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IN THIS ISSUE

Page 1

The Story of The Washington Post
 Transition at the Center

Page 2

Protecting Seniors' Interests
 Market Research Case Study

Page 3

Karofsky Passes Baton to Clark

Page 4

Case Study-Discussion from the Experts

Members' Benefits

The Northeastern University Center for Family Business offers a select group of family-owned businesses these membership benefits:

- Participation in Executive Breakfast Case Conferences.
- Constituent Forum Participation.
- Subscription to Family Business Quarterly.
- Invitations to College of Business CEO Breakfast Forums.
- Access to student interns.
- Networking opportunities.
- A family business bibliography and access to NU's libraries.
- Participation in research.
- Opportunity to link your Web site to the Center's.
- Family Business Web-Based Search Engine www.fambiz.com

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The Story of The Washington Post: Perspectives from the President

Business Perspective

For ten years, Alan Spoon was President of The Washington Post, serving with the famed mother-son team of Katherine and Donald Graham. At this intimate breakfast meeting, Center members learned how Alan managed his role as a non-family member leader of this exceedingly high profile family owned and managed enterprise.

After watching a short video of Katherine and Don Graham discussing the benefits of a family controlled business, Alan Spoon shared some of his personal observations and experiences of working with the Grahams as a non-family member professional manager.

Alan began with a brief history of The Washington Post, describing the growth of the company beyond the core newspaper business into other media such as television, cable, magazines and its highly successful Kaplan education division. The company went public in 1971. Joining the company in 1991, Alan managed a diversified business and together with Katherine and Don Graham they experienced strong growth across five platforms.

At this meeting, rated by Center members as "extremely valuable," Alan described the benefits of a family controlled business. He mentioned how family ownership can be liberating to professional management when family control affords a more patient outlook toward growth by looking at a longer-term perspective. The principals were



Alan Spoon

willing to grow their franchises over time. This longer-term vision proved to be very strategic and was a competitive advantage compared to large public non-family owned and managed businesses that tend to manage for shorter term profits.

Spoon discussed the importance of educating investors and analysts about the advantages to a slower more methodical growth. He told investors that the principals would be fully accountable for the long run with creation of value, but they were not going to run the business quarter-to-quarter.

Discussing the importance of respect between the family and professional managers, Alan noted that there were very few Graham family members at the Post. Members were welcomed, but only in a professional capacity. Saying, "You can't fake it," he claimed the family leadership wouldn't have worked if Katherine and Donald didn't have strong abilities and talent as well as strong respect for each other. "If the company is being run as a lifestyle or as a source of dividends it won't work."

Spoon also mentioned how important it was for the company's Board of Directors to understand the family dynamics. He told Center for Family Business members how the Grahams understood the importance of a quality compensation plan for professional management. Their compensation packages were not only market competitive, but also included long-term incentives to reflect the long-term strategic visions for the business.

"One of the challenges for professional management," Alan said, "was the speed of decision making. Decision-making at The Post tended to be slower, more careful, considerate and reflective."

While not privy to all the intimacies and informal conversations between family members, such as at Sunday dinners, Alan said it was important to keep the professional manager in the loop on relevant family issues as Katherine Graham successfully did so with him.

Transition at the Center: Karofsky Passes Baton to Clark

Paul Karofsky will retire on June 30, 2004 as Executive Director of Northeastern University's Center for Family Business and pass the baton to Ted Clark, Academic Specialist at the College of Business Administration. In this candid dialogue, Clark peers into the future as Karofsky reflects on his years of experience.

TC: Paul, how did you get involved in family business education?
 PK: I had a privilege of growing up in my family's wallcovering business and being the third generation to run

it. After 23 years, as the industry was moving vertically, I felt it was best to harvest and thus sold the business to one of our suppliers. I then returned to school and focused my graduate work on the psychosocial lives of families, specifically the manner in which parents and adult children relate to one another. It then seemed quite natural to blend my life experience, some new academic training and a life's passion for education to work with business families. That was at a time when the field of family business education was emerging.

(continued on page 3)

Catch Your Fellow Members on WBIX Market Wrap

Paul Karofsky will continue his popular interview segments with family businesses on Market Wrap on WBIX radio AM 1060 from 4:50 to 5:00 PM.

