



Intergenerational Succession in SMEs Transition  
INSIST

Review of Family Business Research on Succession  
Planning in the UK  
Final version

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## 1 Introduction

This report has been prepared by members of Leeds Beckett University involved in the delivery of the Erasmus funded Intergenerational Succession in SMEs' transition (INSIST) project. Its aim is to provide an overview of the 'state of play' in the UK concerning the ownership transfer between generations in family firms. It adopts the structure agreed by INSIST project partners and draws on the literature and selected interviews to cover the following themes:

- Definition, roles and importance of the family business
- Socio cultural environment of family businesses
- Strategic issues
- Policy environment, financial and legal regulations

The review emphasizes literature focused on the UK but is not limited. It draws on a comprehensive literature search that identified more than 200 publications associated with family business. The research team evaluated these publications and selected the most relevant for inclusion in this review. The selection of the literature was guided by the requirement to provide a review on the state of play in the UK however it also includes some influential and relevant international research to complement national sources.

### 1.1 Definition

There is no single universally accepted definition of a family business in the UK. In an influential review of the UK Family Business Sector for the Institute for Family Business (IFB, 2011) by Oxford Economics they suggest that a business can be classed as a family business if it meets the following criteria:



- The majority of votes are held by the person who established or acquired the firm, or their spouse, parents, child or child's direct heirs, and
- At least one representative of the family is involved in the management or administration of the firm
- In the case of a listed company, the person who acquired the firm or their family, possesses 25% of the right to vote through their share capital and that there is at least one family member on the board of the company
- For micro (typically sole traders) businesses, subjective criteria are also needed. In particular the Government Department for Business Innovation and Skills (BIS) define it as a business, majority owned by members of the same family (BIS, 2013, p6).

## 1.2 Roles and importance

There are a range of data sources that can be used to identify the role and importance of family business in the UK economy including statistics produced by BIS and research produced by a variety of others including business representative organisations, lobbying agencies, private sector business service providers (such as consultancy agencies and accountants) and academic Departments. The different definitions, research methodologies and analysis techniques provide a rich and sometimes inconsistent picture of family businesses in the UK. For example based on the Survey of SME employers in the UK (a stratified survey of over 4,000 employers employing between 1 and 250 employees) estimates that there are about 1.2 million family businesses in the UK (BIS, 2013) whereas estimates often quoted by IFB based on the combination of several sources suggests that there are almost 3 million family businesses in the UK (IFB, 2011). Most of the discrepancy between the two estimates appears to be accounted for by the inclusion of Sole Traders that employ no employees (over 2 million firms) in the IFB estimates of the size of the business population. The IFB (2011) suggest that two thirds of all the private sector firms in the UK are family businesses and that they contribute to £1.1 trillion in revenue. In an earlier report the IFB (2008) estimated that family businesses pay around £47bn per annum to the Exchequer in taxes, equivalent to almost 10% of the Government's total tax receipts. If the taxes paid by the



The IFB (2011) provide an indication of the relative importance of the family business sector to the UK economy:

- UK family businesses provided 9.2 million jobs, 40% of total private sector employment, or two in five private sector jobs. To place this in context, this is around 50% more than the entire UK public sector and makes family firms the largest source of employment in the private sector
- Family firms generated revenues of £1.1 trillion in 2010, or 35% of private sector turnover. On these revenues, family firms made a £346 billion value-added contribution to UK GDP, or nearly a quarter of the total
- Family businesses are estimated to have contributed £81.7 billion in tax receipts to the UK Exchequer, or 14% of total government revenues in 2010.

In general terms both BIS (2013) and IFB (2011) provide a similar picture of family business in terms of its structure (business size) and sectoral representation.

### 1.2.1 Business size

**Table 1.1. Family business employment by firm size in 2010**

		Number of family firms	% family firms employing more than one	% all family firms
Micro	1-9	638,843	85.8	21.6
Small	10-49	91,172	12.3	3.1
Medium	50-249	13,332	1.8	.05
Large	250+	879	0.12	<.05
		744226	100	
	0 employees	2,215,120	-	74.9
Total		2,959,346	-	100

Source IFB (2011)

Table 1.1 provides an indication of the structure of family businesses in the UK in terms of business size. Despite the methodological differences between the Oxford Economics Study (IFB, 2011) and BIS (2013) Small business survey the statistics suggest a sector dominated by micro enterprises employing under-10 employees. The BIS survey (n-2666), which excludes sole traders and businesses employing over 250 suggests that 83% of family businesses employ under 10 employees, 14% employ 10-49 and 2% employ

between 50 and 250, very similar proportions to those found in the Oxford Study once those businesses with no employees are removed from the analysis (Column 4 in the above table).

### 1.2.2 Sector

The large differences in the number of firms in each sector means that the industries with the highest concentration of family businesses and not those with the highest number of absolute firms. Table 1.2 provides an indication of the sectoral distribution of family businesses in the UK. In 2010 the greatest number of family businesses was in Business Services, including real estate (673,000) and in construction (663,000). Together they account for almost half of all UK family businesses. The industries with the highest concentration of family businesses are estimated to be agriculture, hotels and restaurants and wholesale and retail. The sectors with the lowest concentration are health and social work and other community, social and personal services activities (IFB, 2013).

**Table 1.2: Sectoral distribution of family businesses in 2010**

Sector	Number of family firms	Percentage of all family firms	Number of private sector firms	Percentage share of family businesses
Real estate, renting and business activity	673,073	22.7%	988,010	68.1%
Construction	663,346	22.4%	899,180	73.8%
Wholesale and retail trade, repairs	383,567	13.0%	497,755	77.1%
Transport, storage & communication	308,443	10.4%	515,930	59.8%
Other community, social and personal service activities	204,302	6.9	442,485	46.2%
Manufacturing	160,167	5.4	229,950	69.7%
Agriculture, hunting & forestry; fishing	150,422	5.1	168,785	89.1%
Education	130,781	4.4	224,900	58.2%
Hotels and restaurants	128,185	4.3	151,045	84.9%
Health and social work	106,121	3.6	290,915	36.5%
Financial intermediation	50,940	1.7	75,585	67.4%
<b>Total</b>	<b>2,959,346</b>	<b>100%</b>	<b>4,484,540</b>	<b>66%</b>

Source: IFB (2011)



### 1.2.3 Employment

The UK family business sector is estimated to employ around 9.2 million people (Table 1.2). This represents 41% of total private sector employment in the UK economy. In contrast to the distribution by business size, the distribution of employment is more evenly spread across the micro and small, medium and large sizebands.

**Table 1.2 Family businesses' estimated employment**

		Employment of family firms (thousand jobs)	% of all employment in family businesses
	0 Employees	2,378	25.85%
Micro	1-9	2,400	26.00%
Small	10-49	1,799	19.5%
Medium	50-249	1,298	14.1%
Large	250+	1,360	14.7%
Total		9,235	100%

Source IFB (2011)

### 1.2.4 Geographical location

Due to their relatively high rates of economic activity (and hence the number of firms) the South East and London were home to the highest number of family firms, together accounting for over a third of the total. The Yorkshire and Humber region (where Leeds is located) was home to more than 200,000 family firms, just over 7% of the total in the UK.

## 1.3 Age and sustainability

The evidence suggests that family businesses tend to be older than non-family businesses and tend to survive for longer and therefore promote a more stable business sector and job security (IFB, 2008). The BIS (2013) survey continues to show that a higher proportion of family businesses (47%) compared with 31% of non-family businesses are more than 20 years old. 31% of family owned businesses had been in control of the family for at least two generations.





#### 1.4 Effects of the crisis

Whilst an increase in the failure or dissolution of family businesses has been apparent during and in the aftermath of the financial crisis, the balance of the evidence appears to suggest that family based businesses have proved to be as durable if not more durable than non-family businesses throughout the period. For example, Wilson et al. (2013) points to a significantly lower failure rate amongst family businesses (which may be at least particularly accounted for by sample bias associated with those family businesses most at risk of failure being sold off) and that there is some evidence that relatively high level of financial security has helped many family businesses weather the economic storm. The literature also suggests a number of other factors that have contributed to the durability of family businesses in the recession including rapid and flexible decision-taking (Braun and Latham 2009), the relatively long tenure of senior family managers that provides a high level of accumulated knowledge (Westhead and Howorth, 2007) and social capital (Wilson 2013). Chaston (2012) however argues that the wider contexts in which the family business is located (country, size of business, sector etc.) are important mediating factors in how the family dimension manifests in the business and its performance.

It is also important to bear in mind the generation of the business, with some evidence that strategic changes may well occur when the second generation confronts existing business objectives and strategies, and where a lack of change and generational tensions may have led to underperformance when the older generation remained in charge (Brunninge et al., 2007).

Wilson et al. (2013) investigated specific aspects of governance which may aid the longer term survival of family businesses. In terms of board characteristics which contribute to survival, family businesses are more likely than non-family businesses to (a) maintain longer term board stability; (b) have close communication and collocation of directors; (c) have fewer outside directors (i.e. non-executive or non-family) – possibly because of the importance of hands-on involvement during a time of crisis, or because Non-Executive Directors (NEDs) are more likely to encourage riskier strategies but unwilling to intervene



in family disputes; (d) have higher levels of gender diversity; (e) have older and more experienced directors.

### **1.5 Institutional setting**

The brief review of the contribution of family businesses above highlights the important contribution that they make to the UK economy. Awareness of their role and contribution has increased over recent years however there is no legal distinction between family and non-family businesses. Family businesses remain a subset of the different sizes of firms (micro, small, medium) and legal categories (Sole trader, Partnership and public/private limited companies). It is difficult to discern recognition of family businesses as a discrete entity amongst business representative organisations such as the Chamber of Commerce or the Federation of Small Business. At the Government level there is no Minister for Family Business. Family business succession matters tend to fall mostly under the remit of the Department for Business Innovation and Skills (BIS) and Her Majesty's Revenue and Customs (HMRC).

BIS is the Government Department for economic growth that seeks to invest in skills and education to promote trade, boost innovation and help people start and grow a business, protect customers and reduce the impact of regulation. It funds support for a wide range of businesses in the UK economy in a number of areas associated with its Departmental remit. These include the National Loan Guarantee Scheme, Enterprise Finance Guarantee, Growth Improvement Service and Business Link. The Department's recent work specifically related to family businesses includes bespoke research reports based on its bi-annual survey of SMEs and qualitative research with a small number of family based businesses to inform policy development.

Her Majesty's Revenue and Customs (HMRC) is the UK's tax authority, a non-ministerial department responsible for making sure that the money is available to fund the UK's public services and for helping families and individuals with targeted financial support. It has five policy areas at the current time (i) making the labour market more flexible, efficient and fair (ii) Reducing tax evasion and avoidance (iii) making it easier for HMRC customers to



deal with their taxes (iv) creating a simpler, fairer tax system (v) making the administration of the tax system more efficient. The business and tax environment has generally been seen as being supportive of family businesses (IFB, 2008).

In the UK there are a number of specialist agencies providing support for family businesses. In England, the London-based Institute for Family Business (IFB) has been at the forefront of raising public and policy awareness of family business issues through a combination of advocacy, educational and networking activities. They have focused on several policy areas including the development of a favourable tax regime permitting firms to grow under family ownership; more investment in succession planning and the need to cut red tape. Similarly Families in Business (FIB), launched in 2013, are a membership organisation that provides consultancy and support for family businesses that has established a presence in several English regions.

In Scotland, the Scottish Family Business Association (SFBA) has supported the IFB agenda largely through promotion and marketing activity. The SFBA has also focused its efforts on raising the profile, productivity and performance of family firms in Scotland by emphasising (amongst other things) the importance of business support for best practice and succession planning.

The IFB and SFBA have been supported in their research activities by Research Centres in Higher Education. The London Family Business Research Institute has supported IFB in England and the Caledonian Family Business Centre has supported the SFBA in Scotland. Other Higher Education Institutions in the UK have developed centres for family business teaching, research and/or consultancy including Lancaster University Centre for Family Business, University of Strathclyde Forum for Family Business, Regents University London (Global Management - pathway in Family Business – MA) and the London School of Business and Finance (Professional Certificate in entrepreneurial and family business). Sections of the private sector also provide considerable support for family businesses most noticeably amongst the providers of business consultancy and accountancy services.



