

THE ROLE OF FAMILY IN YOUR BUSINESS AND COMMUNITY

CAFÉ SYMPOSIUM (Canadian Association of Family Enterprise)

Thursday, August 15, 2002
Winnipeg

The following comment has been attributed to Count Leo Tolstoi

“All families are happy in the same way but all families are unique in their unhappiness.”

Family business is often a replay of the works of Shakespeare with alternating tragedy and comedy and plenty of drama. If everything was placid and uneventful you would not be here today. That is why we tell our stories. Our stories are all unique yet they all share the same emotions and hopes. I hope my story will be an encouragement to some and a lesson to others.

Palliser Furniture was started in the basement of my parent's home at the end of the war. Both parents were immigrants – to be more precise – both parents were refugees. My mother and father were born in Russia and met as children when they were internal refugees during the revolution. Both families had a business background and started from scratch in the New World. My father's saga included being a shoe shine boy on the streets of Mexico while my mother swam rivers and walked on foot through northern China. My mother became a University Professor in the United States and my father a grocery clerk for an American company in Winnipeg. They met again as adults and settled in Winnipeg.

My father was fired three times by that company and rehired three times at the starting wage. My mother stated that he would not be humiliated again – he would work on his own and she would manage on whatever he could earn. I remain grateful that Safeway provided the impetus to my father to get into his own business. I tell that story because most family businesses are not the result of a grand strategy. They seldom evolve and grow as a result of strategy either. It should come as no surprise that transition in the nature of the business or leadership is often accompanied by conflict and confusion. Our businesses seldom started with the DNA to solve succession problems.

My father had no technical training and began manufacturing rough wood products. At the age of 3 or 4 the children would sit around the kitchen table and paint the wings on wood goose decoys. At the age of 5 we graduated to sweeping the plant. Before the age of 10 we were operating machines.

We never received a dollar of allowance but were always offered the chance to work. Being taught to work is a gift – and we do our children a disservice if we allow them to grow up with a silver spoon. After the basement of our home the company graduated to a 400 square foot chicken barn and two years later to a small factory. We have built a faithful replica of that chicken barn factory in the midst of our main complex as a reminder of where we came from.

The company grew each year and gained confidence. In 1961 we had a disastrous fire. The damage was exactly equal to the insurance policy and we survived. My father was a person with a very deep and personal Christian faith. He saw his survival through this and other adversities as the blessing of God on his life.

Relationships with the employees were always very personal and many of the employees were immigrants or refugees. My mother always knew when there was a new baby, when someone was sick in a home, when someone lacked for anything. She would visit personally and establish quality relationships.

As a teenager I still remember the Christmas parties where my mother would prepare the food and the children would participate. We had a tradition of giving each employee a turkey at Christmas.

In those days turkeys did not come in a standardized format and 50 turkeys could range in weight from 12-20 pounds. The instructions of my father were that the person with the largest family or greatest perceived need should receive the largest turkey and the single males the little ones – regardless of their seniority or position in the company. This was accepted and has become a metaphor in Palliser for looking beyond seniority and status. We have many programs where we try to level the playing field just a little.

In our environment a union would not make a positive contribution. We continue to operate the business in a manner where relationships are personal and trust is maximized. We have no

unions in Canada and the United States and have never had an election. The laws in some countries make it difficult not to have a union and in those circumstances we work in the same personal manner and seek a constructive relationship with all parties.

The initial employees were all Christians from the Mennonite tradition and my father would have a short Bible Study and devotion with them each week. Over the years this metamorphosed into more formal assemblies but we retain the tradition of addressing questions of values at these events.

We now have over 5000 employees speaking 40 languages from 70 nations and most religious traditions. Our approach to values is much more inclusive but we continue to articulate clear views.

Our Mission Statement was written about 8 years ago by all three generations of our family. It was a challenge to honor the past but to be relevant in the future. The VALUES part of the statement begins with the phrase

“Building on a heritage of faith...”

This is followed by values about integrity, respect for all persons, the environment and so forth.

We now tell our staff that our values grew out of our particular Christian/Mennonite heritage – but most people say that their own religious tradition espouses the same values. Then we say ‘great’ – add your heritage to ours and lets live these values together. However, if your tradition does not value each person equally and does not promote integrity – then don’t bring it into the mix. We do not apologize for that view – we state clearly who we are and ask people to consider that when they join the company.

After the big fire my father asked if the boys wanted to join the business – I say the boys because like many families he had a patriarchal view of life and did not expect our only sister and the youngest child to be part of the business – or at least in the same way. As a result she received a smaller portion of the shares and this created some tensions that the siblings needed to sort out

themselves many years later. There were three sons of which I am number 2. My oldest brother Frank was a production wizard like my father. My younger brother was more of a philosopher, studied theology, became a teacher in Africa and joined the business later. Anyhow, the response was positive enough and my father began construction of the factory that is still our Head Office.