Guests will be as follows:

May 3
 Mark Brown
 Brown Publishing Network

May 10
 Mark O'Day
 Controller Service and Sales

May 17
 Craig Pfannenstiehl
 Educor, Inc.

Save These Dates

May 19, 2004
7:30 am-10:30 am
Lessons from the World's Most
Enduring Family Businesses
Dr. William O'Hara

October 8, 2004
7:30 am-10:30 am
How to Prevent
Hardening of the Attitudes
Loretta LaRoche

November 9, 2004
7:30 am-10:30 am
Hatfield and Kayem
Families

Business Perspective

Protecting Seniors' Interests in a Business Transition

Peter Berenson, CPA, PFS of Forman, Itzkowitz, Berenson & LaGreca recently made a presentation to the Center's Senior's Forum Group. Below is a summary of his presentation.

Understanding business transition risks and how to protect against them requires a brief overview of the two basic transition types: management control and stock ownership. These can occur simultaneously or independently, and gradually or instantly. In other words, seniors can transfer daily and strategic management to the next generation while retaining ownership. Or, they can transition some or all of the ownership to the next generation while retaining daily and strategic management. Or, both types of transitions can occur simultaneously. The major difference between the two types is that as long as seniors own more than fifty percent of their business they have the legal authority to grant and/or reclaim management control. Once the fifty percent threshold is crossed, this legal authority is substantially diminished. Nonetheless, while the degree of risk may differ with either type of transition, the nature of the risks is the same.

WHAT'S AT STAKE?

Not every business transition will be subject to all of the risks discussed below, but any one of them could have profound and unintended effects.

The loss of seniors' financial security is a risk that must be carefully considered, especially if their retirement depends on the future success of their businesses. Perhaps they are looking forward to payments under consulting or non-competition agreements, or from the sale of their stock. In addition, seniors may have personally guaranteed company bank loans, leases or other obligations.

If the business proves unable to meet any of these obligations and the seniors are called on to honor their guarantees, they may have to drastically alter their retirement plans.

It's common for seniors to be concerned about their children's and grandchildren's financial security, even after a business transition has been completed. Seniors may need to consider reducing their life styles if they choose to step in and compensate for the financial effects of business difficulties.

With the high rate of failed marriages in our society, seniors' think a lot about their children joining those ranks. If precautions are not taken, a divorce settlement could adversely affect the proud tradition and financial stability of a family business.

The livelihood of employees, vendors and even the community, while not necessarily direct or legal obligations of seniors, may weigh heavily upon them when they consider a business transition. This is particularly true for businesses that are dominant employers in small communities. The results of an unsuccessful business transition can be particularly severe for these non-family stakeholders.

But, damage to family harmony and relationships is perhaps the greatest risk of all in a business transition. It's not unusual for family members to go to their graves without speaking to each other after an unsuccessful transition.

PROTECTION METHODS

Just as it's unrealistic to completely protect a child leaving the family "nest," seniors' can only use reasonable methods to protect themselves in a business transition. Implementation of these

methods should commence long before becoming a senior and span three phases of life: parent, business-manager, and creditor.

Parent phase

Protection methods during the parent phase should begin in the child's cradle and end in the parent's grave. They begin by clearly communicating expectations and business and personal values. This can often be accomplished by serving as an effective role model and should continue through all three phases of life. Helping a child obtain the best possible education provides the foundation and tools to blend his or her new independence with the values and traditions of the family business. The child should then be expected to build on this foundation by gaining practical experience either within or outside the family business.

Prenuptial agreements can be a difficult discussion topic for parents and their children who are planning a wedding, but they are receiving increasing attention as a tool to protect family businesses against the adverse effects of a divorce settlement. They are legally binding, are entered into usually before marriage, and establish the financial settlement at the time the agreement is executed should there be a breakdown of the marriage. As with any legal matter, it's important to seek qualified legal advice before entering into a prenuptial agreement.

