify it. New products will always be considered from time to time but I don't expect that there will be many additions to the product line. Additions are likely to be few and far between.

Operations

While the last decade has witnessed changes and potential changes in the company's operations, much of the way the business operates has remained the same. The manufacturing of the sauce is carried out from the same recipe and with the same basic process as the original. While some mechanization has occured in bottling, labeling, packing, and materials handling, the process itself is essentially unchanged. The spices are combined with two other ingredients and aged for three years. This mixture is bottled and the waste is sold to another company for further processing into an ingredient for several medicinal and food uses.

After using the same plant facilities since 1905, the company built a new plant near the old site. The new facility was in operation by Spring of 1980. There had been some debate as to whether to add capacity to the existing structure or to construct a new building. According to the family executive:

> The primary consideration was the ability to expand in the future. If we remodeled the old building now, we would definitely have to build the next time extra space was needed. The new building is adequate for expansion into the foreseeable future.

The company borrowed money for the first time in its history to make the plant addition. The interest charges reduced return on sales slightly, but dividends have not been affected.

Distribution of the product is handled through brokers and through direct sales to large national chains. The company provides special sizes and labels for large institutional customers. International sales are handled in several ways. Some of the product is exported directly. The manager in charge of exports reported an extreme example:

> A hotel in New Delhi, India uses about three cases a year. The shipping charge on that would be the same as for a ton so we mail it to them. We lose money, of course; the postage is more than the price of the three cases but the president says "Let them have it; it's only three cases."

In some of the countries where the product is sold, law requires that the company must be wholly or partially native-owned and operated. The company sells raw materials to these companies and provides the formula. In other countries, the company owns stock in a bottling company or franchises the bottling of the product. In at least one country, the company owns the local company through a holding company. Consistency under these varied arrangements is not a problem according to the export manager:

> Since the company controls production of basic ingredients and formula for the product, there are no serious quality control and coordination problems. The company has been in international markets since the beginning and has a loyal following. International sales are the source of most of our growth in recent years.

The product is sold in over 100 countries outside the United States.

Organization

The officers of the company, the President, Vice-President, and Secretary-Treasurer supervise the functional managers but the division of duties has evolved over a fairly long period of time and titles are rarely indicative of the duties of the individual holding the title. As Chief Executive Officer, the President oversees the whole operation but has been particularly involved in sales. The Vice-President has been most active in the agricultural side of the business while the Treasurer listed his areas of responsibility as

> Purchasing raw materials, sales management, marketing, and productions. Before becoming Treasurer, I was Institutional Sales Manager and Purchasing Agent and I carried over those duties into the new position.

A manager whose title was Office Manager but whose duties were handling of warehousing, shipping, and exports commented on the discrepancy between the title and the duties:

> There were times when nobody was here to make a decision. Someone needed to know what to do about something and I'd say "OK, I'll make a decision." The job expanded. Some people might worry about the title, but I don't.

<u>Strategy</u>

The firm is facing a domestic market in which demand increases about 10% annually, and in which competition from larger firms with more resources for head-to-head competition is likely to increase. The continuing growth of foreign sales has allowed the overall growth of the company's sales to continue and the strong weight given to ability to expand in the future in planning the new manufacturing facility is a measure of the optimism of management that this trend will continue.

Management has depended on legal moves to protect the trade-mark and label of its product and depended on an established base of customers to choose that trade-mark on the grocer's shelf. While the price of the product was recently increased for the first time since 1928 it is still considerably higher than the competition. Marketing surveys indicate that this is an item which is purchased about twice a year so management feels that price is not the deciding factor.

The company is not investing significant amounts into new product development but is making most of its investments into improving the agricultural side of the business. The most likely successor to the President who is nearing retirement is the Vice-President and his background in the agricultural side of the business makes the continuation of this emphasis likely.

Competitive Challenges

While many companies produce a product similar to the company's main sauce product, the identification of the brand name with the generic item in the minds of many consumers has given the company a competitive advantage which it has sought to protect by legal action through the years. Historically, the company has been the favorite in such battles by virtue of its size and market share in comparison to its imitators. This situation seems to be changing according to one executive:

> Of course we don't make public our market share or our ROI but there are ways that people with access to the right kinds of data can easily figure out that our market share is high and so is our profit. There are some indications that some companies are getting interested in some of that market.

The most direct indication was the promotion push given to a newly acquired sauce company by a large national food group:

> Very aggressive marketing was used by a food group to push the product. They mounted a large advertising campaign and literally gave the product away with price cuts. They hurt us in the two market areas where they did it. They became number one in those areas.

The company's response has been to wait and see:

> We don't think they can keep this up and make a profit so we're not doing anything other than watching the situation. We feel that when the price returns to normal people will return to our product. The competition is hoping just the opposite and it's too soon to tell who is right.

The other indication of interest in taking away some of the company's market share and profits is the interest that a large national firm has shown in purchasing the sauce manufacturing operation of a competitor. While the competitor makes other products, the national firm has been very specific about its interests:

> The acquiring firm has stated that they are interested only in the part of the business which makes sauce, not the other segment. The competitor has so far resisted efforts to split the sale.

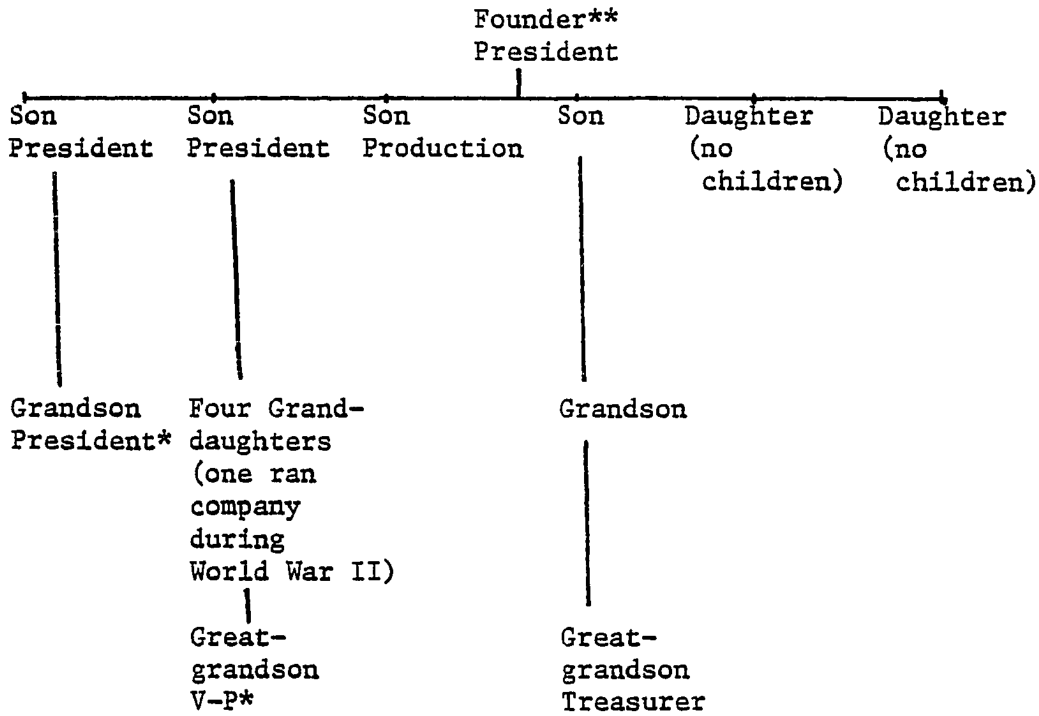
Family-Business Relationship

Only descendents of the founder can inherit stock in the firm and be officers of the firm. There are currently 106 family stockholders and four family members employed in the business. In addition to the three officers, the Assistant Secretary-Treasurer is a member of the family. Figure 3-2 shows the family members who have been involved in management since the founding of the company.

Family-Business Interaction

The President and one other stockholder have a 15% ownership share each while no other stockholder owns more

Figure 3-2: Family Relationships in Management, Specialty Sauce Company



* Current management

** All stockholders are descendants of founder but are not listed here.

than 5% of the stock. Dividends have increased every year with increased earnings although the payout ratio has not changed significantly.

The site of the business headquarters is also the family "home place" and several family members maintain vacation homes there while family members who have remained there have large residences so that the whole family is able to gather for holidays. The practice of gathering for reunions and celebrations has kept the family closer together than the size might indicate and the family has maintained an active interest in the business. This interest was the impetus for creating special positions on the Board of Directors:

> In addition to regular directors there are associate director positions which are rotated among family branches which are not represented on the Board or by the officers of the company. These associate directors are paid a director's fee, are furnished with all information they request and are expected to come to meetings prepared to participate. They don't vote but they do debate issues and ask questions and provide information to other family members.
>
> The president started this because he would go to family dinners and be covered with questions. This way the branches of the family that aren't in the company get directly involved anyway.

A company brochure states that "family control is complete" and this seems to be an accurate statement. There is no question but that members of the family will hold the top posts in the business. As one family member states, "Family managers are always being groomed for succession."

The same family member pointed to the fact that none of the family members in the business were immediate relatives:

> We are very objective about family members in the business because there are no father and son relationships. We are dispersed enough to be objective about each other.

Positions are not created for family members, but when family members apply for openings they are likely to be given preference. The performance of family members is monitored and at least one has parted ways with the company "because he was not productive."

The association of the family with the business has been institutionalized through requirements that officers of the company be family members and the creation of special Board positions to be filled by family members. The frequency of contact between family members and their continued interest in the business over several generations both necessitated the institutionalization and made it possible. Another factor which promotes interest in this business is the fact that it is part of a larger family empire which is centered at the same location. In the early years of the twentieth century, a series of oil discoveries on family property resulted in a dramatic increase in family wealth. The sauce business is part of a mineral and petroleum complex. Interest in the pursuit of larger interests probably carries over into interest in the sauce business, while the existence of the larger interests eliminates stockholder dependence on the sauce business. As a nonfamily manager commented:

> Let's face it. These people are all independently wealthy. They have oil leases that dwarf the income from this company. If things were different, if the company were losing money or they were really dependent on things here, there might be more problems.

The interaction of business pressures and family constraints has consistently been accommodated within the Family stage of the family-business relationship.

Adjustments in Constraints and Business Requirements

When there is a discrepancy between the requirements of the business and the constraints of the family, the adjustment is made in the business rather than in family constraints. Recently an opportunity arose to acquire a facility in a location which would reduce shipping costs. The family opposed the acquisition because it would mean domestic processing would no longer be limited to the traditional location. The family preferences concerning the location of domestic processing prevailed and the opportunity was dropped.

Another instance in which family preferences prevail concerns the search for new products to add to the product line. Patent lawyers have pressured management to add to the product line as a continuing justification that the trade-name is, in fact, a trade-name rather than the name of a specific product. Lack of family interest in new product development combined with very high quality standards for potential product has resulted in a rate of product introduction far below what the patent attorneys had suggested.

The most recent challenge to the company lies in the shift in the structure of the industry toward larger, national firms with considerable marketing expertise and resources. It is too early to judge the implications of this trend but it could create a discrepancy between the resource needs of the business in both the managerial and financial areas and the ability of the family to supply these needs. If the family is not willing to alter its resource inputs, structural change would be necessary.

Stage Characteristics

When the founder brought his family back home after the Civil War he was responsible for rebuilding the family fortunes and was head of both the family and business. The need for sending children away to obtain higher education worked against continuous involvement with the business by his sons. When the founder died in 1890, he was succeeded by his oldest son who apparently had little knowledge about the business. He immediately began a tour of his father's best customers to solicit their recommendations, the goals of the business, appropriate management techniques, and competition.

His two brothers joined him in the family business by 1895 and the company was reorganized in that year with all the children of the founder as stockholders. While the exact time of the transition from prefamily to family business cannot be ascertained, the transition had occured by 1895 at the latest. SSC has been in the family stage for 85 years at least. The transition prceded the birth of all family members now living.

Stage II: Family. The characteristics of Stage I to the extent that they are known and Stage II at Specialty Sauce are summarized in Table 3-3. Stage II characteristics will be the focus of this discussion since there is no source of direct knowledge about Stage I and since the preponderance of the relationship's history and apparently its future is in this stage. The relationship in this business has been marked by a deference to family opinion and a clear division between family and nonfamily managers in distributing rewards. In addition, the information requirements of the family have been of concern to top management. The family has played a central role in providing both managerial resources and family resources.

•Organization and distribution of power. The importance of obtaining consensus among family members for major decisions is underscored by a manager's comment that decisions in the company are based on "What's good for the company and what will keep peace in the family." The participation of nonmanagerial family members on the board of directors is another indication of the dispersion of power

Table 3-3: Family-Business Relationship at Specialty Sauce Company

	Management Characteristics by Stage			
	Organization/ Power	Decision Process	Rewards	Family Role
Stage I (Prefamily)	Direct supervision	Founder made unilaterally	?	Land holdings were first necessary resource
Stage II (Family)	Hierarchy, Functional structure	Consensus	Differentiates between family and non-family	Central source of resources
Stage III (Adaptive Family)	------------------------------------			
Stage IV (Postfamily)	------------------------------------			

in the family. Although these members cannot vote, they are encouraged to participate in discussions and expected to ask questions and express opinions. Not only do family members in management share power but the dispersion of influence is institutionalized in the Board positions.

• Reward and incentive system. Top management posts are reserved for family members and all family managers get offices on the second floor of the company headquarters. There is a differential system of rewards and prerequisites because only family has unrestricted advancement in the business. The nonfamily managers' rewards are primarily monetary. One manager commented on the differences:

> I'm not an officer of the company but I make as much money as some do. It all depends on how you keep score.

Seniority is a key factor in determining bonuses for non-managerial personnel.

• Information. There is frequent communication among family members and the business is sometimes a topic of conversation. The family Board positions were created as a means of conveying information to family members so that family dinners did not turn into inquisitions for the president. In addition to information provided by the company, the Board members have access to all managers who are instructed to provide whatever information the Board members may request.

• Role of the family. The family is the source of managerial and financial resources for the growth of the company. The family is presently in a position to supply both into the foreseeable future. While the sauce business is no longer the main source of income for the family nor the cornerstone of its financial activities, it is the enterprise most closely associated with the family name and traditions.

The stability of the family-business relationship at SSC has been challenged as discrepancies have arisen between business requirements and family constraints but these have always been adjusted and the relationship itself has not changed since the Nineteenth Century (see Table 3-4).

Path of Development

The family-business relationship has changed very little in the last 80 years. More individuals are involved in the relationship but the efforts of management and the continued interest of family members have prevented the rise of indifference or disassociation from the business. There seems to be a concerted effort on both sides of the relationship to maintain it as it is and has been. This effort has been furthered by the ability of the business to fend off competition by other than head-to-head encounters. The business has had room to adjust to family constraints rather than being in situations where business adjustments were virtually impossible.

Table 3-4: Process of Change at Specialty Sauce Company

Impetus for Change	Actual Change	Consequences
Concentration in industry has increased rivalry in certain markets	Wait and see.	Cannot be determined at present.
Need to develop new products to protect trademark	None; family quality standards increase cost of new products prohibitively.	Cannot be determined at present.
Increased shipping costs makes relocation of some facilities closer to markets attractive	None; family prefers to concentrate production in traditional location	Cannot be determined at present.

The future path of development of the relationship will, for these reasons, depend on the changing industry structure and competitive environment which the company will face. A relatively stable environment will favor the relationship as it is, but significant disturbances could require changes in the family-business relationship at SSC.

Both Piedmont Meat Company and Specialty Sauce Company have family-business relationships built on the adjustment of business requirements and/or family constraints as changes in the business, the family, or the competitive environment require. While SSC began operation as an entrepreneurial firm and PMC was founded as a family business, both are primarily notable as examples of Stage II (Family) of the family-business relationship and of the adjustments that are made to maintain the relationship in that stage.

The remaining two cases exhibit an evolutionary path of development and illustrate the process of transition which occurs as relationships undergo structural changes. These cases also provide insight into the characteristics of Stages I, II, and III.

At Valley Food Company, the next case, the family-business relationship is in the center of a transition from Stage II (Family) to either Stage III (Adaptive Family) or to Stage IV (Postfamily). Discrepancies between family constraints and business requirements put pressures on the relationship which could not be alleviated within the existing relationship.

Valley Food Company

For 81 years, Valley Food Company (VFC) has operated as a closely-held business with the family of the founder filling most of the top management positions. From its beginnings on the family farm, it has grown to a company employing over 600 during peak canning seasons. The product line has expanded from the original bottled seasoning sauce to a full line of pickled peppers, 20 varieties of beans, peas, okra, and sweet potatoes. These products are marketed in the Southern United States, the East and West Coasts, and overseas.

History

The founder of the business was a blacksmith by trade, but he operated a farm on which, among other crops, he grew special peppers. These peppers were a special breed from Mexico and had been used to make seasoning sauce since the end of the Civil War. The most famous maker of the sauce had already developed national and international markets for the product, but the founder mainly produced sauce for the local market. Making and selling the sauce provided work and income when the peak farm work seasons were over.

Soon he began to expand his product line:

> As a result of that product, he found that every year when picking the red peppers to make the sauce at the end of the crop when it was time for the frost to come, he had all of these green peppers that never would turn to the ripeness of the red. So he started to think about all of these good peppers that went to waste and were not being used.

> He developed a way of curing these peppers in salt and brine very similar to the way you cure cucumbers and then after curing them in that, he put them in vinegar and bottled and sold them as pickled green hot peppers.

The relationship between the seasonal work on the farm and the expansion of the product line was close in the early years. A descendant of the founder further explained:

> He stayed with just those two, the red hot sauce and the green peppers until around 1920 or 1922. But then he got involved with other types of peppers. If he could pickle one kind, he could pickle other types.
>
> On the farm, they also raised sugar cane and he had a syrup mill. That was a two or three month out of the year project. He would try to find some activity for when the syrup mill was not in operation.
>
> He got involved with an attempt at the packing of sweet potatoes which had been attempted before but was never successful. I guess you could say that this was as much a marketing innovation as it was a canning innovation. They had been canned but nobody had been successful at marketing.