Examples include the BDO Centre for Family Business, Coutts and Co, PriceWaterhouseCoopers and Armstrong Watson.

The IFB (Drake 2009), in a report emphasising the corporate dimension of family businesses identify key professional advisors and their roles that include:

Lawyers providing professional advice in relation to for example

- Drafting the rules under which the limited liability company operates (articles of association)
- Drafting shareholder agreements (which give minority shareholders more protection than they would otherwise have under company law) and family charters (increasingly being used by more established family businesses particularly where some of the owners do not work in the business and where there are non-family members involved in the management of the business)
- Contracts of employment for family members
- The purchase of another business or the sale of the whole or part fo the family business

In the case of larger family businesses there may be one firm of lawyers acting on behalf of the business and another firm acting on behalf of the family.

The accountants/auditors will deal with such matters as

- The preparation and audit (where required) of the financial accounts
- Tax advice (although this might equally be provided by lawyers)
- Share evaluation, whether in the context of share transfers (e.g. to other family members), share buy-back or an employee share scheme and
- The purchase of another business or the sale of the whole or part fo the family business

Bankers will assist in matters such as

- The operation of the company's bank accounts
- Specific funding for projects such as capital expenditure



Larger family businesses may also have a number of additional advisors such as

- Specialist family business consultants who advise on matters like succession planning and family governance and who assist in resolving disputes within the family
- Chartered surveyors or planning consultants who advise on the company's property interests
- Actuaries who advise in relation to pension schemes
- Strategic business consultants who advise on business strategy and processes and
- Corporate finance advisors who advise on mergers and acquisitions as well as the sale of all or part of the family business

### 1.5.1 Succession planning

Succession planning and intergenerational transfer is an ongoing challenge in the UK. It is an issue that is often raised in reports exploring various aspects of family business development and growth. A distinction can be drawn between ownership transition (i.e. the next generation receives – or buys – equity in the business) and management transition (i.e. the next generation takes over running the business), which often occur together, although research tends to focus more on management rather than ownership transition (Nordqvist et al., 2013). Survey evidence consistently suggests that many family firms are ill prepared for succession and transition. A survey of managers in 1,454 small and mid-sized family businesses operating in a wide range of sectors in 28 countries revealed that 48% of family firms had yet to identify their successor (PWC, 2007). Succession is set to become a larger issue as the 'baby boomer' generation reaches retirement age over the next few years.

## 2 Socio-Cultural Environment of Family Business

There is a substantial body of academic and grey literature associated with the importance of the socio-cultural environment when considering family businesses in the UK. There are a number of consistent themes running through the literature and in particular if, how, and



in what way family businesses differ from non-family businesses. It is worth noting at this point however, that much of the research is situated in the medium and large family business context as opposed to the micro context inhabited by most family businesses in the UK. Furthermore that there is substantial heterogeneity associated with the family business population that can be neglected or marginalized in discourse.

### 2.1.1 Family members as founder and managers

*The owner (founder) personality: entrepreneurial or/and managerial skills or “habitus” (leadership style, dominance of the generic or specific (e.g. sector) professional skill, etc.*

Policy discourse in the UK emphasises poor management and leadership skills in the economy and particularly amongst SMEs and by implication family businesses. The London School of Economics World Management Survey (Bloom et al., 2012) argues that across many countries, on average family businesses are the worst managed type of business. Other researchers such as Bacon et al (2013) suggest a lack of skills associated with Human Resources, especially use of best practice when family businesses are compared with non-family businesses. The founder(s) or owner(s) of family businesses have a key role to play in establishing the values, leadership style, systems and processes that influence the culture of the business. Whilst it may be tempting to make generalisations about owner/manager personalities, skills or leadership styles it is important to recognise the heterogeneity that exists amongst family firms and the wider context socio-economic context that influences the culture of family firms.

When we consider the socio-cultural environment of family firms it is important to recognise the potential causes of heterogeneity among family firms that may include leadership goals (Chrisman et al 2012), governance structures (Carney 2005) and resources (Habbershon et al 2003). For example researchers have suggested that the mix of social and economic goals is a cause of heterogeneity and that the relative importance of the goals can change depending on the competitive situation facing the firm (Westhead and Howorth, 2007). One of the areas often contested is the relative economic performance of family and non-

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family firms and the balance between economic and non-economic objectives of family firms. Family owners can be seen as the stewards or custodians of the business and that implies a different set of success criteria, rather than straightforward profitability often associated with private sector enterprise. These criteria can include providing employment opportunities for family members, both currently (Kellermanns et al., 2008) and in the future (e.g. Miller and Le Breton-Miller, 2003), running the business in such a manner as to reflect well on the family owners, making a social contribution (Berrone et al., 2012) and preserving family wealth (Chrisman et al., 2003).

Family businesses differ in the degree of family involvement and leadership and management in the business. Some families will take a role in the day to day running of the business whilst others will take a more hands-off approach and involve professional non-family managers. Some researchers (e.g. Breton-Miller and Miller 2009) suggest that family businesses are slower and more reluctant to professionalise than non-family businesses, particularly in terms of hiring external managers or seeking external advice and support (from both business support organisations and non-executive directors), while the relative lack of external shareholders results in less external pressure to challenge how the family runs the business.

A report on Governance in Family Business in the UK by the subsidiary of a leading bank (Coutts, 2010) suggests the following characteristics and challenges of family business governance including:

- Keeping the family business in the family is a key concern for many business owners
- Complex multi-shareholder family businesses sometimes use a two tier board structure to help govern the family's relationship with the business
- A responsible board plays a crucial role in driving the business forward
- Management succession is as important as ownership succession
- Successful family businesses often employ non-executive directors
- A written constitution





Differences in governance as well as resources arise from the family's involvement in ownership and management and can lead to a wide variety of outcomes. In family firms, accumulation of power unrestricted by external board members or outside owners can lead to personalistic and particularistic behaviours that may deviate from the norm for public corporations (Carney 2005). Westhead and Howorth (2007) suggest that businesses with tight family ownership and management structures are more likely to report family-objectives as a high priority, while first generation businesses or those with a lower proportion of family managers were less likely to report the same. Le Breton-Miller and Miller (2009) suggest that the more embedded family owners are in the family, rather than the business, the more family-oriented their motivations will be, and vice versa. This is likely to occur in situations where different branches of the family are involved (and/or multiple generations) and where there is a lack of external perspectives (e.g. few externally recruited managers, lack of experience of family members outside the business).

It is argued that a controlling family's discretion over strategy and access to resources are very different for family controlled and family-influenced businesses. It is argued that Family-influenced firms access to resources is already open in terms of non-family ownership and representation on the board while that of the family controlled enterprise is not necessary so (Arregle et al 2012). Therefore the behaviour and performance of family firms may be very different owing to the differences in their governance structures. Their empirical tests largely support this assumption however they also suggest that it is important to consider how both the type and amount of external stakeholder involvement affect family firm decision-making. In a different study looking at internationalisation, Holt (2012) proposes that the non-family owners' and board members arguments must be consistent with the controlling family's goals and aspirations. But the success or failure of the arguments will depend on social norms and whether the non-family owners and board members are liked or respected. This highlights the limited influence that non-family owners and board members may have in some family-controlled firms. This would presumably be true in family-influenced firms as well, although the differences in relative power of family and non-family stakeholders would likely cause the negotiation process to play out in different ways.





However other researchers suggest that the characteristics that are seen to hold back the development of family businesses can also be their strength. For example, despite a lack of HRM ‘best practice’ family businesses tend to have better relationships between upper management and employees, particularly in terms of job satisfaction, employee loyalty, staff turnover etc. The Institute for Family Businesses identifies this as ‘people capital’ and their analysis of the Workplace Employment Relations Survey indicates that such measures appear to be higher in family businesses than non-family businesses (Bacon et al., 2013). The positive employee relationships appear to be an outcome of the approach to leadership that is a characteristic of many family businesses. For example, long-term business sustainability requires retaining well-trained staff who buy in to the business and feel a sense of engagement or ‘ownership’ and share the objectives (and successes) of the family. This requires the family owners to recruit carefully, so the employees fit in with the team and the ethos of the business, and treat the staff well to reinforce these values. This may include, for example, and when compared with non-family businesses, a greater commitment to training, a stronger tendency to retain employees during a downturn, higher wages or long-term non-pecuniary benefits such as health insurance, and a smaller salary gap between employees and owner-managers (Miller and Le Breton-Miller, 2005).

### 2.1.2 The founder owner role in the succession process

- *The founder owner role in the succession process* (e.g. anticipative, mentor- teacher, supervisor, cooperative, etc.)

The literature search has revealed a patchy coverage of the founder role in the succession process in the UK. A survey by the Department for Trade and Industry in 2006, now part of BIS (cited in Fletcher 2008 and IFB 2008) found that 77% of firms in the SME sector are controlled by the first generation, 10% by the second generation and 6% by the first and second generation family members. About one third are passed on to the second generation and one tenth reaches the third generation, the rest being closed or shut down (IFB, 2008). Surveys tend to show that the bigger and probably older the firm, the more



likely that it has already been passed onto future generations. Family firms in the SME sector with at least 10 employees are twice as likely as those with fewer employees to be controlled by the second generation. The generation of ownership also varies by sector, with agricultural businesses most likely to be controlled by the second-generation family members.

The literature suggests that many founders and leaders in family businesses do not anticipate or plan for succession. A study published by Barclays Bank in 2002 based on a survey of family firms suggested that most have no definitive plans about what to do with the firm in the future with 61% of owners saying that they had made no decision about what would happen when they stepped down from the helm. Of the remainder 16% had already decided on a successor, 13% planned to sell the business, while 10% planned to close it down (IFB, 2008).

However, it is argued that the founder of a business does have a responsibility and a role to play in preparing for succession. Having a succession plan is a first and important step but one block to this may well be the original business founder. Craig and Moores (2005) suggest that without succession plans, professionalization of the firm is seriously inhibited. Thus internal processes for family businesses (like all businesses) are necessary to include in strategy development. Arguably, what makes internal processes, particularly changing these processes, more problematic in family businesses is the influence of the founder and the preparation for succession.

To achieve effective inter-generational succession, there must be a balance between 'parenting' (i.e. a personal approach) and 'mentoring' (i.e. a more detached, business-focused approach). However the evidence is mixed when it comes to whether the process works best when the mentor is a family or non-family member (Distelberg and Schwarz, 2013). Mentoring by parents has been discouraged because of the many other roles they already play as well as because the inability of most parents to be objective in appraising their children's capacities may lead to serious problems. Barach and Ganitsky (1995) highlight the often extremely valuable contribution that an uncle or non-family executive



can make as an immediate boss and mentor to the successor. Some have argued that mentoring works most effectively when there is distance between mentors and protégés – in this case, non-family members; preferably a trusted senior manager who can provide the successor with knowledge of the principles of the family business and how to run it (Ward, 1987).

The SME Survey (BIS, 2013) suggests that under 10% of SMEs use mentors in the 12 months preceding the interview. Family businesses (7%) are slightly less likely to use a mentor than non-family businesses (10%) and there is some further variation apparent associated with business size with just 6% of micro family businesses compared with 9% of non-family businesses using a mentor. The propensity to use a mentor amongst small and medium sized family and non-family firms is similar (12-14%).

As the family business grows, the interactions between family and business objectives, and the family and non-family members of the management team, become more complex partly because there is only a finite number of family members to act as managers, and not all will be sufficiently skilled or motivated to perform effectively (Breton-Miller et al., 2004).

One of the dilemmas facing the founder or manager of the family business is the choice of the successor. The Coutts (2010) research, based on a small number of case studies suggest that families often find it difficult to choose between siblings when allocating jobs within the family business and choosing a successor. One thing the authors caution against is the allocation of shared roles at the top which can have significant impact on the business and the family if things do not progress well.

