

# Hidden Risks in Family Enterprise: Transforming Vulnerability into Strength

By: Tammie M. Sandoval, J.D., CTFA | Chief Fiduciary Officer

## Introduction

Family enterprises form the backbone of global commerce and community wealth. In the United States alone, they account for nearly two-thirds of employment and an estimated 60% of GDP.<sup>1</sup> Yet despite their outsized role in wealth creation and social impact, family owned businesses remain uniquely vulnerable.

The statistics tell a sobering story: only 30% survive to the second generation, 12% to the third, and a mere 3% to the fourth.<sup>2</sup> These figures do not reflect weak products or poor leadership. They reveal hidden risks that, if left unaddressed, can threaten both the business and the family behind it.

What makes these risks particularly dangerous is their invisibility. Families often focus on growth and operations while neglecting structural vulnerabilities of a more interpersonal nature. Informal governance feels sufficient until conflict arises. Succession appears straightforward until a health crisis exposes the absence of a plan. Wealth concentration appears efficient until a market shock destabilizes both the company and the family's balance sheet. Estate and tax planning are postponed until death or incapacity forces hurried decisions. And interpersonal tensions, often masked by politeness, can quietly erode trust until they erupt into disputes that fracture families and enterprises alike.

These are not failures of intent but failures of foresight. Families assume strength will carry them forward, yet strength without structure can allow resilience to degrade into fragility. The truth is the greatest threats to family enterprises are rarely external competitors. They are internal vulnerabilities that, if ignored, can unravel decades of achievement.

This white paper examines five of the most pervasive hidden risks in family owned business planning: governance gaps, succession blind spots, concentration of wealth, estate and tax planning landmines, and unresolved interpersonal dynamics. Drawing on case studies, global surveys, and fiduciary best practices, it explores how these risks can be transformed into strategic advantages when addressed openly and systematically.

## I. Governance Gaps: When Informality Becomes Liability

Family owned businesses often take pride in trust, loyalty, and shared history. Decisions are made quickly and informally; at family dinners, in hallway conversations, or under the natural authority of the founder. In the early stages, this "handshake culture" can work remarkably well, allowing families to move with agility and avoid bureaucracy.

Yet as ownership expands across generations and family branches, what once felt efficient can become haphazard. Informal understandings may suffice while relationships are close and leadership uncontested, but they rarely withstand the tests of conflict or transition. The very trust that made informality possible can erode when siblings disagree over dividends, or when cousins, raised in different households with divergent values, bring competing expectations to the table. Ambiguity sets the stage for second-guessing, and even honest misunderstandings can foment into resentment.

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<sup>1</sup> EY Family Enterprise Barometer, 2024; Family First Institute Global Data Points, 2023.

<sup>2</sup> Cornell SC Johnson College of Business, *Family business Succession Study*, 2023; PwC Global Family business Survey, 2024.

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Research shows fewer than half of family enterprises worldwide have a formal governance framework in place, even though those that do are significantly more resilient during leadership transitions.<sup>3</sup> The absence of bylaws, shareholder agreements, or voting mechanisms can leave families exposed to deadlock, litigation, or even the dissolution of both the business and the family unity itself.

### ***Case in Point: When Trust Wasn't Enough***

Consider a second-generation logistics company divided equally among three siblings. For years, decisions flowed smoothly through informal consensus, with the eldest naturally guiding direction. As the business grew, disagreements surfaced over whether to reinvest profits or increase shareholder distributions. With no shareholder agreement defining voting rights or outlining how deadlock would be resolved, conflict escalated. Employees sensed instability. Suppliers questioned reliability. Eventually, the siblings turned to the courts. The company survived, but the family relationships did not.

### ***The Psychology of Resistance***

Governance is not only a structural issue; it's a psychological one. Founders often resist formalizing rules because they view governance as unnecessary "when trust is enough." Parents avoid written agreements for fear of triggering conflict among children. Eldest siblings or dominant personalities may resist anything that could dilute their influence. Yet informality is not a substitute for stability. In practice, it leaves families vulnerable to the very disputes they seek to avoid.

### ***Governance is Stewardship, Not Bureaucracy***

Strong governance is not about undermining trust; it's about protecting it. Families that endure across generations put in place the structures that preserve unity even in moments of conflict. Shareholder agreements define how voting rights are exercised and how capital is distributed. Family councils give inactive shareholders a voice without interfering in operations. Independent directors offer neutrality when decisions grow complex. Even family constitutions can serve as touchstones when disagreements threaten to derail unity.

A useful lens for families is to ask: *Is our governance built for the future, or merely the present?* Are voting rights clearly documented? Do mechanisms exist to resolve disputes outside litigation? Do inactive shareholders understand their role? And most importantly, is governance designed to evolve as ownership passes through generations?

