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Chapter 3

Discussion Report Part 1: Legal and Managerial Foundations

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Holger Fleischer: Family Companies and Family Constitutions: Historical and Comparative Perspectives

Stefan Prigge/Katharina J. Mengers: Family Firms and Family Constitution – A Management Perspective

A managerial scholar and practitioner took up Fleischer's analogy of onion layers. He agreed that it fits well into the present context. In his view, family governance could be understood as a security architecture for proper management with different layers (elements) of security, e.g., shareholder agreements and the family constitution. A managerial scholar raised the question of whether all security elements were necessary or partly redundant. Fleischer replied that from a legal perspective redundancy was not that relevant. As long as no negative consequences occurred even partial redundancy would not be a problem. A larger problem in legal practice was no or weak consistency and coordination between different documents. The managerial scholar and practitioner continued that contracts regulated deficiencies, whereas family constitutions could act as a positive codification of shared goals and rules of behavior. The difficulty of family constitutions was the missing binding force.

Prigge, returning to the redundancy topic, stated that the family constitution as part of the security system could also have a positive effect on performance. Thus, it might be better to have more security elements in place, although they are partly redundant because mitigating turbulence might be a positive performance effect. A legal consultant added that the family constitution could increase performance. That was his key take away from another event he had

Family Firms and Family Constitution, 57–59



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attended. For example, board diversity which was often defined or recommended in the family constitution could lead to better performance. Prigge wanted to include the results of academic research on the performance effect of family constitutions and asked Graves about his experience in this context based on the results of his study. Graves explained that their study only considered whether there was a family constitution present, but they had no further details on the content of the constitutions. Thus, for future studies, a governance index would be better rather than a 0/1 variable for the existence of a family constitution. The document was only one governance mechanism among many others, its substance and the process of how the document was put together could be very different and should be considered as well. A managerial researcher and consultant added that a governance index or models, such as the model Prigge presented in his talk, were important for research and discussions because so far it was still difficult to define family governance and its elements. There existed a heterogeneity of terms, e.g., family constitution, protocol, plan, or charta. The same applied to other elements of family governance, such as family meetings, family academies, etc. There was a variety of terms which were not equally used and understood worldwide.

Next, the discussion focused on the role of consultants and the question of whether extant family constitutions were very much alike or rather heterogeneous. Fleischer initiated this discussion when he asked the managerial researcher and consultant whether family constitutions were diverging over time. She answered that this was, according to her impression, actually the case, but mainly due to the variety of terms and their understanding. Fleischer added that in the legal field, they observed that the documents became more and more similar due to consultants. A managerial scholar and practitioner confirmed that this development could also be observed in the field of family constitutions. He reported that there were five large consultants for family governance in Germany. Each family thought they had their own document, but in the end, he could recognize from the wording of the constitution document, who had been the moderating consultant. He was only aware of two families who had set up a constitution without any consultant.

Another managerial scholar reported from her experience that consultants were helpful to establish the first version of the constitution. But what happened afterwards? Was the family really using the constitution? She underlined that this was also an important question, as the usage of the constitution took place without consultants. A further managerial researcher added that the discussion of the consultants' role was important. He talked about his experience in Australia. He knew that consultants sometimes sold family constitutions without a real need for it on the side of the buying family. Put differently, a lot of good reasons for family constitutions existed, but these reasons could not be observed at every family with a constitution. The managerial scholar and practitioner added a reconciling view to this. From his point of view, this could be interpreted in a way that families were concerned about being responsible business owners and thus they tended to follow researchers and consultants, who suggested family constitutions as a tool for responsible ownership.

A legal consultant stated that in his opinion, a family constitution had to be a living document; otherwise, it was not good to have it because the environment and the family changed. A managerial researcher, referring to her own experience, supported the “living document” argument. Moreover, she added, that it was important to manage expectations, conflicts, and discussions, which could get emotional. Therefore, she thought that it was important to have a moderator, whether this was a consultant or a lawyer or someone else.

Fleischer then asked the plenum whether it made sense having a standardization of documents at this developmental stage. A legal consultant replied that basic ideas could be put in a “one size fits all” document, but that the rest had to be individual. The managerial researcher with a family-firm background on her own agreed. A certain general structure could be helpful at the beginning, but based on this there had to be an individualization. A managerial scholar introduced the family structure into the discussion. If a family was complex, not only in size, the need for a family constitution was high. But small firms might not be able to pay expensive consultants. Thus, a standardization with basic guidelines might be helpful for those families, as it could make the whole process less expensive. Referring to the complexity of the family structure, another managerial researcher added that communication was important in this context and that the communication was often perceived as good among older generations, while the young and subsequent generations perceived the communication as weak. Therefore, from his point of view, the power of a family constitution lay in the process, not in the results. The results were good to have, but the process was more important. One could not assess a family’s complexity before talking to the family; one measure of complexity might be the frequency of conflicts.

A managerial researcher and consultant agreed on the importance of the process. She added that the justice perspective was also relevant. Who was involved in the decision to establish a family constitution and also in the development of the constitution? This needed to be transparent and fair. A legal consultant also agreed on the importance of the process compared to the documents in the end. Concerning the adoption of standard documents, he saw two potential dangers: First, there was the danger of conflicts with other documents and contracts. Second, there was the danger of not running through the whole process, which was, as we just heard in this very discussion, really important. There was a large heterogeneity among family businesses and, thus, family constitutions had to be individual as well. The importance of the process in general also raised the question of whether documentation of the process would be necessary in the future.