Frank joined the business immediately but I was still in University. I started out in Math and Physics. After a few days in an underground Cyclotron devoid of sun and girls I switched to the Commerce faculty. I graduated in 1964 but by this time my interest had switched to International matters and applied and was accepted by External Affairs for a diplomatic career. My education did not seem complete and I applied for a deferral to study at a Mennonite College in the US for another year.

Given my pacifist beliefs and the tenor of the times such as the Civil Rights Movement and the Vietnam War it turned out to be a great year and earned me a degree plus an FBI record. That resulted in the loss of my security clearance in Canada and my diplomatic job.

Plan B was the Harvard Business School. This offered me many career choices. I was already married to my lovely and supportive wife Leona. We decided to be more independent like my father and to live in the context of community --that meant a return to Winnipeg rather than New York or Geneva. My father came to Boston to interview and offered me a job. His line was – “I started at the bottom, your brother started at the bottom and you must start at the bottom – you can be in charge of sales.”

My brother Frank and I were great partners in that he would build and manage the factories and I would deal with design, sales and finance. The company had sales of 1.6 million when I joined in 1967 and last year had sales of \$500,000,000. My younger brother managed several factories and was strong on the information technology side. Our sister was active as an owner but never directly in the furniture business itself. In recent years has taken responsibility for the family Foundation and is making a genuine contribution in this way.

Palliser expanded to Calgary in 1969, the United States in 1981, opened plants in Mexico 4 years ago and today has factories or contract relationships in these countries plus Indonesia, Thailand, China, Brazil and others. We experimented with some leather products about 12 years ago and slowly developed our expertise. It was one of those fortuitous events since the leather part of the industry exploded and we rode the front of that wave. Today we are one of the largest producers of leather furniture in North America and it represents over 50% of our business.

Although we had our usual sibling issues we worked together very productively until the early 90's. My father had treated the brothers equally in terms of shares and we had scope for external investments on our own. My father also had the normal problems of deciding how to deal with children in a manner that he deemed to be fair and productive. We were not bothered by the share distribution and paid ourselves identical salaries – the reality was that Frank and I earned more on our external investments than at Palliser. My father appreciated that Frank was older but I was more educated in a formal sense and more of an extrovert. His solution was that after his retirement – somewhat hastened by the death of our mother – Frank, as elder brother should be the next President and possibly after 5 years I would have my turn. That did in fact happen but getting there was a bit more complicated.

After my 5 year term as President I was not interested in being number 2 under family conditions.

Difficulties in our family arose when we began to think about the role of the third generation. Our family has always shared the view that we would remain private and family-owned. Selling the company has never been discussed as an option. My older brother has three children and they are persons of ability and integrity but by now we were dealing with a company of several thousand employees, multiple countries and continents. Palliser was also becoming much more sophisticated in terms of design, marketing and finance. Leona and I have two adopted daughters and at that time they were not married. My younger brother also has two sons. My father had always addressed the question in terms of birth order rather than a test of ability – when one or more family members refuse to abide by that formula you have a problem. Given my personal situation I did not much care for that formula.

A second area of concern was the difference in personality and ambition. My older brother and to some degree the rest of the family enjoyed operating the business as it was or had been and although very competitive became concerned that I was driving the business into too many new markets, making it too complicated and too much debt.

Who can argue with these different perceptions of the future? Some also realized that the company being built could probably not be run by many or possibly any of the members of the third generation.

The result was something that happens in many companies. We would reach a stalemate on many subjects and sorting this out took an increasing amount of family energy. At that point I offered to resign as President, withdraw from the management of the business and purchased the leather portion of the company – at that time possibly 10% of sales. After 2 years I was invited back to run the company and agreed to do so on the condition that I could purchase a majority interest.

This happened in 1996. My older brother purchased several of our supply Divisions and operates these successfully. My younger brother Dave had serious health challenges and remained in the US and is semi-retired. Irene is active in the DeFehr Foundation.

Palliser has continued to expand, has a fully professional external Board of Directors, is changing from a production-oriented company to a more design and Marketing organization. Sales have more than doubled since that time.

I have been speaking about family members but it should be obvious that our success over the years has not been accomplished without dedicated and qualified management. When the family goes through any crisis we need to remember that we add a great deal of stress to these trusted and valuable managers.

Although we went through a period of severe stress in the 90's we always reminded each other that as Christians it was essential to retain our relationships within the family. We are not without our moments of stress but feel we have largely accomplished this goal. As members of

families I encourage you to balance the importance of relationships against financial and other concerns.

In the meantime my daughters married two fine young men – both with advanced education in business and strong personal qualities. One daughter and both son-in-laws currently work in Palliser. In addition one nephew from each of the families of my brothers are playing important roles in the company.

