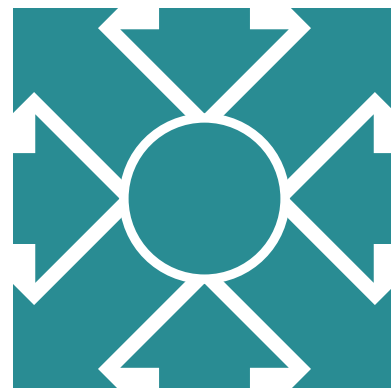


SEARCH



No 27

The Challenges of Family Business Governance

This issue of *Search* explores the dynamic situation of family businesses and their quest to professionalize their activity and build clarity among the roles and responsibilities of business owners, family members, non-family executives and independent board members.

Despite the reticence of some business owners, the importance of non-family executives and external advisors is undeniable. Combining governance and business development strategy, qualified non-family executives bring their experience, extensive knowledge and objective insight to the family business environment.

Achieving the delicate balance between family and corporate governance is key to professionalizing this type of company. Here's a look at the problem from the point of view of three countries where business owners are facing the strategic and organizational challenges of family business governance.

Alexander Hughes

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The economic situation and corporate management practices in Spain have undergone many changes over the last twenty years. These changes have mainly come from a Spanish business model which is similar to that of Italy, Greece and Germany: the family business. Today this type of business organization represents 65% of the Spanish GDP, 60% of exports, 60% of employment (80% of private employment), and 65% of Spanish companies are of similar nature. Alexander Hughes has a collective experience

of this kind of organization which comes from its own entrepreneurial beginning. We have helped many family companies develop their management structures on a professional basis, and we shall continue to provide this service as we are equipped with all the elements to do so: a strong team of experienced professionals, proven methods and extensive market and industry knowledge. Furthermore, we cannot overlook the great value that family companies can offer executives, which is the great role they have in the decision making process. Alexander Hughes Spain is currently realizing a study, in collaboration with the Institute for Family Businesses, the largest body of family firms in Spain,

about the current professional level of a family companies in the country. With this study, which will be carried out for the first time in Spain, Alexander Hughes will identify the current conditions of corporate governance in family businesses and their general interest which Alexander Hughes is dedicated to defending across Europe. The results of this study will serve as a very important reference point to be used to better understand the needs of our clients who head family businesses. Alexander Hughes Consultants will continue offering these clients all the possible assistance and solutions, but with a much deeper knowledge and understanding of their unique situation. ■



MIGUEL CODINA
MANAGING PARTNER
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Interview with Mr. Fernando Casado, General Director of the Institute for Family Businesses (Instituto de la Empresa Familiar) since 1993. Mr. Casado has also been a member of the Executive Board of the Family Business Network International.

What is the Institute for Family Businesses? The Institute is a non-profit organization devoted to creating a better environment for the development of family businesses, such as the professionalism of management, family/corporate relations, and legal and fiscal framework. The Institute is made up of 105 companies, which represent 8% of the Spanish national GDP. It is also involved in a network of different regional family company organizations, which form a group of 900 companies and represent 14% of the GDP.

What is the importance of the internationalization of a family-owned enterprise?

The world trade context is globalization, therefore every company, family or not, must consider global trade. This global trade should result from the internationalization of activities, a process that companies seeking a good position in the future will have to take into account. I think that it would be interesting if there was a bigger tendency to invest abroad, getting into international trade, and involving investments in permanent structures which give more stability to current exports. I think these are the challenges our economy has, especially in emerging countries such as India, China and parts of South-East Asia.

What specific opportunities or advantages does a family-owned company offer an executive?

Family businesses have, first and fore-

most, the will to go on. So a managing director of one of these companies has the possibility to remain in a company which goes beyond other companies. Within this context, and due to the current move toward corporate governance, there are more possibilities for professionals to take an important step within the family company, taking into account that the most important factors are the individual's human qualities.

What is the importance of an executive recruiter/headhunter in the process of professionalizing a family-owned company?

The process {of professionalizing a family business} is complex, because it has to reach family consensus requiring extensive knowledge of the company's culture and what their interests are. The company must be advised by external consultants who can evaluate and estimate these factors not only from the family's point of view, but also from that of the corporate properties and the executive who is to join them. I consider it preferable that this process be carried out by external professionals who will certainly look out for the best interest of everyone involved. ■



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Interview with Alfonso Soláns, President of Pikolin. Pikolin was founded in 1948, and it is now the leading bedding manufacturer and supplier in Spain. Their 180 000 m² surface area makes them the largest bedding manufacturer in Europe and one of the leaders in the world.

