Balance of power in a family business

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Governance in a family business must provide a clear answer to this fundamental question, "who decides what around here?"

In conventional corporate governance the board of directors runs the business in the best interests of owners who provide capital, subject to various legal duties that recognise other stakeholder interests, like employees, creditors and the environment. Relatively few decisions require to be taken by the owners on the assumption that they are a diverse group of varying talents.

This conventional balance of power is obviously usurped in an owner-managed business. Where several owners who work together have different sizes of shareholdings, they might want to distinguish decisions that they make as owners (one vote per share) from those they make as directors (one vote per person). However, this rarely happens and usually the director with the largest ownership stake has the biggest say.

The conventional balance of power can also be unsuitable in a family business where family members who own shares do not work in the business that is managed by a team which may or may not include some of their relatives. In these cases, non-working owners might want to influence decisions that pose a significant financial or reputational risk, rather than delegating these entirley to the board.

The financial controls exerted by family owners could be similar to those in companies whose shares are either publicly listed or who have private equity investors. For example, the shareholders could be given the right to approve a major capital investment, or acquisition of another business, or diversification into non-core activities.

The idea of reputational risk is perhaps more relevant to a family business than other types of business especially where the brand is the family name. For example, the owners might want to approve any change to the corporate brand or its use in sponsorship or advertising. They might also want the final say in relation to closure of part of the business and making redundancies if they fear that this will affect the family's reputation.

It is straightforward to shift the conventional balance of power from the board towards the owners, but what if the owners want the wider family also to have a say in some decision-making?

This could happen, for example, where the owners feel that family should have a say in matters that could affect them now as family members, or as the future owners of the business. For example, if the owners want a policy on employing family members they may want the wider family whose lives will be affected by the policy to have a say before it is implemented.

The possibility of sharing power with the wider family is not even acknowledged in conventional corporate governance and hence taking account of the family in governance design and practice requires a new approach.

The following will help to determine the balance of decision-making power among the owners, the family and the board in a privately owned family business. It starts with the owners and decision-making power cascades down from there.

Sharing power in a family business

1. All power is ultimately with the owners, and they can decide what decisions, if any, they want to influence as owners. Should that be the right to be informed or consulted or the power to make certain decisions?
2. Are there any decisions that the owners would like the wider family to influence?
3. Every decision that is not reserved for the owners or the family is, by exception, delegated to the board.
4. In turn, are there any decisions that should be taken by the full board rather than being delegated to any individual director?
5. Any decisions that are not reserved for the full board can be delegated to an individual director who in turn may delegate appropriately to others in the company, for example, senior management.

This approach creates a bespoke balance of power and clarifies, who decides what around here. Some might argue that this is where family businesses go wrong. They would do better by adhering to the conventional model of governance and let the board make all the decisions, with the owners and the family being pushed to the margins.

The problem with this approach is that, in real life, it is often naïve. If the owners or family members in a family business want to influence decision making they will find a way to do so. If necessary they will infiltrate the board or just take it over, even if that means people being appointed to the board *because* they are an owner or a family member rather than because they are good at being directors.

Instead of insisting that conventional governance is unchangeable, it is more pragmatic to accept the world as it is and create a balance of power that works for each family business. When that is done the owners, the family and the board know what is expected of them and what they can expect of each other. With this level of transparency, there is less likely to be disputes over decision making which too easily can descend into conflict.

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