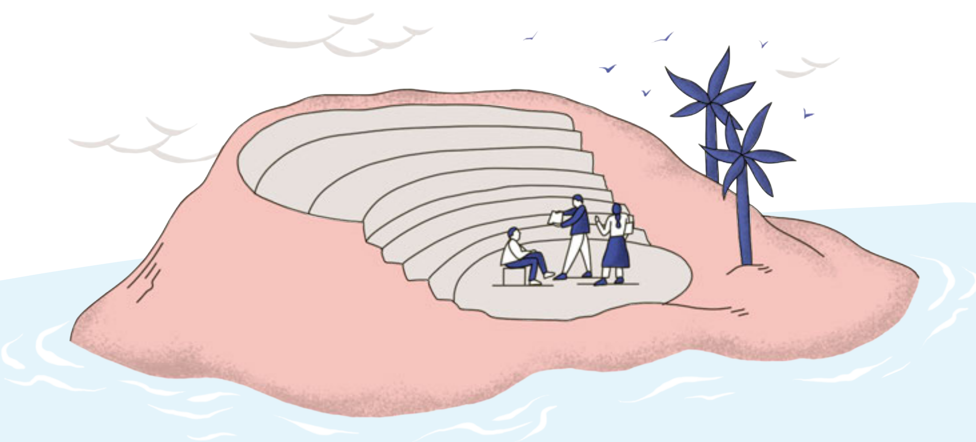
BUILDING ON SOLID GROUND

Family governance is an important and rapidly developing discipline that offers support and guidance for managing the wealth and interests of HNW and UNHW families and can help to ensure a smooth transition between generations.

By John Franklin



Family meetings
Where all family members come together to discuss business matters.

Family council
A decision-making committee formed from the family assembly, limited to 3-5 members.

Family policy and constitution
A fundament of family governance that is recognised by all family members. A strategic document that defines rules for organisation, succession planning, and conflict resolution, as well as a guideline for asset management and family values.

Wealthy families have always existed, but society around them has changed considerably in the past few decades. Today, it might seem obvious that a family's wealth and business will not necessarily go to the eldest son, yet for generations that was not the case. This societal shift, particularly in the West, has introduced a new layer of complexity for multi-generational and multinational families seeking to preserve their wealth, interests, and often businesses.

Professor Nicole Conrad, a partner at ATAG Attorneys and a family governance specialist, knows this better than most. "Today's younger generation no longer feels any obligation to the family business or the management of the family's assets," she says. "In the past, control was given to the eldest son and there was no discussion. Today, the younger generation discuss. They are likely well educated, with their own passions and interests in life. They want to take their own path, create their own family."

It is widely known that family businesses rarely make it to the third generation: a recent PwC survey put the proportion at just 12 per cent. In the first generation, ownership and company management are in the hands of the founder. If successful, a banker, lawyer, and tax consultant are employed, and by the second generation there is often already dual leadership. Division of responsibility begins to occur and structures to deal with differing opinions are required. By the third generation, things become even more complicated.

"The second and third generations have not grown up together, which can have advantages and disadvantages," says Prof Conrad. "The emotional bonds are weaker and people behave more professionally. Their relationship to the family business is more like a shareholder in a public company." Accordingly, this generation focuses more on matters many find controversial: participatory rights, dividend payments, and revision of business documents.

This is where family governance comes in. The discipline, which has developed rapidly in recent decades, can help families to work through and formalise their succession plans. "Family governance can best be described by its purpose: the long-term strengthening and consolidation of a family, and, where there is a business involved, identification with the company," explains Prof Conrad. Difficult situations that arise as a family tries to navigate from one generation to the next can be alleviated by various instruments. These can include family reunions, training and education programmes, and conflict resolution mechanisms. "Although studies have shown that these do not have a direct impact on the positive performance

Family committee(s)
Examples include: an investment committee to manage assets; a non-profit committee; a new generation committee (educating and training for family members); a personnel development committee (for family members working in the business).

of a company, family businesses that have good cohesion and willingness to change are more successful than average."

More important still is the so-called fair process, which is a cornerstone of family governance. This involves creating a set of fair, transparent and verifiable rules for all family members and shareholders, and their access to the family business. These can then be complemented by a constitution that determines the conditions for other family members to work in the business, as well as the criteria to qualify as a suitable successor and guaranteeing security for the next generation. It also helps to mitigate any personal relationships interfering with business decisions, and to ensure coherence between family members. In large families where interests diverge considerably and the potential for conflict is great, this is key, as disputes cause significant damage to the continuation of a company.

Family governance is not just for businesses, though. The same societal changes that have caused a shift in the way family business succession is handled have also altered the way family wealth is maintained and transferred. Younger generations of wealthy families have grown up in a more open society where education, independence, and female empowerment have changed the way they consider and use their legacies. This has not only challenged the preservation of specific family values, but also means a standard 'blueprint' for life as a family no longer exists in a hyper-individualised world. As a result, family governance has become increasingly important for wealthy families too.

Family governance can offer a platform for discussing different views between members, and for mitigating any potential conflicts before they arise. It can also be applied to nearly every situation and can help maintain wealth through family changes such as marriage, divorce, and death.

"Family governance is very valuable when it comes to the maintenance of assets over generations," says Prof Conrad. An example would be if a patriarch or matriarch with no clear successor sells their business.

They are now cash-rich, possibly with a diversified asset portfolio that, if managed correctly, is sufficient to provide income for their family members over generations. “In this context, the establishment of a family office, or the establishment of a family foundation, both of which are instruments of tailor-made family governance, should be considered.”

No two families are the same, so nor are their approaches to business or wealth. A long-established wealthy family in Asia and a newly moneyed family in Europe will have very different requirements, so every aspect of governance must be tailored to the individual situation. In places such as Germany and Switzerland, family governance as a discipline is well established and many global families look to these countries for guidance on how to safeguard their businesses and wealth for the coming generations. However, what works for a family in Berlin or Zurich will not necessarily work for a family in Beijing. “You cannot cut European family governance approaches and paste them into Asia or the Middle East,” explains Prof Conrad. “You must develop specific instruments that take into account how the individual families and societies work.”

Whereas in the past, wealth might have been created by one entrepreneur in one country, passed to the male heir, and expected to maintain the family for generations, today’s globalised nature of wealth means the requirements and considerations of moneyed families are far more extensive and complex. By employing the discipline of family governance, security and stability can attempt to guide assets through periods of boom, bust, uncertainty, and renewal, benefiting not just family members but also a broader spectrum of society as a whole.

Single/multi/virtual family office
Establishing a single-family office is useful for a highly diversified portfolio requiring active professional management, while for smaller or less diversified portfolios a multi-family or virtual family office is a good option. Additionally, this way the family can find and manage the relevant experts to support them.