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SUCCESSION IN FAMILY BUSINESSES

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Instituto Brasileiro de Governança Corporativa

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Preface

We have reached a new age in relation to family businesses and business families, which is profoundly transforming the succession context in family businesses.

The business environment has dramatically changed since the late 20th century. Increasingly faster technological evolvements, in addition to a growing globalization, have been transforming the way business are made. These factors, along with changes in the consumer's preferences and power, are causing industries to change, to ripen and to disappear way faster than before. Under these circumstances, companies must innovate on a continuous basis, act in a disruptive way and amplify diversification, in order to stay alive.

Also, the society is also going through dramatic changes: greater diversity, digital connection and transparency, greater inequality, outdated infrastructure, polarization and political deadlocks, just to name a few. Social tensions are deeper in several countries. In a moment when the benefits of international cooperation have never been so obvious, some governments (including mine) are weakening the main international bodies.

I think back in the time when citizens would expect their governments to handle society's tensions and reduce social convulsion; yet, nowadays, certain governments have the creation of fissures in society as a goal. The Millenials (Gen Y), born 1984 to 2000, are increasingly gaining relevance in society, changing the way of conducting business, caring for the world, and our lifestyles. They have new expectations of flexibility at work and fast career progression in organizations. At the same time, an increasingly number of older individuals (baby boomers), with life expectancies greater than ever, is not leaving the work environment or leadership positions in bulks. I hope that the Gen X fix it.

Nonetheless, the modern business family is being redesigned. The family is becoming increasingly diverse in multiple ways, most geographically spread, even internationally dispersed, more equalitarian and, as of recently, less committed to the family business. Now, many business families are concerned with the life goals of the newer generations, which may not be conciliated to careers within their companies.

In addition, society and companies need to handle periodical and widespread disruptions, such as the tragic COVID-19 pandemic, which is happening while I wrote this piece. It is common to borrow the military terminology known as VUCA (Volatile, Uncertain, Complex and Ambiguous) to describe today's environment. The current environment is all of it and has changed the way we handle succession in family business. How?

The future is increasingly foggy. For families, future is more uncertain and ambiguous than it used to be. Companies now work in a less predictable environment that is in constant change, in which good talents, market knowledge, agility, and constant innovation are requisites to stay as a relevant competitor–and all that is expensive and demands restructuring in many organizations. Add to these factors the fact that abrupt process or product transformations can cause your business model, which used to work, to become extinct in a short time. For many companies, it is not clear (nor should it be) whether they will be able to remain relevant in their current industry in eight, five or even three years from today. Leaders of family companies need to consider: will we still be in this same business when we make the next generation succession? What kind of business am I preparing my successor to lead?

For successors, this fogginess means that the standard path to achieving leadership positions, working to climb the corporate ladder of the family business, can be a dead end. The Generation X successors are dealing with this right now. The rising millennial generation is far more interested in the world of entrepreneurship and less interested than past generations in joining the traditional family business. In research conducted by the Cambridge Institute for Family Enterprise, a quarter of millennials in the business families said they hope to become entrepreneurs. The once revered path of climbing the corporate ladder within the family business and eventually inheriting it is now less attractive to young family members. Given this context, how does a family business attract successor candidates to lead the business?

Finally, the expectations of the generations are misaligned. The assumptions of older and younger generations about when succession should occur are increasingly misaligned. Current leaders are taking advantage of longer careers and life expectations. As a result, in most cases, they are delaying their retirements. At the same time, younger generations (X and Y) want to assume leadership positions at younger ages than we saw before. Where before there was a convenient overlap between one's willingness to leave the leadership position and the other's readiness to assume it, now there is a huge misalignment between expectations, which generates frustration and tension within the family and business. In this scenario, how will family businesses retain the younger generations and keep them motivated?

* * *

This dynamic context is no surprise to those who look out and pay attention. Succession will be different than it was with the last generation, but it can still be planned and managed.

There are several ways to rethink succession today:

Develop a different kind of successor. Given the growing uncertainty in various sectors of the economy, family business leaders need to assess and develop their successors' readiness for the future, focusing less on operational qualifications and more on the ability to make important strategic decisions such as:

- What is happening in our industry and how do we need to reinvent ourselves to stay competitive?
- How must we diversity in order to grow and manage risk?
- What kind of corporate culture will help us be innovative?
- What kind of talent do we need to compete in the new economy?
- What kind of governance and ownership structure will allow us to be agile enough to make the next bold move?
- How must I grow to become an effective leader?

