



Intergenerational Succession in SMEs Transition
INSIST

CASE STUDY

Pillar Ltd. Case

Final version

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The case is based on the history of a family business operating in the Polish building construction market. The name of the company and personal information about the owners were changed at their request.

1. Introduction - Presentation of the Case

1.1. The Story of the Firm in Brief

The Pillar company was established in 1983 in Krakow, Poland, as a small business offering renovation and construction services. Martin and Helena – a married couple - founded the business at the age of 35. At first the company benefited from the shortage of housing in the Polish market, but in the 90-ties changed their profile into a classic property development business. It bought land and built apartments and commercial premises for sale; mainly in the area of Krakow.

Since the business was developing dynamically the owners decided to change the business model to adopt new methods of functioning to match the expanding scope of their business operations. They changed the organizational and legal form and began to build a modern capital group, currently consisting of several business entities conducting simultaneously several development projects.

In the years 2009-2012 the company suffered from a serious crisis of the Polish real estate market. Since the group activities were largely financed by bank loans the company was under tough pressure from the banks that imposed tight deadlines for loan repayments but due to solid foundations of the family business model and consistently carrying out once adopted policies, the company managed to survive and since 2014 the enterprise has returned on the path of dynamic development.

1.2. Main Activities

Pillar company is a property developer. First they select and buy land, then build a single building or complex of blocks. The group runs simultaneously 3-4 development projects at various levels of progress. They usually consist of 40-60 apartments or commercial premises within one project.



Following a business model restructuring, the company ceased the construction operations and outsourced them to external contractors, so its business activities are mainly focused on planning, supervising and marketing/selling new projects.

Apart from property development business, one of the enterprises deals with renting municipal apartments to low income tenants. A partnership with the local government was set up for that purpose and funded through the municipal housing promotion (TBS).

1.3. Ownership Structure

At the beginning the company operated on the „sole trader” principle which meant that the owners were fully responsible, with their whole personal assets for the company liabilities. In the peak phase of the company development it employed 200 people. Then in the late 90-ties a limited liability company was set up and took over the business conducted earlier by the founding parents.

Such solution enabled separation of the owners' private liabilities from the liabilities of the company. Also Polish regulations favour transfer of the ownership through sales and stock donation to limited companies which also allows easy increase and/or withdrawal of shareholders. Such legal entity also enabled construction of modern capital group through setting new, subsidiary entities for carrying out specific development projects. At present, individual special purpose vehicle is set-up for every new development project. The only owners of the special purpose vehicles are the parent company Pillar 2 Ltd. or family members; so far there have been no external investors. The group consists of limited liability companies and also limited joint-stock partnerships. In case of the latter, the parent company is the general partner liable for the limited joint-stock partnership obligations including the ones connected with taxation, transaction payments (trade payables) and other liabilities. Family members are the limited partners and they are not personally liable for the company debts. The use of limited joint-stock partnerships led to the optimization of tax-payments. Until 2013 according to Polish tax law, the net income of the individual shareholders was not taxed until the dividends were paid. This enabled deferring of the tax payments, provided the shareholders did not withdraw their profits from the company, but re-invested it in the new development projects.

1.4. Main characteristics of its market position

The group operates in the competitive local market, where it is one of the major players in the apartment-building sector. In 2014 we observed a slight growth in the local housing market - the number of new dwellings rose by 1.4% compared to 2013 (source: <http://www.portalsamorzadowy.pl/gospodarka-komunalna>).

In recent years, several family companies in the property development industry have gone bankrupt or were taken over. There are also known cases of unfair practices in the industry, which resulted in developers losing trust of customers and contractors. . Companies with large capital also operate in the Krakow market, operating on a wider scale -also internationally. It is estimated that currently there is still a small oversupply of apartments in the local market, and prices are contained by the government's subsidy program for affordable housing. Still the prices of new apartments are relatively high compared to average salaries.

1.5. Employees

Once the company employed up to 200 workers. As already mentioned the company ceased own construction operations and outsourced them to external contractors. This process was accompanied by reduction in employment and the owners encouraged their former employees to set their own micro-companies. Such entities were preferred when selecting subcontractors for construction jobs and cooperation was based on trust built over the years.

At present the company employs 70 people. They are solely highly qualified specialists mainly construction engineers, accountants, sales staff who have been with the company for many years. They hold mainly managerial positions, supervising and carrying out investment processes and also dealing with sales and administration. The number of employees is relatively small due to the fact that construction activities are outsourced.

