THE SAME OLD SAME OLD OR CHANGE AND INNOVATION?

THE OUTSIDE DIRECTOR’S ROLE IN A FAMILY BUSINESS

Gerald Sherman
Pathway Advisors
gsherman@pathway-advisors.com
617-699-2756

The Lawrence family and its 127-year-old business, Ace Machinery, Inc., were institutions in their mid-sized New England city. A family member had sat on the board of the largest local savings bank for over 75 years and the company was an important area employer that had trained generations of young man to become well-paid machinists. Founded in 1865, the company was a leading U.S. manufacturer of replacement “forming” components for medium sized paperboard mills. Paperboard is used in the manufacturing of products such as cereal boxes or similar forms of packaging. The family had always made a good living but had never built the business to a point where they had generated any real wealth.

In the early 1990’s, a new technology for forming liquified pulp into sheets was gaining industry interest. The technology offered the potential for energy savings, the reduced use of toxic chemicals and a lower selling price. For two years the family struggled with what to do - if anything at all - about this new challenge. In particular the CEO, Bob Lawrence, V (The Fifth) and 60% stockholder was happy with the potential for modest growth and what he saw as a lower risk. At the same time, Bob Lawrence VI (The Sixth) felt the necessity to move ahead. During this period, the company’s chief engineer had been given the go ahead to begin preliminary design work. But now the time had come for the family to decide about completing the development process. Nonetheless they were stuck. The Sixth was pushing hard but The Fifth just had not been able to pull the trigger.

THE PLAYERS

Bob Lawrence, (The Fifth): An MIT trained engineer, Bob was 62. While very smart, he was far from a born leader, Rather, he was content to sit in his office developing quotes and acting far more like a CFO than a CEO. Nor was he a good manager. There was no organizational rigor, weak communications, and an undercurrent of employee dissatisfaction. But have no doubt, the Fifth was an autocratic decision maker. Finally, while change averse, he did share his son’s point of view that the company’s niche was evolving technologically.

Bob Lawrence (The Sixth): 34 years old, Bob was bright but never finished college, was ambitious but not always hard working, wanted more and did see himself as the future CEO. As
the company’s lead salesman, he worked in the field most days and was certain that the adoption of the nascent technology was critical for the company to remain competitive. He was a steady force for moving ahead and had teamed up with the chief engineer to support early design efforts. The Sixth was given a seat on the company board when he turned 30.

**Ann Alford:** Ann was the Fifth’s younger sister and 40% shareholder. She harbored a strong resentment about her brother inheriting majority control. At the same time, Ann was well set financially as her late husband had owned a prosperous business and she was a successful lawyer in her own right. Ann became a member of the board when her father died. While both capable and knowledgeable about the company, she was generally more caustic than helpful as a board member.

**Dave Smith:** Dave was corporate counsel and had sat on the board for several decades. He played no meaningful role.

**George Marks,** 41, was first introduced to the company and the family as a business advisor when the company was struggling financially as it emerged from the recession of the early 1990’s. Having helped the company through a successful turnaround, he had become both a business advisor and family friend. He was asked to join the board when the company had stabilized. Given that the group had previously only met annually to review prior year results, George was asked to create a more robust board process. While George quickly became the board facilitator, the Fifth listened but did not make decisions collaboratively. It is important to note that while this was George’s second board position, it was his first experience on a family business board.

**THE SITUATION**

During George’s first year on the board, the introduction of the new technology into their core product was a major topic of discussion at each quarterly meeting. There was a lot on the line. In fact, it was entirely possible that the company’s long-term viability was at stake. Financially, the total investment to bring the product to market was relatively modest, perhaps another $150,000 in development costs. The real risk was the first order. Each component was custom built and could cost $100,000 or more to complete. The real issues, however, were installation and performance. That’s because the entire papermaking making machine had to be shut down for several weeks to get the component ready to function. Accordingly, the first order had to be sold and installed at somewhat below cost. And if the component did not perform to specifications, the cost was almost incalculable. At best, perhaps $250,000 to solve the problem, an amount the company could absorb, but not easily. At worst though, a product failure had the potential to be a lethal blow to the company. And if that occurred, the Fifth’s financial future would be in jeopardy and his wish to see the Sixth take over as CEO would likely go unfulfilled.

All in all, George had begun to feel like he was on a treadmill and his frustration grew as he prepared the agenda for the coming meeting. He liked both the family and their business but found
himself seriously questioning if he could be effective. And this concern was only acerbated by the “family drama” that was present at every meeting. In fact, he considered resigning but concluded that he wanted to do more for the family if he possibly could. With that decision made, he asked himself two overarching questions:

1. Should he become an aggressive change agent, and if so, what steps should he consider?
2. What should he do – or not do – about the persistent family tensions?