In 1996 I faced a future as majority owner of a company that would likely exceed one billion dollars in sales when I was in my mid-sixties. If there was no qualified family succession in sight by my sixtieth birthday we would realistically need to go into a mode of preparing the company for sale.

The development of third generation management combined with an increasingly professional management and a strong Board gives me confidence that we can plan on a third generation of family ownership and management.

We have a Board of Directors with 7 highly qualified external members plus 6 from the family. All spouses of the second generation plus third-generation members who have shares or are working in the company may attend Board Meetings as observers. The purpose is communication but also training for the role of ownership.

A critical decision for all families is whether power is given to one person to manage, whether power is given to one person in the form of legal control or whether the family comes up with a formula or compromise where power is shared. In our family compromise worked for many years but eventually broke down in part because no rules had been established on questions like entry into the company by third generation members and an outside Board of Directors. We resolved this by giving legal control to one person and that also carries with it a responsibility to the others – but it does allow actions and decisions to be taken.

What is our plan for the next generation? My own view is that we need to give meaningful control to the person who best embodies the values of the family and corporate culture together

with the ability to manage and lead the kind of organization we are becoming. Helping us shape that future, preparing the people and giving advice on this question is probably the single most important role of the Board. The Board is also an insurance policy against catastrophe. If something happened unexpectedly to myself or other Palliser leadership my hope would be that the Board would have the interest and ability to bridge that gap.

That is the story of Palliser. I would like to address two other matters that are an important part of the story.

I have a very strong bias in favor of remaining a private company and am often challenged on that question.

First, being private has allowed our family and myself to select a balance of priorities that are not dictated to us by the financial community. Yes, we need to meet the requirements of the banks and others and in the absence of access to many forms of capital this can be a real challenge. On the other hand, we can make choices that flow from our faith perspective or our personal view of society and justice, choices that may be more difficult if we were public. The community of Winnipeg and Manitoba has been most supportive and allowed us to develop and prosper. The greatest gift we can give back is to assure secure jobs for many people and keep leadership in this community by keeping our management here. If ownership moved it would undoubtedly move out of Winnipeg and probably out of Canada. Communities always suffer if control and leadership moves away. As part of the community our people provide a capacity for leadership and our physical presence encourages us to invest back through the Foundation.

Some of the choices we can more easily make are in areas such as the employment of the handicapped, special programs for immigrants and refugees, promotion of multi-cultural tolerance and values. Given that many members of my family for several generations qualified as refugees – we have made a special effort to make Palliser very welcoming to this group.

There is another aspect to the move from a private to a public company that gives me concern. We are taught in our faith tradition that we are stewards of our wealth – and not owners. If I sell the company for some large amount of money two things happen. First, I am capitalizing the

accumulated efforts of my staff – and they need to remain and dig themselves out of that financial hole.

Secondly, I create a pile of money that I will never spend and set up my family and friends for a fight over the proceeds. I would rather pass along the company unencumbered and allow the next generation to harvest the psychological and personal rewards of running the company well – then passing it along again.

A recent example of this view is the dismissal of the President of Bertelsman – possibly one of the best known private companies. His goal was to take the company public. It is interesting to note that Bertelsman survived more intact than any other media company during the recent wild days in that industry. This was in large part due to the fact that the company was driven by a longer-term vision and could sidestep the immediate pressures of the marketplace. Many friends who operate public companies tell me repeatedly that I should stay private as long as possible. The family, the employees, the community and our customers are stakeholders. That is enough. I don't need to be told what to do by casino capitalists.

The second issue I would like to address is the relationship between my personal career and lifestyle and owning and working in a private company. I have been exceptionally fortunate in that I have been able to enjoy the global access that leadership of a major company offers and benefit from the financial freedom.

My father and siblings have been very accommodating, especially in the earlier years in that I had interests and dreams well beyond the boundaries of the company. I will tell that story and encourage you to allow members of your family the freedom to experiment beyond the boundaries of the family enterprise. We should view this opportunity as a special gift rather than penalizing family members for not contributing equally.

Although my diplomatic career died stillborn – I have had the privilege of working on projects and issues around the globe including living in many parts of the world. My personal estimate is that one third of my 35 years since graduation has been spent on projects outside of the company. The longest absence was two years in Bangladesh after their civil war. My position was Director

of the Mennonite Central Committee working with refugees and agricultural rehabilitation. Our Mennonite tradition teaches that we should live a life of service to others – that is the counterpart to the view that we do not participate in war. Pacifism is not an absence of responsibility but a greater responsibility based on the teaching of Christ.