Business manager phase

Seniors should consider additional protection methods in the business manager phase as they look toward a business transition. Advisory boards can be invaluable not only with a company's development and strategic planning, but

also with objectively addressing issues that family owners have difficulty discussing and resolving among themselves. This type of open communication can help family owners form a cohesive team, and to prepare the field for a successful business transition. Advisory boards function similar to boards of directors but their decisions are not legally binding. Few family owned businesses have advisory boards because their owners have difficulty agreeing on the need for one and who should serve on it. Research has shown that the most effective advisory boards are ones that are composed of people in the same or similar industries who have proven track records. A team of professional advisors: attorneys, accountants, bankers and consultants - can be another effective method of protection. Through its collective experience and objectivity, this team can help structure a transition plan that addresses the concerns and needs of all family members within the existing legal and tax environments.

Creditor phase

When seniors transition their businesses and depend upon payments from them to support their lifestyle, they become creditors. After all, they become the financial institution that funds the transition and, like any financial institution, they should protect themselves against the associated risks. They can accomplish this by agreeing with the next generation of family owners/managers on financial goals, benchmarks, and covenants for the business, and consequences for failure to meet them during the transition period. These steps can also help the succeeding generation by establishing a framework of accountability for them.

(continued on page 3)

Northeastern Marketing Research Students Take a Magic Carpet Ride

By Ashly Albrycht, Ann Barnanov, and Sheila Puffer

From January through April, Professor Puffer's students took a magic carpet ride with Arthur T. Gregorian Inc., the family-owned Oriental rug firm located in Newton Lower Falls that has been a trusted name in the Greater Boston area for more than 70 years. A long-time member of NU's Center for Family Business, the company was recommended to Professor Puffer by the Center's Executive Director, Paul Karofsky. He believed that their consumer-oriented products and related services would be ideal for the students to learn how to collect and interpret marketing research data. Vice President Scott Gregorian agreed that this would be a valuable opportunity for the company to obtain information about attitudes and purchasing practices toward Oriental rugs that he could use to fine-tune current business practices.

The marketing research class consisted of 34 students grouped into six research teams. With names including Rug Raiders, Rug Rats, Tassel Team,



and GregOrientals, they were ready to go on a magic carpet ride for three months. Scott Gregorian came to two class sessions early on to explain the company's history and the Oriental rug industry. Each group then designed its own survey based on standard marketing research methodology, and distributed it to 100 people for a total of 600 surveys. Each survey contained basic demographic questions along with more detailed questions about attitudes toward Oriental rugs, redecorat-

ing intentions, and advertising recall and preferences.

After gathering and analyzing the quantitative results from the survey data, the teams began the qualitative part of the research by conducting focus groups. Focus groups comprise an essential part of marketing research because they help elicit a fuller range of ideas, attitudes, experiences, and opinions held by a selected sample of respondents on a defined topic. In our

case, Professor Puffer recruited three dozen Northeastern faculty and staff who were interested in discussing rugs and carpeting to attend lunchtime focus groups on the main campus. Lunch was generously funded by the Center for Family Business, and as a further enticement the Gregorians donated two sets of hand-knotted Oriental car mats valued at \$240 per set to be raffled off to two lucky participants. The agenda and topics discussed in each of the focus groups were developed separately by each of the groups. Within the groups, each student took on a role as either a moderator, note-taker, or technician. The moderators led the discussion and ensured that the participants generally stayed within the set topic areas. Students agreed that the focus groups helped them gain insight about what characteristics of rugs are most salient to consumers. Students were able to access how participants differ on key issues, and with the insights generated through discussion, the students went on to apply them to their recommendations and conclusions in the final research reports they prepared for the Gregorians.

(continued from page 1)

TC: How did you become Executive Director of Northeastern University's Center for Family Business?

PK: After graduate school, I explored opportunities with universities in the Greater Boston area and found that Northeastern was considering the launch of a family business education program. I was asked to consult to that launch and after a few months asked to serve as its Executive Director. That was thirteen years ago.

TC: What is the value you see the Center affording its members and sponsors?

PK: About half of the Center's members are dealing with some issue of major concern, whether around planning for succession or dealing with the differing goals and perspectives of multiple family members. The other half are well aware of the risks and complexities of family held enterprise and wish to be proactive and learn how to minimize the risks of survival. The Center's goal has been to help family members address current issues and look to the future to hopefully prevent problems before they occur. The seminars and workshops we provide are focused on doing just that.

TC: What about the Constituent Forums for which the Center has become so well known?