1.6. Characteristics of the interviewees

The family consists of Martin, Helena and their two sons, Piotr and Paweł. When the first business was set up the boys were respectively 9 and 4. At first both parents were involved in the company activities, but they found it very hard to combine professional

and family duties. That's why in 1992 Helena decided to withdraw from active involvement in family business and devoted her time to the kids and their education. Both sons completed higher economic education, the older son started working for a big international company when he was still a student and then continued working for them at the headquarters in Warsaw. When undertaking the job he envisaged his future in an international corporation and was planning to work also for their foreign branches. While working in the corporation he was responsible for managing a group of employees and was responsible for carrying out sales operations. Both sons were able to acquire some work experience while they were still students by helping their father run the family firm. Immediately after completing his studies, the younger son was employed at Pillar as an ordinary junior employee responsible for carrying out one of the investment projects. At present Martin and Helena have five grandchildren.

The main characteristics of the interviewees - (as of 2015)

Name	Age	Education	Career history	Role in succession process
Martin	65	Not connected with construction business or engineering. Degree from Military Academy	Worked in a state building company in the procurement section. Had contacts with business partners, also foreign ones. Later became the manager and President of Pillar company	Founder / Nestor
Helena	64	Not connected with construction business Degree in electronics	Office work in a state-owned company, later bookkeeping and administration work at Pillar	Founder / Nestor
Peter	42	Degree in Economics and MBA in management	Helped with managing the family firm during his studies. After completing his education he worked for three years for an international corporation, then joined Pillar company	Successor
Paul	37	Degree in Economics	During studies and after studies worked for the family business	Successor

2. Succession Process

2.1. Rules of Entry and Exit and Dynamics of the Family business

There was constant presence of the family firm and its matters in the Pillar family life. During their studies at the University of Economics the sons used to help their parents in daily activities: managing organizational and administrative issues. However, nobody ever discussed any succession plans until they completed their education and received degrees.

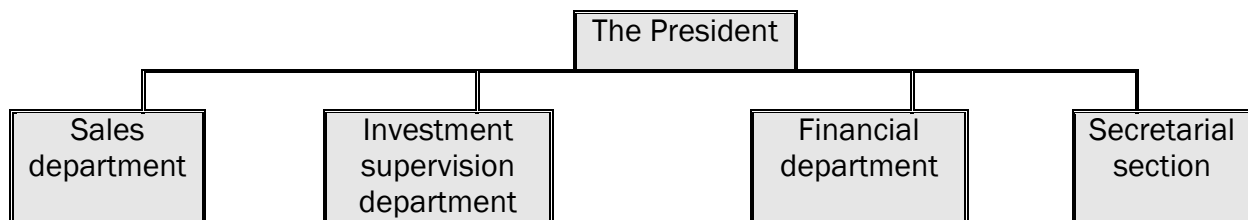
Martin and Helena first realized they should start considering and planning the succession when their older son started working for an international corporation while still being a student. They were surprised he didn't take for granted a career in the family business. Only then did the parents decide to plan and implement a succession process. They started talking with both sons about their possible future roles in the family firm. These conversations about engaging them in the future development of the company lasted for two years. Eventually, the sons agreed with each other and with the parents to undertake cooperation with his father. It should be mentioned that the older son was a bit disappointed with the work for a large global corporation and that was the main reason for changing his mind. In the meantime he gained significant business experience by working for the corporation and obtained MBA management degree.

Succession in the Pillar company has been planned without any external consultants. The final form was designed on the basis of life and professional experiences of the Founder. Both sons were first employed in the holding company Pillar 2, starting from lower positions in the sectors of investment management, sales and finance. After a few years they substituted the operational directors and took over their responsibilities. The elder son, Piotr was responsible for finance and marketing, the younger – for the preparation and supervision of investments. The responsibilities and authority of both directors were formulated in a written document. Even though there was no formal ownership transfer during the initial stages of the succession process, certain firm principle was proposed by the Founder and accepted and implemented right from the beginning: *This is our joint company. Everything is to be divided equally among us, not only incomes but also problems.*

At first the company Founder became the President of the Board, but later the position will be held by the sons on two-year rotation scheme. The position of the President was connected with representative duties and direct supervision over the company secretarial function. In that way each son will consecutively combine the function of managing his own department with the representation duties.

The position of the parent company President does not bring any effective decision power, since all decisions transcending the usual management are to be taken jointly by father and both sons.

Organization chart of the parent company Pillar 2 Ltd.



Meetings of the informal family board composed of father and both sons take place at least once a week. Such a decision process has not been included in the company documents; it is just a result of oral agreement between father and sons. During the meetings the family members take decisions which transcend the single department management, which belongs to the sons' regular duties. In case of varying opinions between sons the problem is discussed in a great detail and the father has the last word. So far during the meetings three family members have exhibited a great deal of consensus building abilities. In case of a conflict the sons usually built a joint position against their father's opinion but they rarely were in conflict with each other. Unwritten rules adopted by father and sons include the necessity of accepting by all of them every strategic decision such as the launching of a new development project. Despite the company functioning according to the present management model for years, competence conflicts between sons –directors sometimes do appear. These conflicts are immediately solved at the weekly meetings and the lists of responsibilities and authorities of both directors are constantly being clarified and specified.