The products were sold through wholesale distributors and by route salesmen who worked the independent retailers. Most sales were local, but the founder was developing markets as far away as New York.

By 1929, 8 of his 11 children were employed in the business, and the founder was ready to assume a lesser role in the business. The company was incorporated for the first time, and stock was distributed to the children of the founder. The company also split its processing facilities between two adjacent towns. The bottling facility and the canning facility have operated at separate sites since then.

The Depression years were difficult ones for the family and the business. Some of the family members took outside jobs to reduce their dependency on the company. One family member refered to this as a time of "sacrifice" when family members went to great lengths to keep the business going.

In spite of problems, several new products were added during these years to increase facilities utilization. This was especially important with the need to spread the higher fixed costs of the new facilities over more units. A grandson explained:

> It was in the late 1930s, about 1938 to 1940, that we first canned peas which was again a way of trying to fully utilize the facilities. They canned okra but at the most okra is available two and a half months out of the year and at that time syrup was starting to die out so to speak. They were looking for something else to utilize the plant and started to can one or two bean items like red beans in chile gravy or just plain red beans and stayed with just those two bean items until about 1955.

The company has continued to expand its product lines to increase facilities utilization and has expanded its geographic scope. Its strongest markets are in the region in which the plants are located but it has also established a market position in large metropolitan areas on both coasts. International sales are growing but presently account for only 5% of total sales.

The president described the competitive philosophy of the company:

> We feel that we have in anything that we offer the top quality product in that category. We are the best available in that category of competition. Our primary goal is first of all maintaining the quality standards and try to be competitive in price. And in combination with that advertise.

Operations and Management Systems

Peppers and vegetables are purchased from contract growers and processed in seasonal packs. While both facilities operate year round, the summer growing season is the height of production activity. Production is somewhat mechanized but several packing innovations which would have cut costs have been rejected because quality could not be maintained. The company has no special cost advantages and has not been able to develop more cost efficient production methods.

Costs have become an important issue as the required spending to comply with government anti-pollution regulations and the pressures of inflation on inventory and depreciation have led to shortages of working capital as well as lowered profit margins. Earnings available for dividend payout as well as the percentage of payout have been reduced.

During most of the history of the company decisions were made in what was described by the president in a committee style:

> It was more of a committee. That was when more of the older generation was still in the company. You could get people together to make a decision without job responsibilities that people had to follow.

This method was not free from conflict according to a family member:

> I've heard how they argued in those days. Everyone said what they thought but when they came out of that room and the decision was made it was as if nothing had ever happened. They argued about business but it was nothing personal.

As the older generation retired, efforts were made to "professionalize" management. A new top management structure was established with three executives reporting to the president (see Figure 3-3, page 113). Several years later a consultant was brought in to see that job descriptions matched actual responsibilities and to reduce the family perquisites. The secretary-treasurer assessed the results as follows:

> The consultant made some changes and they were changes for the better but he didn't go far enough. The changes weren't applied equally across the board and some family members continued as before. Family is still family.

An attempt to institute an incentive compensation system was a failure according to the president:

> The bonus system was discontinued about five years ago. The system began as an executive incentive. With time, there was a tendency to bring in other people because of length of service rather than position. As a result, we thought it best to abandon it because the trend was neutralizing the original executive incentive interest.

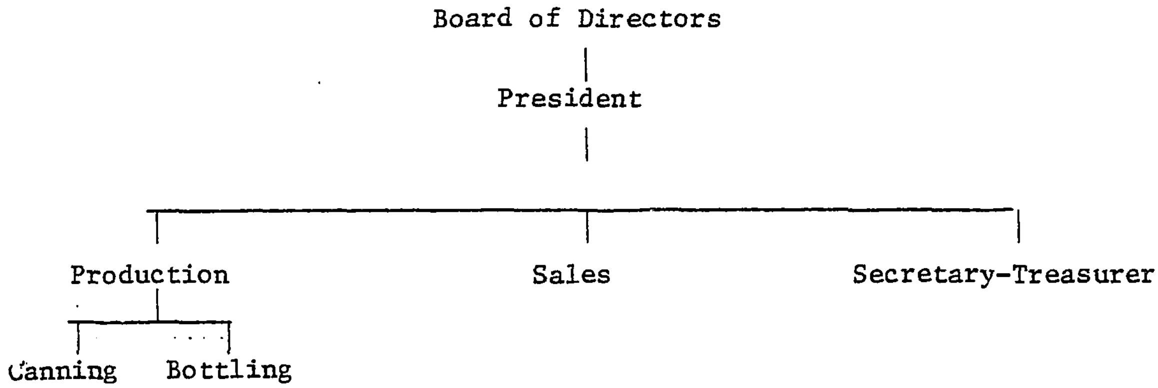


Figure 3-3. Organization Structure, Valley Food Company

Management control of operations also presented difficulties:

> We had a problem with our computer and were six months behind with our information. We finally caught up but when you're running that far behind, comparisons don't mean much.

Long range planning had been indefinitely postponed:

> We had not yet gotten into the long range planning. We were having so many problems with the immediate planning. When we got those solved we were going to tackle the long range. We never got around to it.

Some of the president's time was spent seeking a solution to the growing family problems which he attributed to the more distant relationships which characterized the third generation:

> It was just like a family, but it's not like that at all now. I've always thought that in a family organization there has to be a lot of give and take. Everybody has to give and everybody has to take and it's not a matter of always someone giving and someone taking. But as we go on down in the family lines, we have another generation that's

> never worked together. The family just got bigger and bigger and they are mainly second and third cousins instead of brothers and they've lost the feeling of being a family unit. Of course they've established other family units and you have close ties there, but it's not the same when you have five families instead of one.

The president's dilemma was that family members needed more return on their invested capital than the company could provide. At the same time there was no means to liquidate their assets without losing family control of the business. An observer reported on the activities of one stockholder:

> One of the brothers married a girl who worked in the office. She was some younger than he was and they never had any children. Apparently they never put back much either because when he died she didn't have anything to support her. All she had was her stock in the company which didn't pay the dividends she wanted and which had no market value. What did she do? She got a lawyer and got an offer to buy the company. As it turned out they only wanted the bottling facility not the cannery and they were told it was a package--all or nothing. She wasn't satisfied of course and is still pursuing something along those lines.

Family pressure culminated in a coup in which the president was removed and replaced by his 85-year-old uncle while a consultant was hired and a permanent replacement sought.

Competitive Challenges

VFC competes in selected segments of the canned vegetable, pickled pepper, and hot sauce markets and has generally avoided head-to-head competition with larger firms. Many of the vegetable products are packed in gravy, sauce, or with other vegetables so that the product is unique as packed. The company relies on this differentiation to distinguish its product in the mind of the consumer and reduce its substitutability. In practice the company faces competition from many similar products.

The company bottles several kinds of hot sauces. The president described that market:

> That's a very, very competitive area, but again, you're getting into different classes of hot sauce. We have every class of hot sauce so I guess you could say every hot sauce manufacturer is a competitor but maybe they compete with only one of our products.

In the area of pickled peppers, the competition for shelf space has increased due to additions in the product lines of the large cucumber packers:

> Peppers are getting more competitive than they have been because so many of the packers of pickled cucumbers are getting into certain varieties of pickled peppers. They are adding items into their pickle pack trying to squeeze other pickles off the shelf.

In sweet potatoes, the company is one of the top three packers and it also has the top position in okra. Okra, however, is declining in overall sales.

Additions and deletions are made in the product line on the basis of volume:

> We are always looking for new items that could be added. I think we had some items in the line that we're going to have to drop because the volume really didn't justify them. It was my opinion not to drop those items. Because you never could tell when one of them would catch on, particularly if

> they have good consumer acceptance and the only problem is to get buyer acceptance to put it on the shelf.

In the battle for supermarket shelf space, the company depends on chain buyers, wholesalers, and jobbers. Adversiting varies with the market:

> Generally when we advertise, we try to go into magazines such as _Woman's Day_ or _Southern Living_--sort of an umbrella advertising. This means it covers a large section of the country and gives supplemental coverage in the better markets where advertising money had been generated and will be spent. This type "umbrella coverage" will give some advertising even in poor markets where sales volume will not generate advertising money for a special advertising program.

Another weapon, the sales promotion, has not worked well in at least one metropolitan market:

> Atlanta, for example, is a tough market. We seem to be getting a foot hold on beans. We've been fighting the Atlanta market for five years. It's a real strong market for another company. We've gotten in on these real hot promotions--loss promotions--to get in, but you just can't keep that up month after month. You can buy your way in but when you get back to your normal price, you're out.

Family-Business Relationship

The founder of the firm had a large family. His 11 children produced close to 60 grandchildren and these grandchildren were the stockholders by 1980. Figure 3-4 shows family involvement in management.

Founder

President 1898-1929

ten sons

1. president 1929-1943
2. president 1943-1960

six other sons held
various positions

three grandsons worked
in the business

1. president 1960-1980
2. vice-president--production
3. food processing

two great-grandsons
in the business

1. production
2. sales

one daughter

Figure 3-4. Family Participation in Management, Valley Food Company

Family-Business Interaction

The founder's children worked on the farm as soon as they were old enough and also filled in as needed in the bottling and canning operation. As they grew up, they came to work full time. While some of the brothers were interested in the business from the beginning, several went to college and at least one had begun another career but was needed by his father:

> My father went to college and he taught for a year. Then the war came up and the boys went into the army. They went off and he left the teaching profession to help my grandfather and he stayed in for that time and then the boys came back and he stayed with the company. They grew up with it and they wanted to stay with it, but I'm not sure my father would have gone into it if it hadn't been for the war.

While the founder stepped down from the business when it was incorporated in 1929, he continued to participate in the informal decision-making process which his sons evolved to operate the business. Two of the sons served as president of the company in succession and then a grandson took over the presidency. Another grandson became vice-president of production and still another worked in the food service department. Two members of the fourth generation have entered the business; one is employed in sales and the other in production (see Figure 3-4).

All of the approximately 60 stockholders of the business are family members with the exception of two non-family officers of the company who have one share of stock each so that they may serve as officers under the requirements of the corporate charter. The Board of Directors includes these two managers and seven family members. No single family member is able to vote a majority of the stock.

According to an officer of the company, family members have two main concerns about the business. "They are interested in dividends and in selling their stock. Someone is always asking me if I'm interested in buying their stock." A fourth generation family member concurs:

> My cousins are vets and CPAs. My little brother is the only one who's really interested in what's happening with the business rather than just the dividends.

The president blamed this lack of interest on a natural process of breaking a nuclear family into smaller units:

> The family just got bigger and bigger and they are mainly second and third cousins instead of brothers and they've lost the feeling of being a family unit.

Because of the family's difficulties in working together, he predicts the end of family control or a dramatic change in the ownership configuration of the company:

> I don't think it's possible to run an organization where you have a lot of disharmonies and unsatisfied people. You either have to work together or split up.
>
> I think it's going to be a matter of either disposing of the company or one segment of the family

> buying out the other. If you have one or two segments that can still work together with the same harmony as the original family unit then I think it's possible to continue.

Over the summer of 1980, family discontent came to a head and several branches of the family combined to force a management reorganization. The president was removed from all of his offices except his board membership. The last surviving member of the second generation was placed in the presidency and a consultant was retained to "get the family out of the business."

Adjustment and Transitions in the Family-Business Relationship

The process by which adjustments and transitions have been made at VFC has not been as consistently disruptive as the current upheaval. The early years of the business seem to have been dominated by the founder although information is not available to determine precisely when the transition from a founder-dominated Prefamily relationship to a more cooperative Family relationship was made. By the beginning of World War I, the sons of the founder were in the business as full-time employees and were apparently necessary to operations because at least one other son was pressed into service in the family business when his brothers left for war. As the brothers returned and the business prospered in the Twenties, it seems likely that changes in both the business and the family prompted the incorporation of 1929. On the business side, growth had required capital spending for a new plant and equipment and a corporate legal structure would have been more suitable. On the family side, the need to plan for estate settlement and to distribute income would have argued for incorporation as well. While the business officially ceased to be a founder-dominated firm in 1929, the founder was credited with addition to the product line after that time.

Pressures for another transition in the relationship have been building. The processes of growth of the family and inheritance spread stock ownership among individuals who differed from the previous owners in two important ways. No longer were these stockholders managers in the business and no longer was the cooperation of all of them necessary to make a decision. Consensus of all stockholders was no longer hammered out in meetings; a majority was sufficient. The discontended could be left to "stew." The majority, however, was easily shifted so factionalism became more of a problem.

Another important difference between second and third generation stockholders in VFC was their view of the company. The third generation saw the company as an investment and not a particularly attractive one. Their constraints were wholly financial and with returns rising on risk-free investments in 1979 and 1980, they felt their assets should bring greater returns as well.

At the same time, business pressures were dictating that more earnings be retained by the business to fund debt which was acquired to comply with pollution regulations and for increasing working capital requirements. The president sought solutions for these problems in adjusting the family expectations:

> I have tried to explain that this business is not a high profit margin business but they think that we can do better.

He also explored adjusting the relationship:

> I thought about swapping stock for physical assets and leasing those assets from the family members but the tax consequences ruled that out.

Selling the company or going public was also considered but there was doubt about the market for the stock and bids on the company had not been high enough to suit stockholders or had been made on one part of the company rather than the whole operation.

The president's failure to find an appropriate solution became the impetus for the chain of events which began with the ouster of the president and will apparently end with the restructuring of the family-business relationship through a sale or merger. Table 3-5 (on page 123) summarizes the process of change.

Table 3-5: Process of Change at Valley Food Company

Impetus for Change	Actual Change	Consequences
increased family participation	transition to Stage II	end of centralized control
discrepancy between family financial constraints and performance of business	adjustment attempted and not achieved; transition likely	disorderly succession process

Stage Characteristics

Organization and distribution of power. Table 3-6 summarizes the characteristics of the family-business relationship at VFC. The primary contrast between Stage I (Prefamily) and Stage II (Family) lies in the relative concentration of power in the first stage and the diffusion of power in the second stage. The relations between the brothers in the Family Stage were described as "give and take," a "committee-type organization," and "cats and dogs." This suggests a division of power in which all must acquiesce to decisions. This contrasts with the descriptions of the founder: "he decided," "he added," "he was responsible for."

Reward system. In both stages a differential reward system provided family members with perquisites which the secretary-treasurer described as being slow to disappear in spite of consultant assistance. The differential reward system may have had a role in the difficulties with instituting an executive incentive compensation plan.

Table 3-6: Family-Business Relationship at Valley Food Company

	Management Characteristics by Stage			
	Organization/ Power	Decision Process	Rewards	Family Role
Stage I (Prefamily)	Hierarchical, Concentrated	Unilateral	Differential	Participation essential to survival
Stage II (Family)	Functional, Dispersed	Committee	Differential	Provide financial managerial resources
Stage III (Adaptive Family)	----------	----------	----------	----------
Stage IV (Postfamily)	----------	----------	----------	----------

Role of family. The role of the family in Stage I was critical to the survival of the business because the family connection was the source of manpower and management particularly during World War I. The family remained the chief source of both human and financial resources in Stage II (Family), but as explained previously, is expressing discontent with the role.

Path of Development

While the relationship between the family and business at VFC has followed an evolutionary path previously, the future may hold a change. While there is a possibility that the company can sell some stock publicly while maintaining family control, observers feel it is more likely that the business will either remain in Stage II or move to Stage IV. The first alternative would be possible if some of the family could buy out others; the second alternative would involve sale of all family interest in the firm.

The three preceding cases are typical of many small family businesses. Operations are straightforward and the scope of activity is fairly limited. The relationship is in Stage II and more adjustments than transitions have shaped it. The next case, Sunbelt Foods, Incorporated, deviates from this pattern in two respects. This business is considerably larger, and therefore operations are more complex and organization more systematically articulated. Also, this relationship has moved through two transitions within the memory of current management. The experience of Sunbelt Foods provides insight into the management of a growing family business, and it also allows detailed examination of the characteristics of three stages of the family-business relationship and two transitions between stages.

Sunbelt Foods, Incorporated

Sunbelt Foods, Inc. (SFI) manufactures and markets snack and convenience food items in the United States. Founded in 1919 in a small town in the southwest, the company operated for almost fifty years as a privately-held, regional bakery before going public in 1968. In that year the company's operations were limited to production and sale of snack items in three southwestern states with total sales of $36 million. By 1979 the company had two areas of business: the original snack food division and a convenience foods division. Corporate sales were over $350 million in 1979. While it was ranked as the 95th largest food specialty company in size by a national business magazine in the U.S., it was rated as the third in profitability in that classification. Snack foods are marketed regionally and convenience foods have a national market. The company has production and distribution facilities in eleven states and has over 8,000 employees.

History

Early Years: Internal Growth in the Bread Business

The original partnership from which the company came was formed by two brothers in a small town in the Southwest for the production of snack foods and ice cream. The town was located on a rail line in a primarily agricultural area near the state's borders with two other states. A son of the founder, the Vice Chairman and Chief Executive Officer, described the founding and early days of the company:

> During the early part of this century, my grandfather was engaged in the lumber business in northeast Texas. He decided to move his family here and he and his sons did a research of the business needs in this section of the country. They found that ice cream and snack foods were items that were not being manufactured in this area. In 1919, my father and his brother started a plant to make snack items and an ice cream plant.

During the 20's the founder and his brother decided to discontinue their partnership and as the story is told in the family:

> They ran the business together for several years. When they decided to split this, Daddy gave Uncle John his choice and he took the ice cream factory. Dad ended up with the snack foods plant.

Transportation began to improve during this decade and this improvement was accompanied by increased competition.

> With the advent of paved roads and better transportation all that changed. This gave access to more food processing plants into more communities in our area. The snack business has been through several

> cycles since we started the business. In the Twenties there was a tremendous growth in the number of snack businesses as roads improved and food technology improved. There was a little plant in just about every town in East Taxes and two in some.

The company was stable in these years and grew very slowly. In 1934 the era of the founder came to an end with his sudden death. The CEO described the situation:

> My dad died in 1934 in the middle of the Depression and my older brother had just graduated from college. He was just twenty years old and I was twelve. He had to take over an operation that was running six routes from our small plant here.

