FINANCING THE PRIVATELY HELD FIRM
MBA Block Week, Summer, 2019

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Course: B8464-001
TA: TBD

Course Description, Objectives and Approach:
Financing decisions in a privately held firm, and specifically the family-owned and controlled privately held firm, can be subtly complex in comparison to a publicly owned corporation with well distributed ownership. Whether it is a budding entrepreneurial venture, a growth-stage strategic expansion, or a well-established latter-stage concern, the private firm decision matrix must consider the balance of insider control, timely growth and expansion, and shareholder liquidity needs when making key financial decisions. As the family, business, and ownership subsystems evolve and interact at different stages of development, the needs and desires of the decision makers and various constituencies will change as well. In this course, we will gain a better understanding of the financing decisions faced by privately held firms, and the underlying forces which can greatly influence traditional valuation models and analyses.

Family controlled firms make up a majority of business concerns throughout the world, and account for a corresponding majority of the World’s GDP. In the US, Family firms comprise 70% of all incorporated businesses, 60% of publicly traded companies, 33% of Fortune 500 companies, and account for about half of the US GDP [Poza, Family Business, 4th Edition]. While evidence has shown that family controlled firms fail at an alarming rate before the second and third generation owner/managers have completed their terms, those companies that do succeed for multiple generations often go on to outperform their non-family controlled counterparts. The issue for family firms is not simply survival to the fourth generation and beyond, but creating a blueprint to successfully navigate the family, business, and ownership cycles simultaneously and through time. Financial decisions, and specifically financing the family enterprise, plays a key role in attaining success and longevity.

Financing decisions have a profound effect on the privately held firm beyond the obvious valuation issues. Key financial decisions are sometimes made in reaction to, or in anticipation of, a triggering event, such as a corporate financial crisis, a significant strategic deficiency or opportunity, an immediate need to address competition, or in the case of family businesses an exogenous event such as the generational transfer of control and equity.

In other instances, owner/managers simply need to finance the daily operations and organic growth of their business. Whatever the case may be, issues of control, growth/expansion, and liquidity are often at odds when additional capital is required.
The course is directed towards students who are involved with the management of family businesses, either their own family's or someone else's, as well as towards students who interact with family businesses. The focus of this course is primarily on financing decisions faced by privately held family businesses. We will explore the family, business, and ownership issues found in family owned and managed companies to get a better understanding of how financial decisions are influenced.

Through lectures, case studies, student work experiences and guest speakers, we consider questions of control, growth, liquidity, and the evolving role of governance and the family office in the financing decisions of the family owned enterprise.

The course has the following objectives:

- Develop a system framework to analyze factors influencing family business financial decisions.
- Increase your understanding, effectiveness and commitment as a member of a family firm (either you own family’s or someone else’s) or as an advisor to such firms
- Identify the characteristics that differentiate a family business from other businesses
- Examine the life cycles of family businesses from the perspective of business, family and ownership
- Learn to identify and evaluate situations and problems in family businesses
- Examine best practices and explore emerging trends in family business management
- Develop family business competitive strategies

**Teaching Methods and Course Materials:**

- The course will include case studies, lectures, readings, and discussions
- Cases are assigned which you should read and prepare to discuss in class. Case write-ups for days 2 and 3 are due at the start of class. There are no write-ups for day 1, however, students should be prepared for a full discussion of the cases and related questions.
- Guest speakers will supplement and facilitate further discussion of section topics.

An independent case study of approximately 10 pages in length is required in lieu of a final exam. (See details below.)

**Textbook and Required Readings:**

- Cases and readings: available via links on Canvas/Syllabus

**Supplemental Reading:**

- Family Business, Poza, 4th Edition
- Not required: Offers appropriate background material for Family Business Issues

**Expectations and Grading**

As the course is based primarily on case studies, it is expected that you will prepare the cases and readings and be ready to actively participate in class discussions. Your participation will enhance your understanding of the course material and add richness to the learning environment. The cases are based on real companies and these course materials have been chosen to provide you insights, not absolute answers.
The greater your preparation and participation, the more you will learn. Each student will be expected to submit a written case analysis for each assigned case in Topics 3, 4, and 5. A simple valuation exercise will also be due on the final day.

**Case Preparation Guidelines**
- Cases should be at least 2 pages in length, double spaced
- Answer the assigned questions
- Paper should reflect an understanding of the topic of the session
- Support conclusions with references to sources including at least the assigned readings and where appropriate references to:
  - other books, readings and cases
  - guest speaker comments and insights
  - relevant courses
  - your own personal experiences
- Use course terminology and concepts.

**The grading structure is weighted on this basis as follows:**
Class Participation 35% - active and additive participation
Case Assignment and Valuation Exercise 35%
Independent Case Study 30%

**REQUIRED PREREQUISITES AND CONNECTION TO THE CORE**

The learning in this course will utilize, build on and extend concepts covered in the following core courses:

<table>
<thead>
<tr>
<th>Core Course</th>
<th>Connection with Core</th>
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<tr>
<td>Leadership Development</td>
<td>1. Application of leadership concepts to the family business and the family</td>
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<td></td>
<td>2. Examination of the need to evolve as a leader, the need to understand family dynamics and to develop and apply new leadership styles as a company grows</td>
</tr>
<tr>
<td>Financial Management</td>
<td>1. Application of Financial concepts to the family business</td>
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<tr>
<td></td>
<td>2. Examination of financial decisions as a company transitions through different generations of both family and non-family management</td>
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<tr>
<td>Strategy Formulation</td>
<td>1. Recognition of the need to evolve from an entrepreneurial approach to a more professional evidence based methodology as a company expands</td>
</tr>
<tr>
<td></td>
<td>2. Examination of strategy formulation for both the family enterprise and the family itself</td>
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</tbody>
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Students will be expected to have mastered these concepts and be able to apply them in the course.