Nowadays, it is less useful (but not irrelevant) for company leaders to be premium operators of a specific business, because it may have ended or had its value reduced in a few years. Instead, leaders should think about being more like shareholders, looking beyond operational concerns to consider where to make their "bets" with capital, people, and time. If you're not looking for a successor who is able to act as an active shareholder, you're not looking for the right profile.

Recognize that entrepreneurship is not everything. Younger generations have a growing appetite to build startups. New ventures are a relevant part of our business ecosystem and a source of much innovation. Entrepreneurship is a valuable activity and can help prepare the next generation by teaching them the value of market perspective, how to innovate, escalate business, finance growth, and build good teams. However, for the next generation in a business family, becoming an entrepreneur is not necessarily being prepared to lead or be a shareholder in the family business. Successors need to prepare themselves more broadly to be strategic shareholders, wealth creators, family unifying agents, and also wise business architects. Knowing how to build on the success of others is as important a skill as knowing how to start something new.

Be realistic about the succession timing. The transition needs to occur when you are sure that the company's momentum is strong. Otherwise, the system will either stagnate or go into a tailspin. Today, a company cannot afford to waste this time. It is not easy to recover in a highly dynamic world. More fundamentally, it means starting a change in leadership when the next generation is ready to lead (which is more than just wanting to lead), not only when the current leader is ready to leave the job. Nowadays, CEOs need to be prepared to leave their jobs while they are still effective, even when they are at the top of their skills, their companies momentum demands it. This individual sacrifice is critical to the company's long-term strength and momentum. If you are not prepared to leave your position before your peak and give space to the next leader, you are not aware of the reality of succession in today's world.

* * *

Succession planning and management, along with contemporary challenges to do it successfully, are vital topics for the modern business family. I congratulate the Brazilian Institute of Corporate Governance not only for its leadership with this valuable book, but also for its broader mission of supporting companies in improving and professionalizing their governance.

We live in turbulent times. This is the new normal. Over 31 years, while my colleagues and I have assisted business families with their successions at Cambridge Family Enterprise Group, I have learned that in such times realistic perspective, real planning, and effective succession management are more important than ever.

Profesor John A. Davis
M.I.T. Sloan School of Management
and Cambridge Family Enterprise Group
Cambridge, Massachusetts
2020

Introduction

The succession process rite is one of the greatest challenges for the governance of family businesses. Aware of this, IBGC created this publication with the intention of synthesizing the main aspects involved and sharing some of the best practices adopted by organizations that underwent the succession process. This publication intends to approach the main variables involved in the process, as a guiding tool for all members of family businesses and for the leaders of these businesses. After all, each case is unique and requires specific paths.

In many family companies ✪, the mere mention of the word succession can generate uncomfortable reactions, mainly for being associated to delicate aspects, such as transference of wealth and power, as well as mortality. Therefore, debating this topic is usually taboo among family members. Apprehension, taboos or even fear can feed uncertainties and conflicts, often silent, that hinder the planning of the future, both for family members and the company.

✪ Organizations where two or more extended family members influence the direction of the business through the exercise of kinship ties, management roles, or ownnership rights. R. Tagiuri and J. Davis, "Bivalent Attributes of the Family Firm". *Family Business Review*, vol. 9, n. 2, pp. 199-208.

Due to the importance and complexity it represents for the longevity of a family business, succession must be seen as a strategic process that requires professionalism, foresight, commitment, and individual and collective zeal. It is not an isolated event in the business trajectory, which can be solved circumstantially, but an intergenerational process guided by a long-term vision that will help make the transition from the current moment to a settled medium and long-term future.

This publication addresses succession in the three dimensions that make up the business family ✪ –ownership, family, and business–presenting the technical and socioemotional aspects ⊙ that are determinant in each of them and in their intersections. The purpose of the work, however, is not to give specific directions, but to offer an analytical and reflective framework.

✪ Understood as all family members who are or can become partners and their aggregates.

With this work, IBGC hopes to contribute with information that helps families and business family leaders to discuss in succession in a transparent and harmonious way, so that these organizations and their partners, family or not, can find their own way and continue to evolve, innovating and generating value for society.

