LEADERSHIP

Generation to Generation: How to Save the Family Business

by Boris Groysberg and Deborah Bell

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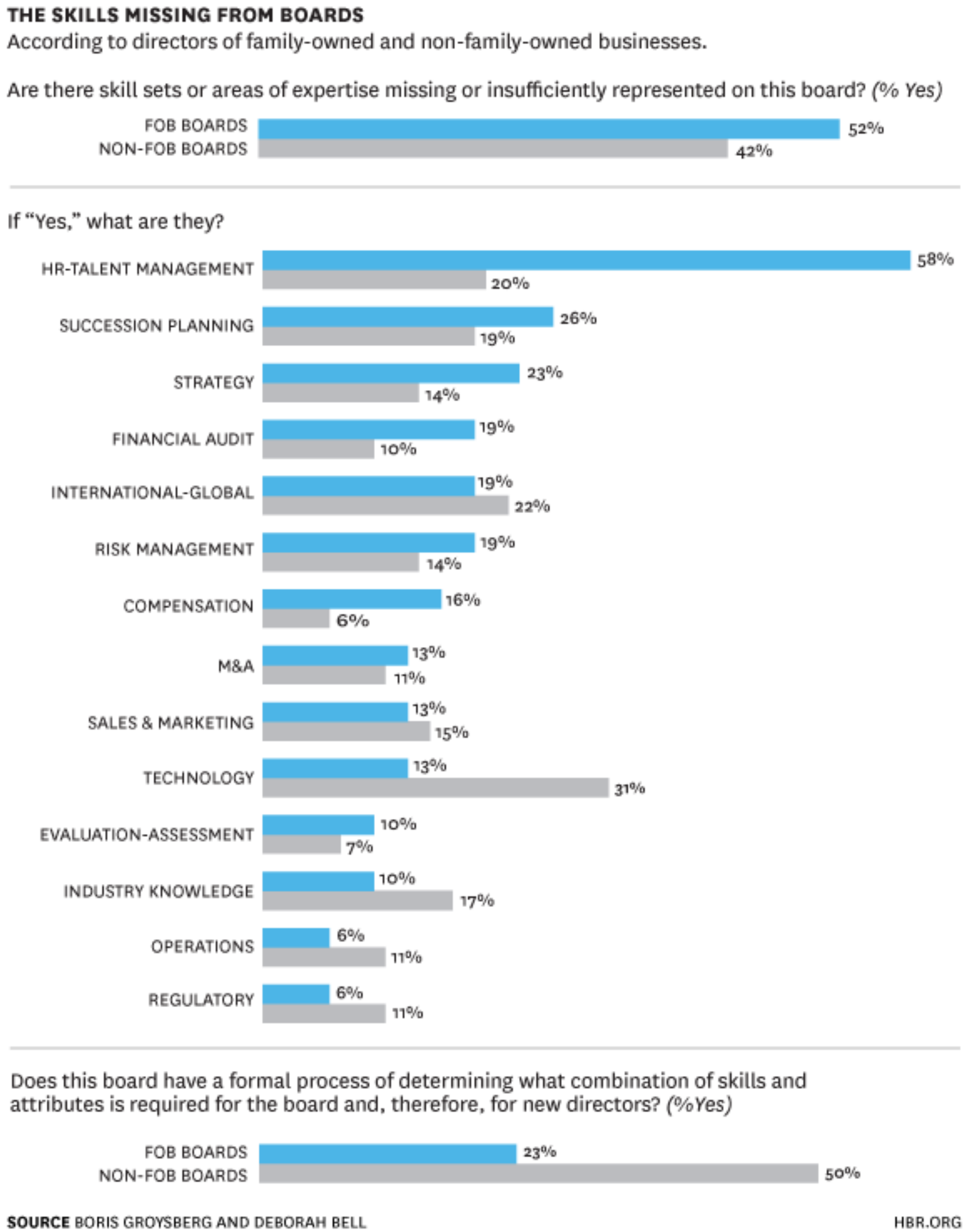
Most family-owned businesses—approximately 70%—last just one generation. Because an estimated 80% of businesses across the globe are family-owned, the low survival rate has alarming consequences. Consider this: In the United States alone, family-owned businesses (FOBs) are responsible for 60% of total US employment and generate 78% of all new jobs. Further, some of the world's biggest companies are family-owned—News Corp, Samsung, Tata Group, and Walmart to name but a few—and more than a third of Fortune 500 companies are family-owned.

