THE HOLLEMAN COMPANIES

*Four Generations of Financial Security Leadership*

# Holleman Business Succession Forum

**KNIGHT A. KIPLINGER**

Editor in Chief and President

Kiplinger Washington Editors, Inc.

Interviewed by Vernon W. Holleman, III

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INTRODUCTION

Mr. Vernon Holleman: Hello, and welcome to another edition of the Holleman Business Succession Forum. Today, I present the interview I did with Knight A. Kiplinger, who is editor in chief and president of The Kiplinger Washington Editors, here in the nation's capital, a position that both his father and grandfather held. Knight will talk in great detail about how the company has survived the 90 years it has been in existence. The point of these forums is for folks to hear first-hand the experiences that other business owners and leaders have gone through in their own family's business, and I think you will gain great insight from Knight on such topics as the loss of a sibling and following a legendary father and grandfather.

Also, on the mechanical aspects, he talks a great deal about shareholders and having both voting and nonvoting stock, and the importance of voting control, issues that arise with every family business on taxes and liquidity, and also how to take care of employees who are not family members.

He does this with great enthusiasm and energy, and I think you will gain a tremendous amount as you listen to him and the things that Kiplinger organization has experienced. I very much hope that you will gain from this.

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Mr. Vernon Holleman: Well, Knight, thank you very much for joining me on the Holleman Business Succession Forum. I'm thrilled to have you.

Mr. Knight Kiplinger: I am happy to be with you.

Holleman: This is the first time I have had a second family member interviewed, so I am particularly pleased about that. I thought that we would have a great opportunity to expand upon the interview I did with your father, who went back all the way to his very early days in talking about the Kiplinger organization and his experience in it. I thought we would expand upon that, and I thought where we might start is with your decision to enter the journalism field and what process you went through--what discussions, if any, you had with your father about that as a career path, and whether you were even invited to start at Kiplinger, or whether he said, "No, I want you [to start working] elsewhere." Take us through those early days, in your thinking.

Kiplinger: I had always enjoyed writing and reporting, in the most general sense of being inquisitive and learning about the world around me. But I had not been involved in student journalism in high school or in college. I did not write for the daily newspaper at Cornell, as a number of my friends did. That was more like a full-time job. But I did have summer college internships in editorial work. One summer I worked as an editorial assistant at the National Association of Counties, the trade association of county government in America...wrote articles, edited newsletters, things like that. Another summer I worked as a writer in the campaign of a friend of mine who was running for Congress. So, I did writing, I did editorial jobs in the summertime.

Holleman: But studied history and political science?

Kiplinger: History, political science, economics. Cornell does not teach journalism in the traditional sense. It is one of the few things Cornell does *not* teach. So, I did not have any opportunity to major in journalism--and would not have majored in journalism anyway.

Holleman: I remember your father had a strong opinion about that.

Kiplinger: Yes. My grandfather, my father and I all feel that it is more important for a journalist to be very well-informed about the subjects he covers, and that's more important than studying the process of journalism, which you can pick up on the job. I would much rather hire somebody who majored in Western Civilization or American Studies or economics or European history or something of that sort, rather than journalism. Now, there are a lot of wonderful journalism graduates who minored in those subjects, too.

When I thought about graduate school, I decided that I wanted to study international affairs, and I went to the Woodrow Wilson School at Princeton, intending to get a master's degree in that, and perhaps work in economic development work overseas---Ford Foundation, U.S. AID, State Department, something like that. It was a bad time to be in college in '69 and '70...student strikes, faculty strikes, moratoriums at two different universities [Cornell and Princeton] in two consecutive spring semesters. I was not able to finish the academic program in the spring of '69 at Cornell and then in the spring of '70 at Princeton, in graduate school, because of [racial strife] and Vietnam protests. Things ground to a halt. So, I dropped out of graduate school after one year. And what did I do? I got a job as a newspaper reporter. It was sort of like this subliminal pull. The attraction of journalism finally worked upon my psyche, and a light bulb went off, and I said, "This is what I want to do." No pressure from my father, no discussion with my father. We never talked about this at all. I got a job at a very fine weekly newspaper in Rockville, Maryland, the *Montgomery County Sentinel*, which had been quite a training ground for top young journalists.

I did not ask my father about working at the Kiplinger organization. He did not offer me a job at the Kiplinger organization. I had an older brother who had just started in the family business. My brother, Todd, went into the Kiplinger organization right out of college and spent his entire life there. There are two traditional paths into a family business. There is going into it right after school--as a green employee, a rookie, working in different departments, rotating among different tasks, learning how the business works. The other path is to get your experience outside the family business, ideally in a related field, and then come into the family business years later with a lot of experience that you bring to bear upon the challenges of the family business. That is the "lateral entry" approach.

I much prefer that second approach. It is impossible for a young family member to get an accurate read on his or her talent as the child of the boss. The boss might say to the department head or the new hire's manager, "Just treat Bill, treat Joan, like everybody else." But it is not going to happen; it is just not going to happen. The manager is internally rolling his eyes, saying to himself, "Yeah, sure, I am going to demote the boss's son for bad performance, I am going to chew him out for being late." It usually does not happen. A young family member should work outside of the family business, work for other companies that do not owe him anything. And they should not be a big vendor of the family business either...

<u>Holleman:</u> Right.

<u>Kiplinger:</u> ...or a business partner.

<u>Holleman:</u> Yes.

Kiplinger: You should work for a company where they owe you nothing, where they are going to treat you, in fact, like every other young employee. If you do really well, you will develop a greater sense of self-confidence and pride and self-worth from knowing that you made it on your own.

Holleman: Sure.

Kiplinger: Even if you carry a famous family name, as I did--and as my father did, as the son of *his* eminent journalist father--even if you carry a well-known name and people are saying, “Oh, he’s got it made, he is a Kiplinger, he’s got a family business to go to”—nonetheless, working side by side with you every day, they are going to make their own judgment on whether you are good or not. If you get promoted to higher responsibilities, you know that it was because you earned it.