<u>1934-1968: Internal and External Growth</u>

An officer of the company described the man who inherited the company at 20 and is now Chairman of the Board:

> He's just one of those rare people that come along occasionally who is highly motivated and very dynamic--a very capable person. That extraordinary energy he has had to find an outlet somewhere . . . If you look at any one thing, you've got to look at his leadership as the thing to point to as significant.

The company was in those years a "one man operation" according to a member of the Board who has been long acquainted with the family. World War II provided an impetus to growth in two ways. The company got into the business of supplying nearby military installations and was able to acquire special equipment by virtue of its role as a military supplier. The CEO reported:

> When World War II came along, I was in college and joined the Navy right after Pearl Harbor. Since my brother was in an essential industry, they would not take him. Because we were serving a lot of Army camps throughout this area, he was able to get an order through Washington to acquire our first modern manufacturing equipment.

During the 40's and into the 50's the first wave of consolidation of snack businesses in the area began. With further improvements in transportation, it was possible to distribute baked goods over a wider area, and larger companies were able to gain production efficiencies when volume justified equipment improvements. The CEO described this process:

> It was during the Thirties and the early Forties that the large national chain operations came into being. This was done by acquiring smaller independents in various cities. During this period, the number of independents and total number of plants shrunk and was approximately 30 to 35% less than earlier.

SFI was participating in the consolidation trend on a small scale and the business was growing so that the founder's oldest son needed his younger brother's help. The circumstances were described by the younger brother as follows:

> After serving a hitch in the Navy during World War II as engineering officer for an air group, my wife and I returned to college and I received a Master's degree in business. Upon graduation, I went to work for a company in California. My wife was home with her folks because we were expecting a baby and she could not travel after a certain time. It was impossible to find a place to live in California.
>
> I was home when the baby was born and talked with my brother about the business. He told me there was a place in the family business if I wanted to come back to South Georgia and go to work. However, he felt

that I should make certain in my own mind that was what I wanted to do. That decision was made a short time after returning to California, and we have never regretted this choice.

When I came home, I went to work nailing up signs and advertising. Of course we weren't very large. I think we had twenty-five routes at that time. It was during that period that we bought a plant in North Texas. One of the men who had been in the business longer than I had went up to run that operation. We had three plants and were about a thirty-five route operation.

It was not too long after returning home that I was made district manager over several routes and then sales manager over the local plant and then director of sales over all the plants. In 1965, I was made President of the company.

Two decisions in the late 50's and early 60's were described by the CEO as being essential for later growth. One was the adoption of a new process and the other was the construction of a new and modern plant. In both cases, the investment required was substantial.

At that time, one of our competitors had a better product than we had and we could not compete. They were making a softer product with a much better texture than ours. We made the decision to buy this expensive new equipment and put it in two of our plants. This was a sizeable investment at that time. However, we got a tremendous increase that put us ahead of our competition.

The need for a new plant was recognized as the market continued to outgrow the capacity of purchased and renovated facilities.

Another turning point was when we decided to build a brand new plant in the north Texas town in 1964. We had to borrow money, and our debt to equity ratio was way out of kilter from the amount of money

> involved in building this plant. It's a beautiful plant and has developed into one of our most profitable plants.

By the early 60's the rudiments of SBI's snack food strategy was in place. The company was lengthening production runs by baking only one or two items in each plant and exchanging products between plants so that all routes had similar lines. The company was achieving further efficiencies through improvements in baking equipment and technology. The company was expanding through acquisition of existing facilities and distribution systems. As the brothers assessed their business, in the middle 60's two concerns developed. One concerned their ability to continue the growth of the company with the funds that could be generated internally and borrowed. The second concern was a personal conviction of the older brother. These concerns were described by the CEO as follows:

> My brother decided about this time, one way that we could pay our country back for all the many good things that we had received was to serve the country in some political capacity. He decided to run for the State Senate. I was his campaign manager. There was a young man here who was very popular and had been active in a lot of community affairs that many people thought would win this race. After a real hard campaign, we beat him two-to-one. My brother served two terms in the Senate and it was during that period of time we decided we needed to grow in order to provide opportunities for all the young people that we were developing in our company and also for some of the sons and daughters and sons-in-law in our own families. We decided the best way to approach this was to become a public corporation. In 1969 we officially became Sunbelt Foods, Inc., and were traded in the over-the-counter market. Our plan was to grow in the food business--mostly in

> snacks but in any food business which would tie into our present operation in order to help us reach the goals that we had set for our company in return on invested capital and equity.

The decision to grow was made in the early stages of another wave of concentration which was described by a corporate officer:

> The industry has become concentrated as a lot of the smaller competitors folded. Our company was one of those smaller plants fifteen years ago, but our Chairman had the vision and the intelligence to see what was happening and he knew if he sat right here with one single bakery, in ten years' time he would be a casualty like so many others. He realized that he could either go into politics for the rest of his life or he could take his company public and do something with it and position it where he could be competitive and survive in a concentrating industry rather than become one of the casualties of it.

With the public offering of stock, the company accelerated its acquisition program and ten years after the initial offering was nationally recognized for its growth and performance. The small, regional plant had become a diversified national food specialty company.

1970's: Growth through Acquisition

SFI's strategy for the 70's has been one of growth through acquisition in the specialty foods industry. In the snack foods area, the company has relied on reciprocal manufacturing and automation to increase volume and reduce costs. A decentralized computer system supports the management philosophy of centralized planning and control and decentralized operations. In the convenience foods area, the company has been expanding into areas with higher value added.

A corporate officer discussed the general strategy of acquisition as follows:

> The food industry is mature in the sense that the total consumption of food per individual is established at X number of pounds per year and is not likely to change much. Within that poundage however there is some leeway as to what products make up the total. There are opportunities to exploit changes in eating habits and methods of preparation. The S. J. Heinz Company is a good example of that.
>
> There are basically three ways a company in this industry can grow. One is to introduce new products; second, you can take market share from other companies; third, is acquisitions. That's the main route we've chosen and we feel the opportunities are unlimited.

The pattern of these acquisitions has been purchase of operations with facilities which need modernizing and strong distribution systems. The company applies its expertise in manufacturing by either upgrading facilities or consolidating the distribution routes into nearby existing operations. A corporate officer describes the process:

> What we've done is buy companies that have gone bankrupt or are no longer making any money because they haven't put any new equipment in because they just simply didn't have the vision or whatever. They're being shut down every day; they're being bought by others. The industry is concentrating. Now it doesn't matter whether SFI buys somebody else that hasn't made a profit in five years or whether he's allowed to sit right there and die on the vine, another single plant can't come in there and turn it around. You have to become part of a larger unit.

> What we've done, by and large, operationally is to establish what we refer to as reciprocal manufacturing. Each plant specializes in a few items to capitalize on long runs. And then in a highly complex transportation system overnight they exchange these products over a couple of hundred miles.
>
> So what we've got is each plant ends up at three or four o'clock in the morning with a full range of items although they may produce only one or two of them. You've got a full line of fresh products and you're able to do it far less expensively than if you were producing all products at a single location.

The importance of automation to the strategy is explained by the President:

> We operate on a least-cost production basis. In the Snack Foods Division we spend money to provide automated facilities. It gives us efficiency, so that nobody can produce products less expensively than we can--a decided competitive advantage.

While the acquisitions in the areas of snack foods are built on the expertise developed over many years, the acquisitions of nonbakery foods companies was a departure from the strategy of applying "least-cost" and reciprocal manufacturing principles to acquisitions.

The acquisition in 1970 of a nearby processor of spent hens for industrial users was the beginning of the convenience food business. The president describes this division as follows:

> The Convenience Foods Division produces frozen vegetables and food ingredients. Our products are sold to national service customers, chains, as well as school and institutional feeding programs. Our retail customers are a cross section of supermarkets throughout the midwest and southeast.

Since 1975, the division has been moving away from the commodity oriented uses for its products and broadened the lines which are marketed to institutional and consumer uses. The essential differences between this business which includes products like canned and frozen vegetable products, frozen fruit cobblers, and the snack business was explained by the president of the division:

> What we're dealing with in this particular area is competitors on a national basis because you're not limited as in the snack industry to a geographical area--to the confines of perishable products like fresh snack foods that have a limited shelf life because they're perishable. Your canned and frozen products are competing on a national basis because the shelf life is essentially two years plus. And so a plant in Portland, Oregon can produce products and sell them in Miami, Florida. Thus you are competing on a national basis.
>
> Secondly, you're dealing with an inventory intensive business versus perishable product when you don't have the constraints of raw material and finished goods inventory which is a much more complex business to deal with competitively and operationally. Of course it means you have a lot more capital tied up in it.

While companies of all sizes compete in this area of the food industry, SFI does not anticipate direct competition with large national firms. The division president said:

> We're looking at specialty products. We'll not be dealing with national food companies; it doesn't make sense. We're in product categories that are too small for them where we can enhance our profits and meet our financial criteria.

While the acquisitions in snack foods areas benefit from the expertise of SFI management as well as infusions of capital, capital is the primary element SFI has to offer convenience food acquisitions. As the division president explained:

> We're willing to allow management of the acquired company to run it under limited constraints versus bringing them into a tight centralized structure.
>
> We feel that it makes sense operationally because we may not know how to run a condiment company so we put financial goals and constraints on them and the results speak for themselves. We aren't going into operations that are not snacks. We have the expertise in that area; we know just what we're doing. We can completely alter a plant, supply it with key people and run it successfully. In other areas we don't have that core, we're going to rely on the management that comes with the company or, if necessary, bring it in from the outside.

The changes in geographical scope of the company, the need to oversee vastly enlarged operations, and the incorporation of nonsnack activities into the business has produced changes in the ownership and management structure of the business and in the family's role in SFI.

Operations and Management Systems

Organization Structure

The organization structure at SFI reflects both the expanding scope of the firm's activities and current management practice. It is organized into two divisions each of which has a functional staff. There is also a functional staff at the corporate level. The responsibility for planning and control rests at the corporate level and the planning of acquisitions has been prominent in the activities of the corporate staff. The corporate staff also serves to insure standardization of activities within the organization.

Each division further decentralizes operations by plants. The president described the system as follows:

> The philosophy that we operate under is that each one of these plants is a profit center and has a plant President who is responsible for the plant, its people, the products, the pricing and the results. He performs within the framework and within the targets which he has set under the direction of corporate management. Management sets the boundaries: specifically, what we want him to do and what he must achieve. Within those boundaries, our plant Presidents have the freedom to do what they need to do in order to achieve the results mutually agreed upon.

An operations committee in each division is the primary coordinating body. The CEO described the committee in the snack division:

> The division president has an operations committee that includes his area vice presidents plus his staff. It meets every four weeks and they review every plant--manpower problems, plans, capital spending--the whole works. That's how you stay on top of what's going on in the forward planning.

Management Control

The primary means of control in SFI revolves around the yearly goal-setting process and the regular flow of information concerning the status of the individual unit in relation to its goals. The CEO provided an overview of the process:

> Every plant has to plan ahead in detail every year on their profit goals. We have profit goals from the top and from the bottom. Our local plant management team sets their profit goals based on what they think they're going to sell on each route. The profit goals that we set from the top, for each plant are totaled up. More than 90% of the times their total will be more than what we set at the top. But still there will be some adjustments. Maybe we've done some capital spending in a plant and the goal they set isn't enough to get the return on what we've spent. That plant will have to adjust its goal upward.

Information is provided on the performance of each unit. The financial officer describes how this is done:

> Our week ends on a Saturday. By Tuesday morning, each of our profit centers, from production line superintendent to corporate president, has a summary P and L statement showing his individual performance for the prior week.
>
> Every four weeks our decision makers receive a detailed report which analyzes 500 separate cost items against the previous year and the budget. These data allow them to identify opportunities for further improvement. The entire control system lies at the heart of our company's management procedure and is the key to goal-setting.

At one point this information was delivered to the plants by bus and later by phone lines from a centralized computer. The current system is described by the controller:

> We've gone totally from a centralized system where everything is processed at the corporate headquarters to decentralized operation where each plant has its own computer and maintains its own records. We've been able to cut our costs in the process of this decentralization. When we're through, we will have trimmed our corporate expenses here in this building by approximately one million dollars, and in the plants, we're taking out anywhere from two to four people per plant. I haven't calculated that out but there are significant cost savings there.

The same goals which form the basis of the control system also determine rewards.

Incentives and Rewards

The financial officer describes the control and reward system as follows:

> All of our managers participate in incentive-bonus plans rewarding superior performance.
>
> An interesting example of how we use this program of cost control lies in receivables and inventory. Each plant President has a target level. If he exceeds it he is charged interest at the current prime rate for the excess. If he comes under his target level, we give him credit for it in his bonus. This system allows each plant President to be aware of the cost of money and the need to control his business as an entrepreneur.

The performance of the company as a whole is the basis on which rewards are distributed at the corporate level. The CEO described the stock bonus plan based on the growth of the company's earnings:

> A grant of performance shares is made by the Compensation Committee of the Board at the beginning of an award period which covers four years. Payment is made at the end of the award period, and the value of the performance shares is based on the value of the Company's stock at the time of payment. The total amount of the grant is paid if we have a compounded increase in earnings per share of at least 15% over the four-year period. That's a difficult goal but it's been achieved for the last six years. A percentage of the grant is payable on a sliding scale if the increase in EPS is less than 15% but at least 8%; if the increase is less than 8%, the payment is zero. Payment for performance shares has been made one-half in cash and one-half in stock; this is so the recipients will have the cash to pay taxes on the award.

A member of the Board identified the reward system of the firm with being the primary means of assuring professional management among family members:

> There is a structured compensation plan which tends to attract professional managers and reward performance rather than closeness to family. The system supports the goal of professional management.

Strategic Planning

One observer of the business described the changes in decision-making and strategic planning processes that had taken place as the company grew as a transition from a "patriarch to a family consortium." Much of the time and energy of the "consortium" is taken up with the identification, evaluation, and negotiation of acquisitions. The process is relatively informal and its success is based on the personal contact among the participants. A participant in this process described it as follows:

> That's a thing we do with a relatively small group of people whether they're at dinner together, talking on the airplane or whatever, it's almost a constant exchange about where you would like to be expanding, what should be done and that type of thing. It's a constant understanding in terms of what we need to do, what's available, what conversations people have had--that type of thing. It's too dynamic an area to try to pigeon-hole it into a classic central planning system.
>
> Our information flows very well. We know what may be for sale, we know what other people are doing, we know our industry so we know what it's leading into. And it's all sensitized, not by someone who does nothing but that, but it's constantly being sensitized in all of us and I think we're able to handle it in that fashion probably far more efficiently than writing it all down and assigning numbers and values to things.

Beyond choosing acquisitions, little strategic planning is done in a formal sense. The officer explains:

> What you frequently do when a company is terribly dynamic in a growing industry, you do those things that need to be done right now and what needs to be done right now is those moments we are seizing. And you don't take time to plan five years ahead; you're too busy doing what needs to be done today. It hasn't got to the point where it is a priority that some of these other things need to take a back seat to it.
>
> Planning is not something that we don't all realize the importance of and it's not something that we don't all realize that, as the company continues to grow, will have to be given more and more emphasis. Things do have to be institutionalized, and as you get larger, communications become more difficult. The dollars involved become greater, the risks that you are exposed to become greater. As you make more decisions and more complex decisions, more sophisticated decisions, you can no longer do that in a small ad hoc group sitting around talking in a staff meeting.

The individuals generally involved in this "ad hoc group" include the Chairman, the CEO, the President, the General Counsel, the Marketing Vice Preisdent, Controller, and Chief Financial Officer. All but three of these individuals are family members.

The expansion of strategic decision making from the two brothers to include a larger if informal group of corporate officers has resulted partly from the need to share responsibilities as the company grew and partly from an individual and organizational learning process that accompanied expansion. In the words of a corporate officer who has experienced the process:

> So really what you've got is a handful of people, using an open door type policy for easy communications. That makes it easy to become assimilated when you can sit in on the meetings where decisions are being made. It's not so stylized that it's hard to understand what the Chairman of the Board thinks because you know what he thinks.
>
> You've got a group of really aggressive people who don't mind making decisions themselves. To some extent the senior people are spared the usurpation of their time by people who make their own decisions very readily. We also know what the senior people want to be informed about in advance and that again is a result of having almost constant dialogue with these people. You don't have to sit around and say "Well now, is this something I should go to the boss about?" It's just a very spontaneous thing. And whether you make the decision in advance or afterward, you keep them informed and their response at that time is part of the continual process of knowing what decisions are important for them to be involved with.

Strategic decision-making is no longer a one-man process at SFI but is in a process of transition from that kind of a process to a more formal, institutionalized arrangement. The continued influence of the Chairman combined with the presence of many family members in the ad hoc group should be noted.

Related to the transitional nature of the strategic decision-making process is the question of management succession at SFI.

Top Management Succession

The original founder of SFI died suddenly and the fact that his twenty-year-old son was the prime candidate to succeed him may indicate that he had not systematically provided for succession. His son's situation is, of course, radically different. The pressures of growth have dictated a management structure which presumably could carry on in the event of his departure, but beyond that, the Chairman has provided for the continuity of the business as he has gradually withdrawn from operations. His role on the executive committee, as well as the testimony of those acquainted with the firm, indicate that he has not withdrawn from strategic decision-making. A corporate officer points to this gradual withdrawal:

> The motivation and the initial direction this company headed on clearly was set by the Chairman. In recent years, the carrying out of that direction in terms of what acquisitions to make, the structure of those acquisitions has not been made entirely by the Chairman but has been made largely by people below him.
>
> I think that from a general standpoint, his recognition of the importance of allowing more and more operations to be run or decisions to be made by younger people in management is further testimony to his management capabilities.
>
> He has shown the ability to recognize the problem by bringing in young people and letting them have the reins fairly early. If the decision is taken away from him, through death or whatever, because of the foresight he had there would not be a cataclismic problem in the company. He's done it on two levels with his brother and the President. Management succession is no problem.

Family-Business Relationship

Family-Business Interaction

As SFI has grown from a single plant operation to a food specialty company with over 17 plants and 8,000 employees, family connections have remained strong. The original company was a partnership between the father of the current Chairman and Vice Chairman and his brother. When the two brothers split the business, the father gave his brother the choice of businesses and was left with the snack plant when the brother chose the ice cream business.