⊙ Socioemotional aspects refer to individual perceptions and feelings, different aspirations, different needs for power, influence, and leadership, different ways of facing the world, the business and interpersonal relationships etc. These perceptions and feelings are peculiar to each individual and largely influenced by the prevailing social, cultural, and economic context. When placed within the collective of the business family members, they require broad attention to generate alignment on key issues and support in addressing other aspects.

1

Succession – What Are Talking About?

1.1 Concept

Succession in the business family system is a process of transition: (1) in the family's leadership; (2) in the exercise of ownership; and (3) in the management of the business from one generation to the next generation of professionals, whether they are family members or not. This process happens not necessarily concomitantly in these three dimensions and may, in some cases, involve the transition from one generation to another or within the same family generation, and also rely on the presence of non-family members, when it occurs in management or in the ownership.

It is a complex and important rite through which an entrepreneurial family passes throughout each generation. A delicate task that must be conducted with wisdom, empathy, and long-term vision, sustained by a greater desire to pass on, in the future, a legacy better than that received from the previous generation or, in the case of succession of the founder, to contribute to the creation of a robust and long-lasting legacy, in the search for the best conditions for business management and family alignment.

Few family organizations go further than the second generation and an even smaller portion can survive the third generation or subsequent ones. Some of the reasons for this difficulty in the generational transition are usually linked to the non-alignment of partners on essential business issues and their strategy, power disputes, immediate needs for liquidity and reinvestment in the business, absence of qualified leaders, absence of rules and formal agreements, among others.

The subject of succession involves a range of complexities, risks, and opportunities, such as: lack of time to simultaneously make strategic and succession changes, the existence of fruitless internal debates with no focus on the company's competitiveness, and the whole range of conflicts that can make it difficult to focus on the business and the greater collective good. On the other hand, the change in command is a great opportunity to build a new pact and a new alignment regarding the future and its requirements for innovation and value creation.

Careful planning contributes to the succession process's success and must take into account the preparation of family members to play their main role: that of partners and members of a business family. It is through the exercise of these roles that family members honor the legacy and heritage they have created or received.

Since succession brings a clear idea of a passing of the baton, there is a mixture of concrete aspects (choice of the best successor and retirement of members of the previous generation) and emotional aspects (fears, yearnings and insecurities) that cannot be discarded and are not easily approached in a rational way.

Therefore, socioemotional issues are the most difficult to address. Without due care, they can contaminate the health of the business as well as the relationship between family members, and cause difficulties to attract or retain good professionals, among other issues.

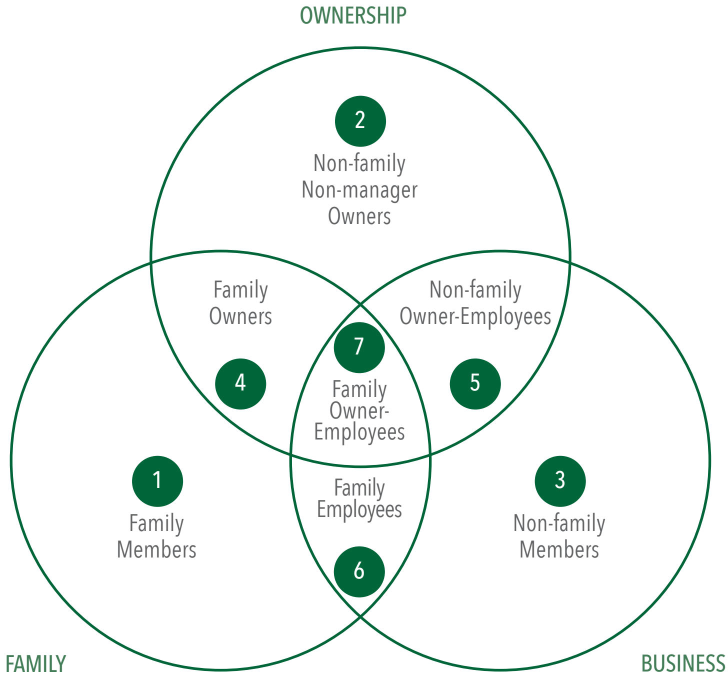
Emphasizing only technical aspects of the process–such as legal, fiscal, financial, and operational issues in the transition–hoping that reason prevails over emotion can be a trap in which many family businesses end up falling. Taking care of the socioemotional elements of the succession, which include relationships among the members of the owner family, cultural characteristics, beliefs and customs, individual desires, and the dilemma of the passage of the baton from those in power is essential not only during the process, but also after the implementation of the agreed-upon change.