What are your views on the current situation of family businesses in Spain?

The main advantages of the family business are the strength that the businessman brings with his family values, their very high growth potential as well as their need to expand and diversify.

Today, family companies have a strong position, with a very favourable trend toward continued growth, further extending their range, all the while facing the challenge of continuity and transferring power from one generation to the next without problems.

How has Pikolin made its management professional?

Pikolin has always had the advantage of having only one shareholder since the company's founder did not have any sibling or external shareholders. This has always been a great advantage. Another



ALFONSO SOLÁNS

"advantage" was that he only had one child, myself, so the transfer was very simple. My father brought me up to share his enthusiasm for the business, so when I had finished my university degree and studied abroad, I joined the family business.

As the company grew bigger, my father incorporated professional managers, and built up an executive management team. We went from having a Staff Manager to a having a Head of Human Resources, the Industrial Supervisor became the Industrial Director, and similar changes were introduced in all of the company's business areas. More than 95% of all those who have joined the company are professionals.

When I joined the company in 1973, I was just another professional, and when I assumed full responsibility, after the death of

my father in 1996, everything continued just as it did before and the Executive Board remained the same. Since then there have been further non-family additions to the management team, and we are now in the odd position of being a family company without a single family member on the Board, not even my children, as they are still studying. I want them to train as professionals, rather than go straight from university into the family business.

Tell us about Pikolin's international growth.

There have been three phases in the company's international growth. In the 1970s we opened branches in Colombia and Venezuela. Expansion in Colombia was not a success but the branch in Venezuela functioned perfectly, and is still trading, although it was sold to Venezuelan investors a few years ago, when we decided to concentrate

on Europe.

In the early 1990s we entered the Portuguese market, because it is similar to that of Spain, which meant that we were able to create a similar brand image. We started by marketing Spanish products with the same brand and two distribution centres. We are delighted with how it has turned out.

In 1996 we signed an agreement with a Belgian group specialized in bedding with factories in several European countries. Later, in 2001, we jointly bought a French company which we now jointly manage. Since then we have grown very satisfactorily in the French market.

We are aware of the imminent expansion of the European Union to include countries with emerging economies, and we are waiting to see how things turn out, observing and analyzing the situation. We are also waiting to see what happens in China, the "sleeping giant".

In our situation, we have to measure

our abilities before taking decisions to develop in areas such as these. First and foremost we have chosen to consolidate our growth in France, while studying and analyzing other opportunities.

What are the characteristics required for an executive to join your family business?

The most important aspects, even though it is hard to recognize initially, are his human qualities. Honesty and commitment are also vital values for the professional wishing to join the company. The sector in which he is working, his relationship with the region, academic training and knowledge of foreign languages are also important factors. A manager must also have the ability to take decisions, lead and motivate. A manager should not do the work of ten, but make those ten people work efficiently. And finally, a manager must be committed to the project, this is fundamental, as is accepting the highly specific values of the family business.

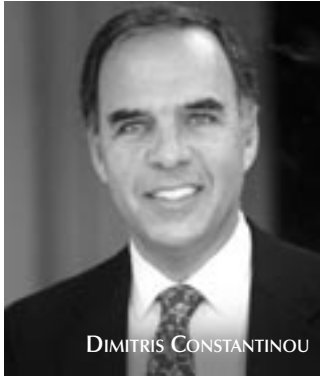
What is the role of an executive search consultancy within the process of professionalizing a family business?

Our policy over the past few years has been to try to fill any vacancies from within the company, by internal promotion. However I must acknowledge the importance of these consultancies, because they know the market, and present alternatives, making it possible to analyze whether it is a good idea to employ a specific person for a management position, and I sincerely believe that the {executive search} profession is essential to the business world. ■

FURTHER READING...

- OWNERSHIP, GOVERNANCE AND MANAGEMENT ISSUES IN SMALL AND MEDIUM-SIZE FAMILY BUSINESSES: A COMPARISON OF ITALY AND THE UNITED STATES by G. Corbetta and D. Montemerlo (Family Business Review, vol. XII, n. 4, 1999)
- FAMILY BUSINESS by G. Corbetta (N.J. Smelser and P.B. Baltes International Encyclopedia of the Social & Behavioral Sciences, Pergamon, Oxford, 2001)
- LEADING FAMILY FIRMS: A DOUBLE CHALLENGE by G. Corbetta and D. Montemerlo (New Frontiers in Family Business Research: the Leadership Challenge, P. Poutziouris and L. Steier, Manchester Business School and Alberta School of Business, 2003)
- PERPETUATING THE FAMILY BUSINESS by J.L. Ward (Palgrave MacMillan, 2004)
- HOW TO BE AN EFFECTIVE SHAREHOLDER, FAMILY BUSINESS LEADERSHIP SERIES by C.E. Aronoff and J.L. Ward (BOR, Marietta, GA, 1998)
- SUCCEEDING GENERATIONS by I. Lansberg (Harvard Business School Press, Boston, MA, 1999)