The father died suddenly, leaving two sons and two daughters. The oldest son entered the business and was the only family member associated with the firm until the younger brother joined him after World War II. Other family members joined the firm over the years and at present there are seven individuals related by blood or marriage to the founder employed at various levels in the firm. Table 3-7 lists title held by family member and relationship to the founder. Family members have relatively high positions in the firm. Two members of the three-man executive committee are related, and two of the three division presidents are family members.

Adjustments and Transitions in the Family-Business Relationship

Sunbelt Foods, Incorporated (SFI) has experienced a number of changes which have been related to changing industry structure and the development of the business itself as well as changes in the family which have redefined constraints for the business. Growth and change in the business was accompanied by growth and change in the family. As more family members matured, the availability of family managers increased and the desirability of having family participation

Table 3-7: Family Relationships in SFI Management

Title	Relationship to Founder
Chairman	Son
Vice Chairman and Chief Executive Officer	Son
Senior Vice President and Chief Financial Officer	Grandson-in-law
Director of Marketing, President, Convenience Foods	Grandson-in-law
President, Baked Foods	Grandson
Plant President	Grandson
Personnel Staff	Grandson-in-law

was increasingly acknowledged. Later a new constraint was introduced as family members sought to reduce the negative connotations for SFI which they feared were associated with family management in general. The decision of the top manager to direct his energies toward building the business rather than a political career was also an important influence on the business.

Important events in the history of the firm and family which were described in the case study are summarized in Table 3-8.

The snack foods operation which was the core of SFI was founded in the first wave of expansion of this industry. In the relatively isolated small town in which the operation was located, there was no direct competition at the time of the founding. The decision to enter the industry was based on the absence of such enterprises in the area rather than the possession of any special competence by the founder in that business. In view of the fact that the founder allowed his brother the choice of businesses when the partnership was split, it seems reasonable to assume that any special skills which had been acquired in the course of operating the businesses were viewed as transferable between the two operations and were probably related to sales rather than manufacturing.

The competitive environment of the business was favorable at the time of and immediately following the founding of the business. The business survived and grew

Table 3-8. Important Events in the History of the Family and Business at SFI

Date	Business Events	Family Events
1919	business is founded	
1934	death of founder older son takes over	death of father
	competition increases in industry	
	growth of business	
1946	second son enters business	second family unit becomes involved
	purchase of more plants	birth of nine children
	increasing debt to equity ratio	
1967		decision to abandon political career
1968	public offering of stock	children and spouses making career choices
	geographical expansion diversification	
1978		stock of older brother (largest single stockholer) passed to daughters in voting trust
1980	strategy of growth by acquisition continues	

modestly under the supervision of the founder. He ran the operation without assistance and his children were too young to be involved in the business under his leadership. His sudden death left the business with no previously chosen and trained head, but his oldest son had just graduated from college and at age twenty stepped into his father's position. He also became the breadwinner for his mother and younger brother and sisters. As head of the business and the family he was in an excellent position to shape the constraints of the family to what he perceived to be the needs of the business. No other family members were in a position to enforce constraints upon the business.

Under his leadership, the firm continued its pattern of incremental growth but at an accelerating rate. The number of routes tripled in the first decade of his management and a plant was purchased in a nearby city. The growth of the business made it necessary to make a transition from a one-man entrepreneurial management to a more delegative arrangement. The person chosen to share the authority was the younger son of the founder. The requirements of the business for more managerial assistance moved the relationship out of the pre-family stage. The entry of the younger brother into the management of the firm was the first of many additions of family members to top and middle management.

The first transition in the family-business relationship was the result of the changing managerial requirements of a growing business. The second adjustment was the result of changes in both the competitive environment of the business and the family expectations for the business (see Table 3-9).

The snack foods industry. While the firm lacked significant competition in the early days, this favorable situation rapidly gave way to competition from both local and national firms as transportation improved and the market for snack products grew. On the national level, snack food producers had participated in the industrial consolidations and trust-building which had characterized the maturing of American industry in the late Nineteenth and early Twentieth centuries. Most of the national snack empires were outside the Southwest so the situation in SFI's area was relatively less affected by this movement than other areas. On the other hand, the Southwest did experience the proliferation of plants which accompanied transportation improvements in all regions, and there was some encroachments from larger firms, particularly in the eastern extremes of SFI's market area.

These plants shared the problems of short production runs dictated by the perishability of the product and the variety of products needed to stock a delivery truck. Frequent changes in product formulas and shapes meant considerable down time for cleaning and change-overs and high labor costs. During and after World War II, SFI was moving

Table 3-9. Process of Change in Family-Business Relationship of Sunbelt Foods, Inc.

Impetus for Change	Change	Consequences
Need for manager at death of founder	adjustment: oldest son steps in	family retains control
Need for more management and constraint for family participation	transition: second son joins business	family constituency expands
Need for more financial resources and desire to maintain family returns	adjustment: increased use of debt	increased opportunity for nonfamily influence
strategic opportunities raise funds requirements, expectation of business providing opportunities for family members, personal decision about political career and expectations for family members	transition: public sale of stock	decreased control, employee adjustments, increased concern about nepotism

toward mitigating these problems. The proximity of the firm to army camps had enabled management to purchase some automated equipment and the search for labor saving devices continued. The company was also beginning to experiment with operating and distribution systems which assigned the production of different products to different plants which then exchanged items so that each had a full line ready for delivery. These practices became the cornerstone of the company's strategy in snack manufacturing.

Other plants were not so successful, and in the Sixties, acquisition of these local plants and distribution system by the large national concerns was accelerating. A strategic opportunity arose for SFI when antitrust action by the Federal Trade Commission prevented the further purchase of these companies by the large firms. SFI's earlier successes at integrating and making profitable losing operations provided them with the expertise to take advantage of a buyer's market for failing businesses if the resources for growth could be obtained.

The funds generated internally by the firm provided dividends for the family and the means of further growth for the firm. As more opportunities for acquisitions were exploited, debt became the primary means of meeting family constraints for dividends while also taking advantage of opportunities for growth. By the middle Sixties, the debt structure was over-balanced and it was becoming apparent that family-ownership constraints were no longer consistent with the continuing growth of the business.

The growth of the family. While the firm had been growing as a result of strategic decisions by management, the family had been growing by natural processes. The two sons had nine children between them and while only two were sons, the older brother had at least one son-in-law who was a candidate to enter the firm. Ultimately, three sons-in-law and one son and one nephew joined the two brothers in the family management group. The question of whether the company in its present state could absorb these family members and provide them as well as nonfamily managers with the kind of opportunities which the brothers felt the business had given them was discussed. While there is no indication that family members outside the management of the business put pressure on the brothers to provide places for the next generation, it was a situation in which the brothers as family heads were changing their expectations about what the business should provide for other family members.

The third factor in the transition to the next stage of the family-business relationship arose with a personal career decision by the older brother. As the younger brother rose to the presidency of the firm, the older brother began to pursue an interest in politics. He won his first race on the state level and formed alliances with several figures of state-wide and, to some extent, national prominence. As an advocate of the free enterprise system, the older brother saw politics as one way of supporting the system and the business as an alternative means of accomplishing the same goal. He decided that business provided a better tool for the advocacy of the practice of free enterprise and decided to focus his activities on bringing what began as a small local business into a profitable big business.

Going public. The means to deal with the emerging opportunities for growth in the snack food industry, the growth of the family and the need for opportunities for family members in the business, and the desire of the older brother to escalate the growth of the company was the relinquishment of the company as a privately-held family corporation and the sale of the stock to the public. The constraint of family control conflicted with the growth requirements of the business so it was necessary to move to a different stage of the family-business relationship. The public sale of stock ultimately reduced the family share of ownership to approximately 20 percent. Family members are no longer encouraged to consider careers with the company and family managers are concerned with avoiding the appearance of favoritism to family members.

The firm's growth and profit record since the public offering of stock have brought it national recognition. The family traded outright control of the firm for the resources needed to fund the growth, and the performance-oriented reward system which directs the firm toward profit goals also insures against family favoritism.

Stage Characteristics

SFI has moved through three stages of the family-business relationship and in the process has decreased family ownership and increased family management. The impetus for accommodations in the family constraints and business requirements as well as the adjustments in the family-business relationship have generally come from the needs of the business. The continuing growth and profitability of the firm and the concentration of family influence into the hands of business leadership have facilitated making accommodations and adjustments to the benefit of the business.

Stage I: Prefamily. The organization of SFI in Stage I was characterized by the undivided leadership of a single individual. The leadership of the business was passed undivided to the second generation of management because of the premature death of the founder and the fact that only one of his sons was old enough to be involved in the business and thus succeed his father. The family, which consisted of the founder's widow and minor children, was dependent on the oldest son. Leadership of the family as well as the business fell on the same individual. The power to make decisions was concentrated in the founder's son.

No information was available concerning the reward system under the founder but his son placed emphasis on rewarding performance. The top posts in management were held by family members in Stage I so that the promotion opportunities were different for family and nonfamily members.

The role of the family was to support father and son in their management of the business but there was no active participation in the business. The relationship was characterized by a unity of purpose centered on the survival of the business and beyond that there was relative independence from family constraints.

Stage II: Family. The company entered the second stage of the family-business relationship with the entrance of the second brother into the company. A nephew also entered the business during this stage.

• Organization and distribution of power. The family members entering the business in Stage II were trained in sales operations in the functionally organized firm. Both began with route deliveries and moved up through the sales organization. The younger brother became President of the company while the nephew became president of one of the divisions.

• Decision process. The addition of other family members to management created new centers of family power within the firm. This led to a consultive mode of decision making, particularly between the two brothers.

• Rewards. The emphasis on performance-based rewards continued as well as the preference for family members in top management positions. As the business grew, the number of upper management positions was increasing so that advancement opportunities were available for nonfamily members in addition to financial incentives.

• Role of the family. The families of the two brothers were reaching adulthood in this stage and the brothers were looking to their sons and sons-in-law to provide management resources for the firm. A positive value was placed on recruiting family members for managerial positions.

Stage III: Adaptive Family. A Stage III relationship is one in which the family trades some of its control for continuing participation in a growing business. In this case, the family traded control of a small firm for investment in and management of a much larger organization.

• Organization and distribution of power. SFI moved from a functional to a divisional organization as part of its strategy of growth by acquisitions in the food processing business. The divisionalization of the firm put operating and strategic responsibilities on the presidents of the divisions and the president of the company. Two of these men are family members while two are not. Acquisition planning is done by an informal group of managers who are not members of the family. The executive committee of the Board includes two family members on the three man committee.

• Decision process. Organization structure and delegation patterns have dispersed authority and responsibility among both family and nonfamily managers. Decision-making is also dispersed with family and nonfamily members participating on the basis of position and expertise.

• Rewards. An incentive compensation system rewards managers on the basis of the overall profit performance of the firm as well as the performance of their unit. A nonfamily member holds the presidency of the firm, but there is speculation among some observers that the Board Chairmanship will, in the forseeable future, be reserved for a family member.

• Role of the family. The relationship between the family and business at SFI increasingly resembles that between any business and its stockholders and managers. Family entry into the business is no longer encouraged and steps are taken to assure that charges of favoritism do not arise. While family members no longer work their way up from routine assignments, the visibility that they are soon given provides them an early opportunity to prove themselves. The family has enough stock and controls enough management positions to insure that family constraints can be imposed. Observers feel that the choice of successors for the two brothers will test the extent to which family constraints can still be felt in the business.

Table 3-10 summarizes the characteristics of the stages of development of the family-business relationship at SFI.

Path of Development

SFI has moved fairly rapidly through three stages of the family-business relationship. In contrast to Specialty Sauce where all managers had experienced only one stage of the relationship, at SFI, all but the youngest have experienced at least two and some have experienced all three.

Transitions at SFI have been purposeful rather than forced by circumstances. The transition at SFI from Family to the Adaptive Family Stage of the relationship was part of a comprehensive response to a competitive opportunity which management perceived and wished to exploit. This is very different from the circumstances which are about to force a transition at Valley Foods.

SFI has followed an evolutionary path of development and appears to have reached a plateau in the relationship. Management has been successful in matching family constraints to business requirements to such an extent that it seems unlikely that a discrepancy between the two would arise that would be serious enough to move the company into the Post-family stage.

Recapitulation

Four case studies have been presented in this chapter to illustrate the processes of adjustment and transition

Table 3-10. Family-Business Relationship Sunbelt Foods, Incorporated

	Management Characteristics By Stage			
	Organization Power	Decision Process	Rewards	Family Role
Stage I (Prefamily)	Hierarchical, Concentrated	Unilateral	Differen-tial	Support founder
Stage II (Family)	Functional Dispersed	Consensus	Differen-tial	Central: pro-vide managerial and financial resources
Stage III (Adaptive Family)	Functional, then Divi-sional, Dispersed	Expertise	Performance-based	Peripheral Provide mana-gerial and financial resources and continuity
Stage IV (Postfamily)	------	------	------	------

which shape the family-business relationship and also to show characteristics of the stages through which the relationship develops. Finally, the case studies should have provided the reader with a feeling for the differences in timing and ease with which the transitions are accomplished.

Piedmont Meat and Specialty Sauce were illustrative of family-business relationships which have exhibited great stability. This stability is seen, in part, as a result of a stable competitive environment or a protected competitive niche and, in part, as a result of careful management of the relationship.

Valley Food Company and Sunbelt Foods have experienced more change in their respective relationships and have approached the relationships differently. Sunbelt Foods has incorporated the family-business relationship into its strategic thinking to a degree that is not in evidence at Valley Foods. The relationship at VFC has been an increasing source of disruption for the business while at SFI, it is a source of strength.

The findings of the research presented in Chapter Two were based on more cases than the four presented here. The remaining case data are summarized in Chapter Four and data from all cases are incorporated iinto the subsequent analysis. This analysis constitutes a more detailed counterpart for the generalized findings presented in Chapter Two.

CHAPTER FOUR

COMPARATIVE ANALYSIS

Overview of Sample

Family and Business Characteristics

The changes which take place in the family, the business and the competitive environment during the time a family has an ownership or management interest in a business produce two kinds of changes in the family-business relationship. In one instance, the change is made in the expectations or standards which the family has for the business or in the strategic or operating policy of the business itself. These changes do not affect the structure of the relationship. The second type of change which occurs is that of alteration of the underlying structure of the relationship by altering the distribution of power in the relationship.

The four cases presented in Chapter Three illustrate both types of changes. These cases were chosen to provide the reader with a sense of the variety of the relationships in the sample and to provide data against which analysis and conclusions of the research can be judged. While formal case studies of the other firms are not included in this document, the data gained from those firms were equally important to the analysis, conclusions, and implications which are presented in this and subsequent chapters.

Table 4-1 summarizes characteristics of businesses in the sample as well as characteristics of families that own and manage them. The largest portion of these businesses is small, single product or single product-line enterprises with local or regional markets. Several market their products in selected areas beyond their own region or overseas, but only one, Specialty Sauce (see Chapter Three), has true nationwide distribution. Most of the firms were small with sales under $10 million and less than 100 employees. Notable exceptions were Sunbelt Foods with sales of $350 million and more than 7,000 employees, Country Eggs with sales of over $40 million, Valley Foods Company with sales of over $20 million and 350 employees, and Specialty Sauce with 150 employees. One of the companies, Country Eggs, had vertically integrated operations while another, Sunbelt Foods, had diversified from its snack origins into other prepared foods.

The companies with the longest family association were Variety Meats and Specialty Sauce both in their fourth generation of family management. While some of the companies had acted to restrict family ownership to family members in management positions, the bulk of the sample had seen the growth of the number of family members who inherited stock and a corresponding decrease in the ownership interest of any single family member.

Table 4-1: Characteristics of Sample Firms

	Basic Business				
General Characteristics	Snack Products	Meat #1	Sauce/Vegetables	Meat #2	Sauce
Primary business activities	Production & distribution	Processing	Canning and bottling	Processing	Growing & processing
Markets	Southern & Eastern U.S.	Southern Miss. Valley	Southeast, NY, Texas, Calif.	Local	U.S., international
No. Employees	7,000+	450	350-600		150
Sales	$250 mil.	n.a.	$20 mil.	n.a.	n.a.
Strategic thrust	growth by acquisition and turnaround	geographical expansion	geographical expansion	additions to product line	patent protection
Organizational Characteristics					
Structure	divisional	functional	functional	functional	functional with subsidiaries
Information and control systems	profit information for all activities		sales and inventories	informal, annual inventory check	
Reward and incentive systems	profit and growth formula	based on family relationship	none	informal	career path restricted for nonfamily debt avoidance
Financial policies	debt/equity	debt/equity	debt/equity dividends	debt aversive	debt avoidance
Family Association					
Ownership	25% of stock	100% of stock	100% of stock	100% of stock	100% of stock
Management	5 corp. officers, 2 others	6 corp. officers, 1 other	1 officer 4 others	all family	4 family managers
Duration	2nd & 3rd generation	4th generation	3rd & 4th generation	2nd & 3rd generation	4th generation
Participation of non-managers	stockholder meetings	minimal	active	minimal	special Board positions

Table 4-1 (continued)

	Basic Business				
General Characteristics	Meat #3	Dairy	Meat #4	Eggs	Meat #5
Primary business activities	production & distribution	processing	slaughter & processing	production & marketing	processing & distribution
Markets	local	local	parts of Tenn., Ga., Va.	regional & Northeast	local
No. Employees	50	100	50	250	50
Sales	$4 mil.	n.a.	$3.5 mil.	$40 mil.	$3 mil.
Strategic thrust	market penetration	market penetration	penetration & geographical expansion	integration; market shift through acquisition	shift from processing to franchising
Organizational Characteristics					
Structure	functional	functional	supervised supervision	functional	supervised supervision
Information and control systems	sales, inventory		amount & cost of production	automated external & internal	product line data for first time
Reward and Incentive systems	based on family relationship	family	profit-sharing	bonus for executives	based on family
Financial policies	debt	debt aversive	debt aversive	debt/equity	debt
Family Association					
Ownership	100% of stock	family managers own all stock	minority stock held by non-family	100% of stock owned by founder	100% of stock owned by family
Management	3 managers	7 managers; 12 others	2 managers, 1 other	1 manager;	1 manager; 1 other
Duration	2nd & 3rd generation	2nd & 3rd generation	2nd & 3rd generation	1st generation	2nd generation

Table 4-1 (continued)

	Basic Business				
	Meat #3	Dairy	Meat #4	Eggs	Meat #5
Participation of non-managers	none	all stockholders are managers	frequent consultation	participation discouraged	consultation on certain issues

General Characteristics	Meat #6	Meat #7
Primary business activities	slaughter, processing; sale to other processors and direct	processing
Markets	local	local
No. Employees	50	4
Sales	$3 mil.	$.25 mil.
Strategic thrust	cooperative efforts; control costs	passive
Organizational Characteristics		
Structure	supervised supervision	direct supervision
Information and control systems	intuitive and observation	observation
Reward and incentive systems	none	none
Financial policies	debt aversive	debt
Family Association		
Ownership	100% of stock owned by managers	100% of stock owned by family
Management	3 managers; 1 other	1 owner/manager; 1 other
Duration	2nd & 3rd generation	1st generation
Participation of non-managers	father of current managers often consulted	sounding board

Management systems and administrative policies in the sample firm varied with the size of the companies with the larger companies having more formal information and control systems and more specification of reporting relationships. Only one of the companies had a staff planning position and this duty was one of several for the individual who held it. All of the companies were functionally organized except Sunbelt Foods which had a divisional structure and the smallest meat company in which all activities were directly supervised by the owner.