### 2.1.3 The successors role in the succession process

*- The successor's role in the succession process (dilemmas of the next generation)*

The dilemmas of the next generation are a key issue identified in the literature. Like business founders, successors are also accused of being the prime culprit in succession



failure. Some successors are accused of lack of ability to replace business founders, usually because of a lack of suitable experience or an appropriate attitude to take over ownership. Research undertaken by Kraus et al. (2011) suggests that successors are also playing multi-entity roles in the succession process. Without knowing, quite often successors are expected to take the role of a filial son or daughter, experienced business owner, professional manager etc. Furthermore, from the successor's perspective, many of them want to play the role of an ambitious owner-manager and to be in charge, while at the same time wanting their parents to keep an eye on the business. With these different roles to play and expectations to meet, it is an extremely difficult, if not impossible, task for successors to please everyone, including themselves. Krause et al conclude that it is important for successors to be well aware of their different roles and conflicting expectations in the family business.

Research focusing on the attributes of successors confirms that family member commitment is a critical component in situations of intergenerational transfer of leadership (Deloitte and Touche, 1999; Handler, 1989; Sharma and Irving, 2005). Indeed, dissatisfaction and lack of motivation among potential successors have been cited as factors obstructing succession with the family (De Massis et al. 2008). Committed family members are more likely to become professionally engaged in their family firm, cooperate in through the leadership transition, and experience higher levels of satisfaction with the succession process (Dyck et al. 2002; Handler, 1989).

Some have argued that trends within families toward becoming more democratic and emphasising individual autonomy in the succession process (particularly with regard to ownership) have made the perpetuation of the family firm more difficult (Gilding, 2000). Difficulties associated with the succession process may arise when life cycle stages in the family are misaligned and when members are anxious, creating resistance to change (Dunn, 1999). Relational factors that impede successful succession also include lack of trust, lack of motivation on part of the successors, incumbent or other family members (De Massis et al., 2008). The inability on the part of the founder to let go, and the difficulty for



the successor to operate in the shadow of the founder lead to conflicts, especially in second generation businesses (Davis and Harveston, 1999; Bjornberg and Nicholson, 2012).

In Bjornberg and Nicholson's (2012) research the collection of themes converges around experiences and sentiments around the NxG's degree of attachment – detachment and identification with the firm, in terms of closeness-distance. Narratives around the two themes were inextricably intertwined with the family history in general, and their relationships with significant others in particular – in most cases parent-child relationships. Reflections around ownership evoked statements about the central role of the family business in the child's upbringing, which often were highly emotionally charged. This led them to theorize that the close connection between thoughts around ownership and actual family relationships may represent an extension of the attachment that children and adults develop toward significant others in the family business system. However, rather than reflecting an actual relationship with another person, it is the representation of those specific relationships that appear to provide the template for the bond that exists as a form of attachment to the firm itself (Bjornberg and Nicholson, 2012).

Family business members, especially business founders and successors, are playing different roles in the family business succession process. These different roles, multiplied by different individual and multi-entity roles, and the underlying needs, values and agenda of each role, make the family business a chaotic organisation (Watson, 1994) during the succession process. Therefore, family business succession can be considered to be a dynamic, chaotic social process between business founders, successors and other stakeholders (Lam, 2011).

There have been a number of models developed to understand the passing of power to the next generation, which involves the preparation of a successor. These models are based on life-span development theories that include several stages through which the incumbent leader through a gradual process transfers power to the successor, and through which the successor learns about the business to eventually become its leader (Long and Chrisman, 2014).



Hall and Nordqvist's (2008) research based on five in-depth case studies, found that possessing formal competencies (which is a form of expert power) is a necessary but not a sufficient condition for success as the Chief Executive Officer of a family business. Instead, formal competencies must be supplemented by cultural competencies i.e. a clear understanding of the family's goals, values, and norms. Perhaps, it is for this reason that family businesses have been found to rely more heavily on mentoring and coaching of next-generation leaders and place less emphasis on out-sourced training programmes, as compared to non-family firms (Gagne et al, Massis, 2014).

Bjornberg and Nicholson (2012) point out that studies overwhelmingly suggest that the survival of family firms depends on the involvement and inclusion of next generation (NxG) family members. Whether as employees or owners, the NxG's commitment and willingness is the key to the continuity of the family firm. Family business scholars have devoted much attention to intergenerational transitions in the family firm (Handler, 1994). Indeed, NxG members are among the groups of stakeholders in the family firm that have received most attention from researchers (Sharma, 2004). Indeed, commitment among NxG members has emerged as one of the key factors that contribute to the effective and smooth succession of leadership (Sharma and Irving, 2005). Bjornberg and Nicholson (2012) argue that the antecedents of commitment and willingness to become a full-time member of a family business can be traced back to the psychology of the relationship between the individual and the family business system, consisting of family, business and ownership.

The IFB (Drake, 2009) have published a practical guide for the next generation working in family businesses. The guide provides an overview of the characteristics of family businesses and emphasises succession in the company environment which account for less than a quarter of all family businesses. It highlights the lack of a career plan for successors as an area of weakness in family businesses and the importance of a mentor to assist and support the next generation.



One of the issues identified by Coutts (2010) is the tendency amongst some family firms for the employment of family members to be dealt with on a very informal basis. The IFB guide (Drake, 2009) suggests that it is in the interests of successors (and the employer) to ensure that the employment relationship is conducted in the same way as the relationship with non-family members. A further issue amongst larger family businesses is the expectation that the next generation will gain experience in the wider labour market role before joining the family business in a management role.

Previous research published by the IFB (Nicholson and Bjornberg, 2007) explores the ability of families to build bridges spanning generations. A central premise is that family 'climate' strongly influences the choices of next generation members and their relationship to the business. This occurs through financial ownership, emotional ties, and professional involvement in the business or just the chemistry of family relationships. The research captures variation and complexity of different models of next generation involvement through in-depth case studies of eight family firms. The analysis reveals 13 themes clustered under three headings: Ties between next generation members and the firm; Family relationships; Decision-making styles and process (Appendix 1)

#### 2.1.4 Guidelines orienting the succession process

- *Guidelines orientating the succession process* (e.g. starting as soon as possible, cooperation between generations, existence or lack of formalised succession plan, joint activity of family members and other colleagues, degree and types of the external help (i.e. legal, financial, commercial consultancy).

To some extent the IFB research identified above provides some guidelines and insights into what to do and what not to do to support successful intergenerational transfer (Nicholson and Bjornberg 2007). There is almost universal agreement that a well-developed succession plan is seen to be crucial (Sharma et al. 2001) in successful intergenerational transfer and succession in the family business. Good practice includes preparing the next generation as soon as possible for succession, cooperation a formalised





succession plan developed with and agreed by all family business stakeholders (including influential non-family members) and the use of experts, often external to the business to navigate the complex and uncertain waters of relationships between family members, visions and values and reluctance of the older generation to step aside (Lansberg, 1988, Sharma et al., 2000). However research suggests that well developed succession plans appear to be a relatively rare occurrence.

The process of succession can be thought to encompass three distinct stages (Stavrou and Swiercz, 1998): (i) pre-entry, where the designated or potential successor(s) are prepared or 'groomed' to take over; (ii) entry, involving the integration of the successor(s) into business operations; and, (iii) finally, promotion to a management position.

It is also worth noting that the larger the business is, the more likely they are to have developed a succession plan, mainly because of the increased complexity, hierarchy and formality which inevitably accompanies growth, while small businesses tend not to plan in such detail (Sharma et al., 2003, 2000). This applies in general to all businesses, not just family businesses, but in the latter the greater complexity of succession planning and the intertwined motivations of the family may make it more complex and urgent to plan in advance, if it is to increase the likelihood of a positive outcome. As Morris (1997, p386) noted, 'family business transitions do occur more smoothly when successors are better prepared, when relationships among family members are more affable, and when family businesses engage in more planning for wealth-transfer purposes'.

Nicholson and Bjornberg (2007) provide some best practice principles that may be applied to the transition process under three broad headings; ties between next generation members and the firm, Family relationships and decision-making style and process (Appendix 1) Outcomes and impacts of the succession process





- *Outcomes and the Impacts (advantages versus disadvantages) of the succession process (e.g. family inheritance, selling in the market, inviting private investors, selling to employees)*

There is a range of potential outcomes associated with the succession process that includes family inheritance, selling part or all of the family business, selling to employees or selling on the stock exchange. The SME survey (BIS 2013) asks participating SMEs about whether they anticipate the closure or full transfer of their business in the next five years. In successive surveys (2008, 2010, 2012) a higher proportion of family businesses anticipated closure or transfer of their business compared to non-family firms. In 2012 26% of family businesses anticipated closure (9%) or full transfer (17%) compared with 18% of non-family businesses anticipating closure (7%) or full transfer (11%). In absolute terms this would equate to around 266,000 family firms anticipating closure and over 500,000 anticipating full transfer in the next five years. Businesses over 10 years old being three times more likely to anticipate closure than those aged four years or less. However the research evidence on the propensity of transition to actually result in a specific outcome, and the positive or negative impact of a specific outcome, is again patchy and likely to be contingent upon specific context and circumstances. One way of framing succession outcomes is through the lens of entrepreneurship, i.e. succession as a process of entrepreneurial exit and entry and it is unclear whether those that anticipate closure actually close the business or close it only to reopen another one.

Small scale case study research with family businesses reveals that many have a very small number of shareholders Braidford et al (2014). Many stated that they had a preference not to involve the extended family or external stakeholders. As one might anticipate, older and larger family businesses were more likely to make provisions to preserve SEW which include:

- trusts or preference shares (providing an ownership stake but no control);
- ownership by a holding company with no other activities, in turn owned by and with a board drawn solely from the family, with the trading company having a majority or wholly executive-led board;



- wholly or partly owned by a separate company, in turn owned by the family and which makes outside investments (e.g. in property, and/or to build up a pension fund for older family members), usually in order to protect and develop family wealth, and to spread risk in a more diverse way than simply relying on the trading company.

Braidford identifies two cases of good practice. They were the largest businesses interviewed and among the (very) small minority which had formal arrangements in place for family involvement – in one case, a family council and constitution (drawn up by an external business consultant/corporate lawyer), in the other a family agreement drawn up by the manager and ratified by a lawyer. The rationales in both businesses for these strategies were similar; they were seen as a measure designed to better guarantee that processes of wealth transfer were effective. Both were ambitious for continued growth and open to diversification, within the core business line and in related and unrelated areas, prioritising cost and quality, and in particular the improvement of internal processes and promoting the brand in order to position the company as a niche leader.

In the first case, this was driven by advice from an external consultant, combined with applying the lessons learned from direct experience of a poorly managed succession.

### 2.1.5 Inhibitors and enablers of the succession process

*- Inhibitors and enables or the succession process (different future views of parents and their children, lack of (suitable) successor, predecessor does not want to retire, children have no affinity to the family firm etc.)*

Many of the inhibitors and enablers of the succession process are discussed in multiple sections of this review. Effective strategic planning is clearly one means to enable successful transition however the literature suggests a number of enablers or inhibitors that may be considered. Many family businesses contain non-family members and the success or failure of succession can be affected by whether non-family managers support or obstruct the succession that in turn depends on the procedural justice climate surrounding the process. Barnett et al. (2012) argue that the strength of the vision and



the extent to which the family and non-family members are bought into the vision are important factors in successful transition. Of course visions will differ between firms and this can be another source of heterogeneity amongst family firms.

The prevailing discourse tends to emphasize poor management which may be exacerbated by in-family succession, inevitably narrowing the pool from which management talent is drawn, and possibly causing resentment and poorer performance (or departure) from other managers, who recognise a limit to how far they can be promoted.

### 2.1.6 Socio emotional wealth

- *Emotional capital accumulation process* (Intra- and inter-generational similarities and differences, harmonization of family and business values, social-cultural impacts on family patterns, etc.)

Socio-emotional wealth (SEW) is defined as ‘non-financial aspects of the firm that meet the family's affective needs, such as identity, the ability to exercise family influence, and the perpetuation of the family dynasty’ (Gómez-Mejía et al., 2007, p106) that has become an influential concept in the study of family businesses. From this perspective, family owners are viewed to be loss averse, leading them to reject opportunities associated with innovation or growth that may threaten the business. Research suggests that the aversion to risk may manifest itself in a number of ways including lower ratios of debt to equity (Gonzalez et al., 2013) and debt to assets (Anderson and Reeb, 2003) and higher levels of liquidity (Allouche and Amman, 1997; Bigelli and Sánchez-Vidal, 2012), plus a tendency to scrutinise opportunities very carefully and eschew diversification into new market areas, unless closely related to the existing line of business (Anderson and Reeb, 2004).

