The Trusted Advisor

THE TRUSTED ADVISOR is our firm's regular publication, featuring not only articles and insights derived from our project work but also guest posts and interviews with leading business figures.
They offer food-for-thought and practical advice on a variety of key topics in the leadership, ownership advisory, governance and strategy domains.

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Finding and binding

Competing for external top talents in family businesses

by Andreas von Specht

Research indicates that the number of younger family members willing and interested to take over responsibility in their respective family businesses in the future is currently at a record low. Family businesses will increasingly have to take part in the global "war for talent" to attract the best suited company leaders – and, almost more importantly, to make sure external managers will also stay and perform with the family business over a long period of time. Here is the challenge for both owners and external executives: most of these external top talents will not necessarily come from a family business background. It requires certain skills, competencies and role-model behaviour from both sides to make this marriage a happy one.

Apart from being an advisor on leadership and governance issues to other family businesses, I come from a family business background myself. Our bank in Germany, the Berenberg Bank, goes back to the year 1590. It is hence the oldest bank in Germany – and the 2nd oldest in Europe. Two family branches which have pooled their votes, together with the external general partners still control far more than 50% of the votes. The year 2015, i.e. the 425th year of the bank's existence, was the most successful year ever. This is the result of a longer phase of significant reinvention and restructuring. The complete and highly successful "renovation" of the bank over the past 10-15 years was predominantly driven by two strong non-family executives. Both were made general partners several years ago and today have significant equity stakes. Even if perhaps different in style to previous generations of private bankers, they were highly successful when it came to reshaping our business model and improving the substance of the bank. And until recently, there was still an active member of the extended family on the board, who carried the family name. The less well known part of the story is this: since 11 years and for the first time in the 426-year history of the bank, no family member is operationally active in the leadership team. The family saw this situation coming and yet we did little to adjust. We didn't change the slightly outdated shareholder agreement which grants the acting general partners an enormous amount of influence, decision making power and control. As long as our dominant family branch was always represented amongst the general partners, this never seemed a burning issue. It might differ now as the bank and its culture is changing. From today's perspective it appears rather unlikely that our family business will be run by one of our family members in the foreseeable future. Is that necessarily a bad thing? Probably not – but it depends on the family's ability to influence and calibrate events as shareholders. One can draw some interesting conclusions and lessons from this family business story. For example: great entrepreneurial genes in a family are not necessarily passed on from one generation to the next. "Good Governance" in a family business is hugely important – to attract external management, but also to protect the family interests. And there are many more.

AvS – International Trusted Advisors and EY, together with a leading university, have just completed a comprehensive study on external managers in family businesses across Europe. When talking to both the family business owners and the external CEOs and CFOs, you understand very quickly that there is a special "Family Business Spirit" in these organisations. Owning families are normally emotionally much attached to their business. The company represents an important aspect of their identity – and is in most cases far more than a financial investment. The "Family Business Spirit" becomes visible in the company culture, in the relationship between family business owner and external management – and in the working environment. Family businesses, even if highly dynamic and innovative, are always long-term oriented. An important, if not the most important objective and challenge for many is to transfer the business to the next generations.

The special "Family Business Spirit" is the bright side of family businesses. If family business owners provide long-term stability, a platform for rapid, independent decision-making, a sense of purpose and strong values – the importance of such positive role-modelling cannot be overestimated. However, this coin also has a flip-side: if family lines and shareholders are involved in underlying or painfully open, unresolved conflicts amongst themselves or with the external management, the risk of departure of external top management increases over-proportionally. Even if there are offspring interested to enter the family's own business that still doesn't say anything about their qualifications. What are the required experiences prior to entering the family business – and who will decide if the son or the niece brings the right mix of critical competencies necessary to make it in the top job? If a succession within the family can't be organised – or if the future entry of a successor from within the family needs to be bridged over several years, external talents come into play.