So I spent 13 years in daily newspaper journalism, outside of the family business. The Kiplinger organization did not do daily journalism at the time. Today, in an Internet world, we do. But back then we did not. My grandfather and my father both started in daily journalism, at newspapers. We all know that daily journalism is the best training for a journalist, with the pressure, the deadlines, multi-tasking among several story assignments at the same time.

I did work with my father for two years on a book about Washington in the early 1970s [*Washington Now,* Harper & Row, 1975]. I took a leave from newspaper journalism to work with my father on the book. I was not on staff, *per se*, at the Kiplinger organization. I was tasked to that project, and that was a very enjoyable project.

Holleman: And it is interesting, because your father also, I think, had come back to Washington [from San Francisco in 1941] to work on a book with *his* father, if I remember correctly.

Kiplinger: That is right. That was just before World War II. He worked with his father on a best-selling book about Washington [*Washington Is* Like *That*, Harper & Brothers, 1942]. He was not on staff; he was doing that special project. But, aside from those two years in the early 1970s, I had no professional contact with the Kiplinger organization between graduate school in 1070 and my arriving in 1983, at the age of 35. In the intervening years I was named the new service chief and Washington bureau chief of the Ottaway Newspapers division of Dow Jones, a chain of 20 daily newspapers. I was probably the youngest newspaper bureau chief in Washington, at barely the age of 30. I enjoyed the work. I probably could have stayed with the Ottaway group or another division of Dow Jones. But by the age of 35, I was married, I had two children and one still to come, and the working conditions of daily journalism-- long hours, high stress and low pay (I call it a perfect combination!)--were getting to me a bit. It took a toll on a young family.

Holleman: Sure.

Kiplinger: I would get home at 8 or 8:30 in the evening, and my wife, Ann, would have fed the kids and they would be ready for bed. So, by 1983 I was thinking it might be time for a change. And once again the subliminal pull of the family business began to work its magic on me. I began to talk to my father. I was 35, he was 65. (It’s always easy for me to remember how old each of us is or was in a given year, because we’re 30 years apart in age.) My older brother, Todd, was not active on the operations side of the publishing business. He worked in asset management, helping to invest the retained earnings of publishing in passive investments.

Holleman: There were just the two of you? There were no other brothers or any sisters?

Kiplinger: That is correct. And we will talk later about the keys to longevity in a closely held family business, and how we have survived for 90 years. We will talk a little bit about genetic luck, and we will talk about careful estate planning and the careful structuring of a business for across-the-generation continuity.

But back to 1983: My brother Todd was not active on the publishing side. He had worked on editorial tasks and circulation sales tasks and a variety of things, but it was pretty clear that he was not destined to be the operating head of the publishing business. That was okay with him. It was okay with my father and me.

So I came to the Kiplinger organization as a vice president. That is the higher executive level that the later-arriving son or daughter achieves by virtue of what they have accomplished already in the outer world. When I came in, I was accepted more readily, as an equal and a peer of the other senior editorial people, because I had a background similar to theirs. I had accomplished things. I was a Washington bureau chief and a columnist, and there was greater acceptance, I think. I often joke with other inheritors and scions of great family businesses about nepotism. I sometimes joke that the presumption of incompetence works in favor of the young family member. The presumption of incompetence lays the groundwork for pleasant surprises. If the family member is actually smart and hardworking and diligent, the "surprise factor" works in his favor. People say with surprise, "Gee, he is kind of smart."

Holleman: Yes...“he can actually string two sentences together”!

Kiplinger: Yes... “He is pretty good, I think that we can work with this guy.” I joke about this with Steve Forbes and Don Graham. Steve Forbes sometimes says that he owes his success in life to his astute selection of grandparents.

So I came into Kiplinger as a vice president. I focused immediately on our most challenging division of the company, our personal finance magazine, then called *Changing Times*, today called *Kiplinger’s Personal Finance Magazine*. It was our least-profitable division. It needed the most work. That is where I focused my attention, rather than the *Kiplinger Letter* and the *Kiplinger Tax Letter*, our smoother-running and more-profitable divisions. I wanted to focus on an area where I could make the greatest impact, and that is where I worked.

Holleman: Did you also have an interest in that area before, or did that just sort of grow quickly overnight?

Kiplinger: I had had an interest...

Holleman: And remind me: the year is now in the early ‘80s?

Kiplinger: Yes, ’83.

Holleman: You are essentially still the only publication focused on personal finance, or is *Money* magazine in the picture at that point, or others?

Kiplinger: *Money* magazine was started in 1972, when the *Kiplinger* magazine was already 25 years old. The *Kiplinger* magazine pioneered personal finance journalism as it is practiced in the world today. *Money* was the second magazine, but with the vast resources of Time, Incorporated behind it, it rose to a high circulation and was capturing the lion’s share of the advertising dollars in the personal finance publishing category in

1983. So we were the number-two magazine in the category in revenue. Editorially, and perhaps in stature among financial planners and investors, we were the top magazine in the category, but commercially we were number two.

Holleman: Some of that competition, I assume, drove you as well?

Kiplinger: That's right. I had long been interested in business and economic journalism, had long been interested in investing. I read avidly in investing theory and strategy as a teenager. I grew up reading the Kiplinger books on investing. So that is how I came to Kiplinger and what I did when I first arrived. I spent much of the Eighties and Nineties focusing on the magazine, increasing its health, working with a very, very capable team. Ted Miller was the editor of the magazine during most of that time, later becoming our senior vice president for publishing. My father was a better business manager and delegator than his father had been. His father, like many founders, held the reins very tightly. He had a few trusted lieutenants, but he really did not give them real decision-making authority. My father was much better at that. He brought in a Navy colleague from World War II who had risen to the rank of rear admiral in the U.S. Navy, Admiral James O. Mayo. When Admiral Mayo retired from the Navy he came to Kiplinger and really became our chief operating officer, as executive vice president. We did not use the titles CEO and COO, but for practical purposes, Jim Mayo was the COO. My father trusted him greatly. Jim Mayo was a great mentor to me.