This strategy permits for a longer time horizon for planning purposes, and for growth plans to come to fruition, facilitating longer-term investment in the business, rather than pursuit of short-term profits for dividends. For this reason, while family businesses may appear to be growing more slowly than non-family ones, longer term that gap may close, as the family



business continues its slow, patient growth route. The security of senior management positions which derive from their family status also facilitates longer term planning and the build up of in depth knowledge and memory, as the business leader is less likely to face redundancy for any short term failure to grow or generate profits (Miller and Le Breton-Miller, 2005).

These characteristics of family businesses are often viewed in a negative way where the aversion to risk may lead to lower levels of innovation, and stagnation within the business, as it simply chooses to ‘tick over’ rather than use the relative freedom that they have to pursue a more growth-oriented strategy (Gomez-Mejia et al., 2007; Hiebl, 2012).

The corollary of the tendencies identified above are that family owners try to ensure the survivability of the business for the next generation, and in particular to build up the social capital of the business which leads to stronger relationships with trading partners, advisers and employees as well as within the family itself. Wilson et al. (2013) note, this ‘survivability capital’ can be seen as a combination of human, social and financial capital, working in a way that distinguishes family from non-family businesses. On the other hand, Wilson et al. (2013) also note that there are certain characteristics of family businesses that may militate against survivability: (i) family conflicts; (ii) altruism towards the wider family: e.g. nepotism in appointments leading to poor managerial choices linked to (iii) an unwillingness to deal appropriately with poor performers and employees; (iv) a smaller chance of taking risks and seizing high value opportunities; (v) strong social capital leading to a reluctance or difficulty in changing strategies, operations or trading partners and lower R&D expenditure.

The SEW framework has been used increasingly to explain and predict differences between family and non-family firms (Chen et al 2014). Berrone et al (2012) classify several different dimensions of the SEW framework among which family reputation and social identity are two key elements. Adopting this analytical lens, family firms want to be viewed as successful and concerned about local communities and as a result they tend to be careful when it comes to making decisions that might affect these perceptions.



More recent work (e.g. DeTienne and Chirico, 2013) has emphasised more diverse pathways of succession, looking through the prism of what exactly SEW means. For example, while transferring the business itself might be seen as ideal, not doing so should not necessarily be seen as a failure. For example, transferring the physical entity of the business itself may be less crucial than the transfer of its core values (Salvato et al., 2010), such as entrepreneurial spirit, or of creating opportunities in general for the next generation, which can be facilitated by the building up of family (socio-economic) wealth through the business. As DeTienne and Chirico (2013) put it: 'Our arguments lead us to conclude that family firms may simply redeploy resources into other business activities after exit'.

## 2.2 Psychological-Communicational Relations

### 2.2.1 Family Business Dynamics

Family firm research recognises that it is the familiness of a business that makes a family firm distinct from a non-family firm (Chua et al., 2003). In the past, arguably, management studies have paid insufficient attention to the unique theoretical and practical problems of family firms (Dyer, 2003). The underlying assumption of the work in this area is that family firms have particular characteristics that distinguish them from non-family firms (Kraus et al., 2011).

A key element of this is the role of the family firm in supporting the need to belong as well as acquire status (Nicholson, 2008). The mere possibility of intergenerational transmission of the title and ownership of the business within a family changes the dynamic of the enterprise, leading to first-generation owner-managed firms being disposed to take a view beyond their own lifespan. As Anderson and Reeb (2003) put it in their study of the performance advantage of quoted family firms: "Founding families view their firms as an asset to pass on their descendants rather than wealth to consume during their life-times" (p.1305)



Of importance in relation to the succession process is the concept of attachment within psychology. Attachment derives from the developmental work of Bowlby (1969, 1973, 1980), who conceived of closeness-distance as an indicator of relationship quality or bond between an individual and attachment figure. In childhood, the availability and responsiveness of supportive others result in a sense of security, whereas absence and unresponsiveness of others result in insecurity expressed as anxious or avoidant behaviour. Although most of the literature on attachment has historically been conducted in family and small child settings, the concept has been successfully applied to adults. More recently, the role of adult attachment in organisational life has attracted attention in the literature. For example, secure attachment has been linked to better work life satisfaction (Hazan and Shaver, 1990), whereas anxiety and avoidance are associated with lower levels of organisational commitment (Mikulincer and Shaver, 2007). Avoidance is also linked with a higher intention to quit (Mikulincer and Shaver, 2007). The Bjornberg and Nicholson (2012) study reported on the emotional aspects of the relationship that exists between NxG members and the family enterprise. Based on the qualitative and quantitative studies, it appears that the emerging concept of emotional ownership is important.

Psychological ownership has developed into a significant avenue for family firm research. The basic model of 'ownership' can be broken down into the following elements: the owner (subject), the ownable subject (object) and the relationship between them (ownership). In family firms, the owner is the connector between the social systems of family and firm (Terberger, 1998). Ownership is not only an economic, but always a psychological phenomenon (Etzioni, 1991).

'Psychological ownership' refers to the relation between individual persons and ownable objects, but does not necessarily also include legal ownership (Pierce et al., 2005). According to Pierce et al (2001) the core of psychological ownership is the feeling of possessiveness and of being psychologically tied to an object. In summarising previous research on psychological ownership, Pierce et al. (2005) conclude that it emerges because it satisfies both generic and socially generated motives on individual persons.



Existing SME research is filled with notions of owner-managers mentally connecting themselves to the firm, which constitutes a central part of the owner's life and self-identity. In this context, the firm is both the ends and the means, being partly the result of action, partly a target of actions, and also an instrument to reach other targets. The owner-manager's mental connection to the firm is very unique – each owner-manager has his own way of looking at his firm and their view is of key importance in relation to the succession process (Kraus et al., 2011).

### 2.2.2 Social systems

- *Social systems* (family business as a "social system", the definition and clarification of roles and responsibilities of the owners, family members, independent members of the board and management is needed)

The blending of family and business social systems provide a unique context for family based businesses. It has been suggested that family firms are able to effect an unusually high degree of cultural control through the high-trust relationships they are able to maintain with stakeholder groups, that provides a tangible competitive advantage (Nicholson, 2008). However, at the same time there is a more gloomy picture painted in line with public prejudices, media horror stories, and fictional sagas, about the dangers of psychological overspill from dysfunctional families into the businesses they run. Nicholson (2008) notes that:

1. Family firms are able to generate unique advantages through their capacity to bind naturally diverse individuals together in a common enterprise and purpose. These centripetal forces enable them to engage in processes and decisions that are much riskier for groups of decision makers who lack such ties. They also enable the family to counter many of the special agency problems that arise.
2. Family firms are also uniquely vulnerable to intra-family conflicts and their spillover into the business. Agency problems identified by researchers compound the risk. Additionally, they face challenges such as integrating non-family executives,





idiosyncratic leadership, and other hazards of the naturally occurring array of individual differences among family actors. (Nicholson, 2008, p.114).

The analysis undertaken by Lam (2011) shows that family business succession can be a lengthy complex social process, and the findings support previous studies which argue that the succession process starts before successors join the company. Lam (2007) points out that what makes a business a family business is the shared understanding about each party's role within it: family members are insiders and are in charge of the business, while non-family employees are always outsiders and will never be considered as insiders. Ironically, what is found to be the main issue giving rise to the failure of succession is family business members' collective lack of a shared understanding about the succession process. There are conflicts within individuals as well as between individuals in the family business. Researchers argue that business founders and successors play different roles in the different phases of family business succession (Handler, 1990). Lam's (2011) research proposes that individuals are playing multi-entity roles simultaneously in the succession process.

For example, the analysis undertaken by Lam (2011) demonstrates that the conflicting self is deep-rooted because of individuals' multi-entity roles and their underpinning needs, values, perceptions and social needs. 'As a result of this, self-conflicting messages were communicated among family members through ongoing social interaction, thus giving rise to the confusion, frustration, disappointment, rivalry and emotional trauma that is commonly experienced by business founders, successors and other stakeholders, including family members and non-kin employees' (Lam, 2011, p.525). The research revealed the multi-entity roles that family business members inevitably play in the process of family business succession.





### 2.2.3 Family Strategy

*Family Strategy* (challenges that the FB faces in the family for generations, family strategic planning options, "Familianness" as the source, and the family strategic job, free and hindered communication, borders and border management, non-linear inheritance, parallel strategy processes, forms of family management: a proactive means of conflict prevention, family constitution, Family Charter.)

The idea of 'familiness' is offered as an explanation for both the superior and sub-optimal performance of family firms. Familiness is created by the interactions between the founder, family members, generations of the family, and the business. This can be a strength of the business but it is not always a positive influence in a family business. Familiness, if not maintained and nurtured, can rapidly become a destructive force. For this reason Habbershon and Williams (1999) distinguish between distinctive and constrictive familiness. Constrictive familiness develops when founder and family capital are eroded and family involvement becomes an encumbrance to the family business. Distinctive familiness exists when family involvement in a family business provides a firm with a sustainable competitive advantage.

The familiness of a business, which results from the interactions between and within the family and the business, cannot be separated from its corporate culture. Corporate culture can be defined as the values, beliefs, and attitudes that influence individual and group behaviour within a business organisation (Miller 2000). Barney's (1986) definition also adds assumptions and symbols as elements of corporate culture. Familiness overlaps with the corporate culture of a family business, as the founder's and founder's descendants' own values, beliefs, assumptions, and attitudes are absorbed in the corporate culture and influence the way things are done in the business. When culture is transmitted, familiness will then be automatically transmitted as well. Culture (and the familiness absorbed in it) affects business performance, but for culture to have a positive influence, it needs to be valuable, rare, and inimitable (Barney 1986). If cultures that enable success are rare and



inimitable, then successful family businesses cannot be said to possess some kind of general "family business culture".

#### 2.2.4 The Psychology of Succession

- *The Psychology of Succession* (identity, values; special paradoxes of the succession process, the parent-child relationship in the family business; the gender differences; "invisible bonds"; open and hidden loyalties, the decision-making process of succession, including the role of emotions and conflicts)

In relation to the succession process, studies focus on the personal emotional and developmental characteristics of the founder-owner in particular (Levinson et al., 1978). The founders of family businesses have been often accused of being the main obstacle to successful family business succession: the business founder's unwillingness or failure to let go, to plan for succession or implementing succession planning, are among some of the accusations. A study undertaken by Lam (2011) suggests that business founders should see that they have varied and sometimes conflicting roles in the family business succession process. Many business founders are reluctant to seek external professional advice in the process of family business succession: many do not see the value and rationale behind it, while others feel that it demonstrates their incompetence to lead a family and hand over the business to the next generation (Lam, 2011).

By helping business founders to realize the multi-entity roles they are playing and the possible self-conflicts that this engenders, it is hoped that this will encourage them to seek external professional advice at a different level. In addition to issues related to finance, law, property inheritance, insurance and taxation, external professional advice can be very helpful in resolving issues that family business members are not comfortable about discussing, such as the owner's departure and the emotional experience that this involves. Furthermore, it helps to take care of some of the roles that the businesses founders are playing and can be helpful in resolving conflicts that have been caused by their multi-entity roles. Most importantly, it helps business owners to understand that seeking external



advice is not a symbol of incompetent leadership or a dysfunctional family: on the contrary, it demonstrates the rationality and confidence of a business owner in their family business. Role awareness is important.

The transfer of top management from one generation from the next represents a crucial strategic issue of the family firm (Barach and Gantisky, 1995). According to Sharma et al. (2001), the business owner's inability of 'letting go' is the most cited obstacle of effective succession. Emotional aspects lead to indecisiveness and delays of transfer (Landsberg, 1999). Kommers and van Engelenburg (2003) also mention the psychological aspect as being the most decisive within this process (Krasus et al., 2011).