In many family businesses you can sense some degree of uncertainty as to how an external recruiting process should be managed. They know intuitively that wrong decisions with regard to the hiring of external top executives will become painful and very costly. And yet, because external hiring of the top positions simply does not happen frequently in most family businesses, many seem to get it wrong – especially the first time. The successful "fit" of an external executive in a family business will often be "judged" after only a few weeks or months. If something feels wrong, even before the honeymoon period is over, it often has to do with a lack of deep understanding: how a family business 'ticks' and the dos & don'ts in this special environment. Many family businesses are difficult to analyse from the outside; their true performance, for example, is often not published. It is still surprising and sometimes almost shocking, how little some executives appear to research and investigate prior to signing an employment contract about the culture and DNA of a family business – and how this might differ quite dramatically from publicly-owned businesses. However, it can be equally surprising how little effort some owners invest into the hiring process and the careful integration of external talent.

The hopes of external top managers will mostly focus on a stable business platform with long-term, reliable investment horizons and decision–making independent of quarterly results. They expect to find flat hierarchies, few decisions-makers, uncomplicated and non-political ways of communication. And they hope to find the bright side of the "Family Business Spirit" – with a value-based entrepreneurial culture and a strong people orientation. The fears of external executives joining a family business will be around potential hidden agendas among family members, a general lack of transparency and irrational behaviour.

The ideal profile of an external executive for a family business will naturally include the most important critical competencies of such an individual. This is not only a question of previous experience, but defines a certain skill-set and the degree to which an individual displays competence in important areas. For example, the ability to initiate change, to modify a business model or to bring about true customer orientation across a large organisation. Apart from entrepreneurial and social competencies, a competence most critical to success is the ability to function in the specific environment of the family business. This is probably "the" central competency that differentiates between suitable and unsuitable executives for family businesses. It can be spotted by 'performance based prediction': what has somebody experienced in the past that allows a forecast for how he or she will function in a special family business culture? And even more importantly: how does he or she do it? In our experience, the majority of external executives don't fail because of functional shortcomings. We have encountered situations where the functionally strong executive appeared completely taken by surprise when he was “suddenly” asked to leave. Simply because he had missed the subtleties of critical feedback on behaviour – which the owner ensured us he had made so crystal clear. Hired on competency – fired on chemistry and style!

Interestingly enough, compensation does not play the decisive role in attracting external executives. What really does influence the decision of external executives to join and stay in family businesses over a longer period of time, is entrepreneurial freedom. The ability to shape and form, to make educated decisions and to take full responsibility. When our firm is called in to support owners with a critical succession or appointment, almost every single brief touches upon “the search for an ‘entrepreneurial’ manager”. Well, if you seek true entrepreneurs, then you also have to treat them as such – and grant the necessary space and trust to let them flourish! And – at the same time – you will have to put ‘good governance’ in place and carefully check the competencies of your external executives.

External managers: searching for outstanding talents with low egos

An interview with Peter Englisch, Partner and Global Family Business Leader at EY

by Andreas von Specht and Felix B. Waldeier

AvS – International Trusted Advisors: To ensure long term success, family businesses face a growing need to recruit external top managers. What changes and developments in entrepreneurial families are responsible for the fact that a family's own offspring are often not interested in becoming the company leader?

Peter Englisch: One of our worldwide studies amongst the biggest family businesses in 2015 shows that young people are becoming less and less interested in joining their own family's business. From my experience, parents should talk to their children at a very early stage about the possibilities of joining the family business. Young people seek clarity and perspective for their own lives and often do not even know what opportunities – also including opportunities for change – the family business has to offer. After all, it is not about pursuing the parents' path, but also about catering for new trends, technologies and changes in the market. This is where the next generation is needed.

If the offspring decides against joining the family business, it's usually an external manager that needs to step in. How can business owners determine if an external manager meets the company's needs? Is there a typical competency profile?