Every family member coming into a business--whether young, as my brother did, or at 35, as I did--should develop strong relationships with key executives in the company who know how the place runs and who will be a good counselor and a good mentor. It is hard for the parent to be as good a mentor as a non-family executive can be. Jim Mayo and Ted Miller and others in the company—for example, Jack Kiesner, the editorial director of the *Kiplinger Letter*-- were key colleagues, mentors and allies of mine as I gradually took over the operating control of the business myself, in the years that followed.

In many family businesses, titles change before authority is transferred. In other businesses, authority transfers before titles transfer. Of the two, it is probably better if authority transfers before the titles.

Holleman: Yes.

Kiplinger: Titles are simply titles...they are symbolic. Let me give you an example. I know family businesses where a young family member is named president at a fairly young age. But the founder is still there. The father or the mother is still there as chairman, and for practical purposes is running the company. The young family member with the title of president often does not really have the authority of the president. At Kiplinger, it is sort of the other way around. My father was very good about gradually passing authority and decision making, not just to me as vice president and later as president, but to other key executives. He was a good delegator. But we were often slower to transfer the titles that went along with the authority. That is no big deal. I was named president of the company in 1992. By then I was 44 years old or so. My father and I got along well. We shared responsibility. He, the chairman, and my brother, Todd, who was vice chairman, and I, as president, conferred on everything. We did so when my brother and I were vice presidents and my father was still president. So the transition was gradual. It was collegial. It was amicable. There was never a time when my brother and I sat around saying, "I wonder when Dad is going to pass the presidency to one of us."  It was a nonissue. We were not that into titles. Maybe this is because we are journalists, and we are sort of down-to-earth people. We are not really corporate people.

Holleman: But, don't you think some of it was because of the experience he had had? My sense would be, his not wanting to have that kind of friction, if you will...

Kiplinger: That is a good point. My father learned a lot of painful lessons about how family succession of control and transfer of control should work and should not work. He learned a lot of negative management examples from watching his father. His father was a brilliant journalist, a highly creative man in American publishing, a true innovator. But he was kind of a quirky person personally. He did not always have the best management style. My father learned from that. My father wanted to avoid, I think, a lot of the pain that he had experienced with his father. I give my father a lot of credit for doing it much better. The transition between my grandfather and my father, in a sense, was sadly aided by the ill health that my grandfather experienced in the 1960s, before his death in 1967.

Holleman: So, you knew him as a young man, as a grandchild?

Kiplinger: Yes, I did. Like a lot of grandchildren in their adulthood, I and they often wish they had spent more time with their grandparent talking about the serious things in life.

Holleman: Sure.

Kiplinger: Occasionally I would talk to him about his recollections of journalism in Washington and politics in Washington in the 1920s and 1930s. A few times I had long conversations in my teen years, when I was in high school at Landon, about those subjects, but not as many as I later wished I had had with him.

Holleman: Sure.

Kiplinger: I read my grandfather's writings voraciously today. He wrote constantly. He would go home from a day at the office and spend a whole evening banging on his typewriter, writing thoughts about the world, family history, recollections of his boyhood in Ohio. So, there is a very rich printed record of my grandfather's thoughts--not just his professional writing but a lot of personal writing as well. I really value that record.

My grandfather never retired...never officially retired. There was never an announcement. There was never a retirement party. My father became president of the company in the early 1960s, or maybe even earlier...it might have been, like, 1959 or so. By the early 1960s he was effectively running the company, in part because my grandfather's health was declining. My grandfather died at the age of 76, having been quite ill with respiratory problems and emphysema in the last couple of years.

My father and my grandfather only worked really closely together for about 11 years, from 1956 to 1967. It was a difficult 11 years, and I do not mean to minimize that at all. Today, my father is 92 and I am 62. My father comes into the office every day.

Holleman: I saw him driving in yesterday.

Kiplinger: Now, it is not broadly known that my father retired several years ago. My father instituted what I called at the time a "stealth retirement." The retirement was simply a personal letter to me, as president, saying that he was retiring from the company. It triggered a variety of personnel and HR procedures and retirement fund transactions and all that. There was no announcement to the staff. No one on the staff knew that he had quietly retired. There was no party, no announcement.

Holleman: No cake?

<u>Kiplinger:</u> No cake, nothing like that. He continued to come into the office every day. He only retired a few years ago, in his late eighties. At 92 he still has an office at the company. He is our non-executive chairman of the board. He is not salaried by the company. He is not even a major shareholder of the company today, and that is something we can talk more about later.

<u>Holleman:</u> Yes, we do want to talk about that.

<u>Kiplinger:</u> So, I give my father credit for hiring good supporting executives, whether family or non-family, giving them real authority, trusting them to make operating decisions daily on their own, and to offer their good advice on major decisions. It worked very well, and my father continued to come into the office every day and contribute in valuable ways for more than 20 years after the age of 65. Now, in large corporations, it is hard to still do that, even though we have abolished 65 as a mandatory retirement age in American society and even though anybody may work forever, under federal law. In most corporations there are contracts or prior arrangements that would move a senior executive out, at least in his late sixties. But my father continued to be a salaried executive of the company and a valuable contributor to the company as chairman of the board for more than 20 years after the age of 65, before finally retiring in his late eighties. Today at 92, he still comes into the office every day. He attends our weekly management committee meetings. He is a valuable counselor. He does not second-guess decisions he might not agree with. He certainly weighs in with his opinion. The last 15 years have been a tumultuous time in American publishing, a painful, tumultuous time that has turned the media world on its ear, on its head (or on any other body part you wish

to name). He has been a valuable counselor to the senior management of the company all through this period, and I am very happy for that.

Holleman: Let's talk a little bit about the ownership structure and some of the success you have had, and the mechanics that have worked, things that have not worked, or things you wished you had done or did not do, etc.

Kiplinger: Sure. Our company is 90 years old this year, 2010, having been founded in 1920. As you know, the survival rate of closely held family businesses through three generations--and 90 years--is a very, very rare occurrence in America. A very small percentage of businesses are still in the family, closely held. It does not happen by accident. It has to have a neat alignment of many forces. Some of them are somewhat random and some have to be carefully planned.

For a closely held business to survive for three generations, let's start with one prerequisite: You have to have at least one family member per generation who is able to and interested to run the business. Sometimes in large families there are several family members working in a family business. That has its own challenges.

