Separating **FAMILY GOVERNANCE** from **BUSINESS GOVERNANCE**

Pay attention to the unique needs of both.

BY CHARLIE CARR

Independent board members may experience an awkward moment in board meetings when the discussion shifts to a conflict among family members or to the family's personal donations to a charity. Are we still talking about the business? Am I supposed to weigh in on what the family does with their family foundation? Should I care that an out-of-state cousin wants greater distributions this year? What do I say when two owners won't speak to each other?

There comes a time when a business-owning family needs to separate business governance from family governance. Family businesses often either ignore family governance (pretending it isn't needed) or handle it within the business governance framework without realizing that is what they are doing. There likely will come a time when both the business and the family require more dedicated attention to their unique needs. As with most family business matters, life is better when the family takes action before the challenges become lava in an active volcano.

Defining governance

Most of us have a good idea of what business governance is. It involves either a fiduciary (i.e., voting) or advisory board of directors, which provides strategic oversight of the business and its key operations and growth. As consultants, we have established boards that are directly tied to a legal entity or a holding company, as well as informal boards that oversee a family's portfolio of companies and holdings without a formal consolidated entity. (Side note: C corporations and S corporations are required to have a board of directors. LLCs, partnerships and sole proprietorships may choose to have a board of directors but typically are not required to do so.)

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Family governance as a concept may not be as clear. The purpose of family governance is to build or maintain unity among the various family branches and to promote and build the family's core values, likely benefiting the family business. The family decides that collectively, leveraging their financial and human capital, they can go much farther than they can individually. This decision signals a belief that the family can be much more than it is. Often, a family will form a family council, which creates and oversees a family charter (vision, values, policies), propagates family history, supports family education, communicates among branches, organizes family meetings and coordinates usage of shared properties.

One key difference between business and family governance is that the business board typically has authority to enforce its decisions, whereas the family council relies upon influence and shared family vision to get the family to comply. Family members can walk away from the collective family any time they desire. We often say that families must have a vision that is exciting and enticing enough that members want to participate and stay together.

Why have separate governing bodies?

We've worked with families where nearly all adult family members work in the business, and the board is composed of family plus a few longtime advisors. Combined governance often works well in such situations, at least for that generation.

However, family businesses usually benefit from having independent board members, perhaps starting with two members and increasing to a majority as the business crosses generations. Such board members desire a professional board, which means focusing on the business rather than the family. On the family side, as the family grows in branches/generations, they may have more family members owning shares but not working in the business. Those family members may prefer having professional board members representing their interests. Also, the family member leading the business may not have the time, skills and/or interest in leading the family governance. It's often an advantage to provide an opportunity for a different family member to get involved.

A growing family will benefit from separately focusing on the family. A family council can help keep family conflicts out of the boardroom, shielding business staff and the community from family matters. The family council also can focus on developing family members to be more informed business leaders and owners, as well as encouraging each member to reach their potential.

Benefits of separating governance

Let's summarize some of the ways the business benefits from separating governance:

- Ability to obtain better independent board members
- Meetings focused solely on the business, perhaps leading to better growth and performance
- Business leaders can focus on the business rather than family conflicts
- Sends a message to employees that the business is professional

The family also enjoys some distinct benefits:

- Greater focus and attention on family communication and unity
- Improved ability to educate and prepare the next generation
- Creates roles or opportunities for more family members to be involved
- Provides a forum for resolving conflict
- Sends a message to the family that family is at least as important as the business

Process for establishing separate governing bodies

If you don't already have a written board charter and family council charter, this is a good time to create these important documents. Each charter should describe the purpose of the governance structure, who serves on it, length of terms, meeting frequency, compensation, etc.

One of the areas that requires careful consideration is the list of topics that the board or council is responsible for handling, often referred to as the "matters reserved." For the board, this might include strategic planning, budgeting, capital expenditures above a defined threshold, new hires in the C-suite and acquiring or selling a business line. For the council, this might include creating the family vision and values, preparing for the annual family meeting, facilitating communication across branches, preparing the next generation and coordinating with the business. It takes considerable discussion and care to ensure the responsibilities of the two governing bodies are distinct.

Formally creating these separate bodies is a process. It likely will take a year or more to define and implement them and perhaps another year for each governing body to get comfortable with their purpose and process. It's important to persist through this time, for the good of the family and the business. The benefits to both the business and the family are worth the effort.

Once you successfully separate the governing bodies, independent board members will be spared the awkward moments when family matters arise in board meetings, the board can concentrate its attention on improving the business, and the family will have a clear venue for raising and addressing family challenges while it continues to develop the family's legacy. FB

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