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DIMITRIS CONSTANTINOU



S.D. Constantinou YALCO group of companies was founded in 1920 by Socrates Constantinou. Today YALCO is a member of the Athens Stock Exchange and is included among the 100 largest commercial corporations in Greece, with revenues of €48 million and a net profit of €3.2 million. After acquiring its major competitor Vellifest in 2002, YALCO became the indisputable leader in the tableware, houseware and general catering supplies sector in Greece. Since 1974, the company has been managed by Dimitris Constantinou, son of the company's founder. Today, the founder's grandchildren are also playing an active role in the business.

FIVOS KIOUSOPOULOS, MANAGING PARTNER OF ALEXANDER HUGHES GREECE: Could you describe the changes that have taken place in YALCO's organizational structure during its 84 years of existence and its transition from a small family business to one of the most significant commercial enterprises in the Greek market?

DIMITRIS CONSTANTINOU: Businesses evolve in ways similar to that of human beings. If you happen to see an old acquaintance after many years since you last met, your first reaction is to think that no changes have taken place. Only when you compare this person to one of his older pictures you realize the changes that have occurred.

YALCO's evolution has been gradual and to a large degree in coordination with Greece's economical development. Between 1920 and 1960 my father maintained a small business in Northern Greece that distributed Greek products locally. The hardships our country faced at that period were many, and Socrates Constantinou built his business on his solid reputation, developing a loyal client base and serving it with a small and clearly defined organization. He relied upon principles such as integrity and order, values that we are still trying to preserve within our organization.

After 1960 and in parallel with the transition of the Greek market to a less regulated status, our company initiated contacts abroad while also expanding throughout Greece. The latter led to a more wide spread organization as well as the establishment of a physical presence in Athens. Another milestone to be considered is the installment of sophisticated information management systems in 1975, a time when our company had revenues amounting to only €200 000.

What do you think the future holds at stake for a family business such as YALCO in relation to the constantly increasing market demands?

The market's globalization has led to fierce competition and increasing consumer demands. Family businesses especially will have to respond to these chal-

lenges effectively in order to avoid shrinking in size and diminishing accordingly. In order to succeed, family businesses must maintain their entrepreneurial spirit, flexibility and speed while constantly trying to surpass multinational firms.

What is the importance of an objective Board of Directors in your group?

YALCO has consistently, and beyond the demands imposed by the Athens Stock Exchange Committee rules and regulations, been working towards the creation of an objective Board of Directors. Due to its members' previous professional experience and impartial view on our every day issues, our Board of Directors has been of immeasurable help to the growth of our company. To this point we have not yet achieved a Board of Directors that is 100% as objective as we would like it to be, but if you examine our board, you will realize that it consists of some exceptional individuals.

What are the advantages that a family business can offer as a workplace to an aspiring executive?

There exist certain distinct advantages, which unfortunately, some executives fail to notice. The direct and daily contact with senior management, the opportunity to participate in the decision making process, the speed of decision making as well as the wide range of issues that an executive might be exposed to, comprise adequate arguments for executives to place family businesses among their top choices as a workplace.

Do there exist any weaknesses in family businesses? If this is the case, how have you overcome these weaknesses at YALCO?

All businesses have some weak points. Some people consider the usual

occurrence of family members occupying the top of the pyramid in a family-owned organization to be a disadvantage. Others point to the small size of the average family business compared to a multinational firm. Finally, we frequently hear that a family business is the result of one or two generations of charismatic entrepreneurs who do not realize that the market has played them out. At YALCO, I think we will respond to these challenges by quoting the proverb "The proof of the pudding is in the eating"!

How can an executive search firm contribute to the better functioning of a family business?

As with every other business, an executive search firm can be a valuable assistant to an organization, as long as it offers thorough and integrity driven services. YALCO has only in recent years retained such services and our experience so far has been very positive.

Is there a magic recipe for success in a family business?