A review of the family business succession literature helps to identify two different views of family business succession. A great number of studies conceptualise succession as an instantaneous happening, a visible event that can be studied closely, the moment when a successor take over as the chief executive officer (CEO) of the family business (e.g. Miller et al., 2003): that is, a 'passing the baton' view (Dyck et al., 2002; Mitchell et al., 2009; Sharma et al., 2001). However, the instantaneous view of succession is challenged by researchers who argue that the succession process is a lengthy process (Murray, 2003; Handler, 1990), almost a 'life-long development process' (Longenecker and Schoen, 1978:5; Lam, 2011).

Handler (1991) identified that three phases in the succession process relate to the path of the successor:

1. Personal development before actively working in the business;
2. Business involvement; and
3. Leadership succession when in charge of the business

Lansberg (1988) observed that not only is the incumbent leader often reluctant to retire, but those employees, family members, family members, customers, suppliers, and other key stakeholders close to this individual encourage such reluctance. Lansberg (1988) labelled this phenomenon the "succession conspiracy" and it continues to feature in research today (Gagne, Sharma and De Massis, 2014).



In referring to the retiring leaders as the “parting patriarchs”, Sonnenfield and Spence (1989) identified four distinct departure styles adopted by these patriarchs based on their identification with the position/stature and a quest for an immortal contribution, combined with a belief that only s/he is best qualified to fulfil this responsibility. These four departure styles are: (1) monarchs, who do not leave office unless forced to; (2) generals, who spend their retirement planning a comeback; (3) governors, who leave willingly and maintain no contact with the firm or its leaders after departure; and (4) ambassadors, who leave willingly and serve as advisors to the firm and its new leaders. Other work in this area has suggested that retiring leaders with strong capacity to disengage from previously undertaken activities and to engage in new ones plan their transition better and are more satisfied with their post-retirement (Gagne et al., 2011).

### 2.2.5 Crisis and Conflict

- *Crisis and Conflict* (the family has a latent vulnerability at risks or succession. The family conflicts quickly impact the business, and affect the lead; paradoxes as a catalyst for conflict; conflict situations in family businesses, conflict and cooperation in the management, escalation dynamics, attribution mechanism, attribution errors, and conflict mediation methods)

If the intensity and depth of trust in controlling a family has the potential to build strong, enduring relationships that help unleash the inimitable competitive advantages for family businesses, crisis and conflicts represent the dark side of the family-business system. Alongside succession and governance, conflict has been a long-standing topic of concern for FB owners and their advisors since the 80's, as it has the potential of disastrous outcomes for the family, and can even cause the demise of the business (Gagne et al 2014).

Family involvement in business introduces complexity in interpersonal and group dynamics. Sibling or cousin rivalries, conjugal problems, ownership dispersion issues,



family altruism, and succession concerns are all potential causes of conflict in family businesses. The frequency and magnitude of conflict has been found to increase with the number of closely affiliated family members with organisational roles, the number of non-involved family members who can affect business decisions, high levels of social interaction, and the presence of the founder's shadow (Davis and Harveston, 1999; Memili et al. 2013). Moreover, the feeling of being locked in the family and/or in the FB may arise from the inability of family members to sell their shares or quit their job in the FB. Such sense of being trapped may trigger resentment and cause conflict.

Another form of conflict that may penetrate FBs is of a more interpersonal nature. As family members on an FB must deal with both the demands of their family and of their work roles, it is very likely that they will experience role conflict at times. Memili et al. (2013) present an interesting model that can serve to test how role conflict in family business may affect the firm's productivity and efficiency. Again, drawing on the theory of relationships may help uncover the issues that conflicting role demands may lead to. Research on work-life balance could also inform such research (Gagne et al. 2014).

Memili et al. (2013) developed a theoretical framework that highlights the role conflicts that emerge among family members working for the family firm. Their model draws on stewardship theory as this theory deals with the sociopsychological factors that determine members' intentions and behaviours in the family business (Davis et al. 1997). Moreover, the stewardship perspective is useful in the family firm context because family members place high value on the attainment of the goals of the family business. Their theoretical framework is driven by two research questions 1. What factors mitigate/ elevate role conflict in family firms? And 2. How does family business members' role conflict impact on firm performance? Their theoretical development implies that family and non-family firms differ in role conflicts due to the duality of family members' roles, family firm-specific psychodynamic effects, such as marital discord, high levels of dependence on human and social capital that are family business employees with kinship ties and family's social networks, long-term orientation and, ultimately, transgenerational sustainability.



Role conflict within the context of family firms has been a particular focus in family firm research. In contrast to employees in non-family firms, family members who work in the family firm have the dual role of being a family member and a family firm employee, complicating the responsibilities of fulfilling both family and business expectations (Gersick et al., 1997). Due to the links and relationship between the family and the business (Arregle et al., 2007), the potential for generating role conflicts within family members tends to have a direct influence on the family business, given that expectations and behaviours cannot be separated very easily.

An individual's 'social identity' as a family member and a family employee can lead to them having an inconsistent and complex array of demands placed upon them. This is particularly challenging for family members as roles become more complex when they require an individual to be simultaneously involved in at least two subsystems (Katz and Kahn, 1978). Thereby, the expectations of family and business subsystems are combined to become the role of the family business member who will have a hard time to set his/her own priorities. If role pressures from work or from the family are incompatible, fulfilling both role expectations becomes an impossible task (Stoner et al., 1990).

For example, if the parent-manager promotes an unqualified child, he/she meets the demands of a familial role by caring for the offspring; however, he/she is at conflict with the managerial role that requires an objective evaluation and judgement and prohibit the display of nepotism in the business (e.g., Jaskiewicz et al., 2013; Kidwell et al 2012). In addition, such actions may also generate a set of unintended consequences that can negatively affect other organisational members (Mellewigt et al. 2007; Wayne et al.,1997). This research, as well as other studies in the area, suggests there is a higher potential for role conflict in family firms than in non-family firms due to the dual roles of family members being a member of the family and working for the business.



### 3 Strategic Issues

#### 3.1 Strategy formation and decision

- *Strategy formation and decision* (participation of family and non-family members, etc.)

Please consider the various roles family and non-family members can take in running business (e.g. board member, shareholder, manager, employee, etc.)

Managing the competing demands of family and business can be problematic, especially so in the context of succession and strategic planning where a family must balance the sometimes conflicting interests of both the owner's family and the business itself. Exploring, interpreting and better understanding strategies and processes at the micro level of analysis can shed light in areas that might be missed by more macro strategic levels of analysis. Nordqvist (2011) argues that the key to understand why family firms may be 'special cases of strategic management is likely to be found at the micro level of social interaction. At this level, everyday interplay and mutual influence of the family and the business are expressed through family and non-family actors who impact the strategy process, as well as where and how these actors interact. Nordqvist goes on to pose two research questions; "RQ1: Which actors are involved in strategic work in family firms: that is, who is the strategist? RQ2 Where and when do these actors meet and interact in strategic work: that is, where and when does the strategic arena appear?" Micro level analysis of strategy in practice can help inform issues of succession planning in family businesses.

Family considerations often overwhelm the strategic realities of the business and hinder the ability to successfully pass the business on to subsequent generations (Jaffe, 2005). As illustrated earlier in this review the socio-economic dimension of family businesses and the juxtaposition of family and business interests present unique contexts for strategy. The heterogeneity and dynamism of family businesses means that generalisation of the various roles that family and non-family members can take in running the business should be undertaken with caution. However, a number of themes and issues are brought to the fore under the heading strategy formation and decision and they include ethnicity, family





bonding; family matriarchs and women's role in decision making; communication and governance.

One area that has gained some attention in the literature is the role that strategic planning plays in the sustainability of family firms over the generations. Researchers have identified a lack of strategic planning as a key mechanism to counteract the underinvestment in family firms that leads to the decline in survival rates across the generations (Eddleston et al. 2013). Both strategic planning (Chrisman, Chua and Sharma, 2003; Sirmon and Hitt, 2003; Upton, Teal and Felon, 2001) and succession planning (Handler, 1989; Sharma, Chisman and Chua, 2003a; Ward, 1987) are identified as mechanisms likely to counteract this underinvestment, encourage appropriate investments, and lead to the sustainability and growth of family firms.

Lumpkin et al. (2011) illustrate that identity theory suggests that family firms have the option of 'interweaving' family and firm when seeking strategic advantage. In a comparison of strategic planning, Craig and Moores (2005) note that in some studies (e.g. *Feigener et al., 1996*), family business Chief Executive Officers (CEOs) have been found to rate strategic planning less significant in successor preparation than do non-family business CEOs. Harris et al. (1994) reviewed the strategy literature pertaining to family business and came up with a list of characteristics that may influence strategy, including 'inward' orientation, slower growth and less participation in global markets, long-term commitment, less capital intensive, importance of family harmony, employee care and loyalty, lower costs, generations of leadership, and board influence on implementation.

Bhalla et al. (2007) explore the role of ethnicity in relation to strategic management paradigms. They draw attention to the role of family bonding in strategy making. Reporting on primary data findings they show that the ethnic origin of the controlling family has a significant influence in determining the dominance of a particular strategy paradigm. However, successful high-growth family firms are not associated with any particular school of strategy. The influence of family bonding on strategy-making was greater in ethnic family firms than non-ethnic family firms. By focusing this research on the formation of strategy





within family businesses that are ethnically owned the context of culture and the role of aspirations comes further to the fore.

Women's role in decision making and family matriarchs are also considered by Bhalla et al. (2007). One particularly noteworthy finding is that, family members who do not hold an official position in ethnic family firms (for example, family matriarchs) nevertheless played an important role in decision-making. Bhalla et al (2007) go on to note that in many family firms, women exercise strong political influence as mediators and enablers, maintaining channels of communication and ensuring that conflicts are amicably resolved. The role of women family members in the formulation of strategy and succession planning is clear. Women family members even when not officially working in the business do nevertheless help to give shape, meaning, influence and direction to family business strategy.

Eddleston et al (2013) point out that succession is rarely a single, isolated event or decision. Succession and planning for succession is a more complex issue than might first appear and throughout and as part of the strategy for succession, communication is a key success factor.

Eddleston et al (2013) draw attention to the fact that different generations of family businesses will have a need for different strategic and succession plans. They argue that firms in different generational management stages will have different needs with respect to both strategic planning and succession planning. Furthermore, founders who are most interested in perpetuating their legacy and maintaining their family's control of the business are most likely to develop a succession plan. Since a business is seen as a reflection of its founder (Davis and Harveston, 1998), with succession planning considered an indicator of the future growth potential of the business (Cabrera-Suarez, 2005), first-generation firms with succession plans should achieve greater firm growth than those that lack such plans. Eddleston et al's (2013) paper usefully explores the links between growth, strategic planning and succession planning and does so from a generational perspective. In so doing the paper recognises that different types of planning are needed for family businesses at different generational stages of ownership.



The strategic needs of the business and what the family wants are not easily reconciled in the process of succession and succession planning. Jaffe (2005:50) suggests that proper financial planning for the future of a family business must include consideration of two dimensions – the family’s desires and intentions for the business, and strategic planning processes for the business future. In addressing these two dimensions Jaffe (2005) puts forward the idea of a planning process based on a board of directors and a family council to reconcile different interests and to set strategy. Jaffe (2005) presents a model of how the planner can help the family business survive into subsequent generations by using a two-dimensional planning process: the family council and the business board of directors. The model helps the family negotiate the boundary between the world of the family and the world of the business. However, the two worlds are not always easy to navigate or negotiate as they are so often interwoven and the idea of a family council and board of directors may not suit all family businesses.

### 3.2 Separation of ownership and management

- *Division of labour between owners and managers (employees). (Separation between of managerial and operational/executive roles, keeping distance between family life and business, etc.)*

Looking at the division of labour between owners and managers (employees), a range of themes and issues emerge from the literature and include: identity management in family firms; micro level strategic processes; family and business; role models and inculcation of bias; the founder and preparation for succession several of which have been explored to varying degrees in other parts of this review.