Competitive Environment

All of the firms were involved in the transformation of commodities into products for human consumption. Most of the companies were able to differentiate their products to some extent and found it useful to advertise to increase brand loyalty. The major exception to this was the egg firm and some of the meat packers who sold fresh meat. Most of the meat packers found processed meats, especially sausage, to be their most profitable product and emphasized processing over slaughtering and butchering.

Although some of the firms dealt in frozen products and canned foods, the problem of perishability was present in most of the industries. Perishability is a problem which is similar to excess capacity in that it tempts competitors to cut prices or otherwise sacrifice margins to spread costs over more units. Fresh meat, eggs, dairy, and snack products were particularly concerned with perishability while processed meats and canned foods and sauces had longer time spans to work with.

The competitive environment of the sample firms had been subject to changes in the long term factors which determine profits in given industries. Three types of changes in these structural factors had occured or were in process. The snack and bottling sauce segments were undergoing concentration. This was more pronounced in snacks and had been occuring for a longer period of time. The trend had been identified only recently in sauce and its impact had not been assessed. The meat industry had experienced two changes. A change in the structure of their buying industry, food retailing, had increased the power of retailers relative to the meat producers and had precluded many of them from the largest market segment, the grocery chain. The second event was the change in the federal regulations concerning the industry which not only increased the entry barriers for new firms but also "upped the ante" for those in the industry who wished to remain. The egg industry was also experiencing changes in cost factors which lowered profits in traditional markets and increased competition for market share in more desirable markets.

Challenge and Response

The changes in the structure of the industries and industry segments in which the sample firms compete represented a challenge to family managers which required responses of several kinds. Operational responses, such as more careful control of costs and changes in product lines, were often accompanied by an examination of strategic issues. The ultimate response was often strategic and involved changes in the business(es) of the company, change from internal to acquisitive growth strategy, and searches for new sources of resources.

Strategic decisions in family firms are made in the context of a family-business relationship. The relationship influences the decision process and is also subject to change as a result of the process. Family constraints concerning the activities and performance of the firm must be considered in formulating a strategic response to changes in the competitive environment. If these constraints are apt to prevent the desired response, the manager must resolve the conflict in order to implement the response. In the sample as a whole, most of the companies reached a point at some time in which conflicts could not be resolved within the existing structure of the family-business relationship and the relationship had to be changed in some fundamental way in order to accommodate the requirements of the business. Several companies changed the structure of the family-business relationship more than once.

Stages of Development

What might appear in a cross-sectional examination of family businesses as different types of family business, emerge in a historical examination of the development of such enterprises as a series of stages through which the relationship passes. The sequence of structural changes represents an evolution of the family-business relationship through these stages. Table 4-2 shows this sequence in the sample firms.

Nine of the businesses were founded by a single individual and managed by him for some period of time. The owner-manager functioned as sole decision-maker and this pattern continued into the second generation of management in some firms because his successor inherited full ownership of the business. This stage is called Prefamily because of the peripheral family involvement. Two firms in the sample were in this stage.

Three of the businesses in the sample included more than one family member from the beginning. The original founders were siblings or partners and children. This stage is referred to as the Family stage because several relatives are involved and decisions are made by consultation with an understanding that consensus is required to take action. With the exception of the two firms still in the Prefamily stage, all of the firms in the sample have been or are in this stage.

Table 4-2: Structure of Family-Business Relationship and Sequence of Structural Change in Sample Firms

	Structure of the Relationship			
Industry of Firm	Managed by Single Owner	Owners; Some Family Managers	Some Nonfamily Owners; Some non-Family Managers	No Family Owners; Some Family Management
Snack Products	Managed by owner-founder until sudden death; managed by son until 1946	Younger brother, then nephew and other family involved	Public offering of stock in 1966	
Meat	Managed by owner-founder till death	Children inherit business		
Sauce/Vegetables	Managed by owner-founder	Sons join business before World War I; incorporated and father leaves in 1929		
Meat	Managed by owner-founder from 1928	Sons join after World War II		Sold in 1969; some remained in management
Sauce	Managed by owner-founder until death in 1890	Sons join firm with oldest as manager; daughters inherit stock		
Meat		Founded by father and 3 sons; daughters have stock		
Dairy Products	Operated as sideline by founder	Sons take over after World War II; family managers later buy out other family		
Meat		Founded by father and son; grandchildren given stock	Minority interest sold to another meat packer	

Table 4-2 (continued)

Industry of Firm	Structure of the Relationship: Managed by Single Owner	Owners; Some Family Managers	Some Nonfamily Owners; Some non-Family Managers	No Family Owners; Some Family Management
Eggs	Managed by owner-founder			
Meat	Managed by owner-founder; then by son			
Meat		Founded by father and three sons; managed by sons		
Meat	Managed by owner-founder			

Three of the sample firms have undergone a second transition process and gone beyond the family stage. One has retained family participation in management and ownership while becoming a publicly held company. Another sold a minority stock interest to the owners of another business. When outsiders are introduced into the ownership structure of the business, the relationship has reached the Adaptive Family stage. A third firm sold the family company to another company and became an operating unit in a much larger organization. When the loss of family ownership control is not accompanied by the end of family management, the relationship is said to be in the Postfamily stage. Family managers and long-time employees may continue to introduce family constraints into decision-making. Some characteristics of the stages are summarized in Table 4-3.

Summary

Events and developments in the internal and external environment of the business and in the family, provide the impetus for change in the family-business relationship. The relationship is generally able to accommodate some changes by adjustments in the family constraints or the competitive activities which do not materially affect the underlying structure of the relationship. When such adjustment is not possible or not viewed as desirable, changes are made in the underlying structure of the relationship. These structural changes affect the relative power and influence of family owners and managers.

Table 4-3: Characteristics of Stages of the Family-Business Relationship

		CHARACTERISTICS OF STAGES			
NAME OF STAGE	TYPICAL LEGAL STRUCTURE	Organization/ Distribution of Power	Decision Process	Reward Systems	Family Role
Prefamily	Proprietorship; corporation with entrepreneur holding most of the stock	Concentrated in hands of entrepreneur and successors	Patriarchal; head of business is head of family	Informal; rewards distributed at owner's discretion	Peripheral; provide support for founder
Family	Partnership, corporation; stock held by several or many family members with holdings relatively equal	Dispersed among several family members (both managers and stockholders	Consensus required among family managers and some stockholders	Informal; rewards for family members differ from those for nonfamily	Central; financial and human resources provided by family
Adaptive Family	Corporation; family and nonfamily stock holders; family holds largest interest	Family shares power with those who provide critical resources	Heirarchical with input from many sources some of which may be family	Performance based for both family and nonfamily	Cooperative; other providers of resources become more critical
Postfamily	Subsidiary; operating unit of larger corporation	Power of remaining family managers based on expertise and worth to new organization	Heirarchical, based on objectives of owning organization	Formal system instituted by parent company	Transitional; family members who remain provide continuity

The developmental experiences of families and businesses in the sample provide some insight into the characteristics of the stages, the process of transition between stages, and the paths of development which different firms take. The next section will examine the transition process while characteristics of the stages and paths of development will be considered in subsequent sections of this chapter.

Process of Transition

A summary of important elements in the process of transition appears in Figure 4-1. These elements are the event or development which disturbs the relationship, the impetus for change which results, the nature of change, and the consequences of the change.

Events and Developments Which Provide Impetus for Change

The internal and external environments of the business are sources of events which can disturb the status quo in the family-business relationship. It is particularly susceptible to disturbance by events which affect the expected profit margin of the business, the financial resources required by the business, and the capacity of the business to employ family members. Changes in industry structure and the growth of the business often have one or more of these effects.

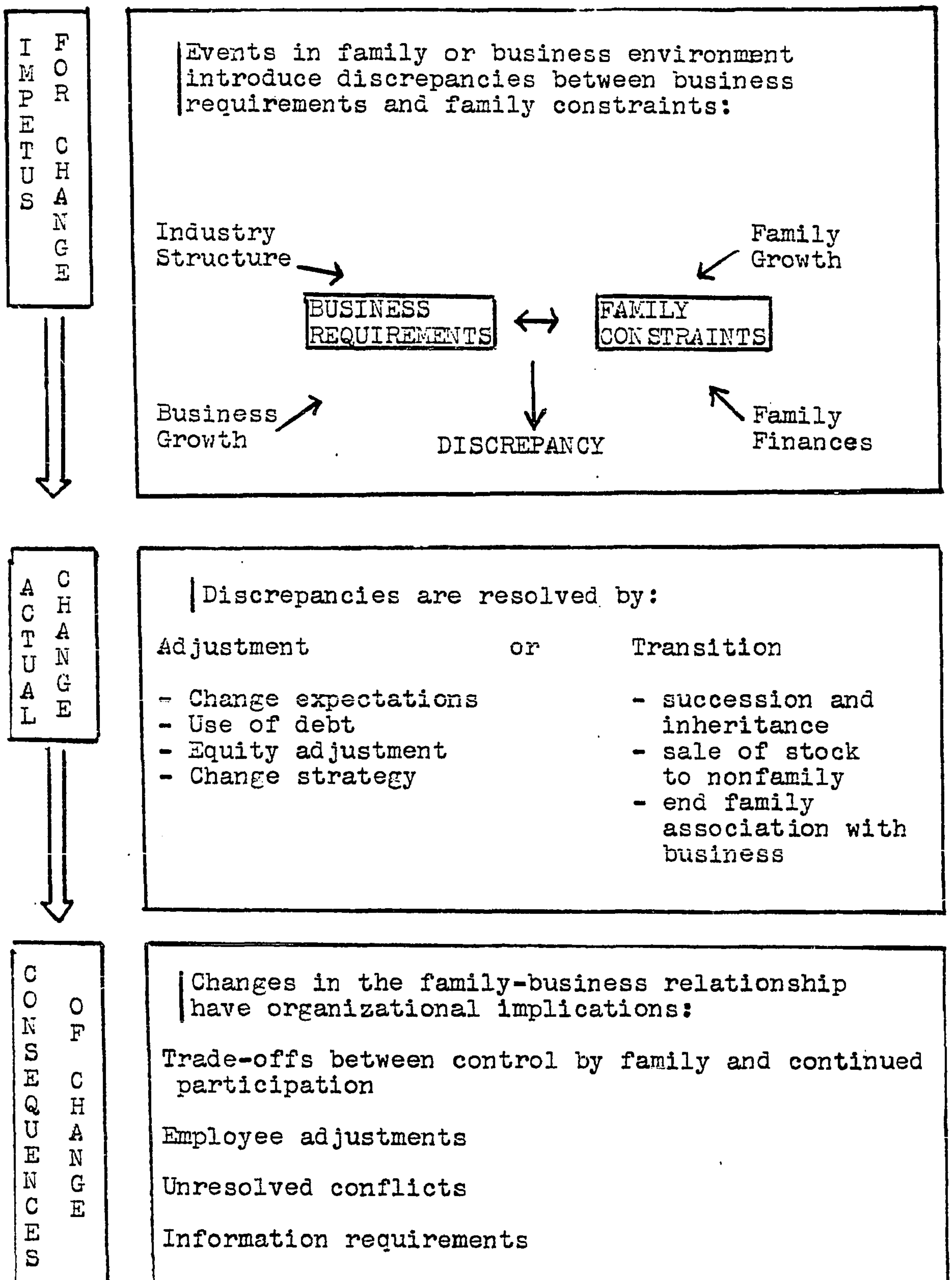


Figure 4-1: Elements in Process of Change in Family-Business Relationship

It is the interaction of these events with family constraints which produces the impetus for change and distinguishes family businesses. When a discrepancy arises the process of change in the relationship is set in motion.

The most frequently mentioned constraint in this study was the income from the business. In some cases expectations in this area were minimal. A meat packer's statement is typical of these companies:

> Last year we did four and a half million dollars worth of sales; still we get just enough profit to support your family and to live on . . . . Nothing fantastic, nothing great; no more than paying the bills, paying the employees. But my family has lived comfortably and I guess that's all we're due anyway. We're not really due that.

A family manager in Sunbelt Foods expressed higher, more explicit goals. The financial returns which were the criteria for decision making were "around a 15% after tax return on invested capital and a 20% after tax return on equity." In another company, the desire to accumulate assets for estate purposes provided an impetus for change:

> We had made money and we were successful but you had to look to the future. If you look at the tax laws, it's hard to accumulate cash for personal assets. You've got to put it back in the business. If you start accumulating cash in the bank it is highly taxed. You must keep expanding or go under; you can't stay still. We never lost money after World War II. We always made money in the business but the family could only get a certain amount of it.

Family pressure for more income from their investment became a primary concern of the president and eventually led to his dismissal (see Chapter Three).

A second area of expectations which family members hold for family business and which may provide impetus for change is the role of family members in the business. In most of the businesses, it was expected that family members entering the firm would be managers. Although family managers often mentioned the virtues of learning the business from the bottom up, it was unusual for family members beyond the first generation to actually follow this advice. As the company grows, the role of the family in providing financial rather than human resources may be emphasized more.

Family members frequently expect the company to provide jobs for family members. Often this expectation may be fulfilled by after school or summer work for younger family members. Families may also expect the company to provide full-time jobs for family members either permanently or until something better comes along. While many of the firms articulated a policy of not creating jobs for family members, it was often understood that a family member would get preference for an opening he desired. One firm adopted the practice of giving family members any job that might be open and assigning duties in keeping with his family connections regardless of the title of the job or the job description.

Nature of the Change: Adjustments and Transitions

Managers in the sample firms have dealt with the conflicts which arise as an impetus to change in two ways. The first option is to work to diminish the conflict by changing the family constraint or by making a change in the business which will eliminate or change the competitive requirement. This is the process which has been referred to as "adjustment." The second method of dealing with this impetus is to change the context in which family constraints and business requirements interact. This is the "transition" process and generally involves a change in the political structure of the relationship.

Adjustment of the Family-Business Relationship

Adjustment of the family-business relationship is possible when the discrepancy between business requirements and family constraints can be resolved by changing either the constraints or some aspect of the business. Managers in the sample firms attempted to make adjustments by persuading family members to revise their constraints, by changing business policies concerning debt and equity, and by making strategic changes in the activities of the business.

Managers were more likely to attempt to adjust family constraints in a positive manner and to let the business bear the brunt of failure to meet family constraints.

Change Expectations

The president of Valley Foods Company described his efforts to convince the family members that their expectations about the amount of dividends the company should be paying were unrealistic. Persuasion is more likely to be successful if expectations are being raised than lowered and he was not successful.

Changing family expectations about participation in management at Sunbelt Foods was a matter of persuading the next generation to enter the business. The brothers helped each other recruit sons and sons-in-law:

> My brother has four daughters; two of his married daughters' husbands work with our company. I helped him recruit his first son-in-law to come to work with us. . . . When my son's Naval hitch was over, he had several jobs available but my brother hired him. In this way we helped each other get our sons and sons-in-law into the business.

The brothers are no longer supporting family expectations of entering the business:

> You can get too much family in a business if you are not careful. We think we have a good balance now and do not anticipate bringing any more family into the business.

Debt

Increased needs for financial resources may provide an impetus to retain more funds in the business. This creates a conflict when family constraints for dividends are fixed. Rather than persuade the family to accept lower dividends, both Specialty Sauce and Sunbelt Foods increased their use of debt to finance capital spending. This adjustment is not readily available in firms in which debt avoidance is itself either a management policy or a family constraint. Two of the meat companies fell in this category. The president of one said:

> We borrow very little at this plant. This little family operation, we let it finance itself. One time a few years ago, we borrowed $50,000 to put in a freeze tunnel, but we've never borrowed very much. It's a personal hang-up. We feel like if we pay as we go we might not go so far. I just want to stay financially sound, just real financially sound. That's one way of doing it; pay as you go.

Equity

At Piedmont Meat Company (see Chapter Three), the adjustment process involved changing the equity structure. In order to discharge their perceived responsibility to maintain the income of their sisters and mother and to marshal the resources of the firm for the investment and curtailment of income which was necessary to bring the facilities up to federal standards, the family managers entered into a personal obligation:

> We took the girls' debentures and made stock out of them in order to eliminate any debt structure. Then we personally bought the stock and issued them personal notes. Temporarily they joined forces with us too.

Strategy

Specialty Sauce decided against splitting its operation and met the family constraint for remaining in the traditional location:

> We had the opportunity to acquire a bottling facility on the West Coast. It would have cut our shipping costs since we have good markets in that area. The family preferred to have all the production in this location so we let it go.

When a small meat packer could no longer meet the competitive requirements for slaughtering beef within family control constraints, he dropped this part of his operation and concentrated on processed meats and distribution. In these situations, family constraints had an impact on strategic decisions.

