Family Business - Looking into the Past to Build a Better Future

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In most countries, family businesses are the backbone of the economy. Some reports show that family businesses performed better than non-family businesses. However, family businesses face complex challenges involving business and investment decisions, ownership issues, and family relationships.

With regards to business succession, the process is frequently fraught with emotions and tension as family members typically have diverging interests, especially if the family firm moves beyond the founder's generation and the number of family members involved increases. That is why most family businesses struggle to survive beyond a single generation if the handover is not planned correctly.

The term family business has been defined by Davis and Tagiuri (1982), as an organisation where two or more extended family members influence the direction of the business through the exercise of kinship ties, management roles, or ownership rights. Drawing from Tagiuri three-circle model, a family business is conceived as a system consisting of three different subsystems – family, business and ownership, partially overlapping and highly interconnected, which cause the occurrence of different problems

Regarding succession problems, research shows that one out of three family businesses successfully transitions from one generation to the next. The reason is family businesses are vulnerable at times of transition in leadership when there is often a conflict between the desire to maintain and respect tradition and the need to adapt and progress the business in response to its changing environment. In most cases, family business succession involves not just the transfer of the leadership of the business but also the transfer of ownership that is traditionally perceived as a transition between a parent and children, in the Asia context, often a father and a son.

Asia has the biggest transition between family members, from the first generation to the second generation. Many of Asia's wealthy second-generation studied at universities away from home, often in the U.S. U.K. or Australia. That time away offers the children of the newly wealthy perspectives and experiences far different from those of their parents, and they often return with extreme ideas of what they want to do with their lives, which are at odds with their parents.

Unlike in the West, which has seen four to five generations of succession, Asia has just 12% of family businesses making it to the third generation (PWC, 2016). So how many of Asia's family businesses will cross this hurdle depends largely on what they do now.

The uniqueness of a Family Business

Comparing a non-family business, the managing of a family business is unique. For example, family businesses in Asia are more inclined to reinvest in themselves to support and build wealth for future generations. This is because Chinese culture believes their money is for the next generation. Therefore, parents saving more means their children will have more. In comparison, people in Western countries tend to want a good retirement and children to become independent.

Unlike a publicly held corporation, a family business can ignore the pressure of investment analysts expecting short-term returns and focus on long-term investment strategy. While operational and functional practices employed in family businesses are generally similar to those of other businesses, family businesses face challenges relating to successor training, relationships between family members and partners, and succession experience.

Succession in a family business differs substantially from that of a non-family business. A wide range of problems provoked by succession can be divided into "soft" and "hard" issues. Soft issues are related to the family and business subsystems and refer to the relationship between family members, individual emotions, personal feelings, communication, successor's motivation and education, transfer of the entrepreneurial role, etc. Hard issues are related to the ownership subsystem and refer to monetary, technical and legislative matters concerning inheritance, financing, taxation, etc.

Hence, the family must initiate and implement changes early to prevent conflicts between the rules, messages, and expectations for behaviour that may weaken the family business's survival. That means putting in place a structured roadmap to equip the next generation with the skills, experience and credibility they will need.

Younger family members can spend time in the organisation during the school holidays. Then, upon graduation, they can work outside the business for a few years to gain experience. Then when it's time for them to join the family business, there should be a plan in place to have them work their way up through the ranks.

Establishment of a family governance

Some research has highlighted the need for the family business to increase corporate and family governance protocols and structures. Successful Ultra High Net Worth families increasingly formalise strong governance across all areas of their operations, businesses and wealth management. This means embracing sound leadership, meritocracy and appropriate decision-making practices. Thus, having a family constitution can be the family's "mission and vision" and extend into more detailed guidelines, such as the roles and responsibilities of individual family members, to investment policies and practices. Ideally, it includes a plan after the current CEO steps down.

Forming a family council or committee act as a form of a governing body that oversees activities and helps in transparency and communication. They will also call for family meetings or assemblies or both on a regular and ad-hoc basis to report on family matters and discuss vital and urgent issues that may arise.

Closely associated with sound family governance can avoid the "entitlement culture", where no employment or board membership is guaranteed to family members and compensation is strictly determined based on role, responsibilities, skill, and performance. Two critical elements of effective family governance are the development of the future family business leadership and having a sound succession plan in place. Moreover, having formal family mission statements and well-defined rules across all generations reinforces family values and governs acceptable behaviour.

Advisors in the Family Business Succession Process

Managing all these issues is essential to successful succession. That is why a multidisciplinary approach is used to manage all of these issues effectively. For this reason, it has been widely recognised that an external advisor can facilitate the succession process and can play an essential role in its ultimate success.

An advisor is an external individual, not directly involved in the family business, who can support the family business in dealing with a wide range of problems, including succession planning.

At the same time, due to the growing complexity of the succession process caused by an increasing number of radical environmental changes and intensifying dynamism of the business world, research has confirmed the critical role of trusted advisors in the business succession process.

Advisors can help to improve the succession process by mentoring both involved parties, the incumbent and the successor. Advisors can act as trouble shooters that moderate the needs of these two parties or by mediating the process of sense-making among family business members in slowing down the decision process, facilitating doubt and thereby bringing new perspectives into consideration.

This can only happen if the advisor succeeds in providing knowledge and advice to both parties; the succession process proceeds smoothly and without many interpersonal conflicts. Otherwise, the less integrated party is likely to feel neglected and express negative feelings, potentially leading to a decreased satisfaction of the successor and incumbent with the succession process, a decline in their commitment, and, in the worst case, a failure of the succession process.

In summary, understanding such practices and adapting them to the values of the family is a useful first step toward keeping wealth in the family across multiple generations. In most cases, business succession planning has to do with liquidity planning, family governance and asset protection. The discussion will include family history, wisdom and values and the establishment of a family constitution and family council. With family governance in place, it can help sustain business continuity, family unity and commitment.

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