Management of identity has an undoubted bearing on the division of labour and role allocation within family businesses. Navigating identity management requires tact and skill because of the many roles one has to play and fulfil; roles are many and varied both within the business and the family and inevitably tensions and conflicts emerge over



expectations. Exploring the role of identity and how it might confer or confirm strategic advantages to family businesses Chrisman et al. (2008), note that when families are involved personal, organizational, and family identities come into play. Because of the multifaceted nature of identity confirmation among family members involved in the top management team, effective relationships can unleash powerful advantages for a family business. Conversely, if handled improperly or neglected, serious problems can occur. The complexities involved in identity confirmation are illustrated by Milton's application of the concept to the succession process, one of the most substantive challenges facing family firms (Le Breton-Miller et al, 2004). The succession process requires changes in the business identities of successors and incumbents, a shift with which they, as well as other family and organizational members, must learn to cope. The role of identity and shifts in identity as a result of succession within family businesses makes for an interesting approach to the study of strategy and family businesses.

Trying to reconcile the competing needs and demands of family and business and of different family members is not something that is always easy to achieve. It is important to take account of expectations of the business and of family life and this is especially important with regards to strategies for succession planning. Jaffe (2005:52) writes, "So before deciding the fate of the business, the family has to define its own goals for each individual and as a whole. Where does the business fit in? For what does the business stand? These questions are broader than just the business direction. The family must look at its own values – about generating wealth, spending or saving it, and how it wants to be remembered in the community. The family council can explore the values and intentions of their older generation and the talents and desires of the younger ones. This may lead to conversations about values, money, and desires for the future." Jaffe (2005) notes that it is important to develop a new generation of family members, regulate their involvement in the business and align the business with the family's plans.

Founders of family businesses should consider what the next (successor) generation can do to improve business performance. Role modelling and learning as being part of a family business does indeed bring a number of positives. However, there can be downsides in



that established business habits may simply be passed on without much thought given as to how they might be changed and improved. What works for one generation of a family business may not work in the next as things (environment, market etc.) change. Lumpkin et al. (2011) refer to the inculcation of biases and addressing this in strategies for succession planning is of undoubted importance. They also note the importance of the extent to which founders of family businesses can or are able to do things that will enable their children to perform better when they take over the family business. Key issues for consideration include to what extent do parents act as role models, imbue value systems, and employ offspring in the family business? To what extent is this process limiting because it involves the inculcation of biases that are detrimental to future performance?

### 3.3 Learning and knowledge transfer

*- Learning and Knowledge development/ transfer in the firm*

The comprehensive literature search revealed few articles relating specifically to learning and knowledge development or transfer in family firms in the UK published in the last ten years. Research more generally draws attention to the informality of learning and knowledge transfer in smaller family firms that is a recognised feature of many SME's in the UK (BIS 2012).

A persuasive discourse in the UK is influenced by the informal dimensions of learning and knowledge development 'on the job' through problem solving and networks. Some researchers emphasize the psychological or cognitive perspectives of understanding entrepreneurship such as confidence, self-belief and self-efficacy; personal values and motivation to achieve; setting and driving ambitious goals. Others identify the social dimension of learning through action and relationships. The concept of entrepreneurial learning offers theoretical insights which can be usefully examined in the context of family business and succession. Studies have most commonly adopted a qualitative, interpretive approach where they often draw upon narrative accounts of individuals reflecting on their experiences in setting up and developing a business (Shaw, 2006). These studies typically



highlight the complex learning processes that occur as individuals engage in different forms of participation in overlapping communities of familial and business practice, resulting in cycles of ‘everyday learning’ and occasionally transformational learning that occur over time.

Within this context coaching and mentoring play a key role in learning and knowledge transfer as family firms generally favour personal, relationship-centred approaches to successor development (e.g. Kaslow, 2005) and in order to ensure the long-term prosperity of succession to family members, ‘mentoring’ is a necessary if not sufficient condition (e.g. Sharma, 2007; Banco and Perez Rodriguez, 2009; Distelberg and Schwarz, 2013). Whilst the terms coaching and mentoring are sometimes used interchangeably it is important to differentiate them.

Coaching can take several forms but ‘business coaching’ is often referred to as a planned and often informal ongoing process for interacting with individual or groups of employees or business owners and/or managers. It is a skilled activity but differs from, for example, ‘executive coaching’ due to its focus is on performance and skill enhancement, rather than career goals. The coaching process typically involves a third party contracted from outside the organization and is intended to be non-directional – focusing instead on providing a process through which clients can solve their own problems rather than providing or developing solutions for them (e.g. Grey et al., 2011; Audet and Couteret, 2012; Fillery-Travis, 2015).

Mentoring is a broad, complex and sometimes contested concept. One way to view it is as a complex human interaction that reflects a unique relationship between individuals (e.g. founder/owner and familial/kin successor; parent and child; father and son; father and daughter; mother and daughter). Mentoring is a dynamic learning process and involves the acquisition of knowledge defined by the types of support provided by the mentor to the protégé. A mentoring relationship may be reciprocal, positive or dysfunctional but is always asymmetrical – the primary goal is protégé growth and development (e.g. Kram, 1985; Clutterbuck, 2008). The general purpose of workplace/organizational mentoring is the



personal and professional growth of the protégé. Organizational mentors tend to provide two primary types of support: i) career-related support prepares protégés for career advancement and helps them learn to navigate within the organization. This can include sponsorship, exposure and visibility, and coaching; ii) psychosocial support helps protégés develop a sense of competence and identity as a professional and occurs through the provision of acceptance and confirmation, counselling, role modelling and friendship to protégés (Kram, 1985; Noe, 1988; Eby, 1997; Allen et al., 2004; Allen and Eby, 2007).

It is also useful to distinguish between formal and informal mentoring. This distinction is highlighted in many mentoring relationships (see e.g. Du Bois et al., 2006; Allen and Eby, 2007) but in this case: formal mentoring takes place in an organized and planned manner as part of organizational policy and includes such elements as mentor assignments; informal mentoring includes all mentoring that is not established and complied with as part of a formal organizational policy (Boyd et al., 1999).

On the issue of succession and leadership Jaffe (2005) suggests that the strategic future of the business involves determining the next generation leadership team and not just the top person, but also several capable people who are young enough and dedicated enough to lead the company to the next level of development. The development of the necessary talent to ensure the sustainability and success of the family firm is often identified as a critical success factor. However, where the talent should reside - amongst one or many family or non-family members and how the talent is most effectively developed appears to be under developed in the literature. Jaffe (2005) points out that succession takes place over a period of time and should not be seen as fleeting moment of transition: “Succession of generation is not an event. It often takes place over many years, with a long period of cross-generational partnership. As life spans and careers lengthen, so do the number of years the two generations, even three, work together“ (p56). The research also recognises that succession is more than just about one leader but rather about the team and developing that team for future success: “The task of succession governance is not simply selecting the next leader. The business is not a prize or a trophy. Rather, it is developing the talent, focus and resources for the business to continue to be successful. Often the



talent is dispersed in the family, or between several managers, and some form of shared leadership emerges” (p56).

Lumpkin et al. (2011) suggest that family firms represent unique repositories of personal and organizational social capital (Steier, 2001) that are hard to duplicate in non-family firms. Furthermore, family firms demonstrate unusual capabilities of transferring this resource, for example, from incumbent leaders to successors (Steier, 2001) and/or from family social capital to organizational social capital (Arregle et al., 2007). In other words, family represents a unique social grouping wherein strategic advantages residing in a relationship can be passed from one member to another and/or between groups. Family firm owners that aspire to maintain sufficient control of a business to pass it on to the next generation weigh long term consequences differently.

Craig and Moores (2005) suggest that for family businesses to remain successful they must generate a new strategy for every generation that joins the business. Strategies recommended include starting a new venture or division of the business, internationalizing the business, and helping successors acquire skills that other family members do not possess. As a firm evolves, learning and knowledge development strategies must be put in place and these strategies need to be communicated to an increasingly diverse group. As the firm evolves, the strategy and the priorities change and a framework is needed to deal with this ongoing evolution.

## 4 Policy Environment, Financial and Legal Regulations

### 4.1.1 Policy environment

- |   |
|---|
| <p>- <i>Initiatives supporting Family Businesses</i> (e.g. operational policy programmes, financial support mechanisms, mentoring programmes, etc.)</p> |
|---|

The Institutional setting for family businesses has been introduced initially in section 1.5. The policy environment has generally been seen as being supportive of family businesses





although public policies are seldom aimed specifically at family businesses (IFB, 2008). UK national policy emphasis has been placed on addressing a variety of tax issues and the reduction of red tape along with introducing measures to improve access to capital (e.g. Loan Guarantee Scheme, Business Growth Fund etc.). Whilst not specifically recognised by policy, family business, as a substantial segment of the more general SME population as a whole, are frequently the intended beneficiaries of general policies to support business and improve the competitiveness of the UK economy.

A positive economic context and a relatively certain socio-economic and political environment are key aims of UK policy. The BIS (2013) survey asks SMEs about the biggest obstacle facing the development of their businesses. Both family (38%) and non-family firms (37%) are most likely to identify the economy (e.g. reduction in demand, pressure to reduce costs, increased costs of resources) as the main obstacle to the success of the business.

However, a sizeable minority (12%) of both family and non-family firms identify Taxation/VAT/PAYE as the main obstacles to success. Whilst the exact nature of the obstacles are not clear from the survey, a combination of the financial implications of such taxes taking money out of the business and the bureaucracy (time and resources) associated with compiling the tax returns are likely to feature highly.

In the UK SME survey (BIS, 2013), SMEs were asked if they considered a range of regulations including those that were sector specific, tax related or employment related to be an obstacle to business success. 14-18% of all respondents identified at least one of these as an obstacle with little difference between the responses of family and non-family firms. 17% of family businesses identified tax related issues as an obstacle with micro and small businesses far more likely to identify this as an obstacle than medium and large businesses. VAT was most likely to be mentioned by both family (58%) and non-family (51%) businesses. The only area of regulation with a +5% variation was associated with Health and Safety where 26% of family businesses and 20% non-family businesses considered these to be an obstacle to business success.



The BIS (2013) survey explored the awareness and usage of a range of business support services provided by the private sector and the government. These included awareness and use of the publicly funded Growth Improvement Service, My New Business, Business Link, UK Trade and Investment (UKTI) and Mentor SME. Awareness levels were broadly similar between family and non-family businesses ranging from relatively high awareness of Business Link Services (74%) to lower levels of awareness of UKTI (24%) and the Mentor SME service (9%).

Family businesses appear less likely to seek information and advice than non-family businesses. At the time of the survey, 43% of family businesses in comparison with 49% of non-family businesses had sought information or advice in the last twelve months (BIS 2013). There is considerable variation associated with business size, with micro (41%) and small (55%) family businesses less likely to have sought advice than micro and small non-family businesses (45% and 63% respectively).

The survey also provides an insight into the sources of information and advice used by family firms. The private sector feature strongly with Accountants by far the most often cited by family businesses (44%) who were far more likely to seek advice from accountants than non-family businesses (34%). Other sources of advice included consultants/business advisors (15%), Banks (13%) and Business networks/Trade Associations (10%) with little difference apparent between non-family and family SMEs.

## **4.2 Financial and legal regulations**

### **4.2.1 Legal Status of family businesses**

Family businesses in the UK do not have a distinct legal status and derive their legal identity from the generic categories under UK business law – sole trader, partnerships and private or publicly quoted companies. BIS (2011) provide a guide for legal forms of business which include Sole Traders, Partnerships, Limited Liability Partnerships, Public and Private Limited Companies. In 2010, nearly 2 million family businesses (66% of the total) were estimated to be sole traders. Incorporated companies (24%) and partnerships (10%) make



up the remainder. There is a marked difference in the concentration of these different legal forms by business size (Table 4.1).