PK: Our Constituent Forums are comprised of peers, meeting together in small groups. They have become learning communities — people who want to learn from each other in a focused and intimate setting. The result is a level of openness and sharing that is extremely rich, though not invasive. Each event typically has a day champion — a person who sets the agenda, prepares in advance and presents an issue of her or his own interest and then involves the rest of the group in dialogue around it. Topics can vary from sibling concerns to parent/child concerns to roles and responsibilities or compensation or how the younger generation "takes hold" and how the senior generation "lets go."

TC: You are remaining as a consultant to the Center for another year. During that time, how do you envision your role?

PK: I'll continue to facilitate the Epsilon Leadership Development Forum through June 2005 and serve as a resource to you in any way in which you want my help, but the management and operation of the Center will be yours. Ted, you also had personal experience in the world of family business. Tell us about it.

TC: My family owned a motel in Harwichport, on Cape Cod for 19 years. We lived on the property year round and were involved in every aspect of its operation — from cleaning rooms to booking reservations. It was a very hands-on business.

PK: What courses are you presently teaching at the College of Business? How do they relate to your new position as Executive Director of the Center?

TC: I teach Entrepreneurship courses in the General Management Group- the introductory to entrepreneurship courses as well as Management of Small and Medium Enterprises and Growth



Ted Clark and Paul Karofsky

Venture Creation. These courses cover virtually every aspect of starting and running a business from identifying business opportunities to acquiring funding to hiring and to managing the operations. I have also taught Marketing, Business to Business Marketing and Strategic Management. I think that my academic experience and "real-world" experience will bring a strong connection for the members.

PK: Will your teaching role compete with the time needed for the Center?

TC: No. I will have a reduced teaching load to provide the time necessary to run the Center. Additionally, I think that my teaching role will complement the activities for the Center and also allow for a greater connection with the College's students — especially those who come from family businesses. Those students and their families have the potential to expand the Center's base of membership and participation. Additionally, by maintaining my connection to the faculty, I believe that I will be able to expand on resources and services available for the members through both faculty research and student consulting projects.

PK: What do you see as the greatest challenges to family members in business together at this time?

TC: Businesses are always facing increased competition. Competition in general and consolidation in many industries is making everybody search for ways to be better, faster, cheaper, while still providing an increased level of customer service. This increasing level of competition puts pressure on businesses but it also puts an extra level of stress on the family. Therefore, it

becomes imperative to understand those competitive business pressures and isolate them to prevent putting an excessive strain on the bonds of the family. In other words, in addition to

being an expert in your field of business and responding to competition, family members need to understand the dynamics of being in a family that's in a business together.

PK: What do you see as your first priorities as the Center's new Executive Director?

TC: I believe that the Center is all about the members, so my priorities are simple: to provide value to the members. For me this drives everything. Simply put, I'm planning to listen carefully to what the Center's members want and then provide it at the highest level possible. By providing the programming and services that meet the changing needs of the families and their businesses, we will create value for the members and the sponsors as well.

PK: How can the Center's members and friends help you?

TC: That's a great question and if I may, I'd like to connect it to your last question as to what I see as my first priorities. My priority is to provide value to the members. So first off, to help here, I need to know what services the members need and value the most. Feedback is invaluable to meeting the needs of the members so I'd like to hear what works, what doesn't, and why. I'd like to hear what types of new programming and services are desired and I encourage all members of the Center community to let me know what they are thinking. Second, I'll add that one of the things that really keeps the Center vibrant is the diversity of membership and program participation. By increasing our membership we can increase the strength of the Center. So, a very important thing that we can all

do is to invite friends and acquaintances to come to our meetings. Once people come to our meetings and see the value of being a member, I believe they will join the Center. This will allow us to further enhance our services and continue to create value for all.

Paul, are there any particular lessons that you've learned that stand out as critically important for members of a family business to address?

PK: First, there are no quick and simple answers. One size does not fit all. As George Berkowitz said, "From a distance all family businesses look alike, but when you get up close they are like snowflakes. No two are ever alike."

About 10 years ago, researchers argued that the most pressing problem in the world of family enterprise was the inability of the senior generation members to 'let go.' Today the focus is on helping the younger generation members to 'take hold.' This, I believe, is where family business education must place its focus.

TC: What is it that has made the Center so successful?

