

The Sale of Fel-Pro

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BY FAMILY BUSINESS EDITORS

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AN INTERVIEW WITH RICH MORRIS, FORMER FOURTH-GENERATION EXECUTIVE
AT GASKET-MAKER FEL-PRO INC.

FEW companies matched its dazzling array of benefits—vacations of up to 12 weeks, a summer day-camp for employees' kids, a government bond for every newborn, \$3,500 a year for college scholarships. Fel-Pro, a manufacturer of automobile gaskets, sealants, and adhesives in Skokie, Illinois, was on everybody's list of the best companies to work for in America. It was also a highly successful business. Founded in 1918 as Felt Products by Albert Mecklenburger and his father-in-law, Hugo Herz, Fel-Pro had been run in the third generation by Mecklenburger's grandsons in the Lehman, Weinberg, and Morris clans. The firm had annual revenues of \$500 million and had a 60 percent market share for its gaskets.

When Fel-Pro was acquired by a larger, public company in 1998, its 3,000-plus employees were shocked. The acquirer was another manufacturer of parts for the automotive aftermarket, Federal-Mogul, based in Southfield, Michigan. Under a new chairman, Richard Snell, the company was being revitalized by a strategy of growth through acquisitions.

In negotiating the \$750 million merger, the family owners of Fel-Pro worked hard to preserve many of the plush benefits its employees had always enjoyed. Business writers and people in the community as well as family members, however, worried about the loss of a unique vision of a company that treated its workers well and earned their best efforts in return. Even before the merger was consummated, it became clear that Federal-Mogul would have difficulty integrating Fel-Pro's "life-

cycle" benefits with its programs at other plants. Last year, moreover, there were signs that Federal-Mogul was stumbling on other fronts and having productivity problems. In September, the company reported lower than expected second-quarter earnings, resulting in a 20 percent drop in its stock.

Rich Morris, 40, was one of two fourth-generation family members employed at Fel-Pro when it was sold. Morris, who has an MBA from Northwestern's Kellogg School of Business, worked for a few years at a large public conglomerate, Gould Inc., before coming to the family company in 1983. He was in a key position to observe the internal debate that led up to the family's agonizing decision to sell; for three years he had been in charge of seeking acquisitions that the family leaders hoped would diversify the company and enable it to survive in a consolidating auto-parts market.

In a recent interview with Howard Muson, editor of *Family Business*, Morris talked about why the family believed its only choice was to sell the company, and how the members now view their decision. The interview provides a revealing look at the gamut of emotions family members must deal with in selling a business and trying to preserve a cultural heritage for its employees.

- The Editors

Family Business: *Why did the family decide to sell Fel-Pro? What led to the decision?*

Rich Morris: We had done a great job of surviving as a stand-alone company through the 1970s and 1980s. But in the 1990's, there was a lot of consolidation in both manufacturing and distribution channels. In a mature market, price is a key issue. Our bigger competitors sold all of the engine components needed to make up a car. They were able to offer lower prices through achieving efficiencies in sales and distribution.

In addition, the automobile manufacturers were "getting it right." Cars weren't falling apart every three years. Engines were lasting longer. The only way we could grow, basically, was by "stealing" market share. But we already had about 60 percent of the aftermarket for our parts. Two other large players together controlled the rest, and it wasn't likely we were going to be able to acquire either one.

FB: *Were revenues beginning to decline?*

Morris: The year the company was sold—1998—we achieved our highest revenues and highest profit. Our trend line for 10 years had been straight up. But the market wasn't growing at that point. We predicted it would start shrinking by 2004 and would continue to shrink after that.

FB: *You had 40 family shareholders, all but six of whom didn't work in the company. Was pressure building to sell from shareholders who wanted liquidity?*

Morris: The word "sell" may have come up in dinner conversation, but never in official meetings. Fel-Pro paid a dividend that kept family members who didn't work in the business happy. We all had moderate lifestyles compared to what we could have had, so there was never pressure to sell because people needed cash.

When the word was mentioned, it was usually because family members felt uncomfortable having the majority of their assets tied up in one place. We knew, for example, that if an electric car came along, our chief assets might

become worthless in a few short years.

The main reason the family never gave serious thought to selling was simple: We were considered a model for other companies in how we treated employees. The family members felt we had something special that we wanted to pass down. We felt, "Look at how much good this money is doing where it is invested."

FB: *Where did this philosophy—this commitment to employees—come from in your family? How did you become a model?*

Morris: We did not start out wanting to be a model. People told us that we were, and that is an important distinction. Our feeling was that treating your employees well was good for business. If you treated them well, they would treat you well.