As far as the sons' and father's remuneration packages are concerned, an analysis of all three family's needs was made, i.e. the families of the successors who in the meantime

founded their own families, and of the parents. Later regular monthly salaries were calculated for each person. As it was mentioned earlier the company was struggling with the crisis in the Polish real estate market and there were months when salaries of all three board members were suspended. So far such a situation has never caused any conflicts.

As far as the process of ownership transfer was concerned, the Founder, Mr Pillar was gradually passing-over his parent company shares to his sons in 25% stock tranches per year. The owner passed all the shares to his sons having only kept within his personal property the minority shareholding of one of the partnerships that deals with renting municipal flats. From the economic point of view, taking financial control over the company didn't require any resources from the successors other than their own work for the company. Both sons hold equal stakes of the company, so none of them is able to formally solely control the group. The Father remains an employee of the capital group and receives monthly salary equal to the salary of each of his sons. All additional income is re-invested in the activities of the capital group. Nestor is still involved in the operations of the group mainly through participation in the weekly meetings with sons and offering advice regarding the running of business on daily basis.

The process of passing the ownership to sons took about 10 years since the day they started to be employed in the company. The owner believes that from 2013 the company has been able to function without his supervision.

2.2. Business and Family Related Goals and Performances

Further development of the company as a family enterprise has been set as the main goal of the future activities. Such a form and ethos assumes keeping multigenerational authentic control over the company. At present, all the assets are under the family ownership, but father and sons accept the possibility of introducing external investors, for example by going public, provided the principle of minority ownership by the non-family owners is obeyed.

In the near future Martin Pillar plans to withdraw from active participation in the group operations. Since his older son reached the age of 40, Mr Pillar would like to avoid his own mistake and has already started discussing with his sons the plans of the following

generation succession. Martin Pillar has five grandchildren. The whole family takes care of the preservation of close family ties. Nestor is trying to form with grandchildren a relationship encouraging entrepreneurship.

2.3. Commitment of the Next Generations

In the process of succession primarily the sons drew from the rich business experience of their father. The key was his technical expertise, and knowledge of market and customers' needs. Now the sons are those who find new locations for development projects and supervise development. Over time, the children brought into the business a lot of new ideas, especially in terms of financial and legal solutions. Their education in business management has helped them to create a modern group. It should be emphasized that they relate with great respect to their father and respect his opinions and views at all times. Mr. Pillar draws attention to the fact that sons often in discussions jointly defend their common ideas, and he remains an opponent. It should be underlined that the whole larger family cares about the quality family ties, and their personal lives intertwine with the company matters.

3. Lessons and Conclusions

The process of succession at Pillar family can be described as successful and almost completed. The presented case could provide the basis for a broad discussion; however, it seems that the most important conclusions are as follows:

1. The critical issue is enabling successors at an early age to have contact with the company's operations. It can facilitate the succession in the future - in the case of the Pillars it certainly contributed to the ultimate success of this process.
2. Delaying discussing the topic of succession with family can lead to successors developing their own careers and arranging their life independent of the family. The history of the Pillar family shows the divergent professional development paths of two sons.
3. Choosing the adequate legal form of the business entity may prevent or facilitate the process of transferring management and ownership. In this case the most useful proved

to be the limited liability company and limited partnership. Succession was carried out through the gradual transfer of shares to the sons and appointing them as board members. Selection of the appropriate legal form also allowed the protection of personal property of family members in the event of business failure and optimization of taxation.

4. All the succession process participants agree that the writing down of the rules of joint management and their subsequent improvement helps to avoid conflicts. At Pillar company the key role plays the list of division of powers between the sons. This list is being all the time improved.

5. Addressing the key financial issues at the early start of succession contributed to the success of the process. Agreed equal remuneration for father and sons, the suspension of payments in times of a crisis has developed the sense of responsibility and solidarity among them.

6. Establishment of permanent monthly remuneration allowing for a dignified life of all families and agreed policy of reinvestment of all profits made it possible for all family members to focus on the idea of building a strong family business for present and future generations.

7. Pillar succession proceeded without major problems. They developed a unified? Management model, where each of the sons is responsible for his departments, and father acts as an arbitrator and advisor, especially during frequent meetings and deliberations. Each family Father and each of two sons have the right to block strategic decisions, but such situations are very rare. All three are characterized by the desire to achieve consensus in matters of business.

8. Nowadays performance of the company is based on an informal agreement between father and sons and their close emotional relationship. Positions of the two successors are equal. It seems that this equilibrium is relatively fragile and this model solution cannot be directly transferred to the next generation.



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