Our research on boards of directors and corporate governance has shed new light on many board practices and reveals the need for improvement in several areas including skills and selection, succession planning, and diversity. Given the vast impact of FOBs on every economy in the world, we were keen to learn if there were differences between the boards and governance practices of family and non-family owned companies.

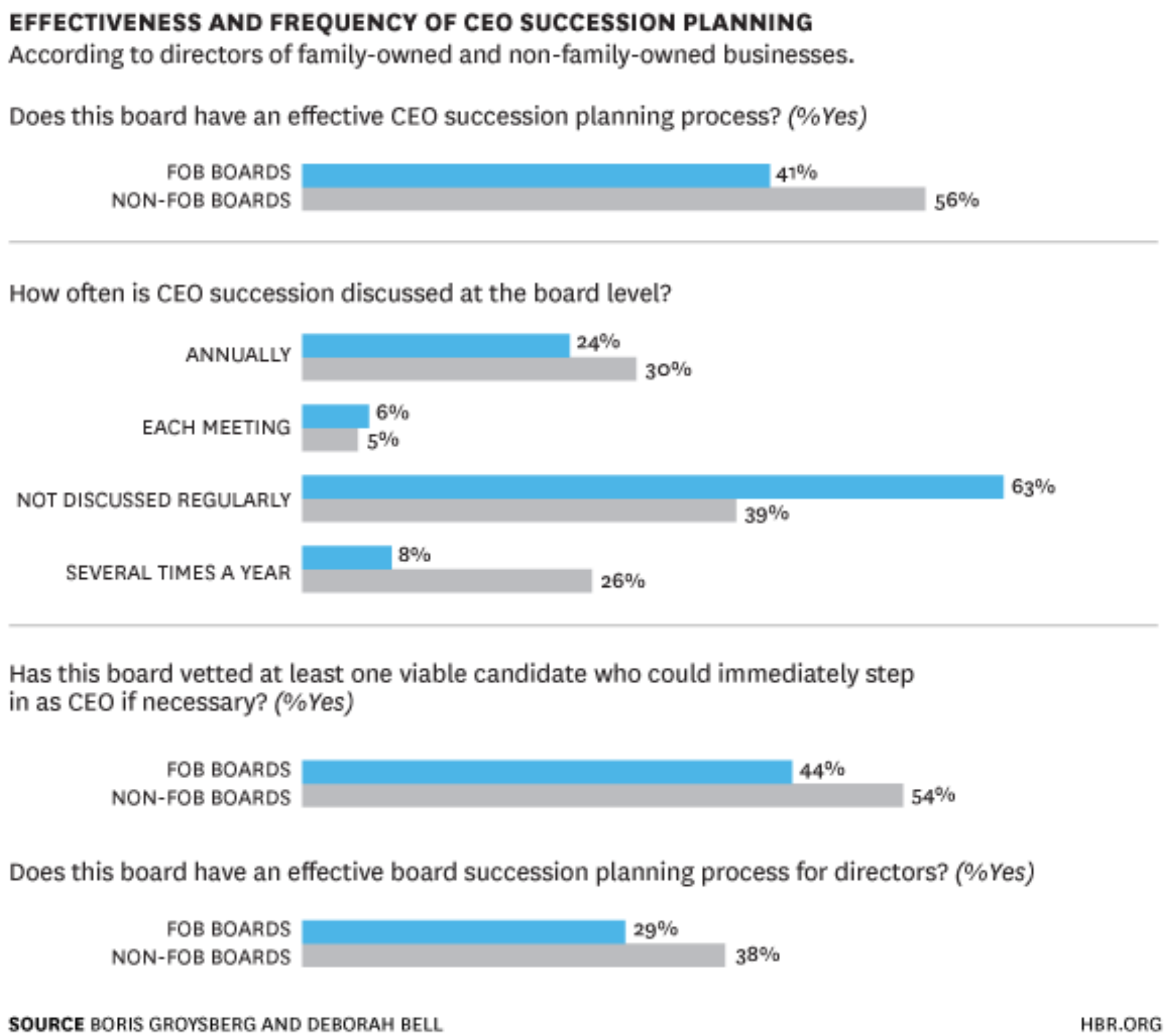
In 2012, we (in partnership with WomenCorporateDirectors and Heidrick & Struggles) surveyed more than 1,000 corporate directors across the globe and broke out the FOB boards from the non-FOB boards. The results were striking: There was not one meaningful measure—from missing skill sets to the effectiveness of succession practices to creating more diverse boards and workplaces—on which FOB boards outperformed non-FOB boards.