Governance is often mistaken for bureaucracy. In reality, it is stewardship. When decisions are made and disputes resolved within a clear framework, families preserve not only the enterprise but the relationships that bind it. What begins as a safeguard against conflict ultimately becomes the foundation of resilience.

## **II. Succession Blind Spots: Assuming the Next Generation is Ready**

Succession is often described as the defining challenge of family enterprise, and the data confirms it. Globally, only one-third of family firms report having a documented succession plan, even though every enterprise will eventually face leadership transition.<sup>4</sup> The absence of planning is not merely a statistic; it is one of the most common reasons family owned businesses fail to survive beyond the founder's generation.

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<sup>3</sup> PwC Global Family business Survey, 2024; EY Family Governance Index, 2023.

<sup>4</sup> KPMG Global Family business Report, 2024; PwC Family business Survey, 2024.

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What makes succession so complex is that it rarely feels urgent, until it becomes unavoidable. Founders delay the conversation, believing continued leadership provides stability. Parents hesitate to raise succession for fear of sparking rivalry among children. Next-generation members often remain silent, out of respect for the founder or uncertainty about their own aspirations.

These dynamics create three recurring blind spots:

1. **The Readiness Gap:** Heirs may inherit ownership but lack the management experience or leadership credibility to guide the enterprise.
2. **The Willingness Gap:** Next-generation members may not wish to assume leadership, particularly if their passions or professional paths lie elsewhere.
3. **The Unity Gap:** When multiple heirs are in line, competing visions or sibling rivalries can derail continuity.

### ***Case in Point: When Transition Became the Tipping Point***

A fourth-generation manufacturing family illustrates these risks. For decades, the company was led by a patriarch who assumed his three children would eventually share control. No plan was written, and no conversation outlined roles or expectations. When he died unexpectedly, two children with successful careers outside the business declined to return. The third, who remained involved, lacked the financial and managerial experience to command confidence. With no structure to guide decision-making, disputes escalated into litigation. Within five years, the company was sold under pressure, ending not only a business, but a century-long family legacy.

### ***Preparation Over Assumption***

Succession failures like this rarely stem from a lack of talent; they stem from a lack of preparation. Families that transition successfully treat succession as an *ongoing discipline*, not a single event. They identify and develop future leaders long before control must change hands, pairing management experience with mentoring, coaching, and objective evaluation. Independent boards often play a key role, offering perspective and accountability that family systems alone cannot provide.

The most resilient families separate ownership from management, recognizing that not every shareholder must be an operator, and not every operator must be a shareholder. They institutionalize development by setting transparent criteria for leadership readiness, creating rotation programs, and encouraging next-generation members to earn credibility both inside and outside the family enterprise.

### ***From Vulnerability to Advantage***

The essential question for every family enterprise is not, “*Who will lead?*” but rather, “*Are we preparing both the people and the systems that will allow leadership to evolve without destabilizing the business?*”

Families who can answer “yes” convert succession from a vulnerability into an advantage, ensuring continuity is guided not by circumstance, but by design.

### **III. Concentration Risk: “All Our Wealth is in the Business”**

For many families, the enterprise represents more than a financial asset. It is identity, purpose and legacy. Generations have reinvested nearly everything back into the business, believing loyalty and

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commitment will secure prosperity for those who follow. Yet this devotion often hides a structural fragility: most of the family's net worth depends on a single enterprise.

While concentration may feel like confidence, monolithic exposure can quietly magnify risk. A family whose wealth is tied to one business is vulnerable to forces beyond its control; market downturns, technological shifts, regulatory changes, or unforeseen events that destabilize both the company and the household balance sheet. According to the EY Family Enterprise Index (2024), nearly 70% of family owned businesses report that more than three-quarters of their wealth is tied to their operating company.<sup>5</sup> Yet, few have implemented meaningful diversification or liquidity strategies.

### ***Case in Point: When Loyalty Became Liability***

The pandemic underscored this risk. Consider a third-generation family in the hospitality industry whose wealth was concentrated in hotels and resorts. When global travel collapsed, revenue evaporated overnight. With no external holdings or cash reserves, they were forced to sell assets quickly to cover debt. What had long symbolized loyalty to the family's legacy became the very factor that threatened its survival.

### ***The Psychology of Concentration***

The psychology behind concentration risk is powerful. Many families equate diversification with disloyalty, viewing any reduction in exposure as turning away from their heritage. Founders, in particular, may resist seeing capital redirected elsewhere. Yet loyalty without balance can endanger what it seeks to protect. Stewardship is not about preserving the business at all costs; it is about safeguarding the family's financial wellbeing across generations.