Family businesses, German ones in particular, are often characterized by modesty and restraint – and hence put company interests over personal matters. Family businesses therefore principally look for decent and competent personalities with a strong track record especially in strategy and leadership topics. Or in other words: They are looking for outstanding talents with low egos.

However, there are many "strong egos" especially in large corporations. Are external managers, without prior experience in family businesses, therefore second choice?

No, external managers are not per se second choice. What really matters is to determine the right person to transfer the family's values and culture into sustainable company growth. This can also be done by external managers and there are many examples of large family businesses whose operations are successfully lead by external managers. When it comes to operations and executive management within a company, competency is king – no matter if it comes from within or from outside the family.

Or, asked the other way around: might external managers even be the better solution when it comes to leading a family business?

Appointing external managers definitely offers advantages. Managers that are not family members will always and only be judged by their qualifications and performance, as well as the way in which they lead the company – and not by their origin or family background. That allows a more objective view and unbiased management of the company – provided that the owning family indicates the long term direction and defines clear competencies.

Why is this of a particular importance in family businesses?

External managers should act within the limits of clearly defined fields of competences. This notably includes and requires a separation of company matters and the personal interests of individual owners. External managers should not therefore become involved in topics such as personal tax or financial investments, nor be compromised with requests for e.g. company cars for non-active family members.

Once an external manager has been successfully appointed, the idea is to retain him/her for the long term. However, this often does not work. What do company owners need to bear in mind in order to avoid an early and unintended exit of the external manager?

An efficient culture of communication with regular and open exchange is crucial to build additional trust. The conversations should take place in a disciplined and coordinated manner to avoid that the external manager constantly has to justify his/her decisions and actions towards family members. In addition, it is extremely important that the family owners sufficiently communicate their values so to successfully introduce the external manager to the characteristics of family businesses.

Are you talking about the much quoted “Family Business Spirit”?

“Family Business Spirit” describes the strong connection between the owning family and the company, as well as the “role model function” that creates a special company culture. Whether the “Family Business Spirit” really exists in the company, and has a positive effect on the workforce, strongly depends on the actual behaviour of the family.

On the other hand, what should external managers bear in mind to ensure that they are accepted by the owning family and to lay the path for successfully leading the business?

To me, it is crucial that an external manager sees himself/herself as part of a bigger “family”. And this requires the identification with the company and the values of the family. Nevertheless, it is important to keep a certain professional distance towards the owners. In a company, roles and expectations are clearly defined, facts and rational choices matter. In the family environment it is also about emotions, appreciation and (sometimes unclear) mutual expectations. This is a difficult terrain for non-family members. Wrong expectations, incorrect behaviour, and a lack of clear competences, as well as the mingling of company matters and private interests of the owning family, are common mistakes when appointing external managers.

That sounds like a demanding and difficult path. Are there even more risks that could lead to failure?

Another risk are objectives that focus too much on short term goals and on financial aspects. Bonus and compensation systems usually reward short term success instead of supporting the long term generation of values and sustainable profits. Long term goals are especially important in family businesses.

Are compensation systems of family companies less attractive, or in other words: do family businesses pay significantly less?

In principle, family companies pay adequately. However, since stock options and other remuneration components usually do not exist, the total compensation can be below that of comparable listed companies. In exchange, statistics show that jobs in family businesses are much safer and that the average family company affiliation is more than three times longer than in similar positions in listed companies.

Besides security of employment, are there other non-monetary components in family businesses that attract external managers?

Company culture, taking over responsibility as well as long term company values and goals are very attractive characteristics of a family business and definitely appealing for external managers. These characteristics are much more present, and lived more intensely, in family businesses than in large public corporations.

Can you point out further differences between publicly listed companies and privately-held family businesses?