Director Profiles. To begin, we compared the profiles of directors on the boards of family-owned vs. non-family-owned businesses and found few differences. A similar percentage held advanced degrees: 75% of FOB directors and 77% of non-FOB directors. When we looked at board service, we found that FOB and non-FOB directors had served on an almost identical number of boards in their careers (5.8 and 6.0, respectively) and were currently serving on the same number of boards (3.1).

Skills and Assessment. Boards cannot govern effectively if they're missing key skill sets. A greater percentage of FOB than non-FOB directors said skills were missing on their boards and the missing skill they named most was HR-Talent Management—to a degree almost 3 times that of non-FOB directors. There were other noteworthy differences: FOB directors said their boards lacked Succession Planning, Strategy, Financial-Audit, and Compensation skills to a greater extent than did non-FOB directors. Furthermore, less than a quarter of FOB directors (vs. half of non-FOB directors) said their boards had a process in place to determine skills required for the board and, therefore, new directors. We also found that FOB boards measured their own performance through regular, annual assessments less frequently than did non-FOB boards (45% vs. 67%, respectively).

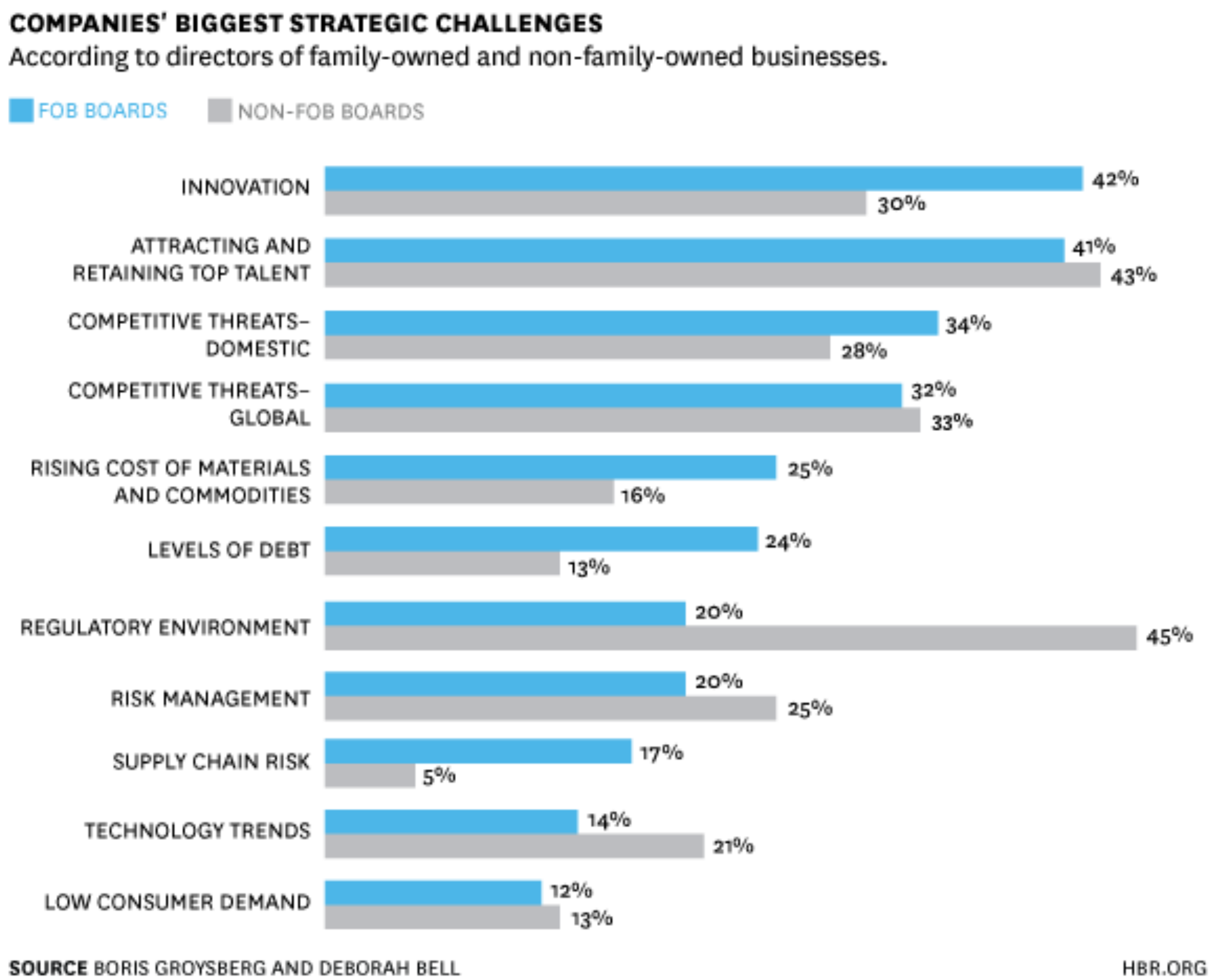


Succession. Just 41% of FOB directors said their boards had an effective CEO succession planning process (vs. 56% of non-FOB directors). Perhaps the most telling finding, however, was that 63% of FOB directors said CEO succession was not discussed regularly at the board level. In addition, only 29% of FOB directors said their boards had an effective board succession planning process in place for directors.



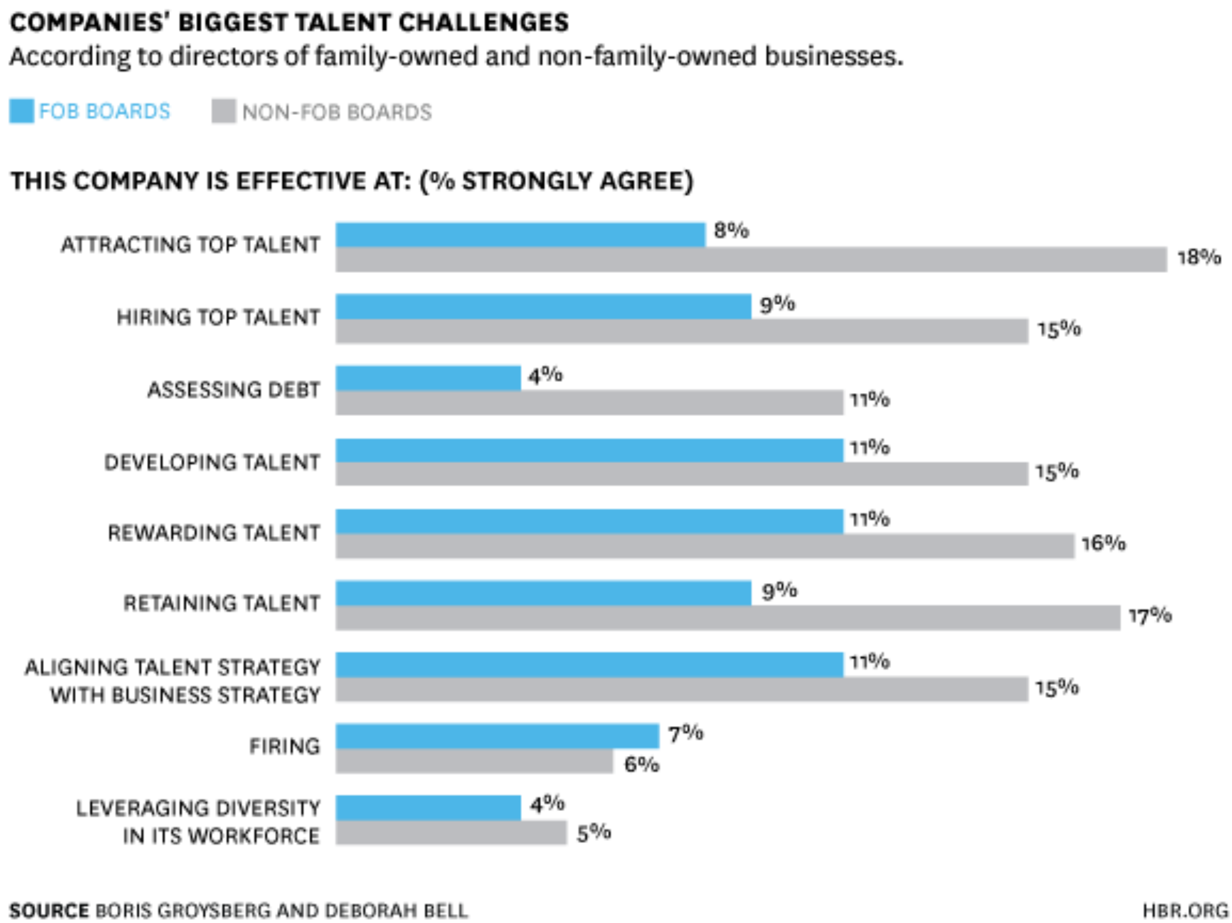
Strategic Challenges and Talent Management. We asked board members to tell us the biggest challenges their companies face achieving their strategic objectives and found directors from family-owned and non-family-owned businesses aligned on many challenges. For example, attracting and retaining top talent and global competitive threats were leading concerns for both.