The Kiplinger family was sized just right for this to work well. My grandfather was married three times, and had children with all three of his wives. My father had a half-brother, who died young. He had a half-sister who died fairly young. He had one full sister, who did not work in the family business. So my father was the clear heir apparent--being in journalism, being smart, being capable, and basically, being my grandfather's only son who could have done that. In the next generation there were other grandchildren by all three of my grandfather's marriages, but only two sons of my father—my brother and I. Both of us went into the family business, my brother much earlier and I somewhat later. My brother and I worked amicably in the family business.

One reason that a lot of family businesses do not go to the second generation, let alone the third, is there is nobody who wants to work in that field; they just have interests that lie elsewhere. The part that is not accidental or genetic, that requires careful planning, is structuring the business for continuity and for longevity.

Here are some of the key parts of it: You have to plan for the estate taxes that are going to come due when a family member who is a large shareholder of the business dies or when the second person, the spouse, dies. There are various ways to plan for that. One way is to disperse ownership in such a way that no one family member's estate is so big that the tax bill will be huge and a burden on the company at that person's death. I'm talking about dispersal of ownership but not control...dispersal of stock which confers financial benefits on family members but not control.

At the Kiplinger organization, like a lot of other closely held businesses, decades ago we created two classes of stock: Class A shares, with voting authority, and Class B shares, which confer financial benefits [primarily dividends] upon the shareholder but no say in how the company is run.

My grandfather dispersed the Class B shares throughout the family--the non-voting shares--to his daughter's family (my father's sister's family) in Dallas, Texas; and to the family of his son by his second marriage, who died young; and a lot of shares to the family of his daughter from his third marriage. So, there were lots of [relatives]--sons, daughters, grandchildren--who did and still do own Class B shares of the Kiplinger family company, non-voting shares.

But the control of the company resided in a stock trust that voted a majority of the Class A shares. My father actually did not personally own the Class A shares through which he controlled the company...they were owned by the trust. The trust named him the agent to vote those shares in all major decisions relating to the company, including even the possible sale of the company. Those Class A shares that controlled the company were not even officially part of my father's estate, because they were in a trust.

There was a succession plan in place for decades, which I call an emergency succession plan. It was not a succession plan that spelled out how control would gradually transfer from W. M. Kiplinger, the founder, to Austin Kiplinger, the son, to another generation or to anybody else. It was not a succession plan for the daily management of the company and who would run the company and who would have such titles, with timetables and all that. There was never a succession plan like that, but there was always an emergency succession plan that would have safeguarded the continuity of the company--its operations, its daily management--in the event of the untimely death, say, of my father, Austin Kiplinger. The voting-stock trust conferred the power to vote those shares to Austin Kiplinger, but if he died suddenly, a group—I think it's three to five senior executives of the company, including my brother and me, if we were living--would be named to vote those shares and run it and really decide the future of the company among themselves. That is what I call an emergency succession and continuity plan, tied to the voting control of the company.

Holleman: Sure.

Kiplinger: Doubling back to dispersal of ownership and how this has been key to our survival for 90 years, the Kiplinger company is very unusual, almost unique, in that it was never intended to be run for the primary financial benefit of the Kiplinger family. The Kiplinger organization was structured and has been run for the primary financial benefit of other people not in the Kiplinger family: our *employees*, not just executives but our rank-and-file employees; and our *customers*, our subscribers, through the maintenance of editorial quality and square dealing with them.

Do I really mean this--a closely held family business that is being run primarily for the benefit of others? Yes, but let me explain further. My grandfather gave a big chunk of his ownership of the company to all the employees collectively 60-some years ago, when this was not really the vogue. He created a profit-sharing and stock ownership trust of sorts, which today we would call an ESOP...Employee Stock Ownership Plan.

<u>Holleman:</u> ESOP, sure.

<u>Kiplinger:</u> They did not exist when he created this for our company. But for practical purposes, he created a pioneering ESOP. He and a silent early investor in the company, a Boston businessman named Paul Babson, both contributed some of their stock. Years later, at the high-water mark of employee ownership of our company, the employees collectively owned over one third of the Class B shares. This third of the company that the employees owned through this ESOP was almost three times the largest individual shareholding in the Kiplinger family.

Normally, if your name is on the door, people assume you and your immediate family own the whole company. Ownership of a company with your name on the door typically means you do whatever you wish, whatever the company can afford--you can pay yourself enormous salaries, you can pay yourself large dividends, whatever. That's not the Kiplinger way.

The stock my grandfather gave to his employees did not include individual shareholdings for non-family executive members.  In a lot of companies there is shadow stock, phantom stock, things like that, or stock options that are given to key executives individually.

But Kiplinger was always sort of a "communitarian capitalist" company.  Benefits were and are equal for everybody.  There are no special executive perks...no executive cars, club memberships, etc., charged to the company. (Benefits might be proportional to earnings, but they are the same benefits for everybody.)

My grandfather also gave a big chunk of his Kiplinger stock to a private foundation that he created, The Kiplinger Foundation.  This was another way that he got this stock out of his personal estate into friendly hands, a private foundation.  Now, today the IRS has rules in place that limit the percentage of a related closely held company that a private foundation can own.

Holleman: Sure.

Kiplinger: When my grandfather gave a lot of stock to the Kiplinger Foundation when he started it, those rules were not in place.  I cannot remember the highest percentage of our company that the foundation once owned; at one point it might have been 10, 12, 15 percent, something like that.  When the IRS put in rules limiting shareholding by a private foundation related to a closely held business, we gradually sold those foundation shares back to the company, or we donated them to charities that then sold them back to the company.  So today The Kiplinger Foundation owns almost no Kiplinger stock, just a negligible amount.

You see what my grandfather was doing here, with these gifting strategies. He was reducing the size of his estate in a variety of ways, by gifting non-voting Class B shares to family members, by giving a big chunk of the company to employees, and by giving away a lot of his wealth to charity, giving both Kiplinger stock and liquid assets to The Kiplinger Foundation.