The “Shareholder Value” model, still highly praised until a couple of years ago, primarily focuses on increasing the shareholders’ wealth so they won’t invest elsewhere. This means that shareholders are investors looking for the highest returns. A strong shareholder orientation is a typical management style in publicly listed companies. Family businesses, in contrast, focus much more on “Responsible Ownership”. This concept is about much more than short-term financial incentives: it is about creating long term values and actively living the company’s responsibility for employees, customers, suppliers and other stakeholders. This concept obviously differs a lot from the shareholder value approach – and successfully proved itself during the crisis.

Looking at the advantages and disadvantages of family businesses, one could ask: do publicly listed family businesses combine the “best of both worlds” for external managers?

This cannot be said, in general. There are a variety of reasons for family businesses to go public, e.g. access to capital markets to finance growth, introduction of Governance Systems, succession planning or to facilitate the compensation of a withdrawing shareholder. Needless to say, a regulated environment also creates more clarity for external managers. However, the Chair and the control of the Supervisory Board usually stays with a family member.

“Good Governance”: over recent years, Corporate Governance has become more and more important for larger corporations. What role does it play for family businesses?

There is a unique challenge in family businesses: corporate governance systems have to be adjusted to the rules and guidelines agreed within the family. This is often called the “Family Governance” – and it defines the long term goals and values of the family, creates clarity with regard to leadership and control, criteria for employing family members, and for dealing with withdrawing shareholders etc. This not only helps the family, but also the external managers, to understand and respect the reciprocal expectations and fields of responsibility. The subject of Corporate Governance is constantly developing and will be of increasing importance in the future – also for family businesses.

Peter Englisch, thank you very much for your insights!

How the Board ensures Good Governance

What to look for – and what to avoid – in effectively operating Boards

by Dr. Christian Bühring-Uhle

The sustainability of a business depends on its sustained ability to attract capable leadership talent, and that in turn depends in large measure on the quality of its governance. Good governance, therefore, is not only important for its own sake but also as a requirement for attracting – and retaining – top management talent, be it external or internal (the good ones have alternatives...). In our practice as advisors to owners of significant businesses we are often asked what it takes to ensure good governance, and the key really is to have an effectively functioning Board, be it a classical Board of Directors or an Advisory Board which can play an almost equally significant role for the quality of governance in a privately held company.

In order to achieve the desired impact, the Board, in the first place, needs clarity of purpose. The primary purpose of the Board, at least in a privately held enterprise, is to exercise the owners' rights and obligations (also vis-vis the other stakeholders), and to protect their interests, ensuring that the company is well managed, that fundamental decisions are taken on the basis of good judgment, and at the right moment. A productive and well-functioning Board, however, is also an indispensable resource for management. The best CEOs appreciate – and seek – the advice and challenge of critical, independent-minded Board members and especially an experienced Chairperson as sparring partner. Another function of the Board, and especially the Chairperson, can be to act as an intermediary, and at times even a mediator, between shareholders and management, or among different groups of shareholders.

Another important feature of effective Boards is clarity of focus. Experienced Board members, led by a capable Chairperson, will focus on the long-term well-being and sustainability of the business. They emphasise strategy over tactics, and distinguish what's really relevant. A truly productive Board uses at least two-thirds of its time to think about the future – instead of reviewing and questioning past dealings or, worse, being presented quarterly reports and figures. A key focus for every effective Board is talent. The Board has to make sure that the company is managed by the best available talent which means not only selecting and employing the right executives, but also to help them integrate, to supervise, support and challenge them, to help them grow, to compensate them adequately, to retain them, and, when necessary, to replace them (in time).

An effectively operating Board will be able to deal with typical problems that can arise. Some Boards experience a large difference of expertise and understanding among Board members, which is acceptable and manageable as long as it derives from a diversity of backgrounds and not from a lack of (time) commitment or meeting management. Another problem can be a clash of personalities within the Board. In general, it is advisable to have strong, and diverse, personalities in the Board room, and if they – and particularly the Chairperson – have the right set of communication skills, there will be productive discussions and a high level of added value. Another problem is directly linked to productivity: sometimes Boards simply don't get through the agenda in the allotted timeframe, and see Board members heading to the airport before the issues are resolved. And some Boards become paralysed because issues remain unresolved or won't even be touched on due to the fear of generating antagonism.