Transition in the Family-Business Relationship

Transitions or changes in the structure of the relationship may occur when a manager recognizes a potential conflict and moves to adapt the relationship before the conflict is felt in the business. In other situations, a transition is a last resort to settling conflict which is disrupting operations. While the former scenario is desirable, it is not always possible to recognize potential sources of conflict nor to make the necessary changes.

Transition involves a change in the power relationships which govern the family-business relationship. Since much of the power in a family business is a function of the distribution of stock and the position of relevant actors in management, adaptation of the relationship is accomplished by changes in the distribution of power between managers and stockholders. Transition mechanisms include succession, sale of stock to nonfamily members, and sale of family interest in business.

Inheritance and Succession

Perhaps the most common transition in the relationship occurs when the ownership interest and management position of the owner/founder is passed to his successor and/or heirs. The concentration of power in the founder is dispersed and the succeeding owners and managers must establish a division of power which is functional. It is the division of power rather than the leaving of the founder which constitutes the transition. This is illustrated by the experience at Sunbelt Foods. The founder of Sunbelt Foods died suddenly while relatively young. His oldest son inherited the business and undivided authority. He was not required to share his power with others in the family until much later when his brother joined the company. It was the addition of other family members to the business rather than the death of the founder that constituted a transition. The business was growing and his brother's managerial assistance was needed. The constraint of maintaining control was not consistent with the competitive requirements of the business so a transition was made. This does not imply an equal division of the power, however. The older brother was described as "never anything but the boss."

Broadening Ownership

At Sunbelt Foods, the family managers recognized that the goals of growth through acquisition and increasing opportunities for family members in the business were not compatible with maintaining family control of the business:

> We decided we needed to grow in order to provide opportunities for all the young people that we were developing in our company and also for some of the sons and daughters and sons-in-law of our own families. We decided the best way to approach this was to become a public corporation.

One of the meat packers was able to acquire access to resources for growth without acquiring unacceptable amounts of debt by selling a minority interest in his company to another meat packer. While his company remained privately held, the addition of nonfamily stockholders and business associates represented a different power distribution from the time when the business was completely in his family.

Ending Ownership

At one of the meat packing operations, the requirements of the business for additional investment conflicted with the family's income and control constraints.

> We knew that we'd have to spend as much money to upgrade our building [to meet federal standards] as we had spent on the business in all prior years.

> We sat and talked about it for six months. We tried to figure out what we would have to do and have to spend if we stayed in. At that time mergers were the thing, and we looked at that too.

The family decided that the desired level of income could not be maintained while the company was trying to meet federal facilities requirements so the family relinquished their ownership in the company. It became an operating unit in a large, integrated agricultural cooperative and several family members stayed on in management positions in the operation.

Consequences of Change

The processes of adjustment and adaptation do not always occur smoothly. In the firms in the sample, several kinds of problems arose as a consequence of these changes. While adjustment and adaptation are, in themselves, problem-solving mechanisms, they are likely to place managers and family members in new situations and new relationships which can create personal and organizational difficulties. Some of these are discussed in this section.

Management Decontrol

The possessiveness which an owner/founder feels toward his business is captured in the metaphor which refers to the business as his baby and his mistress. When such an individual attempts to make the transition from Prefamily to Family, the process may be quite perilous for the owner/founder, his successor, and the business. The literature of succession has addressed this problem.

Planning. Planning for this process was underway at one of the meat packers. The current president had taken over the business at an early age:

> I came here twenty-one years old and I took over the management of the whole thing. Of course, I thought I knew everything at that point. I thought I had all the answers. . . . In a business like this, since I took over twenty-one years ago, I've always made the decisions. I didn't have anybody question me and a lot of times like that, you can get into hot water because somebody else can see some objections or some obstacles in the way that you don't.

His son is in his last year of college and plans to join the firm upon graduation. The president is making arrangements for the son to be in a position to obtain an ownership interest in the firm:

> My father died about six years ago and he still had a half interest in the stock and this year, we merged all of it together and I signed a note to my mother. I'm trying to get ready for my son coming back from college so that we'd be able to know where I stand.

The father is aware of the potential problems of broadening family participation in the business:

> He'll be a big asset to me because he's a very conscientious young fellow and he'll have some new ideas. My hardest job will be to respect his opinions. The biggest problem that I find a small business person has is delegating responsibility. We like to keep our hands on everything. We like

> to be the king pin. We don't want to release that responsibility. You really have to watch yourself. Sometimes you give it to them and you want to oversee it and they wind up being dependent on you. To be able to grow, you've got to turn it loose.

Another meat packer in a similar situation had found it helpful to simply absent himself from the business and pursue other activities as his son was entering a decision-making role with the company.

Integrating nonfamily managers. Firms making the transition from Family to the Adaptive Family Stage face the problem of incorporating nonfamily members into what has been a closed power structure. Professional managers may be at a disadvantage in the early years of their career with a family company. One observer of family business discussed this situation:

> The family member comes into a firm with eighteen years of experience with the firm. All is not hands-on operating experience, but much information has been conveyed informally. The professional manager may receive all he "needs to know" but family members will also have what is "nice to know."

If professional managers are not aware of family constraints, they are more likely to make decisions which come in conflict with family expectations. This analysis has indicated that such conflict is an evitable and useful part of the development of the family business relationship but managers who cannot foresee which of their decisions will produce it are not in a position to manage it effectively.

Dealing with new evaluators. When nonfamily members join the ranks of owners, top management becomes conscious of the added scrutiny which public ownership brings to the operation of the business. Several managers at Sunbelt Foods mentioned this. In the words of one, "We are very concerned about what institutional investors think about us." Nonfamily will evaluate the firm on its response to the competitive environment so that even family members will come to depend more on the proper response to the requirements of the business for their continued tenure in office than on their ability to meet family constraints.

Dealing with new systems. When the family decides to end its association with the company, family managers who remain must establish relationships with new owners. Their position in this is similar to that of a nonfamily manager entering the family firm. The family manager must learn a new set of constraints which may not be conveyed to him under the heading of "need to know."

Employee Adjustment

Employees in family firms are affected by transitions in the relationship. New family managers tend to enter the business at relatively high levels and may find themselves "managing" employees who have seen them grow up. This can create problems for all concerned unless the family member is given an opportunity to prove his capability and required to accept the consequences of his decisions. In most of the firms in the study, resolution of employee doubts about family managers was a function of time and the competence of the individual manager.

Practices. Related problems occur in the transition from Prefamily to Family. Employees may receive mixed signals about who has authority for which decisions or may continue old reporting patterns even though new ones have been instituted. The introduction of new management policies by an acquiring firm also requires employee adjustments as the relationship moves into the Postfamily Stage. The former manager of the meat packer which sold to the large co-op reported the differences in management practices:

> We had operated informally. If an employee wanted four or five hundred dollars for a car, he'd ask for it from us and usually get it without signing a note. If they wanted off to go fishing, we'd let them go if we could. It was loosely run, but we still got the job done. Of course the corporation has a lot of benefits that we didn't offer. They get more vacation, sick leave, and insurance, but they also require people to be there. The employees really had more problems adjusting to the change than we did.

Opportunities. Transitions in the relationship can alter opportunities for both family and nonfamily members to attain high positions in the firm. Family members may be given opportunities in the business because they are family members, but there is pressure to maintain a high performance level. The president of one firm referred to this pressure as a policy of "loading them up to see what they can carry."

While family members felt that this applied to family and professional managers alike, at least one observer of the firm felt that professional managers would be wise to temper their aspirations with the recognition of "a distinct trend or philosophic bent in the [company head's] thinking that he would like to see the family run the company." A nonfamily manager elaborated:

> A situation in which stockholders get involved in a fight over who will be titular head of the company . . . is a potential problem in any company and I'd be crazy not to recognize it, but there are several reasons why I don't think it will happen here. Even if you have a dog fight, or whatever, you have very capable people involved so whoever emerged as the person who is running the company, you'll have a capable person. You've also got a good close working relationship among the family and nonfamily people and there's a great deal of mutual respect. Those circumstances make it less likely.
>
> It will be interesting to see how this company manages. There's a good deal of family and a good deal of stock owned by family. A sufficient amount probably do pretty much what the family wants to do.

Anticipating the effect of adaptations in the family business relationship and minimizing dysfunctional conflicts by making new expectations explicit are part of the transition process.

Long Term Control:
Assessing Trade-Offs

Transition in the family-business relationship moves the family from a central to a peripheral role and ultimately out of the business over some time span. Transition may also be viewed as trade-offs in which complete control of the business in the short-run is given up for less than complete control for a longer period of time. This is particularly true of the transition from Family to the Adaptive Family stage. In the baking industry, the options were to grow to achieve economies of scale or to become increasingly less efficient. Public sale of stock and the accompanying decrease in family control were chosen as the best means to grow for Sunbelt Foods. By making this choice the company survived and prospered:

> What we've done is to buy people who have gone bankrupt or are no longer making any money because they haven't put any new equipment in because they just simply didn't have the vision. They're being shut down every day. . . . The industry is concentrating. The Chairman was one of those smaller people fifteen years ago. He had the vision and the intelligence to see what was happening and he knew if he sat right here with one single plant, in ten years' time, he'd be like the others.

Recognizing and assessing the trade-offs between short term and long term control is one of the prime difficulties of managing the family-business relationship.

Conflict Resolution

The presence of differing opinions and the need to accommodate them affects the response time of the business, the quality of decisions, and the flow of operations.

Response time. The move into the Family Stage from the Prefamily stage by definition involves an increase in the numbers of family members who must agree or at least not oppose important decisions. The need to achieve consensus can slow down the strategic processes of the firm:

> My father and four sons each took an area of operations. We sat down and discussed problems and issues. If everybody was in agreement 100% we went ahead right then. If not, we would discuss it further until agreement was reached.

A meat packer reported the process of deciding to buy a slaughtering facility in a neighboring town:

> We had an opportunity to buy a plant that would increase our capacity and put us in a position to really grow. We were very excited about it and thought it was a good opportunity. My uncle had to be convinced. He reminded us of what the company had gone through in the Depression and talked about the evils of debt. In the end we convined him, but we made the purchase on a lease-purchase plan rather than buying it outright to reassure him. He was always warning us to slow down, but we usually persuaded him to our point of view.

Quality of decisions. The presence of differing opinions which must be accommodated can produce a better analysis. One of the meat packers felt that the fact that he had not had to argue for his decisions had produced mistakes simply because he had not thought through the implications of what he was doing. The need for accommodation can also produce "squabbles" as it did at Valley Foods Company.

Disruption. When conflict in a family firm becomes chronic and personal as it did at Valley Foods Company (see Chapter Three) and at one of the meat packers, it is usually resolved by removing one or more of the combatants through sale of stock or an end to the association through liquidation of the business. This is a disruptive process and is quite different from decontrol through sale of stock.

Managing Information Flows

Some conflict in family firms may be traced to lack of accurate information by family members which results in the formation of unrealistic constraints. In some firms, the only contact family stockholders have with family management is at the annual stockholder's meeting and the only information they receive is an annual stockholder's report. At the other extreme, family stockholders may take an interest in even the most trivial details and because they have frequent contact with managers are able to satisfy their curiosity and make their opinions known.

Business to family. The difficulty for the manager is to balance the amount and type of information which the family receives. A manager at Valley Foods Company reported that family members were "only interested in the amount of dividends." Without information about the strategic plans of the company and the competitive environment, it is difficult to evaluate the dividends.

It is also possible to either present too much information or to phrase it in technical terms which mean nothing to the family stockholder. One such stockholder made the following complaint:

> Sometimes when my brother would talk to me about what was going on, I really didn't understand. I'm not a business person.

When demand for information about the business is high, managers can attempt to meet it or to reduce the demand. Good performance was viewed by managers in the sample firms as the primary means of reducing the demand for information.

Environment to business. Problems of managing decontrol, employee adjustments, assessing trade-offs between long term and short term control, persuasion and conflict resolution, and managing information flows to stockholders which accompany adjustment and adaptation of the family-business relationship are exacerbated by the need to make a quick response. Early recognition of changes in the environment provides management with the opportunity to evaluate the effect on family constraints of proposed changes in business activities and to smooth whatever conflict is likely to occur. When management is slow to recognize such changes, response may be delayed until it becomes a matter of survival and there is little opportunity to deal with family constraints until after the fact. The effectiveness of environmental scanning procedures and the incorporation of environmental change information into decision processes is a crucial element in the family-business relationship.

Alternate Paths of Development

Examination of the histories of the sample firms indicate differences in the paths of development taken by individual relationships. Relationships may be divided into two groups; those which move through the stages in sequence will be refered to as evolutionary, while those relationships in which stages have been skipped will be termed sporadic.

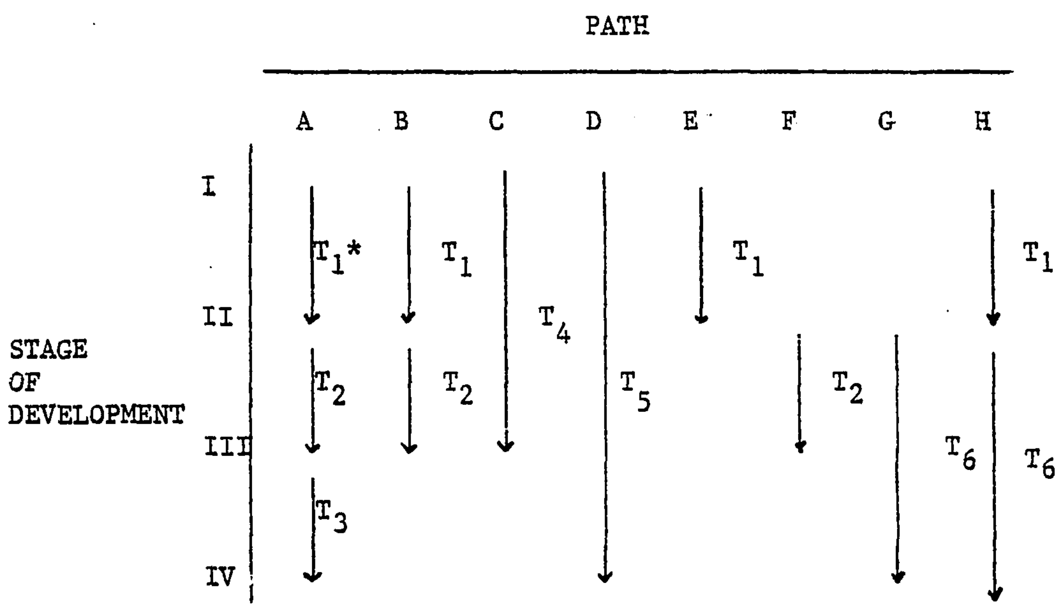
Analysis of paths of development depends on the recognition of the variety of transitions which are possible. Based on four stages of development, the following six transitions are possible:

Transition $_1$	Stage I to Stage II
Transition $_2$	Stage II to Stage III
Transition $_3$	Stage III to Stage IV
Transition $_4$	Stage I to Stage III
Transition $_5$	Stage I to Stage IV
Transition $_6$	Stage II to Stage IV

Figure 4-2 depicts the possible sequences in which these transitions can occur and indicates the frequency of these sequences or paths of development in the sample firms. As the frequency chart indicates, the sample data permit observations about only four of the paths.

Evolutionary Development of Family-Business Relationships

The majority of the sample firms have made only one transition in the relationship and that has been the move from Stage I to Stage II. One firm has made the additional



	A	B	C	D	E	F	G	H
Frequency of path in sample**	0	1	0	0	6	1	0	1

*T_1 = Transition from Stage I to Stage II
T_2 = Transition from Stage II to Stage III
T_3 = Transition from Stage III to Stage IV
T_4 = Transition from Stage I to Stage III
T_5 = Transition from Stage I to Stage IV
T_6 = Transition from Stage II to Stage IV

** Frequencies do not sum to 12 because 3 firms have made no transitions. One of these is expected to follow path D, one path E, and one path G.

Figure 4-2: Paths of Development of Sample Firms transition to Stage III from Stage II. The absence of disruptive conflict seems to be the primary similarity among these relationships.

Paths B and F

The option of selling stock to the public was not available to many of the sample firms because of their size or the uncertainty of their future. The desire to maintain complete family control would deter some firms from following this path (Specialty Sauce probably falls in this category) even if other factors were favorable. A combination of competitive challenges in the snack industry and increasing family expectations for the business prompted Sunbelt Foods to take this path.

Path E

Making the transition from a business dominated by the owner-founder to one in which his descendants share ownership and management of the business is the essence of the often expressed desire of managers to "build something for my children." Maintaining the relationship in the family stage is, on the other hand, the essence of the desire of family managers to "protect what Daddy worked so hard for." Family constraints, in short, are most likely to promote this path of development as long as competitive factors do not interfere.

The evolutionary paths observed in the sample occur in relationships in which the importance of family control and the trade-offs involved receive explicit attention. In other family-business relationships, stages were skipped.

Sporadic Development of Family-Business Relationships

Among the firms in the sample which have skipped stages in their development or seem likely to do so in the near future, family values are not strong or have been displaced by a crisis.

Path D

Family participation has fluctuated at Country Eggs with the owner-founder initially inviting family participation and then discouraging it. He described himself as having a "different philosophy" about family business and has taken steps to assure the company's evolution into a Stage IV (Postfamily) relationship. This plan was said to be an outgrowth of the personal value system of the founder-owner rather than the result of any undesirable characteristics of his family.

Path H

One of the meatpacking firms dissolved the family ownership of the business because the changing cost structure of the industry required a greater investment than the family was willing to make. Valley Foods seems likely to follow a similar path because of irreconcilable differences among family members concerning the management of the business. In both cases, the family association had lost its power to motivate family members to make the sacrifices necessary to maintain family control.

Sporadic development usually involves the loss or diminution of family control and the curtailment of family participation in the business. Sporadic development is likely to be viewed as undesirable when family control and participation are important to family members. Both evolutionary and sporadic paths of development result in diminished family control over some time period. In an evolutionary path, however, there is a greater chance that the loss of control can be made to work to the advantage of both the business and the family in that loss of control results in a greater resource base and family participation continues.