Now, this was not just for tax-savings strategies. The tax savings were a secondary consideration or motivation for this. He did this because he was a relatively simple-living Midwesterner with bedrock values about honoring your employees, honoring your customers, using the wealth you have accumulated for the good of the community, being philanthropic. Those are the reasons he did this. Coincidentally, it reduced the estate tax bill and made it easier for the company to survive from generation to generation.

A word about annual profit sharing at Kiplinger: In any given profitable year, more of the operating earnings of the Kiplinger publishing company passed to employees, in a variety of ways, than to the Kiplinger family shareholders who control the company. Of the operating earnings, a big portion would be directed to year-end cash bonuses, which in the salad days of the company were large...sometimes 10 or 15 percent of an employee's salary. Another big chunk of the operating earnings of the company went to employees in deferred profit-sharing...sometimes another 10, 12, 15 percent of salary. If we paid a dividend, remember that the employees, who collectively owned one-third of the company, got one-third of the all the dividends too.

Holleman: Today you have a formal ESOP?

Kiplinger: No, it was always the Kiplinger Employees Profit Sharing Plan.

Holleman: Okay.

Kiplinger: It was a large shareholder of the company, and it also received each year a portion of the earnings of the company that went into the employee accounts. So, after many years of service, an employee's individual account within the profit-sharing plan grew in three ways: from the annual contributions of the profits of the company; from the dividends paid on the Kiplinger stock that the plan owned; and from the appreciation of the Kiplinger stock value as the company grew.

So, when an employee left the company--not just retired but left for any reason at all--they would receive their calculated balance from the plan. We have had a number of million-dollar retirements from the Kiplinger company...employees who had been there for a long time whose balances in the Kiplinger Profit Sharing Plan--their share of the stock, the accumulated profits from deferred annual profit sharing, the dividends--exceeded a million dollars. (And this is in addition to the retirement benefit they would receive from our old defined-benefit pension plan.) We had fairly low-level employees--a loading dock supervisor, a data-processing clerk, a maintenance person—who retired after many years with $300,000, $400,000 or $600,000 of deferred profit-sharing and their share of the Kiplinger stock in the plan. We had several senior executives retire with well over a million dollars in cash, not including their future pension payments.

So my grandfather was an unusual kind of entrepreneur when he decided to set up a profit-sharing plan for all employees, instead of a profit-sharing plan just for senior executives, which a lot of companies have. He said, "I cannot differentiate among the important contributions of everybody doing his best for this company; so everybody will go into the profit- sharing plan after one year of service. Everybody is in the plan, and the profit-sharing amounts will be the same percentage of everybody's salaries." Obviously, the *amounts* would be greater for senior executives, but it would be the same *percentage*. This was a very unusual ethic and concept years ago.

In the 1930s, when my grandfather's business was really taking off and beginning to thrive—ironically, during the Great Depression--he was making so much money in a business that he owned the majority of himself, that he gave huge year-end cash bonuses to his employees, sometimes equal to their annual salaries.

In recent years at our company, in the financial challenges that publishing has faced, a lot of these things have changed. We began to worry about the liquidity of the employee stock trust, and the ability of the stock trust to cash out departing employees. The plan usually had enough liquidity to cut that big check to a departing employee when they retired or when they left for other reasons. But at times the plan didn't have sufficient liquidity. So the company would have to buy Kiplinger shares back from the employee stock trust. This became a liquidity challenge for the company in years that profits were meager.

In recent years, I also became concerned that too many of our employees had too much of their lifetime financial security riding on the fortunes of our company, and too much of their retirement security tied to their employer stock. As a financial journalist, I am always urging people who work for a publicly traded company--and have a 401(k) that is full of their employer's stock--not to let their employer's stock get to be too big a portion of the 401(k). So a few years ago, the company began to buy back Kiplinger shares from the employee stock trust, to diversify the trust's assets and protect our employees from a downturn in the fortunes of the publishing industry and company. It turned out to be a very good thing for our employees.

At Kiplinger, in the golden days of publishing, we had the world's greatest retirement security package. We had, and still have, a defined-benefit pension plan, of the sort that no company in its right mind would start today and many companies are trying to shed. Like many companies, we are taking steps to get out of the pension plan business. So a couple of years ago we closed the defined-benefit pension plan to new hires and stopped crediting current plan members with higher future pension benefits from additional years of service (a so-called "freezing" of plan balances). But we still maintain the defined-benefit plan for plan members, both current and future Kiplinger retirees.

Holleman: Sure.

Kiplinger: For new hires, we offered instead a very generous 401(k) with an employer contribution, not just a match. Every company--well, most companies--have an employer match, but the employee has to defer his income first, has to contribute first. Then the employer will typically contribute 3, 4, or 5 percent on top of the employee contribution. At Kiplinger, we make a *first dollar* employer contribution, whether the employee contributes anything or not.

Holleman: Yes, good.

Kiplinger: Right now, it is 3 percent. We will put in 3 percent of an employee's pay and then they can contribute whatever they want after that, but they get the 3 percent from us first. So, a few years ago, when we decided that continuing to run a defined-benefit pension plan--with all the future liabilities that that entails--was financially risky for the company (the same decision that many large corporations have made), we created this very generous 401(k) plan for new hires. But as I said, we continue to operate the pension plan for a few hundred retirees and for 50 to 75 or so current employees who have earned significant future pension benefits from their years of service at Kiplinger.

Over the last couple of years, as I noted earlier, we have bought in all the Kiplinger shares that were in the employee stock trust. So there is no longer employee stock ownership of the Kiplinger company, but—in light of the current struggles of publishers like us--this is a good thing for the employees, and the more-knowledgeable of our employees know that.

We bought the employees' Kiplinger shares over the last ten years at ever-higher share prices. So the trustees of the stock trust, on behalf of the members of the plan, were selling Kiplinger shares high, at ever-higher prices, and the last installment--the last purchase of $6 or $7 million of Kiplinger stock from the employees, around 2007--was at the all-time high share price of the Kiplinger company.

<u>Holleman:</u> Do you value the company each and every year?