Business families who share purpose and values in the family and business sphere are better prepared both for succession and for any adversities along the way, as they aspire to something greater and collective, which reinforces aspects of cohesion and alignment around the essence of the business.

1.2 The Succession Journey

Most of the time, succession happens in the intersection between generations, during necessary changes in the family's or the business's leadership, as well as the transferal of ownership (which, like we already mentioned, don't necessarily come at the same time). The Three-Circle Model, created by John Davis and Renato Tagiuri, helps see the family business as a system made up of three sets (family, ownership, and management) which, in practice, constitute the context in which succession happens.

Figure 1. The Three-Circle Model

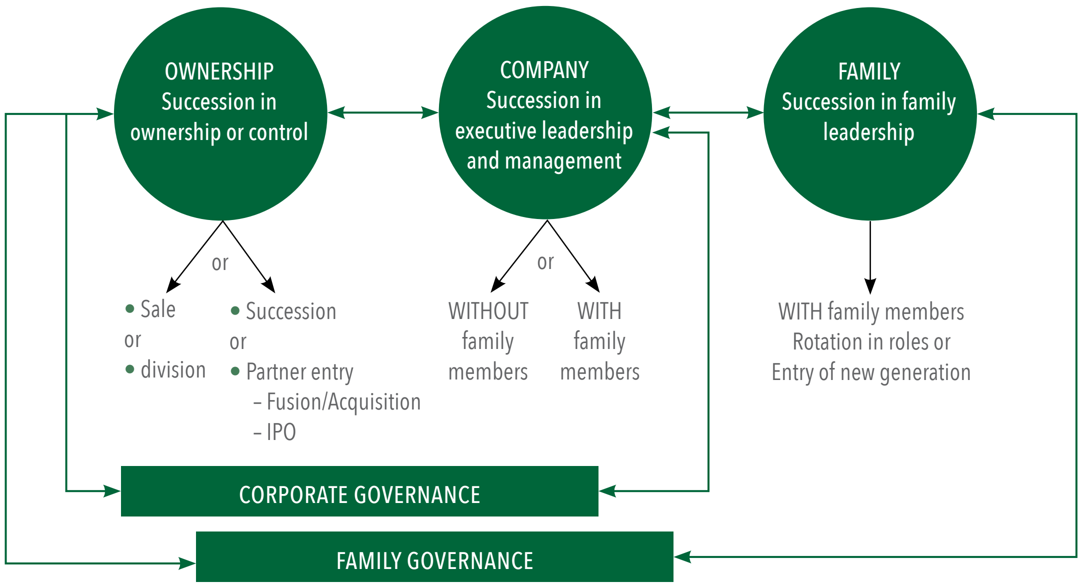


Davis, J. A. and Tagiuri, R. "The Influence of Life Stage on Father-Son Work Relationships in Family Companies." *Family Business Review* (Spring 1989).

In this work, when we talk about succession in the family business, our proposal is to think upon the challenges involved and the possible alternatives in each of the following dimensions:

- **Succession in the family –** It is the transition process in the family, most of the time influenced by the life cycle of its members. It involves learning new roles, readjusting the family system, especially for those who will emerge as a new generation of leaders and who actively exert influence, even within the family context, giving rhythm to the transition process. It also involves, in companies with more advanced governance, the appointment of new representatives to governance bodies, such as the family council.
- **Succession in ownership –** It is the (partial or total) transferal of asset control for the next generation and other heirs. Influenced by the current legislations, in particular applicable tax regimes, and by traditions, the process transforms power relations among family members..
- **Succession in management –** It consists in the transition of people at the top of the business. It is marked by the choice of a new leader (family member or not) to lead the company, preside it or be on the board of directors.

Figure 2. Key events in the succession process



Brazilian Institute of Corporate Governance (IBGC), *Governança da Família Empresária: Conceitos Básicos, Desafios e Recomendações*. IBGC: São Paulo, 2016, p. 29 (Cadernos de Governança Corporativa, n. 15, series). Available at: <https://conhecimento.ibgc.org.br/Paginas/Publicacao.aspx?PubId=22057>. Accessed on: October 9th, 2019.