Arrested Development in Family-Business Relationships

The discussion of paths of development has focused on the sequence of changes. Timing is also an important factor. Sunbelt Foods has moved through three stages during the career of one manager while Specialty Sauce has remained in one stage longer than the lifespan of a given manager. At some point, it seems reasonable to consider the development of a firm "arrested" to the point that the characteristics of the relationship at that stage are permanent. Managers in this situation will be more concerned with adjustments than with transitions. Managers in the opposite situation, relationships which are changing or have the potential for change because of environmental conditions, have more complex choices to make in determining whether adjustments or transitions will be most beneficial to the relationship.

Summary

The characteristics of firms in the sample have been reviewed in this chapter and the key elements and processes in the family-business relationship have been explored with data from the sample firms. The relationship has been described as receiving impetus for change from two sources, the pressures of doing business and the constraints of the family. Actual changes in the relationship take two forms. Adjustments between the business requirements and the family constraints involve changing constraints by influencing family members or changing business strategy, policies, or decisions to match family constraints. The alternate response involves changing the structure of the relationship which has the effect of moving the relationship to a new stage. Four stages of development and their characteristics were described. Finally, the differences between alternate paths of development were explored.

The implications of the findings and analysis are discussed in the chapters which follow.

CHAPTER FIVE

IMPLICATIONS AND RECOMMENDATIONS FOR MANAGERS IN FAMILY BUSINESS

The task that remains for this research report is to link the findings of the research presented in Chapter Two and the supporting and illustrative data and analysis presented in Chapters Three and Four with managers and family members who must function in family-business relationships and with academic researchers who wish to explore the relationship or related issues further. The purpose of this chapter is to move from a descriptive to a prescriptive mode to suggest ways that managers can use the insights generated in the research to manage the family-business relationship. A related purpose is to suggest ways that family members can become more effective partners in the relationship. Chapter Six examines the implications of the findings for future research through a set of propositions.

Managing the Family-Business Relationship

The findings of the research point to a contingency approach to the management of the family-business relationship. It would be logical to consider the stage of the relationship as the appropriate contingency on which to base such an approach. It should be noted, however, that while the stages set the context for managerial activity and define the characteristics of family-business interaction, they are based on aggregate relationships. That is, they indicate how the family as a group will relate to the business as an institution. The stage of development defines interactions, but it does not indicate the resources which a particular manager brings to his task. These resources are a function of the individual's influence in the business and in the family and must be considered separately. The role of power and influence in business situations has been explored by Bower (1961) and Zaleznik (1975).

A second implication of the research is the importance of the competitive environment to the family-business relationship. The impetus for change in the relationships came frequently from the environment and the impact of the environmental setting of the management task must also be considered.

The findings of the study suggest that the manager should assess his role in the family-business relationship in terms of the bases of power that he is able to exploit in the family and the business and in terms of the characteristics of the environment of the business. These concepts are discussed below and recommendations based on the concepts follow.

Managerial Requirements for Making Adjustments and Transitions in the Family-Business Relationship

A manager in a family business has several bases of power which he may exploit to adjust constraints of the family or to initiate and guide the process of transition. Bases of power in the business include position in the management hierarchy with higher positions conferring greater power, stock ownership with larger percentage relative to other stockholders conferring greater power, and experience in the business. Bases of power in the family include seniority and the ability to influence senior family members. These bases of power will determine the extent to which the manager can adjust family constraints to the competitive requirements of the business and give indications about the skills that will be needed to manage the relationship. Figure 5-1 shows two bases of power, the business and the family, and divides each into high and low sectors. The resulting four quadrants are described below.

		POWER IN THE FAMILY	
		High	Low
POWER IN THE BUSINESS	High	Action	Negotiation
	Low	Counseling	Mediation

Figure 5-1: Managerial Orientation as a Function of Family and Business Power of the Individual Manager

Action

The manager who finds himself in a position of power in both the family and the business may be the object of envy of other managers in more ambiguous situations. This manager may be the owner/operator of a small business or the chief executive and largest stockholder of a larger business. A third possibility is that he is the senior member of a family in which no one stockholder has a large share of stock. This is the manager who is in the position to exploit flexibility and, in the words of Cohn and Lindberg, to "turn thought into action."

The manager in this position must be especially conscious of his own priorities in that many adjustments of family constraints and competitive requirements will be internal. That is, the family constraints may be nothing more than the powerful individual's personal objectives. The decision to expand at Sunbelt Foods was a personal one, for example:

> [The older son] planned and made the decision that he wanted to try and build a large food manufacturing and marketing company versus being content with a small, privately held operation. It was a challenge to him.

This can make it easier or more difficult to adjust constraints, depending on the commitment of the individual to his objectives and his assessment of the importance of making the adjustment.

Skills. The manager in this position must develop skills of implementation of strategic and operating decisions. In smaller firms these processes will be mostly direct while in larger firms, the implementation of strategy will require the appropriate organization and management systems. A manager at Sunbelt Foods stressed the importance of leadership:

> Business deteriorates from the top down, not from the bottom up so it all depends on who's running it and what they're going to tolerate.

Another manager made a similar statement:

> He's [the older son] a very demanding person and you don't often see a very successful company without demanding people in positions at the top. He works hard himself and he expects others to.

Pitfalls. The managerial pitfall in this situation is the tendency to view the business as an extension of the powerful manager rather than as an entity in itself. This tendency can result in a failure to provide for succession or to otherwise make adaptations in the relationship. Even at Sunbelt Foods, this tendency was felt:

> He has never been anything but the boss of a company that has grown and become very successful and he will be an extraordinary man if he really can turn lose of the reins. That's the problem; it's not that he doesn't have the vision; it's just simply that it has to be the hardest thing in the world to do. People necessarily always think that there's nobody who can do it quite as well as they can. It's to his credit that he has capable young people. It's to his credit; he brought us in. But no matter

> how capable we may be or he may perceive us to be, he will probably never be able to genuinely decide that those people individually or collectively are more competent than he is.

Negotiation

When a manager has relatively high power in the business but relatively low power in the family, he must depend on negotiation skills. Like the manager in the Action quadrant, he will be judged on the performance of the firm, and his ability to make and implement strategic decisions should earn him credibility where he does not have power. At the same time, when family constraints conflict with the competitive requirements of the business, he does not have the power in the family which the Action manager has to adjust family constraints so he must rely on his political skills to achieve the same ends. The fact that the manager has power in the business gives him a base from which to deal with powerful family members who are presumably dependent on him to a certain extent for expertise in operating the business. Because of his business clout, this manager can afford occasional confrontations but should not allow them to become habitual.

The family manager at Valley Foods was in this situation and emphasized the importance of negotiated decisions:

> I always thought that in a family organization there was a lot of give and take. Everybody has to give and everybody has to take and it's not a matter of always someone giving and always someone taking.

Problems in this quadrant come from the frequency of confrontations between family and management. Since both are operating from positions of power, political maneuverings may subvert the decision process completely. At Valley Foods this occurred:

> When you get enough stockholders outside of the business who are dissatisfied and they are the majority, then they can do anything they want and that's what happened.

Counseling

A manager in a family firm may find himself with low power in the firm for several reasons. He may be one of several managers none of whom have much power individually. He may be appointed successor to a strong leader who never quite steps down. In the opposite situation, he may be still in the business to guide his successor but may have delegated so much of his authority that he has effectively transfered power though he remains in the business. In any case, the manager still has a good deal of power in the family either from seniority or experience or both but has abdicated much of his business power. The role of the manager in this position is that of counselor. He may have much to offer in advice and consultation and will probably have opinions about a wide range of decisions, but his best contribution to the family-business relationship will be to use his influence to smooth the way for the adjustments which others will make. One manager said of his father, "I leaned heavily on him and didn't realize until he was dead how much."

The acceptance of this managerial role may involve a change of style which is difficult for some and impossible for others. Individuals who have developed skills in implementation and bargaining may not be able to take a lesser role. The danger is that managers with declining power in the business will continue to act as if nothing has changed and the development of implementation skills and bargaining skills by other managers will be hindered. One manager anticipating the entry of his son into his business said:

> I'll have to be careful because it's so easy to dominate. You've got to realize this is a young man that's got ideas and you have to listen to him and you have to give him room to express some of his ideas and to try some of these things.

<u>Mediation</u>

The manager who finds himself with little power in both the business and the family is in the most precarious position of all and will need considerable interpersonal skills in dealing from a low power position with both family and business. A former manager in a family business described his role as follows:

> I was in the position of trying to build a compatible relationship between the three [brothers]. I also performed as a sort of "devil's advocate" in hammering out decisions. Sometimes you can prevail as the loyal opposition but, if not, you have to go with the boss completely to make the decision work. When you become employed and

> expect your life to be spent and fortune to be cast with a family business, you have to accept your position.

The ability to generate support will depend on the personal competence of the manager and the ability to communicate that competence in his dealings with individuals.

Assessing Power in Roles

Two further implications of this analysis are critical. The first is that the less power the manager has the more skills he must develop when he is in a family business. For the most powerful role, it is enough that he do his job well. Other managers are no less responsible for execution of their tasks but must also develop political, diplomatic, and interpersonal skills to facilitate the process of adjusting family constraints and competitive requirements of the business.

The second important point is that the ability of the manager to accurately assess the power that he holds will go a long way in guiding his behavior into appropriate paths. The findings of this study provide some insights into what constitutes family and business power. Power in the family is largely a matter of circumstances which follow the organization of the family. Seniority is very important in a family and the oldest brother, uncle, or cousin is likely to have more influence with younger members of the family even when their stock holdings are similar in size. A father retains influence over his sons as a result of a lifetime pattern which began in infancy. Sex is also a determinant of family power although the firms in this research did not present any variation in the male-dominated business pattern that would allow comparative analysis. Any females involved in these business had nonmanagerial positions and did not actively influence the family in business matters.

Beyond sex and age family power also accrues to those family members whose experience and expertise in the firm contributes to the enforcement of family constraints. Former managers who have retired or who have gone on to other jobs are likely to have more power in the family than family members who have little knowledge of the business. By the same token family members who have experience and expertise in any business have more power than those who are not businessmen at all.

Power in the business stems from the position of the manager in the managerial hierarchy and from the experience and expertise which the manager brings to this position. It is not usually possible to assess the power which a manager in a family business wields by simply looking at the organization chart. Family managers tend to make informal arrangements among themselves concerning division of power and the organization chart does not always reflect these arrangements. In one firm in this study, the manager insisted that his father was the most powerful person in the business even though he had neither a managerial position nor stock in the business. The manager in the family business must develop a tolerance for sporadic second-guessing of his decisions while at the same time working to prevent those circumstances from becoming dysfunctional to the family-business relationship.

Table 5-1 lists determinants of power in the family-business relationship.

Table 5-1: Determinants of Relative Power in the Family-Business Relationship

Family power is increased by:

Seniority of manager in family

Ability of manager to influence senior family members

Experience of family manager in business

Business power is increased by:

Higher management position

Longer tenure

Greater expertise

Amount of stock relative to other stockholders

Influence with outside suppliers of resources

The ability of the manager to adjust family constraints as well as the techniques he might use depend on his power base in the firm and in the family. A manager in a family business must consider his position in relation to the family as well as his role in the business. In some businesses, this is the critical consideration because no matter how competent the manager is, he cannot do his job if he cannot maintain his position.

Assessing the Environment

Family businesses are not unique in facing changes in the competitive environment which require strategic responses. All such changes which family businesses face do not require adjustment of the family constraints. Managers must recognize such changes and make the appropriate strategic responses and part of this strategic process will be to determine how the response will affect the family-business relationship and what managerial action, if any, will be necessary to insure that the strategic response is consistent with the family constraints.

Certain areas, notably personnel acquisition and use constraints and financial constraints, seem to require more adjustment than others. Managers should assess the impact of strategic decisions on the firm's ability to absorb family members into management at any given level as well as the expertise required and the mode of training. The establishment of professional standards and job-oriented experience and training requirements is always desirable but may be impossible or impractical to implement in a family business, which exists, after all, for the family.

A change in the competitive environment which requires increased level of financial resources is likely to conflict with family constraints by curtailing dividends or introducing outside investors. Some firms avoid debt as a matter of family policy while others rely excessively on debt to avoid confronting family constraints. While it is easy to prescribe that managers base financing decisions on established criteria for such decisions, given the political nature of such considerations, this is not very practical advice.

At this point it is useful to consider the nature of the competitive environment which the firm faces. While all firms deal with change, there are differences in the rate and intensity of change with which firms must deal which are relevant to the management problems of the family firms. Figure 5-2 shows four possible combinations based on the number of changes which the firm must deal with over some time period and the potential impact of these changes. The management of the family-business relationship should be suited to the situation in the competitive environment.

		NUMBER OF CHANGES	
		Few	Many
POTENTIAL IMPACT OF CHANGE	High	I	II
	Low	III	IV

Figure 5-2: Competitive Environment of the Family Business

Many High Impact Changes

None of the firms in this study fell into this classification. While the literature of organization theory suggests how organizations adopt to such an environment structurally, none of these deal with questions of stockholder relations, let alone family relations. Some have suggested that some characteristics of family business make it unsuitable for such an environment (Glueck, 1972). The actual incidence of family business in such environments is an empirical question not addressed by this study, but the findings did provide some insight into the issue.

The family business deals with change on two levels. One is the business change itself and the other is the change in family constraints and the relationship itself. The relationship is limited in the number and kinds of adjustments it can make and the more changes it encounters with potentially high impact the more likely the relationship will pass through the stages of development and out of the family business category altogether. The other possibility is that dealing with both levels of changes strains the resources of the manager to the point that the business does not survive.

Few Changes with High Potential Impact

Managers who deal with changes in the competitive environment only sporadically may be slow to recognize the need for a response and slow to respond. This may be something of an advantage when the correct response is more important than a rapid response and the cost of error is greater than the cost of slowness. The examples of other firms also dealing with the change may be useful in persuading family members to adjust their constraints. The more protected the market share of the company, the more readily the manager can adopt a wait and see attitude.

Infrequent, important changes are likely to call for significant shifts in strategy and have potentially great effects on family constraints. These potential effects should be incorporated into the strategic thinking of the manager and alternatives for dealing with them should be considered.

Many Changes with Low Potential Impact

The cumulative effect of many relatively minor changes may require adjustments of the family constraints or changes in the family business relationship which go unrecognized because the impact of any given change is not great. The manager in this situation is likely to be surprised by the sudden appearance of family intervention. Managers should periodically assess the status of family constraints and competitive requirements and provide key family members with relevant information so that the cumulative impact of change is not a shock.

Few Changes with Low Impact

This is the environment which some argue is most suitable for family businesses. Managers have few changes to deal with and there is less likelihood of the family losing control because of continual adaptations of the relationship and less problems in the relationship because constraints do not have to be changed. Such an absence of competitive pressures is rare although some firms may experience such a situation for extended periods of time. Management should probably not view such good fortune as permanent.

Recommendation to Managers

Top managers in family businesses may be either family members or nonfamily managers. The family association is commonly regarded as giving the family manager an edge over the nonfamily manager in managing the family-business relationship, but the findings of this study suggest that it is the ability of the manager to exploit his bases of power in both the family and the business that determines how well he manages the relationship. It is not the family association *per se* but the use the manager makes of it that is important. The following recommendations apply to both categories of managers.

Awareness

The first recommendation is that top management explicitly incorporate the concept of the family-business

<u>relationship into their conceptual model of the business and its environment</u>.

The findings of this study point to the existence of a relationship which has an impact on internal strategic processes and therefore on the strategic responses of the firm. While some of this impact is related to the process itself, it is also possible for a manager to take an action and then feel the impact as conflict over the action or as a reversal of the decision. The fact that the impact tends to be issue-oriented further complicates the situation. That is, while the potential is always present, it is usually evoked only periodically so managers are subject to a false sense of being able to ignore the family-business relationship. In practical terms this requires the manager to be aware of the potential sources of conflict in the relationship as well as have some notion of how family members rank priorities for the business and which family members are able to enforce their ranking.

It is in the need for awareness that the family manager may have an advantage over his professional counterpart although the professional with a long tenure becomes something of a family member. Family bases of power shift however, and family constraints change so that managers who operate on impressions gleaned in the socialization process may be in for an occasional surprise as time passes. Long tenure or close association with the family does not, by itself, guarantee that the manager understands the current situation. Periodically the manager should ask the following questions:

1. What does the family expect of the business? What is my evidence for this?
2. Do family members agree on these expectations? If not, who can enforce their constraints? Who is most likely to enforce them?
3. What issues have caused adjustments and transitions in the family-business relationship in the past? How smoothly were they accomplished? What can be learned from that experience?

Assessment

The second recommendation to managers is to assess the current status of the relationship and the bases of power from which the manager is operating.

Awareness of the family-business relationship and the potential issues which could require adjustment or transition in the relationship must be coupled with an assessment of the status of the relationship and the bases of power from which the manager is working. By knowing the stage of the relationship, the manager can judge the relative merits of adjustment versus adaptation and his bases of power will give him some idea of what he can do (see Table 5-2). If this is done periodically, the manager is in a position to develop the skills which are appropriate to his power position before the need arises to test those skills. The recommended assessment can be made by asking the following questions:

Table 5-2: Factors Affecting Feasibility of Managerial Responses

Maintain relationship by making change in family constraints if:

1. Top management of firm is senior family member
2. No family member claims more expertise in business than top managers
3. Top management is personally close to most powerful family members
4. Firm's performance has been such that family members have confidence in management
5. Firm has achieved stability before by changing family constraints
6. Family has other sources of income

Maintain relationship by changing competitive requirements if:

1. Barriers to exit are low.
2. Market niche is protected

Change structure of relationship to restore stability if:

1. Family dependent on firm for income
2. Rate of growth has been rapid and change has been frequent
3. Other attempts have failed
4. Performance has suffered

Ignore change in family constraints if:

1. Family power is weak relative to management
2. Family change can be counteracted by additional information

Ignore change in competitive requirements if:

1. Market share protected in some way

1. What is the stage of the family-business relationship? Have adjustments been made within this stage? Are further adjustments possible? Under what circumstances would a change in the structure of the relationship be necessary?