<u>Kiplinger:</u> Every second year, typically. We had a long tradition of biennial professional appraisals, and we would typically get two outside appraisals, and we would use the average of those two appraisals for all private stock transactions, transactions between Kiplinger family members. By law, you have to have an appraisal before a transaction with an ESOP or an employee profit sharing plan that owns stock. So there were Labor Department, ERISA requirements that we have an appraisal. But we also would do the appraisals for intrafamily transactions.

This would be a good time to double back and say what became of those Class B nonvoting family shareholdings of the sons and daughters and cousins who were descended from the founder, W. M. Kiplinger. For many years, the company paid a modest dividend. The dividend typically represented a yield on the share price of one and a half percent, and maybe some years it hit a 3 percent--not unlike the dividend yield on a share of an S&P 500 blue-chip stock.

In many closely held family businesses, dividends are very high. They sometimes represent a large percentage of the annual earnings. Generally, I think dividends should never consume more than about a third of the annual operating earnings of the company. You should retain more earnings for the future needs of the company. So we always paid a modest dividend, and that was pleasing enough to the aunts and uncles and cousins who owned Class B shares of Kiplinger.

Holleman: How many people in total is that number?

Kiplinger: Good question. The high-water mark of individual family shareholders was 15 or 16 a few years ago, spanning three generations. The family members would see the periodic appraisals of the company stock. They were satisfied with the modest dividend that we paid. They were satisfied with the integrity of my father and my brother and me, confident that we were running the company honestly, that we were paying ourselves relatively modest salaries to run the business on behalf of all shareholders, that we had transparency, and that we were forthcoming at all times about the financial condition of the company.

The key to good shareholder relations with family members who do not work in a family business is square dealing--fair dealing, transparency, and giving them no reason to question whether the family members who work in the business are feathering their nests to the detriment of other family members. The periodic appraisals and a modest dividend, and--even more importantly--making a market in family members' ownership shares, this is very, very important.

Family members who do not work in the family business should never feel that they are trapped in an illiquid asset. The treasury of the closely held family business should have the resources-- the retained earnings, the capital-- to buy in family shareholders who wish to sell for any of a number of good reasons: If their interests go in different directions, if they want to diversify their portfolio, if they think that too much of their financial security is tied to a family business being run by relatives in a distant city and they are nervous about that, or if their financial planner or their estate planner says, "Too much of your worth is tied up in this closely held business that you do not know enough about."

Relatively few of our family's "outside shareholders" over the years wanted to sell. We were rarely being approached saying, "I would like to sell $300,000 of my Kiplinger stock or $1 million of my Kiplinger stock, something like that." They were pleased with the appreciation of the asset, as reflected in the appraisals. They were pleased with the small dividend, and they were, I think, proud to still own a piece of the company.

This changed in the last 15 years or so, for a variety of reasons. When you get down to the third generation--and today the fourth generation, great-grandchildren in some families--you are farther and farther from the founder, the tradition of the company, and what the company means to you as a family member. You have different interests, and I have cousins who do a variety of things unrelated to our family business. You want diversification. You want liquidity. You want capital, maybe to start a business of your own. So we have had more requests in recent years for stock redemptions by family members, and happily, we have usually been able to satisfy those, because we have managed the company very conservatively over the years.

Remember, I said that--after the large payment of portions of profits to employees and small dividends to family shareholders--we almost always had retained earnings inside the company, every year, that we would invest, both in the growth of our business and in non-operating assets. We would invest in financial assets. We would invest in real estate. So, if a cousin of mine or an aunt or uncle of mine called me up or wrote me and said, "I would like to redeem some shares," we were able to honor those requests. We would say, "Well, we had an appraisal a year ago; our board of directors will adjust that appraisal to reflect some recent business conditions, and we will buy your shares at this price. We would be happy to show you how we arrived at this valuation, explain the appraisal to you, and we will make a market in your shares." So it has always been very amicable.

We are in the process--and by "we," I mean my immediate Kiplinger family, my father and I and the company which we control--of more actively redeeming shares of other family shareholders. When my brother died two years ago--tragically young, only 62 years of age--his family needed liquidity. They lost his salary, which was never lavish, and they had been living on his salary. We are trying to liquefy his family as our company finances permit, by buying in shares from his family.

With another branch of the family, descended from my grandfather's third marriage, we have a multi-year installment purchase going on of their Kiplinger stock, and that is about to be completed next year. Some years, we have created a stock redemption kitty for family members who wish to sell their stock. Our management committee and the board have declared a pool of capital available, and we have bought back family stock in proportion to the size of their shareholding. If we have a kitty of $1 million, a family shareholder who owns 8 percent of the company can receive 8 percent of that stock redemption pool, or $80,000, in that year. So we try to be very orderly and very systematic. I do not know another company that has been quite as systematic about this as we have tried to be.

I write an annual letter to family shareholders when the books are closed for the year, telling them how the company did, the things that went well and the things that went badly. They appreciate that. They know that if they want to come to Washington from Wisconsin or Washington State or Texas, I will sit down and go into a lot more detail with them.

As I mentioned, we are in the process of buying in the shareholdings of far-flung aunts and uncles and cousins. There is only one other branch of the Kiplinger family, my father's sister's family in Dallas, who today still own a significant portion of the Kiplinger company, and that portion is probably up in the mid-teens as a percentage of the Class B shares. My aunt is 90-ish, in okay health but not great health. I--as the CEO of the company--have to be looking ahead to the liquidity challenges that the company is going to face, and the requests of family shareholders for the redemption of their shares. I hope we do not have too many redemption requests at the same time. I knock on wood that my aunts and uncles and father and cousins will continue to live long and healthy lives, both for the pleasure of their company and also so it is not a big strain on the company to meet these estate tax and stock redemption demands.

Holleman: You bet. Now, what I have heard, as a description of what you have just described, is sometimes referred to as a "cousin consortium." You get so many cousins owning shares, and you have different circumstances where liquidity is needed or wanted. But it sounds like where you have not had trouble--and I just want to confirm that I am hearing this right--is with the cousins' involvement in management, via the share vote.

Kiplinger: Exactly.

