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'CHAOS' Brings Order to Family Businesses

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Many people make the mistake of thinking that family businesses are simple businesses. Nothing could be further from the truth. The coexistence of two systems with differing ways of thinking—the family and the firm—complicates things. The guiding logic of the “firm” is economic and rational, while “family” dynamics are guided by emotions, which tend to put rational thinking (as well as money) in second place. Family business conflict is often a result.

This complexity is the defining characteristic of a family business and represents a double-edged sword: if the coexistence of family and firm is managed well, the family business will have great potential for success; if not, it can represent a huge risk factor for both the firm and the family. The business might become less efficient, lose money and ultimately fail; the family may lose its harmony and individual family members could suffer.

So, what are the guiding principles to manage this complexity and help both family and firm avoid the chaos that results in bad decisions? From scientific studies and my own professional experience, I've learned that families and their businesses can avoid chaos by embracing some principles whose very acronym is “CHAOS. ” They include Councils and protocols (C), Help from advisors (H), Availability of external resources (A), Organizational clarity (O), and Succession planning (S).

C – Councils and Protocols

The best family firms regulate family/firm dynamics by setting up governing bodies, such as the “family council,” and drafting documents such as “family protocols”. However, except for the largest companies many family firms don't set up these family governance mechanisms.

The family protocol is a document defining the principles regulating family involvement in the company ownership and management. It lists the values and objectives of the family, the skills expected for family members who want to join the company (for example, the type of degree, knowledge of languages and work experience needed), salary guidelines, share transfer criteria, mechanisms for developing new entrepreneurial initiatives (and decision-making rights — who should have the power to act and with how much freedom), philanthropic guidelines and eligible tools for managing family wealth.

The family council is responsible for drawing up the above protocol and revising if necessary. It clarifies the relationship between the family and the firm, making explicit what is and what is not appropriate; outlines an ethical code to discourage opportunistic behavior; guarantees that the articles of the protocol are respected; regulates family activities guaranteeing cohesion and control; and acts as a guide to family values and objectives for the board of directors and top management.

H – Help From Advisors

To guarantee good management of the family/firm relationship, an impartial advisor from outside both the family and the firm may be necessary. An advisor is able to deal with both family and company issues with the appropriate emotional distance, thus ensuring that business decisions and actions are not influenced by emotions and other counterproductive non-financial factors.

A competent advisor can be particularly helpful not only in drawing up the family protocol and in managing the family council (as discussed in above), but also in bringing about the three fundamental actions described in the following paragraphs: deciding when and how to open up governance; making the organization clear and

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transparent; and planning the generational takeover.

Advisors can already be valuable in identifying business problems that the family often overlooks. They help in cases of confrontation between different company players, offering fresh perspectives, ideas and experiences. They help bring about consensus when decisions must be made, and can act decisively to make change happen.

A – Availability of External Resources

Along with the outside advisors, the most successful family firms also welcome players from outside the family to their upper management and board. This can be challenging when families don't want to give up the strategic freedom they've enjoyed.

However, family firms often need entrepreneurial and managerial skills that family members lack. In this case, opening up their control and management structures to a certain degree to outside players can allow them to take advantage of new knowledge and skills that are essential to improve performance.

Moreover, having independent non-family members on the Board and as managers helps both groups function better, because outsiders can distance themselves from the emotional involvement in family dynamics. This helps family members to face company decisions with greater objectivity, too.

O – Organizational Clarity

Family firms, especially smaller ones, lack formal structure, which means roles can be unclear. Sometimes family leaders hesitate to assign clear roles because they don't want to limit their status and ability to intervene in all areas of responsibility. Other families want to avoid dealing with awkward situations. These could include cases where roles may have been assigned with no regard to merit, where several roles are covered by one person or where there is dissonance between hierarchical relationships and generational ones.

Organizations have four levels of power. The first is ownership, followed by the Board of Directors, then the management and finally the workforce. Each level reports to the one above and is responsible for the one following. Their level determines not only what individuals can/must do, but also what they deserve in exchange. Everybody should understand their rights and responsibilities based on their role in the organization, and not on their surname.

S – Succession Planning

One process that can really risk chaotic upheaval in a family firm is the generational takeover. The most successful family firms plan for this by preparing the next generations (if genuinely interested in the family business) through training and experience outside the company, and by making the entry and career paths clear.

Transferring power is not at all easy, since it means handing over authority, knowledge and the spotlight to a new group of leaders. Nor can it take place "in a void;" it is one of many choices, an element of wider strategic change. Other choices the company has made will influence the process of identifying and developing the new leader. It all has to fit together, or be re-evaluated. This is why succession requires planning, even if it's flexible.

It may make sense to pass the baton to non-family players and give them at least a partial stake in the company's ownership and management. What is important is that the successors are the right ones regardless of their surname, and can contribute to the well-being and success of the company in the interest of all the stakeholders.

Summary: Taking Positive Action

To summarize, family businesses can manage complexity by:

- Establishing a family protocol and a family council;
- Courting the opinions of external advisors;
- Opening the board and the management team;
- Formalizing the organizational structure; and
- Planning succession with care.

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