FAMILIES AND THE BUSINESS OF GOVERNANCE – PRASAD KUMAR

A family business refers to a company where the "voting majority " is in the hands of controlling family including the founder(s) who intend to pass the business on to their descendants.

THE IRONY

Several studies have shown that family-owned companies outperform their non-family counterparts across several business parameters. It is also a fact, that many family companies have a very short life span beyond their founder's stage and that some 95 percent do not survive the third generation of ownership.

THE STRENGTHS

Their inherent strengths include – commitment, knowledge continuity, reliability and pride and the entrepreneurial drive.

THE PROBLEM

The main cause for such high premature mortality rates is poor governance. The primary difficulties in governance arise from:

1. Complexity: Family businesses have to engage with an additional variable that their non-family counterparts do not have to: the family. Adding family emotions and issues to the business increases the complexity.
   The "capitalistic" thinking required for successful business has to intersperse with the "socialistic" thinking necessary for family harmony. Family splits and tensions occur when the business hierarchy and roles do not match the family hierarchy.
   They have to deal with the conflicts of interest, ideas, perspectives and priorities arising from the multiple and simultaneous roles that family members have to play of being owners, managers and family at the same time.
   As the business and the family grows, further complexities arise.
2. Informality: Because most families run their businesses themselves (at least during the first and second generation) there is usually very little interest in setting clearly articulated policies, processes and procedures in the areas of business, family and ownership.
   As the family and business grow larger, this situation can lead to many inefficiencies and internal conflicts that could threaten the continuity of the business.
3. Lack of Discipline: The 'owner and entitlement' mindset leads to a lack of discipline amongst family members – from time keeping to life styles and professional conduct in business.
   A single fused identity between family and business, makes good governance a very difficult proposition.
   Family life style and social status expectations, rise over later generations and interfere with the discipline required for proper governance.
   The double edged 'devil in disguise' – the ego and other human failings of greed, arrogance, lust, envy, ignorance and anger contribute to severe disruption in relationships and trust levels.

FAMILY GOVERNANCE

The family aspect is what differentiates family companies from their counterparts. As a consequence, the family plays a crucial role in the governance of its business.

A well functioning family governance structure will mainly aim at :

a. Discovering, renewing and communicating the family values, mission and long- term vision to the family and all stake holders
b. Keeping family members (especially those who are not involved in the business) informed and abreast of business accomplishments, challenges and strategic challenges.
c. Ensuring participation in decisions and communicating the rules and decisions that might affect family members employment, dividends and other benefits they usually get from the business.
d. Establishing formal communication channels that allow family members to share their ideas, aspirations and issues.
e. Providing for a 'fair process' for managing differences

Developing such a governance structure will help build trust among family members and unify the family, thus increasing the viability chances of the business.

The major constituents of a family governance structure are:

1. Developing a family constitution. This document clearly states the family mission, vision, values and policies regulating family members relationship with the business. It enshrines the policies and principles on a wide range of issues – employment, entry, exit, decision making, media, life style, fair process, succession and so on. A participative process is important to ensure commitment to the outcome.
2. Family Institutions: which can have different forms and purposes e.g family assembly, family council and other family committees.
3. Appointment of an effective Board/ Advisory Board – external independent directors who constructively challenge family perspectives.
4. Processes for a leadership pipeline for the CEO and senior management succession.
5. Agreed processes for managing differences within the family, by the family, for the family.

It requires the spirit and skills of stewardship, to instil a strong family governance process that will inform corporate governance in family businesses, so that it is possible to 'manage the family like a business and the business like a family.'