A friend always ends her email messages with the reminder:

“If we all live by the dictum of an eye for an eye we shall soon all be blind”

Leona and I have been privileged to be able to balance our business career with other interests, to balance our life in Winnipeg with experiences around the world and to add new friends in addition to our wonderful community here. A second assignment abroad was Thailand in 1980 where I was involved in the restoration of Cambodia at a time when the war was still in full gear. In 1982 I was invited to lead the United Nations refugee program in Somalia – at that time the second largest refugee program in the world and very controversial. The Cold War and tribal war were well mixed. Further assignments included Ethiopia during the famine and later Sudan. In 1989 I returned to explore the family roots in Russia and that started a whole new adventure that is still part of our lives.

Some of these efforts also translated into activities back at home. The experience of famine in Bangladesh provided insights that led to the development of the Canadian Foodgrains Bank – a very successful program that is still operating. In 1979 we leveraged our international refugee experiences into efforts that led to the refugee sponsorship program that has been so effective in Canada.

Other projects included a role in starting a private University in Lithuania, irrigation programs around the world and the Canadian Mennonite University in Winnipeg.

As part of the Business Council of Manitoba, enhanced immigration is an area where my experiences allow me to make a contribution. The plan is to triple immigration to Manitoba as a way of driving our economy. Immigration can be good for all parties if done intelligently.

The family business in the early years allowed both time and financial freedom. My siblings and father would cover for me during my absence and my business salary allowed me to take assignments that often did not pay. Frequently I was able to initiate interesting projects because we could use the Family Foundation funding without the hassles or delay of fund-raising. A career in the United Nations or other organizations would have had all of the limitations of institutional politics. I have frequently been able to leverage my business role to gain access that would have been difficult if I was working inside those organizations.

Did the business pay a price for these absences and an eclectic career? Probably. If net worth is your only criterion – then my example may not be very inspiring.

The next time you attend the funeral of a friend consider whether a 50% greater net worth makes any difference.

There have been many unexpected bonuses from these extra-curricular activities. Most important, our only two children are adopted daughters from Bangladesh. They have given us great joy and have married two outstanding young men. The adoption process itself could be the occasion of another long story.

We also met many interesting people and made great friends around the world. I was part of the walk from Selma to Montgomery with Martin Luther King and during the Somalia assignment one of my colleagues was a promising young man named Kofi Annan. I have been a member of the World Economic Forum meetings in Davos the past 10 years allowing me to meet and be inspired by many world and business leaders.

There are also those times that make great stories if you survive. On one occasion I was between the armies of Vietnam and Thailand who were shelling each other over my head. During the 1991 coup in Russia Leona and I went inside the barricades of the Russian White House with our Russian friends. My mother witnessed the beginning of communism and I did not want to miss the end.

In Lithuania we negotiated for the founding of a private College in a Parliament surrounded by Russian tanks – with the tanks aimed at the Parliament.

We have also experienced many tragic and also uplifting interactions with people who by our standards have no hope – yet can exhibit great personal strength. In other words, we have been vastly enriched by all of these experiences and would not trade any of them for a slightly higher Return on Equity.

In closing I would like to tell you a little about the DeFehr Foundation. My father started the Foundation over 20 years ago as a way of organizing our donations and removing the artificial deadline of the financial year-end. We donate 12% of our pretax income and more or less spend the entire amount in the following 12 months.

Giving is a wonderful way to unite the family. Try talking about how much you will collectively give away and where it should go rather than how much each of you should receive. It does change the tone of the conversation.

The Foundation operates like a typical charity but is also designed to operate its own programs. With proper documentation we are able to support causes around the world that do not have a charitable number and could never get one in our legal sense of the term. Given our work around the world we have many contacts that do not have access to the large pools of funding in Europe and North America. We try to level that playing field a bit by supporting people and causes that do not have the access of the highly organized charities. In many cases we support causes where employees or family members have a direct interest.

You might be interested in how we see the future of Palliser and the family. I will share my personal vision. If we can keep Palliser private and family owned and if the senior generation is not interested in pulling out its equity - that creates some interesting options.

My preferred view would be that the next generation should receive the shares free. We are already structured to allow that to happen. Instead of selling the company and creating a legacy to be fought over and at best donated after our death, Leona and I would prefer to give that

legacy away in our own lifetime. If the next generation does not need to pay for shares, those funds can be used in other ways.

My proposal will be to increase the amount of donations from the 12% to some higher percentage and allow us to have the pleasure of allocating those funds in our lifetime. Besides being very tax efficient this will allow the gifting to reflect the success or problems of the company over time and not add unwelcome pressures. When we are gone – the generation in control can then set its own priorities. Given different times and priorities they will set their own course for the future.

Family business has the unique ability to take a genuinely long-term view – often extending over several generations. To avoid the pitfalls takes a great deal of wisdom and grace. However, the rewards are substantial if you get it right.

Thank you