Planning succession taking into account these dimensions helps to segregate the interests, rights, and obligations of those involved; to predict how possible changes will affect the family, management, and ownership; to develop strategies to deal with these issues; and to prepare those who will be succeeded, those who will succeed, and other groups involved. This process will require, among other measures:

- Defining, rethinking or implementing the rules established in the partners agreement and the ownership structure.
- Defining and respecting corporate and family governance structures.
- Nourishing family values and a culture of entrepreneurship.
- Preparing the next generation members for their main role as partners.
- Preparing family members to play the roles defined by family and corporate governance.
- Attracting the best talents to compose the leadership board in the company.
- Ensuring legitimacy to executive successor from family members and the owners.

Retreats may be necessary, since not everything works as expected and new subjects may emerge throughout the process. Such movements, however, need to be meticulously communicated in order not to generate discredit or future resistance. It is important that family members are aware of the desires and proposals that the one who will be succeeded intends to implement.

The fear of addressing socioemotional aspects and answering difficult questions (such as the examples highlighted in the following chart) may bring the senior generation leader to postpone the succession process fearing conflicts, possible ruptures or the economic impact on the business.

Box 1 – Some difficult issues that need to be addressed

- What impacts will the choice of an heir or external professional to lead the business have in the family's relationships?
- How will the family member who will be succeeded react? What about those who aspired to be successors and weren't chosen?
- What consequences will the total or partial transmission of assets bring to the family?
- What liquidity needs have to be addressed?
- What investments will be needed to develop the new generations so they can have a role in the governance system of the family or the business?
- What importance can personal and professional development have in order to be independent from the business?

Experience shows the agility in bringing these and other issues to the table without delay is the process's biggest ally, since addressing all of them requires dialogue, maturity, and time.

1.3 Succession in Different Contexts

The different ranges of subjective and emotional issues of the family, the legal and tax aspects and strategic decisions for the business make the dynamics unique in each case. This applies not only to the different types of relationships cultivated in each family and the various ownership structures, but also, in a very special way, in each of the company's life cycle.

The succession from the first to the second generation is always very important, because it represents, in most cases, the first transferal of power in the organization. The departure from the scene of the entrepreneurial figure who created the business and often printed his personal brand in everything that involves the company is never an easy change. However, other types of succession (such as from a generation of siblings to a generation of cousins) can be as challenging and complex as that of the founder to his or her children, because it involves a greater number of people, with a wider diversity of views about the business, interests, and expectations.

Equally complex is the succession in multi-family societies, usually founded and led by entrepreneurs who are either friends or come from different family nuclei. It is common in this context for some heirs or successors to ask themselves:

- I didn't choose these partners or this business. Do I have enough interests and affinities to go on with the partnership?
- What connection and affinity do I have with this business purpose? Are there strategic choices for innovation or differentiation?
- Does staying together as partners add or destroy value for the business?
- Do we have a conjunct interest (whether partial or total) in reinventing this business?

Answer to these and other questions may generate alternatives for alignment, management professionalization or even generate liquidity options (like partial dilution or total sale of business shares).

Another factor that greatly influences the succession process is the company's financial health at the time of succession. Making the transition in an economically healthy organization which distributes results is completely different than conducting the same process in a business whose competitivity and financial health are affected. The pressure for short-term results might contaminate the family environment and amplify the natural obstacles and resistances to be expected in this type of transition.

Unexpected events are another worry that reinforces the need to define a strategy and the succession planning. For various reasons, the administrator can be unable to run the company–for instance, passing away prematurely–and this will precipitate the succession. In these cases, a well-defined plan ensures that the family business won't go into a leadership crisis. The following box identifies some of the aspects that need to be analyzed and agreed upon.

Box 2 – Points for Attention

- When to start? What is the senior generation's challenge and role? Is some level of rupture necessary for an effective succession?
- When to prioritize the company and when to prioritize the family?
- What are the most important criteria to identify successors for leadership in the business and the family?
- What is the bare minimum in family and corporate governance to fulfill a succession process?
- What can we do when there isn't room for all family members who want to occupy executive or leadership positions?
- How can we enforce meritocracy in the choice between family members or professionals for executive or board positions.
- How can we give feedback to a family member about their performance in a relevant position within the company?
- How can we avoid that the leader's values and paradigms keep the new generation from adopting innovative ideas?
- How can we equate conflicts between professional vocation and duty to the family business?
- Should spouses be included in the decision circles? How?

Since context and circumstances can be very diverse, planning, vision of the future, and, especially, the identification of all those who need to be involved in the process is key to keep emotional factors from becoming an insurmountable barrier?