2. How much informal influence do I have with powerful family members? How much stockholder support can I muster?

3. Does my experience and expertise in the business make me hard to replace?

4. Do managers in the business generally support me? Do any of these managers have more power in the family than I have?

Anticipation

It is recommended that efforts to manage the relationship focus on information handling. Armed with an assessment of the status of the relationship and his position in it, the manager should be able to anticipate how changing family constraints and changing competitive requirements will interact and to take steps to actively manage the relationship. As family and business become increasingly separated, family constraints may become less realistic, more subject to capricious change, and less easily adjusted to competitive requirements.

Both the nature of the information received by the family and the formal and informal channels through which the family gains access to management are important.

1. Is the family properly informed about the business?

2. Does the family have channels of communication with management which allow conflict confrontation and resolution rather than promote escalation?

3. Is informing the family incorporated into the implementation of strategy?

Participating in the Family-Business Relationship: Role of the Family Stockholder

While the primary focus of the study was the managerial implications of the family-business interaction, it is appropriate to consider whether the findings have any implications for the other participant in the relationship--the family stockholder. Stockholder roles in the sample firms ranged from the passive, trusting attitude of the family of Piedmont Meats to the activists at Valley Foods. Most family members fall somewhere in between the two extremes. Their opinions are expressed privately rather than through stockholder uprisings or suits, but they do have opinions. While it is tempting to assert that more productive relationships avoid the extremes, the data indicate that these roles may be as much a matter of family style as anything. Rather than prescribing stockholder behavior, these recommendations will take the form of general suggestions concerning family participation in the different stages and how family members can facilitate or hinder the processes of adjustment and transition.

The Family in the Stages

The first stage (Prefamily) and the last stage (Postfamily) of the relationship are by terminology and definition stages in which there is little or no opportunity for family involvement other than that of family members employed in the business. The lack of involvement in the first stage is likely to result from the predisposition of many entrepreneurs to maintain close and undivided control of operations or from the fact that family members are too young to be more than peripherally involved. The lack of involvement in the last stage by nonmanagerial family is a matter of the legal right to be involved being severed by sale of family stock. In the second and third stages, ownership of stock together with personal acquaintance with business leaders provides many opportunities for interaction between family members and managers. In Stage II (Family) particularly, the central role of family members in providing resources to the firm can lead to a kind of blackmail if family support is withheld pending management favors.

<u>It is recommended that family members recognize the effect of any perquisites received on the income of the business and thus on family returns</u>. Family members have the right to define their returns as they see fit. They should however be explicit about the trade-offs they may be making.

<u>It is recommended that family members meet management efforts to keep them informed half-way</u>. Attendance at stockholders' meetings and reading the stockholders' reports are the point at which their effort should start. Managers give cues as to the level of family participation they seek, and family members should try to meet these levels. Several

managers reported frustration with stockholders who showed little interest in the business.

It is recommended that family members consider that their requests for information constitute additions to overhead costs and moderate them as much as possible. A family member in doubt about the reasonableness of his requests might compare the type and frequency of data he requests to what is available to a stockholder in a publicly-held corporation. A family member in a Stage III firm might also compare what is available to him as a family member to what is available to nonfamily stockholders.

It is recommended that family members view the Board of Directors as their representatives and should work to change the composition of the Board when dissatisfied but not meddle in the business. Direct intervention by family members in the affairs of the business serves no useful purpose and can severely hinder the process of replacing personnel if the goal is achieved.

The Family Role in Adjustments and Transitions

The findings suggest a complimentary relationship between adjustments and transitions which should be considered by family members when enforcing their constraints for the business. This relationship is simply that adjustments can, at least in the short run, prevent transitions. As long as discrepancies in the requirements of the business and the constraints of the family can be adjusted, transitions, in particular those beyond Stage II, can be avoided. It follows that one way to avoid losing family control is to make adjustments in family constraints as needed. The irony is that the ability to enforce family constraints is the heart of family control.

If family control, particularly the trappings of family control, is an important family value, it is recommended that family members be ready to make adjustments in family constraints and to promote these adjustments with other family members.

If financial performance is important, it is recommended that family members assist and promote the process of transition.

These two recommendations reflect a trade-off between short-run control and long-run financial returns. The family is unlikely to be able to fund the growth of the firm indefinitely and some control must be offered to new providers of resources. Partial relinquishing of control to acquire new resources is likely to preserve family participation in the business and may result in an equal or greater return. It also enhances the liquidity of the family investment which may be a more useful feature of the loss of control.

It is recommended that family members inventory their significant constraints for the business and inform management. It is the joint responsibility of family members and managers to see that family constraints are not violated through ignorance when awareness of the constraint would have indicated an equally satisfactory alternative. It is always easier to play the game if you know the rules.

The role of the family member in the family-business relationship is primarily one of providing support and resources for managers. This role will be a more productive one if family members recognize the limits of their privileges as well as the extent of their responsibilities.

Summary

The family-business relationship should receive explicit attention from both managers and family members. Managers must be aware of the bases of power from which they operate and use their position in the communication system to direct the relationship. Family members should recognize that participation adds to overhead and should restrict their activities. Family members who place prime importance on maintaining family control of the business should make a practice of adjusting family constraints to meet the requirements of the business. Family members who are concerned about financial returns and liquidity of investment should support transitions.

Propositions concerning the family-business relationship and directions for future research are reviewed in Chapter Six.

CHAPTER SIX

IMPLICATIONS FOR FUTURE RESEARCH

When research is of an exploratory nature, it is expected that the findings will not only provide some immediate insight for managers into the subject of the inquiry but will also generate questions which will provide the direction for future research. The purpose of this chapter is to consider what directions future research into family business might profitably take. The first part of the chapter deals with general implications of the descriptive framework while the last part presents a series of propositions dealing primarily with the dynamics of the family-business relationship.

General Implications

Utility of the Framework

The concept of stages of development of the family-business relationship has proved to be a useful way of thinking about the interaction of family and business in the firms in the sample. The generalizability of the framework is an issue that requires more formal statistical procedures including a random sample of businesses. Factors such as size and complexity and volatility of environment should receive explicit attention in such a study.

Future research should take into account the differences among family firms indicated by the stages of development and beware of using a unitary concept of family business.

Family Constraints

The findings of the research indicate that family constraints are a key factor in the development of the family-business relationship. The study has assumed that these constraints are readily and accurately perceived by management. The speed and accuracy by which constraints and changes in constraints are perceived should be related to communication processes in the relationship and to the performance of the firm.

A comparison of constraints between family firms at different performance levels and in different competitive environments would give some indication as to how and whether family members fit constraints to specific situations.

Finally, it would be useful to determine how family members rank constraints and whether this ranking differs with changes in variables such as size of firm, power of family, participation of family in business, and nature of environment.

Competitive Environment

An effort was made in this study to choose firms with fairly similar competitive environments. The incidence of family firms in different competitive environments should lead to some conclusions about how specific environmental variables affect the family-business relationship. In this context it would be particularly interesting to identify environmental situations in which few family firms exist and identify the correlates of success in those firms.

Comparative Studies

While many have examined the consequences of management control as opposed to owner control, these comparisons include family businesses on both sides. It would be helpful to explicitly compare family businesses and nonfamily businesses along such variables as the speed and nature of responses to changes in the competitive environment, the constraints which managers perceive to be operating under, and the performance of the firm.

Another area of interest would be a comparison of the transition process based on subsequent performance of the business.

Strategic Management

Readers familiar with the work of Bower (1961) and Zaleznick (1975) will not have been surprised at the emphasis on political processes found in the study. The findings provide further evidence of the importance of explicitly incorporating political factors and considerations into any examination of the strategic management process. The dynamics of the power relationships are explored further in the propositions.

Propositions

The key finding of the research dealt with the way the family-business relationship developed through a series of stages as a result of a process of adjustment and transition to changing family constraints and competitive requirements of the business. This descriptive framework for the family-business relationship explains the diversity found among family businesses and also predicts how the relationship will develop.

The purpose of this study was to provide a descriptive understanding of the family-business relationship in order to provide a theoretical foundation for further research as well as to provide insights for managers and owners of family business which will assist them in managing the family-business relationship. The propositions represent an attempt to identify areas for management attention and suggest what form action should take as well as to highlight relationships for further testing.

Dynamics of the Family-Business Relationship

The first propositions deal with the process by which the changing family constraints and competitive requirements of the business are brought into congruence.

> Proposition 1(a): A change in the competitive requirements of the business must be met by a corresponding change in the family constraints for the business if the two come into conflict as a result of the initial change.

Proposition 1(b): A change in the constraints which the family has for the business which affect the ability of the firm to meet its competitive requirements will require a redefinition of the competitive environment.

Proposition 1(c): If corresponding changes are not made to match family constraints with the requirements of the business, the family-business relationship in its existing form will become untenable and the relationship itself must be adjusted.

The tension between the constraints which the family places on the business and the requirements of the competitive environment have been noted by several students of family businesses and are a specific instance of the larger problem of general management of matching the strategic competancies and objectives of top management to the threats and opportunities which arise in the environment.

Determinants of Managerial Power

The manager in a family business must deal with a stockholder constituency to which he has ties which go beyond the traditional economic and ethical responsibilities by the manager to the owner. He must also (if he is a family member) deal with the fact that his own objectives may be internalized family constraints and thus be in potential conflict with the requirements of the business. The power of top management relative to the family is a function of several factors and sets the bounds on managerial responses to changes in constraints and requirements.

Proposition 2(a): The fewer family members who have equal or greater experience in the business than top managers, the greater the freedom of the manager to choose an appropriate response.

Proposition 2(b): The more family members who are managers in the business relative to family members who are stockholders, the more freedom the managers have to choose an appropriate response.

Proposition 2(c): The better the track record of management, the more freedom they are likely to have to make an appropriate response.

Proposition 2(d): The larger the proportion of stock owned by management, the more freedom they are likely to have to choose an appropriate response.

These propositions lead to the following general propositions concerning the political elements of the adjustment process.

Proposition 3(a): The more bases of power which the management has relative to the family, the more freely management will be able to adjust the constraints of the family to the requirements of the business.

Proposition 3(b): The more bases of power which the family has relative to top management, the more limited management will be in adjusting the constraints of the family to meet the competitive requirements of the business.

One result of this limitation of responses is to ignore the inconsistencies or to treat them as temporary. If the competitive environment is changing rapidly or if family power is likely to shift in the short term this may be a satisfactory response. Another strategy is to enlist the help of outsiders. Bankers, lawyers, accountants, consultants and other outsiders with either expertise in certain areas or an ability to establish constraints for the firm because of their relationship as resource suppliers may increase the options of a relatively weak management.

> Proposition 3(c): Outsiders who supply resources to the firm are a potential base of power for management.

Adjustment and Performance

While family constraints should not be construed as a hindrance to the manager's attempts to meet the competitive requirements of the environment, the assumption is that such requirements should come first in strategic decisions. This assumption is formalized in the following proposition.

> Proposition 4(a): Family business-relationship benefit the long-term performance of the firm to the extent that family constraints are adjusted to the competitive needs of the business in a timely fashion.

When a point is reached at which family constraints cannot be adjusted for whatever reason, the relationship itself must undergo a change. While any number of adjustments can occur within a stage, there are only four stages of the family-business relationship so that the ultimate result of the development of the relationship is its end.

Impetus for Change

The two forces which operate on the family-business relationship have important differences. The constraints which the family places on the businesses are personal in that they arise from individual and group goals and objectives and are espoused by individuals. By contrast, the competitive requirements of the business are impersonal; they are the product of events which are sometimes distant and frequently unnoticed. Competitive requirements are less subject to managerial influence than family constraints; however little power the manager may have relative to his family, he has less relative to the structure of industry or the government. These differences affect the manager's choices of responses to changes also.

> Proposition 5(a): Managers perceive themselves as having more influence over family constraints and seek to adjust them first.
>
> Proposition 5(b): Managers are more likely to ignore changes in competitive requirements than to ignore changes in family constraints.
>
> Proposition 5(c): Managers perceive changes in family constraints more quickly than they perceive changes in the competitive environment.

The thrust of these propositions is that management becomes aware of changes in family constraints more quickly than changes in the competitive environment because there is someone to bring them to his attention and he is more likely to deal with them in a timely fashion because there is an individual or group pressing him.

Other differences also exist in these two forces which have an impact on the manager's choice of responses. The competitive requirements of the business are certainly open to interpretation but are less mutable than family constraints. There is some time frame in which the competitive challenge must be met or the performance of the firm will suffer. Family constraints may or may not have such a time frame. While competitive pressures are present constantly for most firms, family constraints may appear sporadically as when the time comes to choose and train a successor to the top manager or when performance declines suddenly. These differences tend to further support the inclinations identified in the foregoing propositions.

Managing the Relationship

While the managerial implications of the findings were explored in the last chapter, the inventory of propositions would not be complete without some indication of what constitutes effective management of the family-business relationship. Effective management must be considered in relation to both the forces which affect the relationship. "Keeping the family in line" is only half the job; the manager must also be concerned with the changing environment and how these changes will affect the ability of the business to meet the constraints of the family.

> Proposition 6(a): The more effective the management of the firm is at scanning and analyzing the external environment, the better able it will be to manage the family-business relationship.

Proposition 4(a) stated that the timely adjustment of family constraints to the competitive needs of the business is the key to a family-business relationship that benefits the long-term performance of the firm. With this in mind, the goal of management would usually be to facilitate those timely adjustments. Thus management techniques which contribute to adjusting family constraints should improve the long-term effectiveness of the firm.

> Proposition 7(a): The provision of relevant informaation to family members supporting adjustments of constraints facilitates adjustments.
>
> Proposition 7(b): Negotiating and bargaining skills provide managers with the means of adjusting constraints.
>
> Proposition 7(c): Personal relationships with family members facilitate the adjustment of constraints.
>
> Proposition 7(d): Participation by family members in the activities of the business facilitates the adjustment of family constraints by management.

While the managerial task of managing the family-business relationship deals more frequently in adjusting family constraints than in making transitions, the same principle would apply.

> Proposition 8(a): The more effective the management is at scanning and analyzing the competitive environment of the business and the resource requirements of the business, the more readily it can guide the relationship through a strategically required transition.

Since transitions involve mobilizing family support, management techniques which facilitate adjustments also facilitate transitions.

> Proposition 9(a): The provision of relevant information supporting the planned transition to family members facilitates the transition.

Proposition 9(b): Negotiating and bargaining skills provide managers with means of making transitions.

Proposition 9(c): Personal relationships with family members facilitate transitions.

Proposition 9(d): Participation by family members in some activities of the business facilitates transitions.

Paths of Development

The final element of the descriptive framework for the development of family-business relationships is the path of development of the relationship. Two patterns were observed. In one, the firms appeared to be passing through the stages in sequence while in the second, the firms were skipping stages. Relationships were termed "evolutionary" when the stages were being followed in sequence and "sporadic" when this was not the case. In addition, some of the relationships were moving much more rapidly than others. Those which had remained in a single stage for a long period of time were labeled "arrested." A connection between environmental change and path of development is hypothesized.

Proposition 10(a): Evolutionary development occurs in environments which change at a moderate rate.

Proposition 10(b): Arrested development is possible only in environments with a low rate of change.

Proposition 10(c): Sporadic development is likely to occur when the rate of change in the environment suddenly increases.

While arrested development in the Family Stage may be the goal of some families, this situation is more vulnerable to loss of control.

> Proposition 11(a): An arrested path of development is more likely to become sporadic than to become evolutionary in the face of environmental change.

The argument behind this proposition is that managers in a relatively stable environment are likely to be alarmed by sudden changes and the result is a panic sale. Another possibility is that the change is ignored or unrecognized past the point at which salvaging the relationship by changing its structure is possible.

The pattern of managerial responses identified in Propositions 5(a-c) has an effect on the speed with which the relationship moves through the stages to ultimate severance of the relationship.

> Proposition 12(a): The more successful the manager is at adjusting family constraints, the more likely the relationship to remain in a given stage. The longer the relationship remains in each stage, the longer the family retains control.

The role of the rate of change of the competitive environment is also an important factor. The more changes the family faces the greater the chance that challenges will arise that simply cannot be met by changing family constraints. If enough such competitive requirements arise, the family will eventually lose control.

> Proposition 12(b): The more volatile the competitive environment, the shorter the amount of time which will be required to move from Stage I to Stage IV.

Family-business relationships which develop in less competitive environments or which are able to develop some special expertise leading to a market franchise will be more enduring.

Relationship of Family and Business

A final general proposition is necessary to clarify the relationship between the business as an economic entity and the family which provides it with resources and determines the constraints under which it operates.

> Proposition 13(a): The financial performance of the firm and the financial interests of the family tend to converge in the long run.

The notion that "what's good for the business is good for family" is one which has not been formally tested but one which is widely held.

Summary of the Research

The propositions and directions for future research presented in this chapter and the implications for managers and family members in the preceding chapter are derived from the model of family-business interaction presented in a general fashion in Chapter Two and elaborated with representative cases in Chapter Three and analysis of all collected data in Chapter Four.

The thrust of the research was two-fold. The first objective was to shed light on the nature of the interaction of family and business in a family-owned and/or managed enterprise and the second was to examine the consequences of this interaction for the strategic management of the business.

The findings of the research indicate that the interaction exhibits four different stages of development and that a particular relationship may be described by the current stage and the timing and sequence of transitions which brought the relationship to that stage. The findings also indicate the processes by which family and business interact within a stage (adjustment) and the process by which the relationship moves to another stage (transition). Finally, the research indicates that the management of the family-business relationship is an exercise in the assessment and use of bases of power in the firm and in the family. Management of the relationship may be institutionalized or handled in an ad hoc manner but because of the role of family members in providing human and financial resources to the firm, the relationship must be explicitly factored into both the strategic management processes within the firm and the strategic response to changes in the competitive environment.

The research was intended to be exploratory and to generate a theoretical framework for the study of family business. The stages model of the development of the relationship and the concepts of adjustment and transition provide a way of thinking about the family-business relationship which will allow future researchers to focus on both static and dynamic aspects of the strategic management process.

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