PK: I think you really answered that earlier. It's the support of the members and the sponsors. Our membership and sponsorship attrition has been among the lowest in the field. The commitment to life-long learning has been a driving force. Feedback on the evaluations of the 300 plus programs we have presented tells us that we have been meeting members' needs. Your philosophy will ensure the continuation of this.

TC: Are there any messages that you would like to give to the members of the Center?

PK: Yes, a very warm and personal 'thank you' to all. To the Center's founders: Joe Blum, Richard Narva and Tom Davidow for their vision. To Chris Cassidy and to Dean Ira Weiss for their confidence in me. To Senior Associate Dean Jim Molloy, my able mentor, guide and coach. To our sponsors for their intellectual and financial capital. To David Gumpert and the members of our Board of Advisors for their wisdom. To the Center's members for their passion for family enterprise and readiness to explore new ideas. To my extraordinarily capable assistant, Debbie deCarvalho for her consistent attention to detail and her patience with me. To my wife, Lisa, for her unending support and love and to our daughter and son-in-law, Jody and Larry and our son and daughter-in-law David and Jenny and to our spectacular grandchildren: Adam, Sydney, Matthew, and Lily. They are the future and my inspiration.

Ted, on July 1, 2004 the baton passes to you. I have great confidence in your vision, energy, and enthusiasm and your ability to guide the Center to a whole new level. Thank you for making this transition as seamless as possible.

Protecting Seniors' Interests in a Business Transition (continued from page 2)

The following are examples of the kinds of financial goals, benchmarks, and covenants that are similar to those imposed by institutional lenders:

- Inventory turns will be no less than 2.75 annually.
- Compensation for the next generation of family owners/managers will not exceed their current levels plus 50% of the increase in net income.
- The company will make no loans to the next generation of family owners/managers.
- The next generation of family owners/managers will deliver quarterly financial statements and aged accounts payable and receivable schedules to the seniors within 25 days after the end of each quarter.
- Total company debt will not exceed 1.75 times stockholders' equity.
- The next generation of family owners will schedule and arrange quarterly family meetings, led by a facilitator, to review the company's success in meeting the goals, benchmarks, and covenants.

Failure to meet these could result in the seniors, at their option, terminating or postponing the transition, or in reclaiming management control.

It's important to remember an estate planner's response to a survey published in Silver Spoon Kids by Eileen and Jon Gallo. He said "[I say] to my clients whose children are disappointments, lazy, and fail to live up to their potential: no device that I can draft will make up for lessons that weren't learned as a child."

The owners of a third generation family business are often faced with many challenges of change including the pressures of sales growth, the competitive environment, declining margins and the increasing scrutiny of bankers. When these are coupled with a rapidly consolidating industry, it's sometimes necessary for a younger generation family member to reconsider his or her own career.

Southern Flooring Company's growth had been on plan for more than a decade. The offshoot of a third generation company, the wholesale-distributor grew rapidly through increased market share and major acquisitions. After a period of grand success, Southern Flooring found itself squeezed between vendor pressure, soft consumption, lower margins, and tight cash flow.

With a changing business climate, Southern Flooring was forced to take a fresh look at its strategy. The third generation CEO and principal owner knew that survival of the business meant recapturing control of its own destiny. He hired a strategic planner and, along with key executives, the company's leaders reviewed their strategic alternatives. These options included, purchasing a manufacturing facility, expanding into retail with a chain of stores or the sale of the company. The principal considered all these options taking into account what would be best for the company and the 250 families it supported and what would be best for himself and his family. The CEO then met with his trusted financial advisor and the duo confirmed the advisability of what appeared to the CEO as the least desirable option: selling the business.

This is the gist to a three part case discussion at the March Executive Breakfast meeting featuring the Center's sponsors as a panel of expert advisors. What follows are some of the discussions and advice provided by these experts.

Banking issues. Susan Dunnigan of Citizens Bank discussed some of the

financial issues the company's bank would be concerned with. She mentioned that financial reporting requirements would be more stringent. Taking on the additional debt was a "doable deal" especially if the bank were provided with a well-prepared set of projections and if the business adheres to the stricter reporting requirements. An important part of the agreement is to ensure that there are sufficient assets to serve as collateral. The growth of the assets appeared to be able to provide the collateral required, noting that advance rates on inventory and receivables will be negotiable, so long as the bank felt comfortable with the viability of the company.