There are a number of simple operating methods that set apart the productive Board. In our experience, a well-organised Board:

- Operates on the basis of a well-thought-out agenda, with relevant topics, a reasonable order and time allocation, distributed with sufficient lead time, asking members to comment and make suggestions, so as to avoid last-minute changes.

- Plans and respects adequate breaks, which are long enough so that Board members can be 100% "present" during the sessions, i.e. no one is distracted by smart phones etc.

- Receives all relevant materials with sufficient lead time, typically one week, and everyone comes to the meeting having read the materials, allowing to focus the discussions on questions, comments, suggestions, i.e. discussing the issues rather than taking in the information.

- Cultivates an atmosphere of candid, reflected discussions, where ideas flow freely and respectful disagreement is encouraged rather than suppressed.

- Generates meaningful minutes, recording the decisions and the "to dos", as well as whatever is essential to document their reasoning, rather than producing a sort of transcript that no one will read; minutes are distributed immediately (no later than three working days) after the meeting and any comments are received well in advance of the following session.

- Undergoes periodic evaluations of its performance, either in an auto-evaluation or, preferably, with the help of competent external experts; the evaluation is frank and confidential, so as to allow an honest discussion among Board members as to how to optimise the way the Board works and adds value to the company.

The value a Board generates for the company is highly influenced by its composition. Being a Board member is a challenging, potentially inspiring and fulfilling, but above all a demanding, sophisticated task. Board members have to be individually suitable to this task, and collectively capable to act as a team so as to bring the members' abilities to bear for the benefit of the company and its stakeholders. As individuals, they have to be well chosen on multiple dimensions:

- Relevant Experience – which can be functional, industry or topic-based, or simply as business (or other) leaders.

- Analytical Strength – Board members have to process large amounts of complex and sometimes ambiguous information.

- Judgment – being able to take decisions based on limited facts (no "analysis paralysis"),

- Motivation (and time commitment) – wanting to really make a difference, not just collecting prestigious titles or feeling obliged to someone they know.

- Integrity – above all, the highest degree of honesty, integrity and independence. And, allied to this, an ability to work in groups (being able to listen to and value differing points of view, wanting to contribute to group results without looking for personal recognition or benefit).

The effectiveness of this group also depends on how it is composed, i.e. how the individual capabilities, personalities and perspectives complement each other. An assortment of great musicians will not automatically form a well-honed band or orchestra. When egos are big, and spirits competitive, the opposite may happen (and often does): personalities and (often pre-determined) opinions clash, everyone tries to dominate, and all the energy produces more heat than propulsion, putting off and frustrating management rather than supporting and inspiring it. A well-functioning Board requires a significant degree of humility from its members: dedicating time, attention, energy, doing one's homework, and limiting one's interventions to what benefits the group rather than seeking confirmation for own actions and attitudes, and serving one's ego. And the more diverse the group, the higher the challenge of working productively. But so too will be the benefits be higher in terms of richness of ideas and soundness of decisions. We still see too many "monochrome" Boards that are male dominated or composed of nationals from the home market.

To make the most of the potential offered by the "raw material", the group of individual "musicians", is the task of the Chairperson who, not unlike the conductor of an orchestra, makes sure that the total is more than the sum of its parts – and not the other way around. An effective Chair instils in the Board an operating culture of openness, seriousness, respect, humanity, humility, professionalism and discipline (which does not preclude a certain degree of humour, companionship and fun). At the same time, the Chair is a serious sparring partner and mentor to the executive team and personifies the identity and the values of the company and their owners.

