

Family Business

THE GUIDE FOR BUILDING AND MANAGING FAMILY COMPANIES

Deanne Stone

The Outsiders

People with firsthand experience in running a family company are excellent candidates for your board of directors. Several outsiders who have been invited in discuss what they have

When Jeff Hester succeeded his father, Del, as president of Pierce Foods in 1990, he had no one to guide him in running the fast-growing business, which supplied poultry products to restaurants. "My father was the quintessential entrepreneur, a great idea man and thinker," says Hester, 49, "but he lacked experience in managing a large company. My transition would have been a lot easier if we had had a CEO from a big company on our board to mentor me."

Hester's family sold Pierce Foods, which was based in Winchester, Va., to ConAgra Foods in 1997. Now freed of the responsibilities of running a big company, Hester gives to other family firms the kind of advice he believes would have benefited him early on. Hester, who today is president of Collaborative Resources, a Winchester-based consulting and investing firm, serves on two family business boards. The experience has turned him into an enthusiastic proponent of outside directors for family businesses. "There's a Chinese proverb that says: If you're not in the game, you can easily see the next move," Hester says.

Governance specialists have observed that outsiders are often the only directors willing to challenge a family

company's leadership. In fact, Hester has found that he does his best work when disagreeing with a family member.

"I concentrate on what's best for the company," he says. "I may side with one person on one issue and another on a different issue, and over time, if I'm lucky, they'll see that I don't play favorites. I make a point of never repeating any 'he said/she said' conversations. It takes diplomacy to explain why I see things differently, and it takes time to develop the family's trust."

Donald Jonovic, a consultant with Family Business Management Services Inc. in Cleveland, estimates that only about 25% of family businesses have outside directors on their boards.

Family company leaders are often more comfortable having outsiders on their advisory boards, which have no authority to act on behalf of the company, he notes. "Family businesses are caught between the competing interests of wanting privacy and needing outside guidance," Jonovic says. "They're used to playing close to the chest, so bringing in an outsider is like

disrobing in front of a stranger for the first time. Taking that initial step is hard to do."



The board of M&C Specialties Co. in Southampton, Pa. Seated, from left, are Donald Rauch, president and CEO; Kathleen A. Taylor, retired managing director; and Daniel A. Cistone, CFO. In back row, from left, are John Boose, outside director; Ron Rowe, chairman of the board; and Stephen Kelly, outside board member.

That was true of Don Rauch, the president and CEO of M&C Specialties Co., a third-generation family business in Southampton, Pa., that fabricates and converts tape products for use in various industries. In 1996, he hired a consultant who recommended that M&C Specialties add an outside director to its board. Rauch knew it made sense; his

company was operating in a tough market, and he wanted to ensure the company would be strong when it passed to the next generation. Nonetheless, it took six years before he acted on the consultant's recommendation.

In 2000, Rauch was invited to serve on the board of Leidy's Premium Pork Products, a third-generation company in Souderton, Pa., that already had two outsiders on its board. Impressed by the wisdom and leadership they showed, Rauch was convinced that his company would benefit by having outsiders on its board.

Two years later, Rauch took the first step by identifying outsiders to join M&C's board, then composed of Rauch; his sister, Kathleen Taylor; and M&C's vice president of finance. "I was looking for people who could understand the spirit and mission of our business and offer practical advice and direction," recalls Rauch, 59. "I also wanted outsiders to help us assess the next generation and give them an objective view of the business." Rauch wrote to people he respected, asking them to suggest businesspeople who met four criteria: those who had integrity, had run companies larger than M&C, had come through tough times and had faced decisions similar to those facing his company.

Rauch had learned from his service on Leidy's board that outside directors did not have to be experts in his company's industry or understand the day-to-day operations of the business. "I didn't have to slice a pig to give advice to a family in the pork-processing business," he notes. "At the board level, decisions are about people, vision and long-term strategic directions, and those abilities are transferable from one business to another."

After interviewing prospective candidates, Rauch selected an executive from the music industry who had rebuilt a floundering business and understood a floundering business and understood people and working relationships. "I knew this person was the right fit for our company and the right person to be board chair," says Rauch. "The number one lesson I learned from serving on the Leidy's board was the value of having outsiders serve as board chair. When they're in charge you get real accountability from the CEO, and board meetings are about more than just management issues."

The second outsider, an executive in the metal fastener industry who had taken his business from a mid-sized company to a large one, filled the slot for a director who knew how to grow a business. Later, Rauch added a third director who had worked in sales and marketing for one of the leading computer firms. Adding the three directors did more than fill in the skills gap on M&C's board; it also gave non-family directors a majority presence on the board—a situation Rauch and his sister say they are comfortable with.

One step at a time

Jonovic, a consultant who also serves on multiple family business boards, says bringing outsiders onto the board can be a slow process for family business owners, who are invariably enmeshed in day-to-day problems. "They keep putting out brush fires until some motivating event comes along—the business is growing fast or moving in a new direction or, most often, they have to plan for succession—and that galvanizes them," Jonovic says. "Newer businesses, however, would be best served by first appointing outsiders on an advisory board until they have certain things in place, like a sound financial accounting system, an understanding among shareholders about the

company's mission and the right management team. After they get a governance structure, then they can consider outsiders on their boards [of directors]."