**Table 4.1 Legal Status of family businesses (p15)**

Type of firm	No employees	Sole Traders	Partnerships	Incorporated Companies	Total
<b>Micro</b>	0	1743905	155987	315228	2215120
	1-9	188831	101885	348128	638843
<b>Small</b>	10-49	23188	32371	35613	91172
<b>Medium</b>	50-249	139	458	12735	13332
<b>Large</b>	>250	0	10	869	879
<b>Total</b>		1956063	290711	712573	2959346
<b>% by legal status</b>		66%	10%	24%	100%

Regulation for the Sole Trader is minimal with no requirement for a formal constitution for the business, and no need to register or file accounts and returns with Companies House. Sole Traders are treated as self-employed for tax purposes and must register with Her Majesties Revenue and Customs (HMRC) and make an annual self-assessment tax return. Profits from the business are treated as personal income subject to income tax and national insurance contributions. The vast majority (89%) of sole traders fall within the BIS definition of a micro firm (0 employees). This compares to 54% and 44% of partnerships and incorporated companies respectively. A higher share of incorporated companies are in the medium and large category and this may reflect the dynamic nature of family businesses which have a tendency to alter their legal structure as they grow.

Some of the key distinctions between these forms of legal structures are outlined by Drake (2009) in a report for the Institute for Family Business.

- Shareholder liability – shareholders in a limited company enjoy limited liability. Partners or members of a limited liability partnership also enjoy limited liability (subject to certain exceptions) while the partners in a general partnership have unlimited liability
- A limited company is taxed on the profits that it makes, whereas partners or members of both a general partnership and an LLP are taxed personally on their



share of the profits. The Shareholders in a limited company are taxed on any dividends or salary they receive.

- Public disclosure both limited companies and LLPs are required to file financial accounts and other information with the Registrar of Companies. Subject to certain exemptions for small businesses the accounts must be audited.

#### 4.2.2 Financial relations

- *Financial relations between the Family and the Business. Financial preparation of the succession process.* (E.g. mixing family and business, family assets as collateral for the business, the share of business in the family wealth, financial planning of the succession etc.)

The financial relations between the family and the business are often complex and uncertain. Disentangling family and business related assets and sharing the liabilities and benefits of success are often contested issues. Succession issues are a constant challenge for family firms and some argue for a focus on the family (rather than the business) for understanding wealth creation and transfer in the family business context Habbershon and Pistriu (2002).

From a regulatory perspective the owner of a family business owns both business and personal property (often in conjunction with other family members or business associates). This makes their estate more complicated in the event of for example death or spousal separation which may threaten the sustainability of the business. One of the major themes in the literature is associated with business transition following the death of an owner (e.g. Gaffney-Rhys and Jones 2013). As a business run by a sole proprietor is not a legal person, business debts belong to the owner just as the business assets do. If there are insufficient business assets to meet the debts, the deceased personal property must be used to pay the creditors. It is the responsibility of the personal representatives to pay the deceased debts before any payments are made to beneficiaries. The sustainability of the business can be threatened as this could mean that personal assets or even the business itself



would need to be sold to satisfy creditors. However the evaluation of family business is often a complex and subjective process. Much of a value of a business resides with the family members and the extent to which they contribute and continue to contribute to the business is often a key issue. Practical complications can arise if the business property, for example vehicles or computer equipment is also used by the owner or family members in a personal capacity. This makes the valuation of assets and the passage of property more complex as ownership can be contested.

A relatively small proportion of family businesses in the UK are partnerships. An ordinary partnership is not a legal person, it is merely a relationship that exists between individuals who run a business in common with a view to profit. Partnership property thus belongs jointly to the partners rather than the firm itself. One partner may allow the firm to use his or her assets but retain ownership to them. Consequently it is not always clear whether property belongs to the partners jointly or to an individual partner and this can cause problems if one of them dies.

Under s33(1) of the Partnership Act 1890, a firm is dissolved on the death of one of the partners unless the partners agree otherwise. The partnership will either be wound up (i.e. the assets are sold, the debts are paid and any remaining funds divided between the partners) or the surviving partners can agree to continue running the firm. It is relatively common for surviving partners to continue to run a firm after one partner has died or more accurately they immediately operate a new business that replaces the dissolved partnership. Indeed, the formal articles of partnership often expressly provide for this. However, members of the deceased's family are not automatically entitled to become partners in the new firm as new partners can only be admitted if all existing partners consent. If the original partnership agreement does not allow a person's family to inherit the role of partner, he or she will need to persuade the partners to agree to a variation. If the partners refuse to do so, the deceased's share will need to be valued (often a complicated matter), paid to his or her estate and distributed in accordance with the deceased will or the will of intestacy.



Another form of legal identity adopted by family firms can help to support the succession process. Limited liability partnerships (LLPs) have been in existence since 2000 and a very small proportion of family businesses adopt this legal form. LLPs have corporate status (see below) and this more closely resemble a company than an ordinary partnership. Like registered companies LLPs have perpetual succession and are therefore unaffected by the death or loss of their members.

A small proportion of family businesses are registered companies. As a company has a separate legal personality, business property belongs to the company itself rather than the members or the directors. Furthermore, a company has perpetual succession which means that it continues even if all the members die. When a member of a company dies, his or her shares will automatically be transferred to the deceased's personal representatives but this does not make the latter a 'member' until he or she is registered as such. If the new member wishes to take an active role in the management of the business he or she will need to be appointed as a director. Such appointments are made by shareholders or the directors depending upon the constitution of the company. Of course a family member who inherits shares in a company might not want to become involved in the management of the company or wish to sell their shareholding. The articles of private limited companies will often provide existing shareholders with pre-emption rights i.e. if one member wished to sell their shares the remaining shareholders are given first refusal. In family run companies, pre-emption rights are important as they can ensure that the business remains in the family after one member has died (Sund and Bjuggren, 2007). To a certain extent, such complications can be avoided if the original member /director discussed future involvement in the company beforehand and drafted a will ensuring that shares are inherited by a family member who would not wish to sell them however research constantly identifies a lack of preparation for succession or transition amongst family businesses.



### 4.2.3 Financial management

- *Financial management, practice of borrowing and indebtedness (avoiding financial risks, features of the financial management, degree of indebtedness, loan-financing etc.)*
- *Source of capital, capital raising non-family resources, sales (extensive use of family resources, practice of “boots-strapping”, prudence toward external capital sourcing, difficulties related with the value-assessment of the family business, etc.*

The concept of SEW (section 2.1.7) is influential in the discourse associated with financial management and attitudes towards a range of policies and practices associated with family business financial risk in the UK. A body of research has emerged associated with aversion to financial risk, reluctance to borrow from external sources and a finance gap that hampers the ability of SMEs to grow.

It is argued that, theoretically, a family firm will prefer to use internal rather than external finance to fund investment projects and working capital and (or) cash flow needs because it is cheaper and carries less risk. Bootstrapping i.e. starting and building a business without external investment would appear to be a common business model for many small and young family firms. Research by Oxford Economics (IFB, 2008) illustrates a reliance upon internal funds, suggesting that family firms hold greater reserves compared to other non-family counterparts. This suggests that they benefitted, on average, from a more cautious approach to debt in the run up to the economic crisis and that they were in a better position to navigate a path through the crisis due to the relative strength of their balance sheet. Corporate insolvency rates rose sharply for both family and non-family firms during the recession but family firms remained less likely to dissolve, possibly reflecting stronger balance sheets prior to recession.

On the one hand family businesses are seen to be oriented more towards longer-term business survival and retention in the hands of the family rather than shorter-term, more profit-oriented objectives of non-family businesses (Harris et al., 1994). This may lead to





turnover growth and profitability being smaller, and the business being less likely to take risks, to diversify its offering etc. These more cautious objectives can lead to reluctance to seek outside funding – for example, from external equity investors or even from debt finance, especially debt with a short term of repayment – compared with non-family businesses. However, the level of leverage tends to increase as the business grows larger; the motivations of newly established businesses and those that remain small are dominated by risk-aversion, but larger businesses require a higher level of debt due to their motivation to retain control and finance growth opportunities (Gonzalez et al., 2013). An ‘empathy gap’ between family objectives and the institutional conditions attached to equity funding has been identified. This means that the financiers cannot understand the businesses, nor adapt their funding offering to take greater account of family business finance preferences (Poutziouris, 2001).

There is a considerable literature associated with attitudes towards and perceptions of various sources of capital for investment in family firms. A key differentiator between family businesses and other firms is the fact that the majority of family businesses view maintaining control over their company as a key success factor, which can make financing options limited. Some family businesses may look to private equity or corporate strategic partners, but such financing options limit or reduce control for the family business owner. In a recent report (KPMG, 2014), the potential of connecting family businesses seeking to grow with High Net Worth Individuals (HNWIs) is explored. The research suggests that nearly half of family businesses (not a representative sample) have previously raised financing from HNWIs suggest that the majority of HNWIs in these instances are close friends or relatives of the family business owners.

In a similar vein, Business Angels have been a feature of the UK landscape supporting SME growth for a number of years. The UK Business Angels Association represents and connects all those involved in the angel investment market, including early stage VC funds, Banks and also non-traditional sources of finance, as well as advisers and intermediaries; policy makers and academics with a view to ensuring a coherent ecosystem for financing



the growth of start-up and early stage businesses (See the UK Business Angels Association for further information).

#### 4.2.4 Tax regime

- *Impacts of the Tax Regime on Family Business Succession* (inheritance tax, example a balance sheet of an “X” firm at the date of transfer (“best example”), tax due on retirement, Law on inheritance tax or fee (levy) etc<sup>1</sup>.

The type of tax paid by family firms will differ according to the category of firm. Family owned sole traders, for example, primarily pay income tax. Corporates on the other hand, primarily pay corporation tax. However income and corporate tax are not the only tax payments family firms make; for example they will also pay employers’ national insurance contributions and business rates. A key policy development in recent years was the introduction of 50% business property relief (BPR) in 1987, increased to 100% in 1992 which exempted the transfer of most business properties from inheritance tax. Since then, government legislation has been broadly supportive of the SME sector where the majority of family firms are concentrated. Table 4.1. shows some of the main measures which have been introduced in recent times to help SMEs. These include the introduction of capital allowances and a research and development (R&D) tax credit, as well as a reduction in the length of time business assets must be held before they are eligible for capital gains tax taper relief to just two years.

Table 4.1. Some government measures to support SMEs

1997 onwards	Capital allowances introduced and subsequently made permanent which allow the cost of capital assets to be written off against taxable profits
1998 onwards	Gradual reduction in the length of time business assets must be held for before they are eligible for capital gains tax taper relief
2000	R&D tax credit introduced, which allows companies to deduct up to 150% of qualifying expenditure of R&D when calculating taxable profits

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2000	Enterprise Management Incentives Scheme, introducing tax-advantaged share options in order to help small firms recruit by offering tax free incentives to employees
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Source: (IFB 2008)

Some of the more negative measures include the rise in the corporation tax rate for small business from 18% to 21% in the 2007 budget although the headline rate for all companies was cut from 30%-28%. Other notable developments have included Entrepreneurship Relief which was introduced as part of the reform of capital gains tax introduced in 2008. It may be claimed by individuals or trustees who sell shares or dispose of whole or part of a business providing certain conditions are met. The relief can reduce the effective rate of tax on lifetime gains of up to £10m from 28% to 10%.

For many family businesses in the UK, issues of family and business wealth are intertwined and come to the surface when faced with transition. Anecdotal evidence suggests that minimising tax liabilities often feature highly on the list of important issues for family businesses. Although it is beyond the scope of this paper to discuss liability for tax in detail, a brief explanation is required as it is a crucial element of inheritance planning. Inheritance tax of 40% will be payable on the value of the deceased's estate that exceeds £325,000 (the nil rate band). If the assets of the business owner are currently more than the nil rate band, the individual in question will probably consider how liability for inheritance tax will be kept to a minimum. Key points to note include the fact that property passing to the deceased's spouse or civil partner and bequests to charity are exempt from inheritance tax. Business owners should also be aware that some forms of business property are exempt and the proprietor of a business can reduce liability by making lifetime gifts. It is thus seen to be essential to seek financial as well as legal advice when considering succession in order to make the most of exemptions, allowances and reductions that are available and whilst many family business owner managers to do this, many do not.

