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Toxic Loyalty In Family Offices: Risks, Practical Solutions To Remain A Healthy, High-Performing Organization

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If loyalty is what we all strive for, which has tremendous personal benefits and business attributes, is there ever such a thing as "too much loyalty"? The author of this article asks what happens if the answer is "yes" and how to manage this.

Loyalty is an important quality in families and the family offices they create, but it can turn "toxic" in particular situations. Rich Wolkowitz (more on the author below), founder of Xylogenesis Family Office Advisory, explains how to spot signs of trouble, what the challenges are, and how to ensure that family offices succeed in their mission. The editors are pleased to share these views; the usual disclaimers apply. Email tom.burroughes@wealthbriefing.com

Humans strive for many things in life, loyalty chief among them. It helps to create and reinforce trust, which is something that we all seek from others but often give sparingly. Loyalty is developed over time; it is special and rare.

When there is mutual or reciprocal loyalty it opens the way for acceptance, even love. This allows one to feel safe, secure, happy, and confident. Over time and through experience, repeated acts of loyalty create an almost impenetrable bond.

From a professional or business perspective, we work diligently to create loyalty with our business partners, employees and colleagues, community of vendors, and in the marketplace of customers and analysts. This is the essence of branding and having a strong reputation.

The business of loyalty

The greater the loyalty, generally, the deeper the bond and connectivity. Hence, the greater the chance for continuity, care, and concern in our dealings with and for each other (i.e., higher performance), and to achieve both endearing and enduring relationships which often lead to repeatable, scalable, and more businesses (i.e., higher revenues). Simply put, deep loyalty creates the opportunity for employees to work at a higher capacity and for consumers to purchase goods/services at a greater frequency, perhaps, even a higher price point.

Entire industries have evolved to encourage loyalty through loyalty rewards programs and employee/customer incentive programs. Industry tools and benchmarks, such as Net Promoter Scoring, have been established to understand and measure one's own comparative loyalty to others in the same or different industries to provide a competitive advantage.

Is there such a thing as "too much loyalty"

If loyalty is what we all strive for, which has tremendous personal benefits and business attributes, is there ever such a thing as "too much loyalty"?

There can be too much or extreme loyalty, leading to "toxic loyalty."

Family business or family enterprises are ripe for toxic loyalty. In founder led businesses, there is often the "cult" of the personality. In successive family generations, there is a deeply established and devoted culture. Outsiders or newcomers are often judged on "their fit" within that culture where conformity is prioritized, sometimes above everything else. Multi-generational family businesses/enterprises are often composed of multi-generational family employees, including non-family multi-generational employees, vendors, and customers. This serves to reinforce a self-contained, closed environment and to reinforce and drive loyalty to an extreme.

Family offices, like family businesses, have an even greater potential for the pitfall of "toxic loyalty," as their very essence is dynastic family and wealth legacy. This is often supported by another layer of insiders and a deep structure of multi-generational board members and trustees who know the family intimately and intensely.

Intense life cycle events are not theoretical but actual and ever-present in a family office, by its very definition of supporting life-cycle business/wealth, personal, and philanthropic events and endeavors. These shared experiences create greater bonding and loyalty.

Non-family employees of a family office can be so entrenched that the proverbial "jump in front of a bullet" for a family member is often offered and expected. This only serves to intensify an already intensely loyal environment. And this deep commitment can lead someone to look out for another's interests, possibly even to the detriment of oneself.

Most businesses strive for the type of loyalty found in family offices, family businesses, and family enterprises. The rewards can be positive and create a dynamic culture that is rare among other forms of business organizations.

While there are tremendous positives for loyalty, as with any extreme, it can also create certain risks, particularly when loyalty becomes blind or uncritical.

Consequences of toxic loyalty

Toxic loyalty in a family office is a situation where those in the system remain loyal despite negative behaviors or poor performance. This can be harmful because it may lead to:

1. **Inefficiency:** An incompetent family (or non-family) member might hold an important position because of their perceived loyalty, leading to operational inefficiencies and poor decision-making.
2. Stifled innovation: A fear of challenging other family (or non-family) members can discourage new ideas and innovation, limiting the business's growth potential.

3. **Lack of growth and improvement:** A system based on loyalty and not on merit may miss opportunities for organizational improvement, self-improvement, or an inability to acknowledge and address weaknesses.

4. **Resentment**: Family (or non-family) employees may feel undervalued or marginalized, leading to resentment and decreased morale due to an unhealthy culture.

5. **Conflict avoidance:** Problems within the business might be overlooked or ignored to avoid confronting family (or non-family) members, which can worsen things over time.

6. **Lack of objectivity and diversity:** Inability to discuss, disagree or challenge because it is considered disloyal or insubordinate, leading to "groupthink," an organization of "yes" people, and less diversity of thought.

