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Beware Conventional Corporate Governance

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Conventional corporate governance is based on distrust.

That is not a typographical error. In conventional governance, codes and guidelines, formal mechanisms and stringent enforcement are felt to be needed to mitigate opportunistic and self-interested management behaviour that could result in reduced shareholder returns. Various corporate scandals lead to a demand for more of these rules, which is interesting given how often the complaint is heard that there is too much red tape.

Anyway, more corporate governance of the conventional type will be to the detriment of an approach to governance that reflects the following attitudes.

- Based substantially on relationships of loyalty and trust.
- Encourages teamwork.
- Avoids unnecessary bureaucracy, management by rulebook and short-term performance measurement.

The type of governance just described appeals to many family businesses. They naturally develop governance based on relationships of loyalty and trust. Management responsibilities are allocated among family members, and the outsiders who are treated as part of the family, based on trusting each other's talents. They know each other well enough to understand their respective strengths and weaknesses, and trust each other to deliver. As a result, each business function is handled by the fewest number capable of doing so; you don't need others looking over their shoulder to keep them honest.

Hierarchical, top-down governance structures, with excessive monitoring and reporting are <u>not</u> what many family businesses want. Even so, it is often suggested that conventional governance should be adapted for use in family businesses. This seems odd and maybe it is time to suggest that the argument is the wrong way around.

In 2012, the UK government asked Professor John Kay, a visiting Professor at the London School of Economics, to recommend ways to transform UK equity markets. His report[1] recommended that there needed to be a change of culture in the stock market, away from short termism in favour of restoring

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[1] https://www.gov.uk/government/news/kay-review-publishes-report-on-uk-financial-sector

relationships built on long term trust and confidence. It also speaks glowingly of stewardship being a strategic objective for companies.

Governance based on long-term relationships, trust and stewardship? These terms are frequently used to describe family businesses. Could it be that that the family business model, so often disparagingly dismissed as dysfunctional, now represents the best hope for companies on the world's stock markets?

That debate is worth having. For the moment, we can surely argue for the view that families in business together should look at conventional corporate governance with care, and even a bit of cynicism. If they feel they suffer from the problems that conventional governance is trying to solve – lack of trust between owners and management – then some aspects of conventional governance could fit. Otherwise, a family in business together needs to develop governance that reflects their own values and aspirations.

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