The factors that can be listed are endless and perhaps experts could describe them more efficiently than myself. Overall, I do not think that secrets of success really exist. However, the following are some of the

critical ingredients that seem to have a significant positive influence on a family business:

- The whole family gives 100% of its effort – directly or indirectly
- A charismatic leader exists within the family
- Speed and flexibility characterize decision making
- Profit is constantly reinvested without pressure from outside shareholders to distribute dividends
- The development of a creative spirit is enhanced, free of the bureaucratic hindrances frequently seen in larger organizations. ■



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Matching Family and Business Governance: Ingredients for Success in Family Companies

by Guido Corbetta¹ and Daniela Montemerlo

Italy has recently been under the scrutiny of the international press because of a few large family business crises. Despite this negative media attention however, it is not to be forgotten that Italy is also the home of a kaleidoscope of successful cases of family-owned companies. We consider them successful for their long-term profitability and growth as well as the continuity of relationships between the businesses and the controlling families themselves. We view them as a kaleidoscope because of their great number and their wide range of generations, family stakes, family complexity, family involvement, and family commitment to the local community.

Within this kaleidoscope of family-run businesses, each company has a fascinating and unique story to tell. However we can observe a *fil rouge* that has marked their success, and it is interesting to see how scholars from various countries – and even quite different ones like the US and some Latin American countries - converge on most of them. This *fil rouge*, in essence, is the capability to match family and business governance, so as to keep the family-business system in a dynamic balance. In such cases, the balance is rooted in the *family owners' values and vision*, is nurtured by *open communication among family owners*, translates itself into the proper *distinction of roles and professional governance and management systems within the business*. Last but not least, the equilibrium is continuously *renovated* through *generational transitions*.



GUIDO CORBETTA

Successful family businesses feature a strong and compelling *vision* of their future development, which is the characteristic horizon of family businesses as opposed to other ownership models. Such a vision has to be sustained by *entrepreneurial values* like respecting the company as a public good, to be preserved and developed to the benefit of all relevant stakeholders, meritocracy as a guiding principle of both family and non-family personnel management and entrepreneurship as a constant pressure towards innovation. Developing the vision also requires a careful assessment of company needs both in terms of financial and managerial resources; family ownership commitment to provide the most qualified resources either directly or by including external contributions is a fundamental condition for sustainable growth.

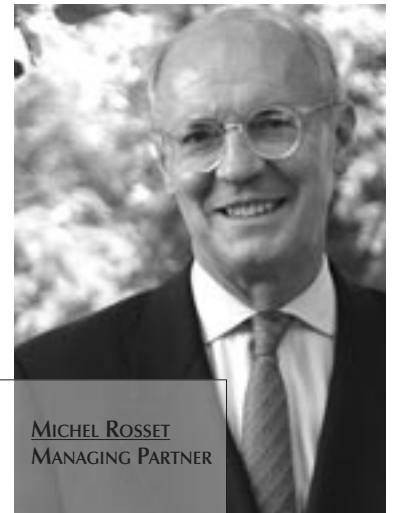
Sometimes, vision and values are implicit and somewhat “hidden” behind entrepreneurs’ thoughts and ideas. On the contrary, in successful companies these values are shared by all owners, whose cohesion is constantly kept alive and monitored through open and

systematic *communication*. This is a fundamental challenge for family businesses, as they tend to neglect the importance of communication in the erroneous belief that being part of the same family naturally makes it happen or, worse, means it is not really necessary. Instead, even within the same family, lack of communication undermines trust amongst its members; in turn, decreased trust undermines unity which will sooner or later affect the company, therefore decreasing the quality of decision-making. Effective communication requires, first and foremost, a deep awareness of its importance combined with *family guiding beliefs and attitudes* such as transparency, openness, straightforwardness, objectivity, respect for people, and the quest for harmony. Then, it is important to dispose of appropriate structures such as family meetings and corporate governance bodies like shareholders’ meetings and boards of directors at both holding company and operating company levels.

Third parties can also facilitate communication processes by helping analyze problems objectively, focusing on business rather than interpersonal issues, finding win-win solutions for both family and companies and also helping both parties avoid getting too emotional. Third party involvement is also critical to foster company development and generational transitions.

If this is the experience of many successful family companies, it has to be recognized that, generally speaking, family businesses are quite resistant to this kind of involvement, especially if third parties are “real” outsiders.