We also found that if people come to work every day concerned about whether their child is flunking school, or who is taking care of their elderly parents, and so forth, they can't focus on their jobs. By offering benefits like day care, baby-sitting for a sick child, tutoring for kids that need help, you get more productive employees and improve the company's bottom line. It makes good business sense.

FB: *Was there much internal debate over whether or not to sell the company? Were there differences of opinion in the family?*

Morris: There was some tension over where and how we could expand. I think one of the things that prompted the decision to sell was my search for acquisition candidates.

One group of folks thought we should stick to our knitting and stay in engine parts. That was what we knew the most about and so was the least risky course. Another group felt that would be very risky, however, because the internal combustion engine might someday be replaced by one of the newer engine platforms—in electric cars, for example. This group felt that we should extend our automotive line to other kinds of products needed in cars—such as new electronic mapping systems, brakes, and windshield wipers. But others felt that would have stretched us beyond what we

knew how to do.

Tensions also arose when we looked at how big we would have to become to get enough mass to compete with “the big boys.” By my estimates, we would’ve had to become a \$2 billion company by the year 2002 and a \$10 billion company by 2010 to keep up with competitors who were growing and rapidly consolidating the market by acquiring other companies. There was no way we could have gotten bank loans to finance that kind of growth. It was clear we would have to go out and get public equity, and that would have changed the nature of the business.

FB: *At what point did you conclude that selling was the only alternative?*

Morris: About nine months before the sale, we had a meeting at which we all looked at each other and realized any acquisition strategy would be very difficult. We decided we should at least explore the alternative of selling the company. Interestingly, I at first saw this mostly as a way to prod us into actually jumping into one of the acquisition strategies. I didn’t think at that point that we really wanted to sell.

FB: *Where did these discussions take place? At the board level?*

Morris: Ken Lehman and Dave Weinberg, the co-chairmen, discussed the options in our meetings on strategy. Then, yes, it went to the board, which was made up of eight family members, including three who were retired.

FB: When you finally did decide to sell, a broker brought you a number of suitors—12, according to news reports. How did you choose to go with Federal-Mogul?

Morris: The companies we talked to were invited to the party for two reasons: First, because we felt there would be good synergy between their business and ours, providing a good shepherd for Fel-Pro’s future and a reasonable price for us. Second, and just as important, because we thought they could align themselves with what we saw as our good business model and our morals.

FB: *And you felt Federal-Mogul met those criteria?*

Morris: I don’t know that we would have invited the old Federal-Mogul to the party. But we felt that under the new man in charge, Dick Snell, the company was changing and becoming something different. He said all the right things about how people were important to him and that he wanted to learn from our culture. After Federal-Mogul took over, I realized practically from day one that what he said and what his company was going to do were two different things.

FB: *What led you to that quick judgment?*

Morris: The way the company was treating the employees, the way he treated me and other family members, this isn’t the most horrible story in the world, but it was symptomatic. During the sale talks, the family leaders didn’t negotiate any non-competes or contracts to stay on. We felt that we owed it to shareholders to first negotiate the best possible price for their stock. Then, after the sale, each family manager who wanted to stay on could negotiate his own contract.

Personally, I didn’t much care whether I stayed on. I had a list of reasons why it would be fun to stay, and a whole host of reasons why it would be better to leave and do something else. But when I inquired of the new management whether or not they wanted to keep me, I received no response. The way I found out was that someone in Fel-Pro’s benefits department called and asked if I wanted to go on the COBRA plan to extend my insurance. “What are you talking about?” I asked. I was told, “Well, you are not going to be retained.”

FB: *How much staff turnover has there been since Federal-Mogul took over?*

Morris: I’m most familiar with the Skokie facility, where there are about 2,000 employees. My rough guess would be that 350 people have left or been fired.

FB: *You knew at the time of the sale that Federal-Mogul was planning to consolidate opera-*

tions, so there would be layoffs. Do you feel any promises were broken?

Morris: They really didn't lay off anyone in the manufacturing facility; some of the folks in manufacturing were, in fact, promoted. What we were told was that they would look at consolidating people in accounting, marketing—anyone that didn't touch a piece of machinery. At a meeting a couple of days prior to the sale, employees were told that "the best of the best" would be retained. In reality, politics took over. The Federal-Mogul managers in charge of the consolidation tended to choose their own people over Fel-Pro's.

That, naturally, raises some questions: If Fel-Pro had a 60 percent market share and Federal-Mogul only about 20 percent, why would they get rid of Fel-Pro's marketing people? Why would they get rid of Fel-Pro salespeople, who were better accepted in the industry and had earned a larger market share for the company?