2

Balancing Technical and Socioemotional Aspects

Family companies unite two universes that, at first sight, are opposite: the business world, governed, theoretically, by pragmatism and rationality, and the family world, governed by emotional ties. Often, situations experienced in a family business can lead to a clash between these two worlds. In succession, this tension is quite common

In general, those responsible for conducting the succession process tend to devote much attention to technical aspects, such as the technical capacity of the successor, tax, corporate, and other legal aspects. This is an important and necessary posture to reduce costs and minimize risks, but the exclusive discussion of these issues does not solve the most challenging problems of the generational transition related to possible socioemotional obstacles.

> "No matter how hard you try to sterilize the succession and turn it into a highly planned, easily replicable process based on the science of talent evaluation, it remains an essentially human effort—often confusing, complex in essence, always specific to each situation."
>
> (M. B. Nadler, "CEO Succession: An Owner's Guide for directors", in Leblanc, R., *The Handbook of Board Governance: A Comprehensive Guide for Public, Private, and Not-for-Profit Board Members*. Hoboken, New Jersey: John Wiley & Sons, 2016, p. 121.)

Socioemotional issues have a strong influence on the perception and behavior of family members and can guide individual interpretations of the entire succession strategy and, consequently, decisions about it.

Studies indicate that decisions in family businesses are guided mainly by this socioemotional component and not so much by technical aspects. Not considering this relevant component can put family harmony at risk, with negative impacts on the whole process.

B. J. Debicki et al., "Development of a socioemotional wealth importance (SEWi) scale for family firm research". *Journal of Family Business Strategy*, 7(1), 2016, pp. 47-57.

Box 3 – Relevant Aspects in the Socioemotional Dimension of Succession

Based on I. Lansberg, "The Succession Conspiracy". *Family Business Review*, vol. 1, 1988, pp. 119-143.

Founder/current leader

- Reluctance to accept one's own finitude when one still feels strong and capable.
- Difficulty in giving up power and control in the company and in one's own family.
- Fear of losing an important part of one's identity and being ignored in the family and community.
- Fear of having to rely more and more on others.
- Fear of competition and jealousy towards possible successors.

Family

- Children who wish to alienate the founder to gain autonomy may sabotage their own chances of succeeding him as a result of the feeling of guilt.
- Fears from parents of abandoning roles linked to the business or of seeing family disharmony installed.
- Fears, uncertainties, and a feeling of inability to "fill the place" of the current leader or founder.
- Fear of being seen as greedy or inelegant for addressing the issue.
- Concern of having someone perceived as equal (brother or cousin) in the role of leader.
- Difficulty of children to talk about the feelings that surround the loss of parents.

Managers

- Reluctance to move from a personal relationship with the founder to a more formal one with a successor (for many, personal ties with the owner is the main benefit of having worked for a family business).
- Fear of one's own aging and retirement.
- Fear of losing one's job.

- Fear of losing autonomy and influence because of the formalization of structures and the adoption of new systems.
- Frustration for feeling that you are better prepared than a family member.

Other partners

- Ties of friendship or loyalty with the founder can prevent open discussion about succession.
- In the case of minority shareholders who are founders of other companies, resistance in discussing the topic of succession so as not to have to approach it in the organization itself.

Environment (other groups)

- Clients and suppliers who grew having the founder as their main contact in the company fear losing the connection with the management.

Addressing technical and socioemotional aspects in an integrated manner can help not only the family, but all the groups directly or indirectly affected by the succession–like managers, partners from outside the family, suppliers, customers, employees, and the community itself–to develop the necessary trust to dialogue about the process and move forward.

For instance, it is important to discuss the owner's anguish regarding the role he or she will play in the business and in the family after the transfer of power. It is also important to look for ways to promote early connection of future generations with the family business and its executives.

2.1. Choices that Are Sometimes Incoherent

Some conceptions and feelings awakened in the succession process are inherent to each individual involved. Some of them may be out of rational control and strongly affect their decisions, even if unconsciously. These are the so-called heuristics, preferences or judgments that influence perceptions and actions practically automatically, without being perceptible. They are almost always adopted with the purpose of deciding the easiest, least conflicting option. There are situations in which it is possible to make quick and efficient decisions, reducing the time to process the information. Sometimes, however, the heuristics can also provoke biased judgments, which lead to wrong choices.