**Independent Case Study Requirements:**
You will be assigned a case at the final class section.
Topics to be included in the write-up:
1. Company History and Description
   a. Detailed account of the firm’s history including why and how it started
   b. Any significant milestones in the company’s development
   c. Organizational ownership structure
2. **Current Analysis**
   a. Current goals and objectives
   b. Current strategy
   c. Financial Analysis – give a brief overview (to the extent available)
   d. Competitive landscape

3. **Family History**
   a. From the founder through the current generation, develop a brief history of the family including where the family originated and any myths, rules, etc.
   b. Family members in management positions and in ownership
   c. Their title
   d. Job responsibilities
   e. Career goals

4. **This is the most important section of your paper. You should devote appropriate attention to the following:**
   Using the models and concepts developed in class, analyze the decision matrix faced by current management and discuss the options in the context of control, strategic growth, and liquidity. What do you think is the best solution for the firm, and what do you think actually happened? Are there other options not mentioned in the case that you think would be viable? Be sure to analyze the manner in which the structure of the family, family dynamics, management of the business, personality styles, and ownership structure will influence or affect the ultimate decision.

**Independent Case Study Due Dates:**
- **Term Paper: Case to be assigned**
  o Students will be assigned a case on the final day of class.
  o Students should individually write their case study – this is NOT a group project
- **Term Paper Assignments: Due Friday, September 13th**
  o Paper should be approximately 6-10 pages; typed in 12 pt. double spaced with normal margins and footnotes or end notes
  o Papers must include a bibliography as well as any supporting Exhibits (Note: these are not included in the 6-10 page length).
AN OVERVIEW OF THE COURSE
The course outline is provided below. It may be necessary during the term to adjust the sequence of sessions or modify teaching materials to accommodate guest speakers. If this should occur, you will be informed by the Professor or the course TA.

Preparatory Readings;
- Generation to Generation (GtG): Introduction
- Evolution and Revolution as Organizations Grow (HBR), Link

August 28 AM, Topic 1, Introduction – Systems Models and Company Valuation:

*How do Privately Held Firms, including Family Firms, fundamentally differ from other types of companies? How do these differences influence financing decisions?*

Readings:
- Note on Valuing Control and Liquidity in Family and Closely Held Firms, Villalonga, Belen, HBS Note 9-209-104.
- Case Assignment: Kohler Co. (A), HBS, Canvas, Kohler (B) to be handed out in class

Guest Speaker: Professor Daniel Wolfenzon, Corporate Valuation Methods

August 28 PM, Topic 2, Capital Structure and Financing Options in Private Firms:

Venture Funding, Old School M&A, the Control/Growth/Liquidity Tradeoff

Readings:

August 29 AM, Topic 3 – Maintaining Control – the Founder’s Dilemma:
How and why do controlling families retain control of their companies? Do these mechanisms add or detract value from the underlying company. How does the desire to maintain control affect financing decisions in the firm?

Readings:

- GtG: Part I, Section 2, The Family Developmental Dimension
- GTG: Part II, Section 4 – Founders and the Entrepreneurial Experience
- Kachaner, Nicolas, Stalk, George & Bloch, Alain; What you Can Learn from Family Business (HBR), Link:
- Case Assignment: Reclassification at Facebook, Columbia Caseworks, Canvas
- New York Times Co., HBS, Canvas

August 29 PM Topic 4 – Financing to Grow/Expand/Diversify - the CEO Dilemma:

How do Families balance retaining control of their companies with capital needs for growth and expansion?

Readings:

- GtG: Part I, Section 3 – The Business Developmental Dimension
- GtG: Part II, Section 5 – The Growing and Evolving Family Business
- Baron, Josh & Lachenauer, Rob; What to Do If a Feud Threatens Your Family Business (HBR), Link
- Stalk, George & Foley, Henry: Avoid the traps that Can Destroy Family Businesses (HBR), Link:

Case Assignment: Spyder Active Sports, HBS

Guest Speaker: Alan Goldberg, Lindsey Goldberg Private Equity

August 30 AM Topic 5 – Milking the Cash Cow – The Shareholder Dilemma:
How do families balance the need/desire for liquidity and the need for growth of the business, and both of these with the desire to retain control?

Readings:
- GtG: Part I, Section 1 – The Ownership Developmental Dimension

Case Assignment: Ford Motor Company’s Value Enhancement Plan (A) HBS, Canvas

August 30 PM, Topic 6 – The Role of Governance in Financing Decisions and the Expanded Family Office

What role can governance and the expanded family office play in alleviating the tension between control and capital needs?

Readings:
- GtG: Part II, Section 6 – The Complex Family Enterprise
- Selections from “Financing Transitions: Managing Capital and Liquidity in Your Family Business” by Francois M. de Visscher and John L. Ward, *
  * Handed out in class

Case Assignment: Nash Engineering, Canvas

Questions:
- Describe the situation Nash finds itself facing in the case.
- Discuss the various financing options available to Nash. What are the pros and cons of each option, and how important are these issues to the Nash Family?
- What choice do you think the Family chose, and why?
- What are the key strengths and weaknesses of the Nash Engineering Company and the Nash Family?
- What are their options? Evaluate the three strategic alternatives that are being considered: (a) Stand Alone (b) Sale of the Nash Engineering Company and (c) Recapitalization with Elmo/Siemens. Are there any other approaches you would suggest?
- What type of financial and ownership structure would best support an acquisition, as well as shareholders' long-term goals?
- What would your final recommendation be?

Guest Speaker: Eduardo Rossi, The Expanding Role of the Family Office