FB: *Federal-Mogul didn't appear to try too hard to keep the know-how and experience of the family, even for the short-term.*

Morris: I don't disagree with their decision not to retain the family. Quite frankly, they did not need the family. To be honest, the family members knew how to run a family business. They did not know how to run a multibillion-dollar business, which requires a different skill set. I think the family members may have had a hard time shifting those gears. I would have, too.

FB: *Did any family executives stay on?*

Morris: Just Ken Lehman, and he stayed only for a short time.

FB: *I'm sure you realized during the sale negotiations that Federal-Mogul had fewer and less generous benefits than Fel-Pro offered its employees. They were going to have problems maintaining Fel-Pro's programs when employees in their other plants didn't have them.*

Morris: We raised that exact question and they told us they wanted to evaluate our benefits

and see if some of the better ones could be applied to the rest of the Federal-Mogul family.

Federal-Mogul, like many companies, had a core group of benefits. Some benefits were actually better than Fel-Pro's—their medical plan, for example. The biggest dollar amount spent on benefits goes for medical. What was missing were many of the benefits we had, what I call "life-cycle benefits." These don't actually cost as much as core benefits because they are spread out over an employee's lifetime and so are not fixed expenditures. For example, our pre-school program and our summer day-camp for children were used at different times by employee families than our college scholarships or our support for eldercare services.

FB: *What did you do to encourage Federal-Mogul to adopt some of these benefits?*

Morris: We actually agreed to fund some of the benefits for a period of one to five years, in order to give them time to study the programs and possibly put them in throughout their organization. It is clear that this money was wasted because they never intended to study them at all.

FB: *I've read that you "left \$50 million on the table" to continue some of the benefits.*

Morris: I don't know if that's an exact figure. But I'll give you a couple of examples. We let them have the building for our day-care center, basically rent free, so they could maintain that benefit. We rented the space to them for the summer camp for, like, a buck a year, and continued to pay for counselors and maintenance of the grounds. We put aside money in a bank-account to fund the scholarship program for the next five years.

FB: *You feel that as far as benefits are concerned, Federal-Mogul did not honor its commitments?*

Morris: Federal-Mogul was very careful about how they couched their words. From a moral perspective, I don't think they followed through. From a contractual standpoint, I believe they have. Now I know why they were so careful about what they put in writing.

FB: *As far as you know, has the changeover in ownership at Fel-Pro affected performance?*

Morris: We used to have a 97 percent “fill rate.” If the customer orders 100 parts and gets 97, that’s a 97 percent fill rate. We had 8,000 part numbers. Sometimes a few are not available when ordered, so it’s hard to achieve a 100 percent fill rate. If you have less than a 90 percent fill rate, however, customers don’t usually want to deal with you. One of the ways we achieved 60 percent market share was by maintaining a 97 percent fill rate.

In the last 20 years I can’t ever remember our company’s fill rate going below 94 percent. But I was told that in the two or three months after Federal-Mogul took over, the fill rate went down to 85 percent.

FB: *What evidence do you have that the fill rate has fallen?*

Morris: A friend of mine who worked there at first refused to discuss it with me when I called him. He was eventually let go and later told me that, yes, the rate had dropped to 85 percent and it was a real problem. In fact, he said the person put in charge of manufacturing by the new owners had been moved out of the job for that reason. After a period of time, it became pretty public knowledge that the rate was no longer over 90 percent.

FB: *What conclusions do you draw from this?*

Morris: For the first time, I think we can see proof that treating employees properly and having good benefit structures really makes a difference. There’s no way to prove it beyond a shadow of doubt, of course. But basically you have the exact same factory, the exact same people, the exact same procedures. The only difference may be that people simply aren’t motivated to make the extra effort that is needed in certain situations.

Let me give you an example. A lot of our products were sets of 30 or 40 parts. One group may have made some of the parts ordered in a set, and another group may have made the others. To put together sets for a cus-

tomers, someone has to coordinate the two groups and make sure the parts are all available and come together in time to fill the order. If morale is low, no one may be willing to make that extra effort.

FB: *It has been about a year-and-a-half since the sale. What have your personal feelings been and how have they evolved?*

Morris: I took some time to log some of those feelings in a diary. My emotions have run the gamut from elation to anger. Of course, obtaining financial freedom from the company, as you might expect, was nice and stimulated elation; the prospect of doing something else with my life was also interesting and exciting.

But not being able to go to a place I loved on a daily basis was sad. I also had fears about how the employees we left behind would do. Fel-Pro had been my life; it was a lot of who I am as a person. People who own businesses don’t realize how much of their identity is tied up with the business.

