TRANSITION FROM FAMILY OWNED STRUCTURE TO CORPORATE STRUCTURE

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GLOBAL TRENDS

- FoBs generate 70 percent of global GDP, $60-70 trillion of turnover annually and 60 percent of global employment

- Exhibit stronger performance in all crises situations with Higher Total Shareholder Returns (TSR) from better operational performance

- FoBs shared increased economic profits – 2.2 – 5.5 times compared to non-FoBs and have created more value and impact over the past decade

- Over 85 percent of the US/Europe businesses are family-run. Walmart, Ford, Samsung, Li and Fung, Koch Brothers, Sabanci

- In India, 45 percent of the industrial output, 40 percent of exports come from FoBs with 60 million employees – they create 1.3 million jobs and produce 800 quality products

PAKISTAN LANDSCAPE

- A majority of FoBs – Micro, Small, Medium enterprises
- 3.2 million SMEs account for 90 percent of all private businesses, employ 78 percent of non-agriculture labor force, contribute 30 percent to GDP, 25 percent of exports of manufactured goods, 30 percent of manufacturing value added
- Distribution among sectors: Industry: 20 percent, Service Providers: 22 percent, and Retail, Wholesale, Restaurants and Hotels: 53 percent
- Micro: Rs. 1 million, Small: Rs. 1-20 million, (Rs. 150 million sales turnover), Medium: Rs. 20-80 million (less than 250 employees, less than Rs. 10 million assets for Manufacturing, less than Rs. 50 million for Services, less than 50 employees in Services, turnover Rs. 150-800 million)
- Less than 173,000 SMEs or 4 percent currently borrow from the banks

FORMS OF FAMILY BUSINESSES

- Sole Proprietorship
- Partnership
- Private Limited Company
- Public Limited Company

	Sole Proprietor	**Partnership**	**Company**
Ownership	Single	Several	Shareholder
Access to Capital	No	No	Yes
Management – Ownership Separate	No	No	Yes
Business Owners Exposed to Hassle	No	No	Yes

CORPORATE STRUCTURE

- Board of Directors – Family Members, Independent Directors
- Management – Professionals empowered but held accountable
- Private Equity – Injected,
- Nurture and groom the children

NATURE OF FOBs

i. Founder: owns, manages, operates the business

ii. Family Owned: run and managed by the family members

iii. Management: In the hands of professionals but control, governance, and supervision rests with the family; managers accountable to the family

iv. Family Controlled: Diverse shareholders but the control is held by the family, Public-listed companies fall in this category.

ADVANTAGES OF FOBs

- Quick and timely decision-making and problem-solving
- Crisis management
- Long-term outlook
- Recognizing and grasping business opportunities
- Adapts to change
- Value system – Integrity, honesty in dealing with suppliers, customers, employees, tax authorities

DISADVANTAGES OF FOBs

- Conflict, disputes, differences, disagreements among siblings permeate throughout the company – some want to expand, diversify, acquire, while others continue in the existing mode
- Second generation problems – agreeing upon clear rules of succession, family empowerment, compensation, family shareholding, retirement
- Maintaining harmony among the family members drifting away to informality
- Evolving consensus on family's financial relationship – dividends vs retention of earnings
- Trouble ownership transfer, stock buy-out process, shareholder responsibilities and rights
- Clash on intergenerational value system

SALIENT FEATURES OF A SUCCESSFUL FOB

- Human Resources – technical, managerial skills by attracting, retaining, and motivating professionals
- Develop capabilities needed for technology assimilation, innovation, and continuous learning and development
- Labor productivity – 40-50 percent lower, on-the-job training
- Organizational structure and processes – delegation of authority but accountability
- Credibility and public disclosure, ethics and trust, clean balance sheets, not suppress information

SALIENT FEATURES OF A SUCCESSFUL FOB

- Scale economies – expand, merge, acquire
- Digitalization and Automation: branch-off to E-commerce
- Brand and marketing, product quality, durability, reliability, timely delivery
- Leadership – vision and execution capability, taking people along
- Culture – working environment in which the employees show commitment and loyalty to the company
- Coordination and control
- External orientation

HOW GOOD GOVERNANCE HELPS FOBs

- Adopt Code of Corporate Governance and family constitution for working together – passing the baton.
- Global international investors pay a premium for well-governed companies across a wide range of sectors show superior valuation
- Streamlined business processes lead to better operating performance and lower capital expenditure
- Family firms with formal advisory boards perform better than those without such boards

CORPORATIZATION

Advantages	Disadvantages
Improved marketability of shares	Loss of privacy
Improved financial position	Loss of autonomy
Potential increase in the value of shares	Increased liability
Greater visibility, transparency, and disclosure	Possibility of take-over
	Additional costs

CAUSES OF CONFLICTS AND TENSIONS

- Death of a key individual who was able to keep a balance
- Matrimonial disputes: favorite daughters-in-law
- Tax problems – suppress or understate incomes, others for full disclosure
- Competency of heirs to manage the business in the absence of a clear succession plan, employment of younger members – at what level, what educational qualifications, inclination towards running business
- On what level of benefits to be appointed and on what basis?
- Disposal and dispersal of interests in the business versus those who wish to keep it intact
- Excessive spending by some members of the family

CAUSES OF CONFLICTS AND TENSIONS

- Role of spouses – comparison of lifestyles and endowments
- Keeping information to the chest, lack of trust, misrepresentation of facts, suspicion and doubts
- Sibling rivalry, son-father rivalry, intra-family friction spillover to the associates and subordinates
- Conflict with managers and executives
- Fear of failure – Elders: established companies, assured returns, risk-averse, status-quo; Younger Generation: adventurous, risk-takers, new untested and untried ventures

WHAT CAN BE DONE TO RESOLVE OR MANAGE THE CONFLICT AMICABLY?

- Follow the Code of Corporate Governance and agree on a family constitution that specifies the roles, responsibilities, accountabilities of family members in running the business, succession planning, recruitment, compensation, etc. of family members

- Tilt the decision-making more towards professionals rather than family members or heads of the family, while keeping oversight, governance, strategy, accountability, for results within the board, with strong representation of the family members

- Open regular communication among all the family members – information sharing and addressing concerns and questions raised is helpful

- External Advisory Committee in which family members have faith and trust, and seek their advice in matters of dispute

- Allow the family members to establish new ventures or run the business subsidiaries independently

- Let them take their share, quit the family business, and start their own