This will become evident especially in times of crisis when the Board, and particularly its Chairperson, makes sure the company reacts in a calm, reasoned and expedient manner. And that the executive leadership is up to the task, backed and supported by the Board where appropriate – or replaced in a timely manner, if and when necessary, and in accordance with a succession plan the Board has developed well ahead of any crisis situation.

AvS News

Recent news and developments at AvS – International Trusted Advisors

The past months were marked not only by interesting client projects, but also by exciting developments within our firm that we are delighted to share with you in this edition of THE TRUSTED ADVISOR.

Publication of a European study on “External Executives in Family Companies“

Only 20% of students from entrepreneurial families plan to continue in the family business. Even so, there seems to be insufficient awareness of the growing risk caused by this lack of succession. This gap can be closed by a deliberate decision to recruit an external manager as an alternative to family members. The results of the study titled “External Managers in Family Businesses”, conducted by AvS – International Advisors together with EY and supported by ESCP Europe (Berlin), show that in this context, family businesses seek not merely employees but “co-entrepreneurs” who are suited to the company and the family — so the aim is to find a good emotional and cultural fit. Based on an initial qualitative study, a quantitative research was conducted in which hundreds of owners, as well as non-family top managers in big family businesses in Germany, Austria, Switzerland and The Netherlands, have been interviewed. Please click here to download the study English, French or German.

Andreas von Specht speaking at events in Monaco, at INSEAD and in the Baltics

In June, Andreas von Specht participated at the “EY Global Family Business Summit” in Monaco. He addressed approx. 400 delegates from around the world and then moderated a panel discussion on “Effective Leadership: attracting and retaining top talent in family business”. Members of the panel included James Wates CBE, Chairman of the UK-based Wates Group, who was one of the ‘Entrepreneurs of the Year 2016’ – and with whom Andreas discussed the importance of good family governance as well as the challenges in recruiting external talent for family businesses.

Later in June, Andreas was invited to address the ‘Family Enterprise Day’ at INSEAD in Fontainebleau. He introduced the concept of the ‘B Corporation’ and later participated in a panel on “A Practitioner Perspective on Entrepreneurship & Innovation in the Family Business”.

In October, Andreas was asked to speak at a series of family business roundtables in the Baltics (Lithuania and Latvia). Many family businesses in this region are currently transitioning (or about to do so) to the second generation. In front of the leaders of these businesses, Andreas spoke about “The Art of Managing Family Businesses” and how to facilitate this important transition, followed by a panel discussion with family business practitioners in which Andreas shared his insights on Family Business Governance.

News from our Latin American practice

Together with the German-Colombian Chamber of Commerce and with the support of the regional office of the IFC/World Bank Group and the CESA, a renowned local business school focusing on privately enterprises, AvS – International Trusted Advisors organised the first "German-Colombian Congress on Family Business" in September. 60 representatives of Colombian entrepreneurial families discussed strategies of family and company governance with our three regional Advisors, and experts from the sponsoring organisations.

Christian Bühring-Uhle, Head of our Latin American practice, was appointed Honorary Representative of the Free and Hanseatic City of Hamburg ("Hamburg Ambassador") in Bogotá by the Lord Mayor of Hamburg, Olaf Scholz.

Endeavor, the leading global high-impact entrepreneurship movement, also selected Christian Bühring-Uhle for its pool of distinguished Mentors, who serve as sparring partners to a highly selective group of high-potential young entrepreneurs.

New staff at our Frankfurt office

As part of the ongoing growth of our German activities, we are happy to welcome two new team members at our Frankfurt office. As of the end of September, Karin Wollmann has joined our Research Team as Project Coordinator and will support and steer our different international assignments. Having successfully worked with Karin over the past years on a freelance basis, we are glad to have her on board as a full team member. In mid-October, Julia Brüssow started in her new role as Partner Assistant and Office Manager. As the primary contact for all administrative concerns, you can reach her at +49 (69) 2713975-21.t

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