But we also identified notable differences: namely a greater percentage of FOB than non-FOB directors viewed innovation as their top challenge, and FOB directors were also more concerned than their non-FOB counterparts about the rising cost of materials and commodities, levels of debt and supply chain risk. Conversely, a far greater percentage of non-FOB directors than FOB directors were concerned about the regulatory environment.



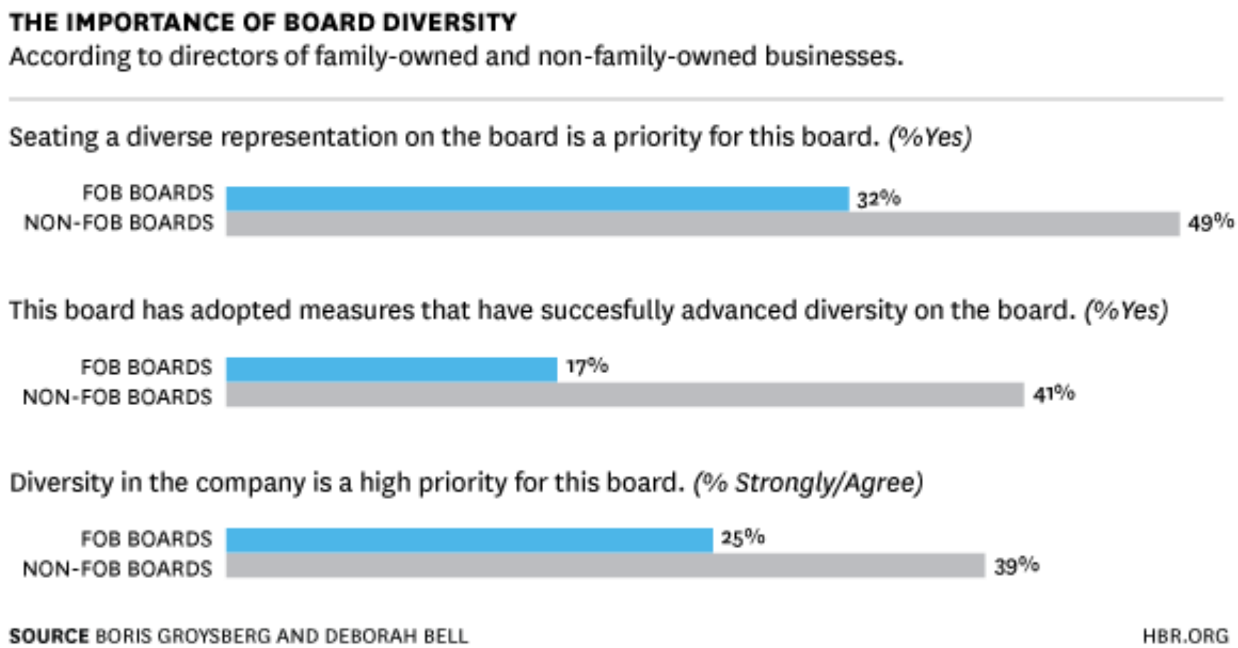
As we noted above, attracting and retaining top talent, was a foremost challenge for directors on both family-owned and non family-owned business boards. In our survey, we asked board members to rate their companies' performance on nine dimensions of talent management: attracting top talent; hiring top talent; assessing talent; developing talent; rewarding talent; retaining talent; firing; aligning talent strategy with business strategy; and leveraging diversity in company's workforce.

