5 reasons why a family business fails

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Family business is big business yet each year in Australia, a number of them fail. Why?

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Family business is big business: today, more than 50 per cent of the Australian workforce is employed in a family business.

As family business advisors, we keep an eye on trends in the family business sector to better advise our clients and frankly, what we're seeing is disquieting. We believe that the sector is facing unprecedented challenges that will cause many family businesses to fail over the next ten years.

Why?

The reasons aren't new: poor **succession planning**, lack of access to capital, governance issues and other obstacles have always been issues for family businesses.

But coupled with the largest generational transition in history, these problems will create a tsunami that will sweep away many firms.

This is also a problem for the thousands of CPAs who have family business clients who may not be ready for the important transitions facing their firms.

The scope of the problem is enormous: A 2013 PwC survey found that while nearly half of Australian family businesses (worth approximately $1.5 trillion to the economy) intend to pass their business on to their children, less than 44 per cent had put a formal succession plan in place.

As the decade progresses, a wave of aging baby boomers will be looking for the exits and their businesses, families, and heirs simply aren't ready.

Here's why:

1. Few businesses have family governance structures in place

Next to succession, family governance is one of the issues most families are reluctant to address because it forces them to confront major changes in the way they manage the business.

Governance structures formalise the way that businesses are managed and delineate the separation between family and business. Without family governance, businesses are open to the risk of internal discord and ownership issues down the line.

2. Leaders lack education about succession planning

Many business leaders don't know how to get started with succession planning or view it as a single event instead of an ongoing process.

Surveys show that many current-generation leaders are delaying retirement and struggling with the reality of leaving their business in another person's hands. However, leaving succession planning too late is very risky; a sudden death or unexpected illness can harm the business and compromise the family's financial health.

3. Businesses have limited access to capital for liquidity events

Family businesses that have sought outside funding for expansion or liquidity events might have experienced the tough road most of their peers face.

Banks, private equity firms and other traditional sources of business financing generally aren't interested in the long time horizons and complex family dynamics inherent in family businesses.

Without sources of funding, liquidity events due to retirement or family member exits can put a serious strain on business cash flow and limit exit options.

The solution that we frequently present to clients is access to capital through a network of global family businesses that are seeking to diversify their holdings by investing in like-minded family businesses.

4. Businesses fail to leverage their 'family effect'

Research has repeatedly shown that family businesses tend to outperform their nonfamily peers. One study found that family firms on the S&P 500 grew their annual revenue at more than double the rate of their corporate peers.

These results are averages, however, and many family firms simply aren't harnessing the power of their "family effect"- the intangibles that differentiate them from their competitors.

By not effectively branding themselves and leveraging the trust clients have for family businesses, they are throwing away one of their greatest advantages.

5. Families focus on estate planning instead of management succession

Many family businesses are aware of their succession problems and are actively working towards a solution.

Yet many business leaders make the mistake of confusing estate planning with succession planning and rely too much on so-called drop-dead plans.

Estate planning is not management succession planning. If leaders truly want to ensure that their businesses will survive after their transition or death, it's critical that they begin training up a successor and laying the groundwork for the future success of the business.

Next steps

CPAs who work with family business clients are frequently considered one of the family's most trusted advisors – a view supported by research – and they are the first line of defence against many of the issues discussed here.

However, traditional business education and professional training often focuses solely on the financial and regulatory side of the business, leaving many CPAs without the specialised knowledge needed to navigate complex family matters.

In our experience, many CPAs can feel overwhelmed when confronted with emotional family dynamics and may be unsure of how to help their clients resolve these challenging problems.