### ***Loyalty Made Sustainable***

Addressing this risk does not mean abandoning the enterprise, but it means fortifying the family's financial foundation, so no single business carries the entire load. Families that navigate this well often pursue recapitalizations that release liquidity without ceding control, minority equity sales that fund diversified portfolios, or family investment entities designed to complement the core business. Insurance and credit facilities can also provide safety nets in times of disruption.

Ultimately, every family must decide: *Will our financial security rise and fall entirely with the business, or will the business be one of several engines of prosperity?*

Families that choose the latter gain the flexibility to weather downturns and to invest in new ventures that expand, rather than end, their legacy.

In this light, diversification is not disloyalty. It is loyalty made sustainable. It ensures the business remains a pillar of family wealth, not the whole structure itself.

## **IV. Estate & Tax Planning Landmines**

Few issues generate more anxiety for family enterprises than taxes, yet estate and tax planning often remain the least prioritized. Discussing them requires confronting mortality, wealth transfer, and fairness. All of which are topics families understandably avoid. But postponing these discussions can transform ordinary complexity into existential risk.

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<sup>5</sup> EY Family Enterprise Index 2024; UBS Global Family Office Report 2024.

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### ***Case in Point: When Delay Became the Costliest Decision***

A family-owned agricultural enterprise valued at roughly \$45 million illustrates the danger. When the founder passed away, heirs faced an estate tax liability in the millions. Because nearly all wealth was tied up in farmland and equipment, liquidity was scarce. The family was forced to sell core acreage to satisfy the tax liability, fracturing an operation that had thrived for more than a century. The estate plan had overlooked liquidity, and the cost of delay became the permanent loss of legacy.

### ***The Integration Gap***

Such scenarios are common. A UBS Global Family Office Report (2024) found nearly 60% of family-business owners lack a written estate plan addressing liquidity or tax mitigation.<sup>6</sup> The irony is that tools to solve these problems, such as Grantor Retained Annuity Trusts (GRATs) or Irrevocable Life Insurance Trusts (ILITs) are well established. Buy-sell agreements between shareholders, or between the company and its owners, can provide liquidity when capital is needed. Charitable vehicles, including donor-advised funds and family foundations, can align tax efficiency with philanthropy.

What often undermines families is not the absence of options, but the lack of integration. Estate, tax, governance, and succession planning are often handled in isolation by different advisors. The resulting patchwork may satisfy compliance requirements but fail to preserve continuity when a triggering event occurs.

### ***From Planning to Stewardship***

Forward-thinking families treat estate and tax planning as an ongoing stewardship discipline, revisiting strategies regularly as tax laws, valuations, and family circumstances evolve. They ensure liquidity to meet estate obligations without sacrificing control, and they convene all advisors, legal, fiduciary, and investment, around a unified table to coordinate decisions.

Ultimately, estate and tax planning are about forms and filings. The goal is to ensure when transition inevitably arrives, decisions are guided by purpose rather than pressure. Families who plan early preserve what matters most: control, continuity, and peace of mind.

## **V. Interpersonal Dynamics & Silent Stakeholders**

Family enterprises succeed when ownership, leadership, and purpose remain aligned. Yet beneath even the most successful families lie undercurrents of tension, resentments unspoken, expectations unmet, and affirmations assumed. These interpersonal dynamics are among the most underestimated risks to long-term continuity. They are rarely about business strategy; they are about relationships.

The most vulnerable group in this dynamic are what might be called “silent stakeholders.” These are family members who hold ownership stakes but are not involved in daily operations. Their silence is often mistaken for harmony, when in reality it may conceal frustration or disengagement. Over time, that silence hardens into resentment, especially when questions arise about dividends, compensation, or perceived fairness.

Research consistently shows family conflict is one of the leading causes of enterprise failure. A PwC Global Family business Survey (2024) found that over half of family businesses cite internal conflict

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<sup>6</sup> UBS Global Family Office Report 2024; Ernst & Young Private Tax Insights 2024.

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as a major threat to long-term success.<sup>7</sup> These conflicts often emerge not from malice, but from a lack of process. When families fail to institutionalize communication, every disagreement becomes personal.

### ***Case in Point: When Silence Becomes the Story***

A second-generation services firm, owned equally by three siblings, provides a cautionary example. One ran the business full-time; the other two pursued external careers. For years, tensions simmered as the active sibling drew both salary and dividends while the others relied solely on distributions. When reinvestment priorities reduced dividends, resentment surfaced. Without a family charter or agreed-upon distribution policy, disagreements escalated into accusations. Eventually, the inactive siblings demanded a buyout, at a valuation that strained both finances and relationships.

