HARCOURT BOARDROOM RESOURCES

DO FAMILY BUSINESSES NEED CORPORATE GOVERNANCE?

One expects the answer to this (rhetorical) question to be an unqualified “yes”. I do not believe this to be so! I will argue that the usefulness of “corporate governance” for family owners is determined both by the definition of governance and the character of the family itself. I will draw on my long year experience as a CEO in a family-owned company and several assignments as an advisor to entrepreneurial families.

Why did governance become a passionately discussed issue both in Europe and the USA in the last decades? Two causes can be identified: First and foremost the failure of large companies to sustain competitiveness, with ensuing share price erosion, and in some cases bankruptcy. And second the seemingly growing gap between shareholders’ interests and management actions. One might justifiably argue that the discussion in the US was more focused on the first issue, while in Europe shareholders’ rights held center stage.

Is better corporate governance the solution to these perceived negative developments? Certainly not by itself. Governance should be viewed as a tool, which can be of great use in some, but not all corporate issues. Governance is sometimes defined as a system of structures and procedures for preparing, taking, and controlling crucial decisions. This definition is not wrong in itself, but it leaves out the more important quality of attitude. We all know the basics of the US one-tier and the Central European two-tier architecture of Boards (by whatever name). They both have their advantages and their drawbacks, of course, but it would be hard to argue that one is better than the other. They both work as tools if they are handled right, or to put it differently, if the board leadership is up to its task.

Do family companies need governance? On the basis of what has been said before, the answer is “no” if it means taking a set of structures and procedures so to speak “off the shelf”. It is “absolutely yes” if governance is perceived as an attitude, a mental method if you will, to dealing with major interdisciplinary business problems. (Interdisciplinary: because these problems will usually be a mixture of factors like personnel, finance, strategy, marketing, production etc.)

Let me use as an example an entrepreneur who has built up a successful business. He has not written any rules, and has not drawn up organization charts. His greatest asset is his belief in himself. Does he need governance? His answer would be emphatically “no”. Simply put: he doesn’t need it, because he has it.

But situations change. Our entrepreneur might want to groom successors coming out of his family. He might see the need of hiring a strong outside manager to handle the growing complexity of his business. He might set up daughter companies in foreign countries which in their management demand a different approach than in his home country. He might want to have a sounding board to hear comments on his business plans. In all of these and other instances he would have to ask himself: How did I do it, how do I do it?

It is not easy for successful entrepreneurs to reflect on their own style of management and on their basic attitude. In most cases, they will refuse to write down the result of their self-appraisal. But they must be willing to share their thoughts and experiences. Only then will others be able to make the greatest possible input, be they family members or outsiders. Therefore the most important first step in such times of change for any family controlled company is to take a sober look at itself. It must identify its strengths and its weaknesses. But entrepreneurs (and their families) rarely want to take an objective look at themselves. There is always the fear of family frictions tending to be uncontrollable.

Qualified facilitators can be an important if not indispensable help in this process. They can ask the right questions, they have no personal interests beyond the task at hand, they help in formulating the results, they are not seen as serving their personal interests. They should be impartial catalysts. The outcome of this self-appraisal is not determined by the pre-conceived notions of such mediators. They would not be the right people if they pushed for any standard solution.

What would be the results of such an exercise? The nature of the business would be clearly defined and with it the strategic issues which will determine its future. The entrepreneur who had initiated such a process would have a better idea of the qualities and the shortcomings of his co-operators. He would be able to start a clearly defined initiation program for his children to ensure their qualification as potential successors.

And, of course, he would see where a more formal governance could be help and not a hindrance. But in any case it would be strictly tailored to his personal intentions and the nature of the expected developments.

Experience shows that formalized corporate governance in public companies does not function well without a large dose of informality. A Chairman and a CEO do not cooperate only on the basis of their “job descriptions”. They must go far beyond that in establishing a truly working relationship.

For family companies the reverse is true: informality alone will not suffice. There must be a degree of guidelines (rules) for the sharing of information and decision making. The names of such alignments are secondary. They can be called Family Boards, Owners Councils or Shareholders’ Committees. But they must be tailored to the needs and intentions of the entrepreneur and other family owners. They must ensure for their members a set of information and for well- defined areas a share in decision-making. Only then will they align, develop and commit to the right “attitude”. With the clear goal - to create new, sustainable value for their business(es) and Family itself.

Author: Prof. dr. Helmut Sihler, has served as CEO of Henkel, Chairman of Porsche, Chairman and CEO of Deutsche Telekom, Lead director of Novartis, Director of IBM...