Insurance issues. Carrie Seligman of Northwestern Mutual Financial Network reviewed some of the insurance issues that the company should consider. She said the company should be concerned with the fate of key employees. The company should look into key-man insurance for the principals. This insurance can provide the company with the ability to repay the loan to the bank or provide additional collateral. Insurance is readily available depending on health issues of the individual. She also discussed some of the management issues, including delegating many of the CEO's responsibilities to key people in management, taking some pressure off a single person. During the discussion a member of the audience brought up the importance of disability insurance coverage.

Strategic and M & A issues. Marguerite Piret of Newbury, Piret & Company led a discussion of strategic options the company should consider. These included forward integration (buying a retailer), backward integration (buying a manufacturer), selling to a strategic buyer, selling to a private equity firm, and doing nothing. Factors to be considered must be the timing of the market, whether management wants to stay in place, the risk tolerance of the owners and the impact on suppliers and

customers. She mentioned that right now the private equity market has high interest in deals of this nature.

Investment issues. Jonathan Oliver of U.S. Trust Company reviewed some of the investment issues that should be considered including the timing of selling the business, family goals and cash requirements, earn-out and lump sum disbursements. His firm runs financial simulations taking all the variables of the market into account. These are called stochastic or Monte Carlo analyses. After running these simulations on different financial plans, with varying assumptions, investment advisors are able to recommend the best type of asset allocation.

Legal issues. Jeffrey Wolfson of Goulston & Storrs started by saying that one person at each table will sell his or her business in the next five to ten years. Demographics show that in the decade after World War II a lot of businesses started up and the founders are now reaching their retirement stage. The market is currently experiencing increased activity due to pent up demand by both buyers and investors. He mentioned that historically strategic buyers pay more for companies than financial investors. He also encouraged sellers to consider retaining the real estate, which helps to reduce the overall price for the business by making it more attractive to a larger pool of buyers, while preserving a rental income stream. The buyer can always have an option to buy the real estate at a later date. Jeff urged that employment plans be kept flexible since some transactions are contingent on retaining management for a period of time. Jeff said, "Consider the ramifications of selling to an industry source and the impact it might have on your suppliers. And are you ready for the due diligence process? There might be some tidying up to do first." Jeff also encouraged a review of any unwritten agreements and getting them in writing, especially agreements with key suppliers as well as a review of any potential environmental, accounting

and tax issues to prevent surprises. Financial issues. Peter Berenson of Forman, Itzkowitz, Berenson & LaGreca discussed some of the personal financial planning and tax issues that should be taken into consideration. Peter said, "Determine the risk factors in the form of payment in the sale transaction. If the transaction is stock, will it support your lifestyle? If it's an earn-out over time, is the company viable long-term? If you are dealing with an international buyer, be sure to take currency risks into consideration." On tax issues, Peter said that whatever form of payment (stock, real estate, assets, non-compete agreements, goodwill) is best for the seller is usually a detriment to the buyer. He also told potential sellers to take into consideration the new depreciation tax rules that expire at the end of 2004. Currently you have the ability to write off the cost of assets up to a certain level all in one year. Bonus depreciation allows you to depreciate 50% of assets within the first year. Sellers need to be careful. If they use these depreciation methods now and later sell the depreciated assets within a certain period of time, the depreciation may get recaptured and come back as ordinary income.

At the end of the discussion by the panel, Paul Karofsky mentioned that once in awhile when we present these cases we are fortunate to have one of these principals with us. He then went on to identify the case as his own former family business: Northeastern Wallpaper Corporation. He walked through his decision to sell in 1988 to a multi-billion dollar Swiss supplier that wanted a distribution presence in the United States. He mentioned his personal issues of being 44 years old, and his father wanting to retire. Paul also discussed his concerns for the long-term viability of the business not having a lot of confidence in the industry and the impact consolidation had on the market. The sponsors were available at the end of the meeting to meet with members on more specific questions of their own.

37 The percentage of Fortune 500 companies that are family-owned.
(The Graziadio Report, Spring 2001, citing M.C. Shanker and J.H. Astrachan)

50 The percentage of the GDP that family businesses account for.
(Financial Planning, November 1999)

24 The average life span in years of a family-owned business.
(Ernest Doud, Sr., "Unraveling the Mysteries of Family Owned Business,")

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