Ken Longacre Sr., CEO of Farm & Home Oil Company in Telford, Pa., has been in and around family businesses all his life. His family had owned Wampler Longacre (previously called the Longacre Family Poultry Company) in Franconia, Va., for 43 years. Longacre now serves on seven boards, though not all of the companies in question are family businesses. Longacre, 72, estimates that he spends 15 to 25 hours a month as an outside director—attending meetings, reviewing information and answering telephone calls.

"I like to serve on boards of companies in different industries so that I can get a feel for what's happening in the economy," Longacre says. "I also pick up information from the other directors—experts in their areas—that helps me in my business. I'm there to do my best and I work hard but if my advice is routinely ignored, I don't stick around. My time is too valuable."

Despite Longacre's board experience, his family has opted not to have outsiders on his oil company's board, at least not yet. As of summer 2006, he was the sole board member of Farm & Home Oil, which he bought in 1990. Having gone through a somewhat bumpy transition when his father transferred leadership of the family poultry company to him, Longacre promised not to interject his opinions about the business after he transferred authority in the oil company to his son, Ken Jr., in 1998. "We agreed that when he felt the time was right to expand the board, he'd let me know," the elder Longacre says. "My son and two employees are coming on the board later this year. We haven't ruled out including outsiders but, for the

time being, this is the right direction for us.”

Learning from others

Dennis Kessler was a fourth-generation family member at Fel-Pro, a Skokie, Ill., manufacturer of automotive gaskets, for 38 years. The family sold the business in 1998. Although Fel-Pro didn't have outsiders on its board of directors, Kessler says it valued the contributions of outsiders on its advisory board and encouraged family members to learn from other family firms. (See “The sale of Fel-Pro,” *FB*, Winter 2000.)

Kessler, 67, says his decade of service on two other companies' boards yielded benefits for Fel-Pro. “I brought back to the company specific information, like how to make our financial statements more accessible to all our stockholders by writing executive summaries in lay terms,” he recalls. “I was also exposed to new ways of thinking about strategic planning that helped our business.” Serving on other boards also gave him a new appreciation for his relatives, he says. “I saw other families that didn't communicate well. That gave me a renewed respect for my family's practice of setting aside an hour a week to talk about big strategic issues or family issues, the kinds of things family businesses usually blow.”

One of the trickiest aspects of serving as an outside director is walking the fine line between business and family issues. Outsiders who have worked in their own family businesses understand the culture of privacy; they are sensitive to family conflicts and don't discuss them publicly. Knowing when to push and when to back off is a test of their diplomacy, and keeping confidences a mark of their discretion. Kessler, now a principal in Family Business Innovations, a consulting firm in Northbrook, Ill., currently serves on three family company

boards. He says that if family conflicts were to interfere with the work of the board, he would have to speak up. “You have to be delicate in how you discuss these things,” Kessler cautions. “Outsiders can never know the whole history of family resentments; they can only be aware of the surface issues. Part of my job as the outsider is getting everyone on the board on the same page. The biggest value an outsider can bring is helping the family find consensus on a plan of action for moving ahead.”

Jonovic agrees. Having a clear understanding of their roles can prevent outsiders from getting swept up in complicated family dramas, he says. “Outside directors are not shrinks. They're businesspeople trained to focus on business problems,” Jonovic points out. “But if they are confronted with a family situation, say, a rivalry between siblings for leadership, they could help move things forward by defining the leader's role and structuring a communication process that acknowledges that both siblings want to be leaders.”

Retired CEO Jeff Hester says that after he joined the boards of two family companies, he interviewed family members and managers individually to learn about their strengths and weaknesses as well as those of the company. “It's the best way to learn the most in the shortest time,” he says, “and the best defense against a family member saying you don't know what you're talking about.”

Board service is a major responsibility and requires a significant time commitment. Successful businesspeople who choose to be outside directors typically have a strong sense of service and a genuine desire to see family businesses flourish. One of the boards Don Rauch serves on has five all-day

meetings a year. Rauch says that while he is well compensated for his time, no one in his right mind would do it just for the money. “I serve because I get a terrific education and the satisfaction of helping others,” Rauch says. “There's no way a family business can put a dollar value on the contributions of a good outside director.”

Effective outside directors must take time to learn about the business and time to think about what it needs, which is why retired CEOs make desirable non-family directors. Older CEOs such as Ken Longacre, who have turned over the daily responsibilities of running their businesses to the next generation, find constructive outlets in offering their expertise to other companies. “There's no way I could have served on so many boards before the transition of leadership in my company,” Longacre says.

Others like Jeff Hester, who sold their businesses when they were still relatively young, serve because they want to give something back. “I still have a lot of tread on my tires,” Hester says. “At Pierce Foods, I had experience with our family business only. Serving on multiple boards, I get to learn about different businesses and talk with top professionals in their areas. I enjoy the interaction and peer recognition, but the biggest reward is the feeling that I'm helping to preserve family businesses for the next generation.”

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