For many family businesses, the connected nature of personal and business wealth makes making a will a critical feature of personal and business forward planning. Research



suggests that about one third of adults in the UK have made a will although the research provides no indication as to whether business owners were more or less likely to write a will than other members of society (Brooker, 2007). In a relatively small-scale survey of small businesses in South Wales (n=250), Gaffney-Rhys and Jones (2013) report that that almost half the respondents had made a will, significantly higher than the average among the general population. They suggest that one possible reason for the higher propensity to make a will is that business owners are in contact with professional advisors who inform them of the need or desirability to make a will. Gaffney-Rhys and Jones found that company directors were more likely to have made a will than partners or sole traders which seems to be linked to the level of formality required to operate each business form and the fact that the company directors participating in the study were more likely to have a regular solicitor or accountant. The reasons given by business owners for not having made a will are often consistent with those cited in national surveys and included apathy and being too young to think about death.



## 5 Concluding Remarks

The contribution of family firms to the UK economy is substantial on any measure or definition adopted. However there are concerns that the economic contribution of family firms may be constrained by a number of factors. First, family businesses are smaller on average than non-family businesses and a large majority are very small (no employees). Employment and sales growth tends to be lower and less frequent and the slightly lower average size of family businesses and this may imply that their contribution to growth is somewhat lower than their proportion of all SMEs might suggest. The sectoral distribution is another factor with family firms prevalent on a variety of lower value adding sectors including hospitality and retail that reflects lower contributions to economic prosperity. One of the areas that is contested is the relative economic performance of family and non-family firms and the balance of success when measured against economic and non-economic goals.

A defining feature of family business is the intersection of family and business values, objectives and relationships. Some family members may take an active role in the leadership and management of the business whilst others may not. Some may professionalise and welcome external advice and guidance whilst others may not. Some may wish to grow rapidly and internationalise and others not. Some choose to formalise the legal entity of the business whilst the majority do not. Some may have tight family ownership and management structures whilst others do not. However it would be misleading to present these as dichotomous relationships as they are more useful as dynamic continuum where a myriad of other options may be pursued and outcomes achieved. There is a substantial heterogeneity associated with the family business population that can be neglected and marginalised in discourse.

Where there is some consistency in the family businesses literature in the UK is in the finding that family businesses often resist or are not open to succession planning. This can be found in first-generation family firms as well as subsequent generations. The literature also suggests that strategic behaviour is an important factor in the survival and



growth of family businesses. It can be used to help reconcile family and business issues and to provide a foundation for further development of the business. Understanding the varied areas in which they operate the complex nature of what they do and the rich mix of different types of family business can inform succession strategy . The evidence suggests that different approaches are needed to address different generations' need for succession planning. It also suggests the need to view succession as a long-term, multiple stakeholder process with the navigation of various social, economic and psychological factors a key to success. Whilst there are 'good practice guidelines' available, the variation and complexity of succession in practice should not be underestimated. Despite a considerable body of research exploring strategy and succession planning in the family business context there would appear to be a lot to learn about the processes that different family businesses adopt to transform their enterprises strategically as they grow, professionalize, and introduce external capital and non-family managers. But do all family businesses want to grow or professionalise? Do they want to change their financial foundations as many policy makers and intermediaries would like to encourage them to do?

Financial relations between the family and the business are often complex and uncertain. The multi-dimensional concept of socio-emotional wealth has become an influential concept in the study of family businesses. On the one hand this view is seen to constrain the growth of family businesses whilst on the other it is seen to contribute to their resilience and sustainability. More recent work has emphasised a broader pathway to succession in terms of various forms of business transfer. An issue that features highly on the agenda of many family businesses facing succession is that of inheritance and the tax implications of this. For many family businesses the connected nature of personal and business wealth makes personal and business forward planning essential but like succession planning more generally, only a minority of people in the UK do so.

Much of the policy analysis is based on distinctions between family and non-family firms without recognising the differences that exist among family firms. Although both areas are important, there is evidence that the variations in behaviour and performance among



family firms may be as large as, if not larger than the variations between family and non-family forms of organisation and a more nuanced understanding is required to reflect the socio-cultural context at the micro level of the firm. Normative approaches, which tend to emphasize the need for structure and to systematise, bear little resemblance to the practice of business adopted in many of the smallest micro enterprises in the economy and new, innovative ways of intervention are required to engage family businesses in succession planning.

The policy infrastructure in the UK is generally viewed in a broadly positive light by those representing the interests of family businesses although there are constant calls for changes to the regulatory environment to promote greater competitiveness and/or a fairer society. This wide ranging review provides a basis to move towards the consideration of the policy implications at the national and European levels in the next stage of the INSIST Project.





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Appendix 1 (Nicholson and Bjornberg, 2007; p84-92):

**1. Ties between next generation members and the firm**

- Manage the boundaries between people who own but who do not work in the business, those who do both, those who do neither, and those who work in the business but do not own. All have a legitimate interest in what goes on in the firm and this needs to be recognised in how they are communicated with, and how family and business decisions are made.
- Create opportunities for education, insight and experience in the family firm, however avoid pushing too much information onto the next generation. Study visits, summer jobs and gatherings can all help to generate a spirit of personal responsibility, choice and attachment.
- Make selective use of mentoring and coaching. Different kinds of support are needed for next generation members in our four categories of association. It is especially important to help individuals manage relationships within the family across the divide between the ownership and those members working in the business, and in relation to non-family employees in the business.
- Conduct an active inquiry about the interests of family members who seem emotionally disengaged. There may be good and acceptable reasons for this. On the other hand there may be feelings of rejection, alienation, disenchantment and grievance that need to be addressed.
- Develop clear expectations about who is to be included in which processes. This decision is best handled in a consultative manner, rather than top down.
- Find ways to involve non-working owners and other family. This should not be just a palliative for the sake of appearances, but because their input is needed for culture building within and around the firm.
- Beware of the elaborate family governance system that fails to deliver. Consult widely to get agenda items for family meetings that have real substance and importance for family members.



- Individuals need to learn with what it means to be an owner, who has a right to be informed but who does not to have the right to intervene in business decisions. Responsible ownership means awareness and respect for these boundaries.
- Recognise the importance of feeling involved. Raising emotional ownership can bring unexpected benefits in terms of next generation contribution. Ensure that the governance structure enshrines a clear boundary between family and business issues. Do not expect the governance institutions to solve emotional problems. They may require separate family counselling.
- Support next generation members in their personal development needs. This could involve career planning, coaching and mentoring. Raise the skills and competence of the next generation – engaging them in projects that help them stretch and grow.
- Establish clear hiring and promotion policies. Back these policies with clear communications, directed to both the next generation and to existing employees, so that the merit of individual cases is transparent. If the company recognises the value of family leadership, then that should also be communicated to the rest of the firm.
- Build support groups. Next generation members can get a lot out of building their own support groups. This can be applied internally in the business and externally through professional networks and other groups.
- Make a decision about what kind of family firm you wish to be. Develop a strategy for involvement and introduction that is consistent with the model. This needs to be revisited periodically as the firm and family move through phases of growth.
- Consider the timing of involvement. A staged approach can be recommended from informal socialisation through to points of transition, when more formal invitations and opportunities for involvement are offered to the next generation. An ad hoc approach carries dangers of inequity and ambiguity.
- Entrepreneurial spin-offs from the main business can be a vehicle for learning and involvement. A family can form its own mini-venture capital fund for next generation incubator projects. This requires a serious investment in raising the business knowledge of the next generation.



## 2. Family Relationships

- Succession planning should take place early, against all eventualities. Family members want clarity about process more than certainty about outcomes.
- The process should also include bottom-up exploration. Research should be made into the needs and emerging capabilities of the next generation.
- Doubts of the seniors need to be openly addressed. The senior generation often have misgivings about the competence of the next generation. There is also the fear of exposure that the seniors face with succession and the impact on their lives.
- Some competition within and between the generations can be healthy. It should be handled openly and sensitively. Take care to distinguish constructive rivalry from destructive envy.
- Emotional guidance and coaching needs to be on hand for next generation members. Such support particularly helps during ownership and management transitions.
- Senior generations should strive to be good role models for the next generation. This includes an appreciation of work–life balance issues and a demonstrable ability to delegate.
- To create trust think teamwork, and do the things that foster team-building. The following strategies can help: setting shared goals, consensual division of responsibilities, open communications, avoiding personality clashes, and celebrating successes.
- Discuss values and style. Everyone needs a coherent idea about what it means for them to be a business family.
- Break down traditional gender roles – consider part-time work, flexible hours, child care arrangements – gear both male and females in preparation for joining/owning the firm.
- No matter how difficult a family member may be it is important to keep lines of communication open



### 3. Decision making style and process

- Read the situation and adjust the norms of authority accordingly. In particular consider that high-profile leadership may have one effect on the business and quite another on up and coming family members. You don't have to use one style in all circumstances.
- Delegation has to be practised and carried out methodically. It is more than just allocating tasks – there has to be explicit agreement about responsibility, resources and accountability, as well as what monitoring and support will be given.
- Empowerment means raising the capability of junior people – a mixture of coaching and delegation against a background of trust.
- Enhanced interpersonal skills are needed on all sides. The next generation needs to learn how to influence and communicate with the senior generation as much as vice versa.
- Raise awareness of justice issues, and the importance of both types – procedural and distributive.
- Accountability and transparency need to go hand in hand. This applies especially when it comes to decisions that affect people's lives, welfare and futures.
- High involvement strategies often forestall controversies over fairness. The next generation need to have a sense of co-ownership of the governance systems that apply to them.
- Meetings need to be well conducted with good active listening. A climate of open debate needs to be created where issues of justice can be raised without fear.
- Clarity and transparency about how ownership will be transferred between generations is a critical issue. Shareholder agreements often do not capture enough of the key concerns of the next generation.
- The vision and values do need to be discussed and if possible written down. These should not be empty and vague statements or slogans, but ideas that really define what is unique in the family firm and what it stands for.
- The next generation need to be actively involved and encouraged to take initiatives. Activities can include the running of family assemblies, setting up special next



generation interest groups, editing newsletters, helping to codify and write the family business history, acting as ambassadors in the community, playing a role in formulation of social responsibility or philanthropic initiatives, and helping to oversee the family office, if there is one.



## Appendix 2

How can family businesses make themselves attractive to HNWI investors? (KPMG 2014)




1. Keep it personal. HNWIs value the personal touch in family business investments. While more formal procedures and arrangements may be necessary, family business managers would do well to maintain regular personal contact with HNWIs and foster good relationships with them.
2. Consider offering a board seat. HNWIs are highly attracted to the idea of having board-level involvement in family businesses as this gives them a degree of influence on how the company is managed. For family businesses, this can formalize and define the scope of the HNWI's involvement, helping to manage the concerns around interference highlighted particularly by non-family executives.
3. Ensure some level of formal governance structures are in place. The potential for conflict or drama between family members is the main deterrent for HNWIs investing in family businesses. With the right, formalized corporate governance structures, such as a professional and independent board of directors and clear lines of control, family businesses can allay these concerns.
4. Demonstrate that the business welcomes outside input. Many family businesses value the perspective and experience outside investors can bring – and HNWIs are very well placed to offer these, given their experience of family businesses. Recognize the benefits in addition to capital that HNWIs can bring.
5. Highlight the tangible benefits of investing in your business. When it comes to making an investment, HNWIs prioritize tangible business factors, such as being managed for the long term, good profitability and strong opportunities for organic growth – these are positive attributes that need to be emphasized when seeking HNWI investment.
6. Recognize the long-term horizons common to most HNWIs. Like the perspective of most family businesses, HNWIs take a long-term view with their direct investments. Spend time outlining what your long-term plans are and how you plan to develop the business. HNWIs will also appreciate the personal investment and stake that



family members have in the business – its importance to the family offers HNWIs a degree of comfort when investing.

7. Spend time building and widening networks. Most HNWIs have experience of running or being involved with their own family businesses and are likely to be part of family business networks. With better networks and connections, family businesses will increase their chances of finding the right partner for their company.

Have an open dialogue with HNWIs. Many family businesses would consider offering equity in return for HNWI investment, but prefer to retain control. HNWIs often seek to realize a controlling interest. Nevertheless, mechanisms can be designed for both parties to get more of what they want, such as the ability to intervene and contribute without antagonizing the family business's prized strategic independence.

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