FB: *How about the feelings of employees?*

Morris: Their emotions, too, ranged from elation to anger, with everything in between. Some employees were happy for our family, and also because they felt there would be opportunities for them to grow with the larger company. But they were also angry and fearful. They were afraid the company would no longer be as safe a place to work, that they might get fired, and so on.

FB: *Did they know the sale negotiations were going on? Did you talk to them about it?*

Morris: My own experience may help other owners in this situation decide whether or not to tell employees about a possible sale. Many are going to have an urge to tell people they are selling the company, because they’ll want to be truthful. My best advice is to tell only those who need to know and leave the rest uninformed.

I know that sounds cruel and harsh. But, first, if the company is going to be sold, there’s nothing the employees can do about it anyway. Sec-

ond, if they do know, they may sit around talking about these issues and morale will go down.

Because I had basically lost my job when we started to sell—we weren't making any acquisitions, obviously—I spent a lot of time lending an ear to people who had been let in on the negotiations and were quite upset. I can tell you that from an emotional standpoint, the friends I didn't inform did much better than the ones I did.

FB: *How about outsiders? Did everyone assume you were just doing it for the money?*

Morris: Well, during a visit to my doctor, he spent more time talking about how much money he thought I was getting than my physical ailments!

Yes, some outsiders concluded we were "selling out." But, you know, people will say inappropriate things even when they don't mean to hurt you. For example, at the Bar Mitzvah of my son, which happened during the time of the sale, a friend came up to me who was, basically, very angry that we were selling. He felt there was no way any buyer would be able to maintain the benefits that existed at the company.

I'm still this man's friend. What people like him don't realize is that it may be better to sell a company so that most of the employees can keep their jobs, than to go out of business and leave 3,000 unemployed.

FB: *Did members of your immediate family have to deal with such reactions as well?*

Morris: My kids had to deal with a lot of questions, because [the sale] was a very public event. My son went into Charles Schwab's Web site and pulled up an article saying we were selling the company for \$750 million. Now he didn't know what percentage of the company we owned, but he knew that was a lot of money. My younger kids were concerned that I no longer had a job.

FB: *What did you tell the kids?*

Morris: My wife, Linda, had a wonderful way of presenting this to the children, who were 13, 10, and 4 at the time. To paraphrase, she told them, "We are no wealthier today than we were yes-

terday. What has happened is that our money was tied up in hard assets [the company] which are now being transformed into investments like stocks. So our standard of living will not change. We will make as much money from the invested assets as your father drew in salary."

It was important to reassure the children that we would still have food on the table. But we didn't want to send the wrong message. We didn't want to say, "We've got millions so don't worry about it."

FB: *Do you think you'll have to deal with other questions when the children get older, such as: "Why did you sell Great-great-granddad's company when I might have worked there and even been the head of it?"*

Morris: My son, now 15, has already posed that question. And the answer I gave him was just what I have said to you: We had no choice.

The business needed to be sold and put in the hands of a larger firm that could shepherd it forward. And even though the buyer hasn't shepherded it in a way I would have liked, I still believe the employees will be better off in the long run than if we had maintained ownership.

FB: *What are you doing now, Rich? How do you see your career developing?*

Morris: One of the things you need to do in the first year or two after you sell a business is to reinvest the assets. I have spent about half my time doing that. The other half has been spent teaching marketing [to graduate students at the Lake Forest Graduate School of Management] and doing marketing consulting.

I am also doing some consulting to family business owners who are considering selling their businesses. To date, I haven't yet participated in an actual sale of anyone's company. In fact, I try to convince them that it's not a good thing to do and assist them in finding ways to avoid it. But if they need to do it, I'll help them through the process.

FB: *What are other family members who were principals in the firm doing? Have they found other interests?*

Morris: Many of them have. My cousin Dave Weinberg is teaching graduate students at the University of Illinois about excellent personnel practices. He also consults with companies who want to set up benefits programs such as we had at Fel-Pro. Another cousin, Denny Kessler, has a management consulting firm that deals with many of the same things that Dave and I do. His son, Keith Kessler, was the other member of the fourth generation working at Fel-Pro; he has purchased a firm that makes high-end closet furniture. The three principals from the Lehman family have gotten involved in setting up an institute that will attempt to show how treating employees' right makes financial sense. All of the family members now have more time for our philanthropic activities as well.

FB: *How has the sale of the company affected family relationships?*

Morris: Without mentioning names, I would say that some family members have become much, much closer, and some have become more distant. We never had any feuds. Everything we did was by consensus, and although family members were sometimes disappointed with decisions we made, they never went away angry.

Nevertheless, one might have predicted that after the sale the families would go their separate ways. While there has been some drifting apart, I find, to my great delight, that most family members still talk to each other and see each other on a regular basis. When we get together we act more like a family than just people in business together. ■

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