Holleman: It sounded like that your grandfather did a tremendous job of putting the company in a position so that you did not have family shareholders saying, "Hey, I do not like the way you handled this, or I am voting this way." So, you have been able to have a little bit more diplomacy.

Kiplinger: Exactly. The reason that a lot of family businesses are sold prematurely, sold outside the family to a third party, is the dispersal of the shareholdings are *voting shares*, and a raider can go around to a lot of disaffected cousins and gather up voting shares--sometimes a majority from a lot of small shareholders, or at least a plurality of the shares--and can get themselves a seat on the board and can get themselves a voice, or in some cases they can actually buy out the majority of the company from six or eight or ten cousins who all want to sell. Suddenly this outsider controls the company.

If every Class B shareholder in the Kiplinger family ten years ago--when there were 16 or so of them--all wanted to sell their shares to McGraw-Hill or Dow Jones or some other publishing company--it would not have made a bit of difference in how our company runs. The prospective acquirer would quickly see that these were non-voting shares and could not ever control the company, and it probably would not want to buy the shares on that basis.

So, in a sense, when family members own non-voting shares, the family members who control the company really have them over a barrel. This is why in many companies there is a history of acrimony and suspicion, because sometimes the family members who run the company really are not giving a square deal to the other family shareholders. They are paying themselves very high salaries. They are living high on the hog. They are expensing a lot of personal living to the company. We have never done that at Kiplinger. At Kiplinger, we have never had company executive cars. The company has never paid club dues. We have an employee vacation resort in Florida, but it is not an executive retreat for eight people in senior management. It is an employee retreat that every employee of the company with a year of service, however low their position, can go for two weeks with six or eight or ten friends and enjoy a Florida vacation. (Family shareholders can use it too.) This is the egalitarian tradition of the Kiplinger family. So, we have never given employees or family shareholders any reason to be suspicious of the progressive stewardship of our company by W. M. Kiplinger or Austin Kiplinger or Knight and Todd Kiplinger. We are very transparent about all of this.

<u>Holleman:</u> In your experience, when you talk about private company businesses, do you have a feel—from what you have experienced yourself and what you have seen--that there is a certain number you cannot exceed in that control group? I mean, how many chefs can you have in the kitchen?

Kiplinger: Good question. Our senior management group is small, and we like it that way. We have always been a small-ish company, and we're even smaller today than we used to be, for strategic purposes. Years ago we were what was then called a "vertically integrated" publishing company, that provided a lot of the support services of publishing to ourselves. We once owned a large printing company. We once owned a large mailing and data processing center that did all of our mailing and customer service and subscription maintenance, that sort of thing. This company once had over 600 employees. Most of them were in what are called "cost centers," and the earnings of the company were being generated by a relatively small number of professional employees in "profit centers." Today, we are a small publisher of publishing professionals and editorial employees who produce our publications, and we buy the support services of publishing from other companies on the outside.

Holleman: Sure.

Kiplinger: Today we're only 125 employees instead of the 600 employees who worked in all of these support functions many years ago. A lot of companies went through the same thing. *Reader's Digest,* the *National Geographic* and many other companies outsourced the support functions of publishing. Our company has always been effectively run by a small inside group of key senior executives, vice presidents and department heads and group publishers, and that has not changed much. My grandfather ran the show much more himself for the 40-some years that he ran the company. My father, as I mentioned, was a good delegator. He built a good executive team. He shared decision making much more, and I do today myself. Our chief financial officer, Corbin Wilkes, in many ways functions today like a COO, chief operating officer--a very capable, multifaceted executive...a CPA, ex-Arthur Andersen. He's a great CFO but also a very trusted counselor to me in running the business. We have got a crackerjack vice president for editorial policy and publishing, Kevin McCormally, who really keeps watch on the editorial quality, which is the keystone of our company's success. We have a very good vice president for administration and human resources, Patricia Trudeau, and a very good vice president for sales and marketing, Denise Elliott. So we have a fine management team in place, and they are really running their divisions and their departments, so I can focus on the high-level strategic decisions.

This is a very, very challenging time in the publishing business. Just look at the travails of *The Washington Post* or Time, Inc. or The New York Times company. The Washington Post Co. gave away *Newsweek* for virtually nothing, just to get the operating loss off of its books. McGraw-Hill gave away *BusinessWeek* for very little to Bloomberg, just to staunch the bleeding of those operating losses. Our company is not doing any better or any worse than these other major publishers. Because we are closely held and our financials are confidential, we have the luxury of bleeding in private rather than bleeding on the business pages of the daily newspaper, as our publicly owned peers have to do.

Since our financials are not laid out for the world to see, a lot of people mistakenly think we must be doing a lot better than our peer publishers in print journalism. We are not. We are facing the very same challenges, and we are dealing with them internally.

Our electronic division--Kiplinger.com, our website--is doing well and growing in traffic and ad revenue. Our new-media projects, whether DVDs or custom publishing, are growing. Our business forecasting group, anchored by *The Kiplinger Letters*, continue to be solidly profitable. Personal-finance publishing, as a division, has been the most problematic the last few years, because that is where the most competition is, and it is also more dependent on advertising dollars. The newsletter division is not at all dependent on advertising dollars. It exists on subscription revenue. The more dependent you are on advertising dollars, the more vulnerable you are to the fickle decisions of advertisers to pull a big schedule out of your magazine and put it on somebody else's website, or even on your own website, which is not as lucrative as print pages of advertising used to be. So these are very difficult times.

There is not likely to be a fourth generation coming into this business. My brother's children work in other fields. My children are all in their twenties, and they are highly accomplished young professionals in different fields. They are all independent. They derive no income from our family business, because the company is not paying a dividend at present. They get no financial support from their parents. They live on their modest salaries in the nonprofit sector (two of them) and the profession of interior architectural design. So they are highly accomplished, but they do not have a professional interest in this field of journalism and publishing. Nobody in the fourth generation does.

So I will be facing over the next few years the challenges that every business owner and CEO in a closely held business faces. There is a management team in place that could run the business very well if I were hit by a truck tomorrow. My father has gradually divested himself of his Kiplinger stock, so he does not have a significant ownership stake in the Kiplinger company today. He is retired from the company. He is our non-executive chairman, and even that might change in the next year or two. I said that we have gradual transitions of titles. Some people would say this is *real* gradual! If your non-executive chairman is 92 years old and the president of the company is 62 but does not carry the title of chairman, this is the essence of gradual succession transition.