7. **Family and financial strain:** Poor business decisions driven by toxic loyalty can lead to financial losses and jeopardize the company's sustainability and durable family (and organizational) harmony.

8. **Lack of accountability:** Family members may escape accountability for their actions, leading to an unhealthy work culture. High performing employees may exit the business, leaving less qualified employees who all think and act alike.

9. **Succession challenges:** Inadequate succession planning due to toxic loyalty can hinder the transition of leadership to the next generation, risking the future of the business because of burnout, stagnation, and a lack of work-life blend.

10. **Decline in reputation:** Continual poor performance due to loyalty-based decisions can damage the reputation of the business in the industry and lead to unethical conduct and behavior, perhaps even wrongdoing.

Toxic loyalty can erode the overall health and success of a family and their family office, making it crucial to prioritize competence, open communication, and merit-based decisions.

Solutions to mitigate toxic loyalty

It's important to foster a culture of loyalty that values critical thinking, open dialogue, and ethical conduct.

Encouraging diverse perspectives, constructive dissent, and a willingness to challenge ideas can help mitigate the risks associated with extreme loyalty and create a healthier and more resilient organization. Having "difficult conversations" is critical to a healthy family and family office, and there is an art to having disagreements, without being disagreeable.

Addressing toxic loyalty in a family office requires careful consideration and proactive measures. Consider these solutions:

1. **Professional development:** Provide ongoing training and development opportunities for family (and non-family) members to enhance their skills and knowledge, ensuring that they are well-qualified for their roles.

2. **Clear roles and responsibilities:** Define clear job descriptions, roles, and responsibilities for all family (and non-family) members based on their qualifications and expertise, minimizing favoritism.

3. **Outside advisors**: Seek advice and guidance from external consultants, advisors, or independent board members who can provide unbiased insights and recommendations.

4. **Transparent communication:** Foster open and transparent communication within the family and the business, encouraging discussions about challenges, expectations, and potential conflicts.

5. **Merit-based promotions:** Implement a merit-based promotion and compensation system that rewards performance and contributions, rather than blind loyalty.

6. **Performance metrics**: Establish objective performance metrics and key performance indicators (KPIs) to evaluate the effectiveness of family (and non-family) members' contributions.

7. **Conflict resolution:** Develop a formal process for resolving conflicts and addressing issues, ensuring that concerns are tackled constructively and without fear of retribution.

8. **Succession planning:** Create a well-structured succession plan that outlines a clear path for leadership transitions based on competence and qualifications, rather than familial relationships and extreme loyalty-based actions.

9. **Diversification of leadership:** Consider involving non-family professionals in leadership positions (board, management, and operations) to bring fresh perspectives, new ideas, and expertise to the business.

10. **Ethical standards:** Establish and uphold a strong code of ethics that emphasizes values such as fairness, integrity, and accountability in all business dealings.

11. **Regular reviews:** Conduct regular performance reviews for family members, offering constructive feedback and opportunities for improvement.

12. **Rotation of roles:** Encourage family members to rotate roles within the business to gain diverse experiences and prevent complacency.

13. **Outside directors:** Appoint independent outside directors to the board who can provide unbiased oversight and strategic guidance.

14. **Conflict of interest policies:** Implement robust conflict of interest policies to manage situations where personal and business interests collide.

15. **Counseling, coaching and peer groups:** Provide counseling or coaching and peer groups for family members to address interpersonal conflicts, improve communication skills, and promote a healthier work environment.

By implementing these solutions, a family and their family office can mitigate the negative impacts of toxic loyalty and create a more effective, innovative, and sustainable enterprise.

Extreme-anything can be unhealthy and damage any organization. Especially in a family office, even loyalty must remain in balance.

About the author

Rich Wolkowitz is founder of Xylogenesis | Family Office Advisory and serves as a family advisor with more than 25 years of experience of multiple family offices (of all types). Rich's background is in law, business, independent board of director service, management, operations, financial services, and professional service firm leadership with a focus on serving multigenerational families and their full business and life continuum of needs.

Wolkowitz began his legal career in The White House, and then joined an AM 100 law firm where he was an equity partner, chair of the firm's hiring committee, and practiced international and domestic M&A and business transactions, serving as outside general counsel and consigliere to public, PE/VC-backed, and family enterprises.

Wolkowitz then joined his own family's third-generation enterprise before managing two different single-family offices as non-family leader. Prior to founding Xylogenesis | Family Office Advisory, he managed a global family business consulting firm. He now consults for family offices, whether existing or in concept, supporting the family and their family office staff, and team of multidisciplinary trusted advisors. Wolkowitz graduated from the Georgetown University Law Center (LLM, International Transactions and Comparative Law with distinction), Gonzaga University School of Law (JD, cum laude and editor of The Law Review), and University of Illinois - Champaign-Urbana (BS, Agriculture Economics with honors) and resides in a suburb of St Louis, Missouri.