For example, non-family functional managers, who in most cases have grown up inside the company with the entrepreneur and his family, are sometimes not delegated full responsibilities and actually act like “quasi-managers”. This kind of contribution is fundamental to get entrepreneurs used to progressive delegation of tasks; at the same time, it may not be sufficient, especially when major strategic and organizational challenges need to be coped with. From this point of view, *experienced non-family managers*, possibly hired from bigger and more complex companies, can introduce fresh knowledge and skills, stimulate change and be important mentors for the next generation. But the experience of many companies shows that relationships with them are very delicate and may not last long, ●●●



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●●● for several reasons: entrepreneurs may not make their expectations explicit and find it too difficult to respect managers' autonomy; above all, they may not trust managers and consider collaboration with them from a partnership perspective, but consider them as "mercenaries" with a short term and opportunistic attitude. On the other hand, managers may find it difficult to understand family businesses culture, and particularly to accept the family's strong presence in the company; similarly they may also not be used to being accountable to such visible ownership; on top of that, managers may underestimate family businesses and their owners, considering only public companies to be "real" companies.

Another category of third parties that can make important contributions to family business growth is *outside external non-executive directors*, members of the board of directors that are neither family members nor company managers. Particularly, they may help bring in competences that the company does not have, monitor non-family managers and help them cope with the delicate relationships described above, facilitate dialogue on the company's key issues between managing and non-managing shareholders, improve the decision-making process, and train successors. It has to be acknowledged that shareholders are also rarely part of a family business's board of directors as it is often formally "family only" even in large companies. Entrepreneurs fear that a functioning board may bureaucratize the company, so they are often resistant to the idea of opening up a governing body where confidential family and ownership issues may be discussed; and, in general, they do not like to report to someone else about their strategic vision, plans or results either. In turn, outsiders may have trouble getting used to family business dynamics and succeed in being constructively critical and supportive at the same time.

Including the above-mentioned third parties in a family business can be decisive to *distinguish key roles of ownership, governance and management*, especially in first and second generations, these roles often overlap because the same people may assume more than one. However, when the company is growing and family ownership is extended, it is necessary to understand that these roles differ in content, require specific structures and competences and are transmitted according to different rules, which can be dangerous. Particularly, a big risk is to consider business ownership as a right rather than a responsibility to be prepared for, and to believe that the simple fact of being owners automatically means possessing adequate governance and management skills. To avoid this risk, one effective way is, again, to dispose of appropriate structures like boards of directors and executive management committees. And a key condition for them function correctly is to compose them differently. Family and ownership bodies, typically shareholders' meetings and family council meetings, also need to function well in order for family owners to play their role responsibly and for their successors to learn the values and behaviours of responsible ownership.

Managing *generational transition* in all roles, especially in leadership roles, is still a fundamental issue for family business continuity. As Alberto Falck, founding President of the Italian Association of Family Firms has said ², every generation has to undertake the challenge of "buying back" the company. This requires, first of all, to



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be able to thoroughly understand the company's guiding values and vision and to apply it to a competitive, economic and social context that may have significantly changed. Then, to become entrepreneurs, it is necessary to develop special aptitudes that are latent in many people; particularly young candidates to succession who need to cultivate personal features such as love for the company, a considerable level of self-esteem, tenacity and the willingness to sacrifice. They should develop creative insight as well as concrete skills, build generalist but not superficial competencies, learn to behave in different contexts and evaluate people wisely. Above all they will have to learn to take decisions.

All this requires proper training both in and outside the company, measurable objectives and tasks, progressive assumption of decision-making responsibilities; this is a careful balance between time spent with the entrepreneur and time devoted to develop one's own autonomy. Strong commitment from the entrepreneurs and third party collaborators, external mentors, other relatives, and other entrepreneurs is essential.

The possibility of team leadership is also a key issue for family firms. The many cases in Italy and all over the world of groups of siblings, and even cousins, playing an entrepreneurial role in the companies they inherited from their parents makes it obvious that teams at the top can be successful. But a number of conditions must be developed, such as: mutual esteem, complementary competencies, a clear division of responsibilities, a high degree of communication, even distribution of shares among team members, absolute unity of team members in front of collaborators, management systems for integration within the team and between the team and other collaborators. Once again, the transfer of values and living examples from the previous generation is decisive.

Today, succession and other transitional processes are taking place under particular pressures, due to more and more turbulent environmental dynamics in all industries. The tough times that companies are experiencing requires the family to be particularly united and committed to defining ambitious goals and carrying them out. Crises like those mentioned at the beginning of this article have generated pessimism around the world, as well as within some family companies. It is absolutely necessary for family business owners to overcome this negativity in order to work under the right conditions they need to play a prominent role in the future. ■

² D. Kenyon-Rouvinez, G. Adler, G. Corbetta, G. Cuneo, Sharing Wisdom, Building values. Letters from Family Business Owners to Their Successors. Family Enterprise Publishers, 2002

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