Holleman: Yes.

Kiplinger: But, as I said earlier, titles are not a big deal to us in the Kiplinger family. It does not matter to me if my father wants to remain chairman forever and carry the title to his grave. He is in extraordinary good health and vitality at 92. He looks like a very youthful, maybe 75-year-old, if that.

Holleman: Of course, we have seen a number of circumstances where kids surprise people and come, to some degree, out of nowhere to take an interest in the family business. Given where they are now--nieces, nephews and your own children--if somebody came and said, "Hey, I have an interest," what would you have them do? Would you send them somewhere else?

Kiplinger: Yes, indeed. Early in this conversation we talked about my preference for lateral entry at an older age, when you have had experience that is relevant to the business. "Relevant" is the operating word. It does not have to be in exactly the same field, but it should be experience that is useful to bring into the family business. So, yes, go someplace else. If you want to be a marketing officer, learn sales and marketing someplace else, not necessarily in the same field. If you want to be a CFO someday, learn accounting and learn internal business management.

Holleman: You obviously have had an opportunity to write and to focus on family businesses and the continuity. Clearly, part of what you have benefited from is good early rooting. Where are the biggest mistakes you see that are relatively easily correctible in family businesses?

Kiplinger: As a business journalist, I have read about a lot of situations where a young family member came in and tried to change too many things too quickly. They may have felt that change was essential and overdue, but they did not build a consensus for it. They did not listen carefully enough to knowledgeable people inside the business, and I have seen businesses destroyed by young executives who did not respect enough the traditions of the company and the ethic of the company.

But I have also seen young family members come in--sometimes unexpectedly, because of the unexpected death of a parent--and they brought fresh thinking to a company. They brought long-overdue new ideas and new ways of doing things, and they did build consensus and they did make a compelling case for the need for change. That has worked out well. I have seen both examples, probably as many of one as another.

My father changed a lot of things in the company, gradually, from the way his father ran it. I probably changed more things. The stresses that my father felt working with his father for 10 or 11 years were personal stresses, stresses based on management style and personality. The stresses I have felt most acutely in the past 15 years are not interpersonal stresses. They are the external stresses of a rapidly changing publishing and media world, occasioned primarily by the rise of the Internet. So I faced enormous imperatives--stressful mandates--to restructure the company, to change things, to address compensation and benefits issues, retirement security issues, and to divest divisions of the company and subsidiaries of the company that were no longer central to our mission. I tried to do it as compassionately and generously as possible. That is a hallmark of the

Kiplinger organization. But in the last two years of the severe national economic recession and slump in media, we had to lay off our first employees in history, the first business-related layoffs, and the first pay freezes in our company's history. This has not been fun.

Holleman: Sure. One of the things you mentioned earlier is that you had utilized some estate planning tools. Do you want to talk a little bit about this, as we finish up?

Kiplinger: Yes. I mentioned that a key to keeping a business in the family through several generations is being prepared for the big estate tax bills that come periodically.

There are two ways to prepare for it. One, you can retain a high level of your profits every year and build up resources within the business, as we did at Kiplinger, or pay out the earnings so individual shareholders can build their own wealth outside the family. We prefer keeping it within the company and providing liquidity to shareholders through stock buybacks I described earlier. And two, you have to have a lot of life insurance.

I am a big fan of huge amounts of life insurance for estate planning purposes. Now, we do not know where the estate tax law is going. It is not going to be abolished, but the rates will probably be lower in a year or two, and the exemptions will probably be higher. But, even at a lower level of estate taxation, a lot of people with closely held businesses need to have a lot of liquidity to handle those estate tax bills.

If you are not going to save for it—with simple living and deferred gratification for years and years and years, as we did at Kiplinger-- you have got to have a lot of life insurance. Most business owners, most high-net-worth people, are woefully underinsured. I am always beating the drum for buying as much life insurance as you can. When you are young, you use term insurance to protect your young family at premiums you can afford. For estate planning purposes, there are a lot of whole-life, permanent-life vehicles.

At Kiplinger, we had key-man policies on my father, my brother and me. We still do, with premiums paid by the company. We all know that tax law permits this as eligible business expenses, because the continuity of the company often requires buying in shares of stock from family members, and you can use those key-man insurance proceeds to liquefy the family of your deceased fellow executive who was a large shareholder of the company.

Holleman: Was that an important component when Todd died?

Kiplinger: Yes. We are using some of the key-man insurance proceeds that were paid to the company to gradually buy some of my brother's Kiplinger stock from his estate. Because of the financial challenges facing the company today, we are not able to liquefy his family as rapidly and as totally as we anticipated, but we are on the way to doing that. If I were to die suddenly tomorrow, the key-man insurance proceeds that would be paid to our company will be similarly useful to my wife and our children for liquefying my estate. So there is a lot of life insurance on us. The premiums are large. A lot of business owners gag at those high premiums and they say, "Well, maybe I will never need it." That is the essence of insurance. Sure, maybe you will never need it, but you just might.

Holleman: Right.

Kiplinger: It is risk management. That is what it is all about. It is the reason that you rent a tent for your daughter's wedding. You can roll the dice that it is not going to rain in the backyard that day, but who wants to take a chance? Then it is a beautiful day on the wedding day, and you say, "Gee, I wasted the money on the tent." Life insurance is the same way. So, editorially--in *Kiplinger's Personal Finance Magazine,* in books we write and in my public speaking--I am always beating the drum for having more life insurance than you think you will ever need. If that emergency hits, you will never regret having that in place. Most young families with children are very underinsured, and most business owners are underinsured. Yes, the premiums can be a burden year after year, but it is well worth it.

Holleman: Well, we certainly wish you all the best as you deal with the challenges in the current environment, and are certainly proud of the 90 years that your organization has had thus far, and we will look forward to watching the next 90.

Kiplinger: Thank you very much. Stay tuned.

Holleman: Thank you.