BNY MELLON
WEALTH MANAGEMENT

Strengthen Your Family Business With a Family Governance Plan

Most family businesses take on the characteristics of their founder or founding family, especially in their formative years, operating under a system of consolidated decision-making commonly referred to as a "benevolent dictatorship." As the company grows, the family expands and the founder begins to transition ownership and control to future generations, the need to establish effective models for cooperation and joint decision-making among family members becomes more important.

According to the PwC Family Business Survey, 71% of family firms do not have procedures for resolving conflicts between family members.[1] The more stakeholders who are involved (whether they are family owners, family owner-employees, non-family owners or non-family executive management), the more important a formal set of processes becomes. Furthermore, as the owners become further removed from daily operations of the business, or as the business expands beyond the family's scope of expertise, systems must be put in place to engage professional management teams and a board of advisors to help the company grow and prosper.

WHAT IS FAMILY GOVERNANCE?

Family governance is a framework for joint decision-making among family members based on shared values, a common mission or purpose, and a collective vision for the family's future. It can help families recognize and manage their wealth, define roles, set boundaries for individuals and enable members to manage competing and interrelated interests. If implemented successfully, it provides a platform to allow families to resolve conflicts that would otherwise lead to dissolution or sale of the family enterprise, the destruction of family wealth and a breakdown of family unity.

Typical issues addressed by a family governance framework include:

- The roles, rights and responsibilities of family members
- A system regulating the appropriate inclusion of the family in business discussions
- The formation of a "family council" to oversee strategic decision-making for the business and strengthen business-to-family communication
- The creation of family employment, development and compensation policies
- The formalization of business relationships between family members
- A mechanism to sell ownership interests
- A succession process for leaders
- Dividend and distribution policies

Many of these policies are often memorialized in the form of a family constitution, a document created by the family council and approved by the broader family at a family assembly.

A PATHWAY FOR SUCCESS

When a family first begins to organize itself, it often meets once or twice a year to exchange information about the business between operators and children and to foster group communication and decision-making skills. These family business meetings may be ad hoc and informal in nature, taking place around the kitchen table or during holiday gatherings.

Family Council

As the family begins to expand, producing a generation of cousins (the founder's grandchildren) that have shared economic interests in the family business, core representatives of these primary stakeholders may consider forming a family council. These representatives may initially

[1] https://www.pwc.com/gx/en/services/family-business/governance.html

include the founder's children, who represent each branch of their respective families and hold more formal regular family business meetings with the founders.

Family Assembly

As the founder begins to think about retirement and grandchildren reach maturity and begin to create families of their own, the family council may find it useful to hold regular "family assemblies" for the larger group. These meetings serve as a platform for the family council to report to the broader family members on the state of the company, its outlook and any other topics it finds of material importance. It also serves as a forum to teach and reinforce the family's core values and culture. Spouses and children are encouraged to attend these gatherings to develop and deepen relationships with those they may otherwise interact with only periodically, yet may need to cooperate with in the future.

Activities can include presentations about the business by family and non-family managers, discussions around the strategic decisions leaders have agreed upon during the year, changes in ownership of the business and the impact of new tax laws or policies that will impact the business or its owners.

Educational workshops can also be incorporated into these meetings and may cover a variety of topics, such as the family history, the business and its customers, financial statement analysis and basic estate planning.

Family Association

As founders transition economic ownership of their business to several generations simultaneously, such as to their children and grandchildren, elections will need to be held to choose members of the family council to represent the larger group. A "family association" is a more exclusive meeting than a family assembly, where members with direct ownership interests can elect the family council. It may not be appropriate for family members, such as spouses and children without an economic interest in the business, to attend these meetings.

Owner's Council

Similarly, an "owner's council" made up of senior family members representing large blocks of ownership interests may be formed to meet as needed to coordinate their estate plans so the business is not harmed by conflicting tax and estate planning structures.

Board of Advisors

Finally, when leaders find aspects of their business have grown beyond their expertise, it is time to form a board of advisors. This group should consist of independent, multidisciplinary experts from inside and outside of the business's core industries who can provide guidance and help with unbiased strategic decision-making without fear of retaliation by any of the family's constituents. Should conflict arise amongst family members, the board of advisors can resolve conflicts and reinforce family business governance and structure.

MANAGING FAMILY MEETINGS EFFECTIVELY

Making decisions together as a nuclear family is difficult. Expecting consensus from the gathering of an extended multigenerational family is even harder. It is no wonder that many family businesses begin as benevolent dictatorships and transition into malevolent democracies, ultimately failing to preserve family wealth and unity.

In order to maintain harmony and effectively manage family meetings, it is important to take the time to learn about one another's strengths, interests, skills and communication styles. It is also important to find commonalities to work toward, such as shared family values and a common vision for the family. Once camaraderie is established, the family can focus on developing family business policies and create a framework for joint decision-making in order to effectively pass control of the family business to future generations of stakeholders.

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