We found that directors from FOB boards rated their companies lower than directors on non-FOB boards on eight of the nine dimensions while both groups gave themselves an almost identical rating when it came to effective firing practices. The biggest differences were on the practices of attracting and retaining talent—with FOB boards rating themselves considerably lower than did non-FOB boards. What's more, for the majority of practices FOB board ratings did not exceed single digits. If FOBs want to perpetuate their business through generations it is critical that they be able to attract and retain top talent.



Diversity. We contend that in order to see greater progress in seating diverse boards, change must occur within three spheres: at the country, organizational and individual levels. Furthermore, although we have seen movement at the country and individual levels, much greater effort must be made at the organizational level, which we think may be the most determinative lever of change. Given that the majority of businesses in the world are family-owned, greater action on their part to create diverse boards and workplaces could have a substantial impact.

We found, alas, that FOB boards trailed behind non-FOB boards on diversity. Less than a third of FOB directors (vs. 49% of non-FOB directors) said that a diverse representation on their board was a priority. And when it came to actually implementing diversity, we discovered a stark difference: only 17% of directors on FOB boards said their board had adopted measures that successfully advanced diversity on the board (vs. 41% of non-FOB directors). Last, a smaller percentage of FOB directors than non-FOB directors said that diversity in the company was a high priority for their board.



How to Fix the Problems

Although our analyses found room for improvement on the boards of both family and non-family-owned businesses, we discovered that FOB boards lagged behind non-FOB boards—often substantially—on several important measures of board practice and governance. In fact, we tried to identify meaningful practices that FOB boards did better but could not find even one.

The lesser performance on family-owned business boards does not seem to be related to major differences in talent on FOB and non-FOB boards. Though our measures are very limited, we found director profiles and experience on both to be very similar. If a talent differential is not a factor, the lag would seem to be due to a greater extent of poor or non-existent practices and processes on FOB boards.

The good news is this can be fixed. It starts with the boards themselves. First and foremost, we recommend that FOB boards establish effective succession planning processes for both CEO and directors that include regular discussions of succession at board meetings. Not doing so could significantly limit the prospects of the business surviving into subsequent generations.

Second, FOB boards must institute a productive and regular assessment process of board and director performance. Regular assessment will help boards identify areas in need of development or change and also should help to identify skills needed on the boards—and when assessments are done at regular time intervals boards add a valuable contextual dynamism to the process.

Third, FOB boards should exert greater effort to make not only their boards but also their companies more diverse-especially in light of their concerns about innovation and performance on talent management. Improving their talent management practices with an eye toward adding talent with a diverse mix of backgrounds, skills, experience, and knowledge may help to address gaps in skills and spur innovation.

Overall, family-owned business boards need to become better at governing by implementing best practices and processes because good governance may lead to higher survival rates and smoother generational transitions.

Methodology

We surveyed more than 1,000 board members in 59 countries. For the family-owned business breakout: FOBs made up 8% of the sample and non-FOBs constituted 92% of sample. The following multiple choice list of 14 skills was used for skill sets missing from the board question in the survey: Compensation; Evaluation-Assessment; Financial-audit;

HR-Talent management; Industry knowledge; International-Global; M&A; Operations; Regulatory, legal and compliance knowledge; Risk management; Sales & Marketing; Strategy; Succession Planning; and Technology. Participants could choose as many as applied (plus there was a write-in option of "other").

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profdrmarcelhuelsbeck 5 years ago

First of all, thank you very much for this post. I really enjoyed reading it. I am not surprised that FOBs do not outperform non-FOB boards and that both could be more effective. From a corporate governance viewpoint I strongly suspect this to be an effect of the Anglo-Saxon one tier board system with it´s CEO-centrality. Like a previous comment said, with power-motivated CEO it is very likely to get a board of yes-men or just a nice old Buddy clubhouse. On the other Hand if a board is properly used to exert decision control and leave decision management to the CxOs (see Fama and Jensen 1982) FOBs can really outperform non-FOBs as measured by financial performance. Unfortunately the decision structure within one-tier boards is hard to observe. Some studies use data from countries with two-tier board Systems where there is a strict demarcation of the roles of the executive and supervisory board. These studies Show the beneficial effect of family-owners on supervisory boards in FOBs but no positive effect of family members in executive roles. If you are interested in this matter I suggest the following paper (by David Audretsch, myself and Erik E. Lehmann): http://www.sciencedirect.com/s...

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