### ***Breaking the Pattern of Silence***

The psychology behind these breakdowns is predictable and even understandable. Families avoid discussing money and fairness because silence feels like peaceful alignment. Parents shy away from difficult conversations to preserve unity. Siblings suppress grievances to maintain appearances. In-laws, often unacknowledged but influential, can amplify divides. Left unmanaged, these patterns corrode trust precisely when cohesion is needed most.

Mitigating interpersonal risk requires more than documents. It demands a cultural commitment to dialogue. Families that thrive across generations institutionalize communication through structured forums: family councils, charters, or periodic retreats that bring shareholders, active and inactive, to the same table. These mechanisms surface disagreements early, providing frameworks for resolution to forestall strife.

Some families even develop conflict-recognition frameworks. These are practical ways to identify tensions before they escalate. Signals such as silence in meetings, withdrawal from discussions, or emotional distancing among siblings often precede open disputes. Acknowledging those early indicators allows families to intervene constructively, sometimes with the help of neutral advisors or mediators.

Conflict itself is not the enemy. Unmanaged conflict is. Families that face tension head-on, with clarity and empathy, strengthen the very trust that built the enterprise. Those that allow silence to masquerade as peace risk discovering too late that what was unspoken was also unresolved.

### ***Conclusion: Turning Hidden Risks into Strategic Advantages***

Every family enterprise begins with a vision: to create something enduring, to provide for the next generation, and to carry forward values alongside financial success. Yet the history of family enterprises reveals how delicate that vision can be. Most family owned businesses fail to survive beyond the founder's grandchildren.<sup>8</sup> These outcomes, however, are not inevitable. They result from risks that remain invisible until they are forced into view.

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<sup>7</sup> PwC Global Family business Survey 2024; Family business Consulting Group, *Resolving Conflict in Family Enterprises*, 2023.

<sup>8</sup> Cornell SC Johnson College of Business, *Family business Succession Study*, 2023; Family Firm Institute, *Global Data Points on Generational Continuity*, 2024.

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Across governance, succession, concentration, estate planning, and interpersonal dynamics runs a common thread of silence. Families delay addressing these issues not from neglect but from optimism and trust. Informality feels comfortable, authentic. Growth is prioritized over continuity. Yet in that silence, vulnerabilities multiply.

The lesson from resilient families is clear: when risk is confronted directly, it transforms from a threat into an advantage. Structure and transparency do not weaken trust. They preserve it. Formal governance strengthens relationships. Proactive succession planning ensures stability. Diversification protects loyalty by spreading risk. Estate planning safeguards choice. Open dialogue may be awkward, but in its absence silence can lead to fracture.

For fiduciaries and advisors, the opportunity lies in helping families see what they cannot by bringing discipline into emotion, foresight to planning, and structure to vision. Even the most impressive businesses built by stolid progenitors are not guaranteed to pass through change unscathed; legacies are ensured by proactive planning, by families who choose courage over comfort and stewardship over silence.

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## Appendix: A Family Enterprise Risk Readiness Checklist

### Purpose

This checklist is designed to help family owned business owners, fiduciaries, and advisors identify potential vulnerabilities before they become crises. It can be used during family council meetings, strategic planning sessions, or advisor reviews.

#### I. Governance & Decision-Making

- Are shareholder agreements and bylaws current and signed by all relevant parties?
- Do independent directors or outside advisors participate in major decisions?
- Is there a defined process for resolving disputes short of litigation?
- Are roles and voting rights clearly defined across generations?

#### II. Leadership & Succession

- Has a written success plan been developed and shared with key stakeholders?
- Have next-generation leaders received structured mentorship and external experience?
- Are ownership and management roles intentionally separated where appropriate?
- Is leadership viewed as an ongoing discipline rather than a single event?

#### III. Financial Concentration & Diversification

- Does the family maintain liquidity outside the operating business?
- Are contingency plans in place for market or sector disruptions?
- Is the enterprise one of several engines of family prosperity, not the only one?
- Have recapitalization or minority-sale strategies been evaluated?

#### IV. Estate & Tax Planning

- Is there an up-to-date estate plan addressing both liquidity and tax exposure?
- Are GRATS, ILITs or other structures used to balance control and efficiency?
- Are all relevant advisors (legal, fiduciary, and investment) coordinated in planning reviews?
- Are estate plans revisited regularly to reflect valuation and tax law changes?

#### V. Family Communication & Alignment

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- Is there a formal forum (e.g., family council or annual meeting) for discussion among shareholders?
- Are expectations for dividends, compensation, and reinvestment clearly documented?
- Are inactive shareholders informed and engaged in major strategic decisions?
- Does the family proactively address tensions before they become disputes?

### **Reflection Prompt:**

Which of these areas would cause the greatest disruption if left unresolved, and which could become a source of strength if addressed today?