Understanding the existence of this phenomenon helps family members to reflect on the choices they are making. For example, it is common, but not necessarily fair or effective, to compare the candidates to the succession with the current leader, because their experience and stage of preparation are totally different.

There are cases in which the current leader is reluctant to start the succession because he or she considers that the heirs are always unprepared to replace him, even if they already have relevant professional experience. In other cases, the company founder might give preference to a daughter in the succession because he fears the competition of a man in the position, or, on the contrary, choose his son because he believes that a woman is not qualified to occupy the position.

The heirs, in turn, may have a mistaken perception of rights during the transition, because they understand that the condition of members of a family business guarantees them a position in charge of business, or even executive leadership positions. In fact, it also represents another chance to show whether or not they are prepared to take on this challenge, in a technically complex process marked by difficult choices of socio-emotional character.

Since these are subjects that can–and generally do–create conflicts, it is recommended, in some cases, to involve an external, neutral professional who knows the dynamics of the familiar companies and can facilitate these emotional discussions. In many situations, therapy or family or individual mediation can be part of the process.

Understanding how these complex forces work is a vital first step in successfully managing intergenerational transitions. Often, technical and socioemotional issues will be strongly linked to the decisions of an entrepreneurial family. This will become clear in the next chapters, in which these aspects will be addressed in the dimension of ownership, family, and business, often in an associated manner.

3

Succession Is a Process, Not an Event

Succession in a family business isn't only a changing of the guard, nor the mere transfer of assets. It is a continuous, long-term intergenerational process which needs to be planned and executed very well, since it means passing on a legacy, an organizational culture, of a tangible and intangible heritage and a leadership that will allow a success story to continue or not. After all, the family business only exists as such while the family is willing and prepared to transfer control of the business to the next generation.

3.1. Planning

Planning means understanding the current situation, projecting the desired future situation, and defining the path to make this crossing. It also means defining scenarios and the path to minimize and deal with risks and uncertainties over time. Planning the concrete aspects of succession, even if logical, can awaken a myriad of perceptions in the people involved, such as loss, gain, jealousy, envy, and competition, among others. All these reactions need to be considered and treated as part of the process. It is recommended to pay attention to seven essential aspects of a successful transition:

P. Leach and Trusted Family (Producers), "7 essentials for smooth succession in your family business/family office", 2019. [Video webinar]. Available at: <https://trustedfamily.net/insights/2019/4/26/growing-aresilient-family-and-building-a-sustainable-enterprise>. Accessed on: August 19th, 2019.

Seven Essential Aspects of a Successful Transition

1. **Values –** Family values (whether implicit or explicit) are essentially important in the process, since they help formulate a coherent speech and keep vanities or interests to overlap the group's interests.
2. **Business purpose –** When everyone understands the purpose of the business and agree with it, it is easier to align goals and accomplish the rite of passage. Often, however, the purpose needs to be revised during the process.
3. **Communication –** Fragile relationships can lead to poor communication. Improving communication and empathy among people requires making their relationship solid enough to resist "tough conversations." For an effective communication, people need to be able to talk about usually uncomfortable subjects without creating conflicts that put the business's prosperity at risk or make it impossible for it to stay under family leadership.
4. **Qualification –** Every member involved must be adequately informed about the business, ownership, and family governance. They must understand the company's context, the risks it faces, as well as their own roles, duties, and responsibilities.
5. **External facilitator –** Having an external facilitator is recommended, because of how he or she can contribute with different points of view and knowledges, of the methodology of conducting the process, and, especially, for their independence and emotional distancing regarding the family and the business.
6. **Process –** Every succession is a process, and it must be transparent. People have to understand what the necessary steps are, who is responsible for which activity, and what is their own role. They also need to have a schedule with well-defined marks so the advancement can be monitored and so that possible problems are corrected.
7. **Tenures/incentives –** Shareholders must formalize clear tenures and incentives which are right for the leaders and coordinators in the process. Without this, it is hard, for instance, to convince members of the future generation of leaders to leave lucrative market activities and dedicate themselves to the family business, often facing a tense family environment.

In an organized and gradual process, a trained successor develops under the supervision and guidance of the one being succeeded, with the partners' consent and according to a plan discussed and agreed upon in advance with all family members and partners of the company.

In the opposite scenario, where the person being succeeded and other family members avoid talking about the future command of the business, the succession can occur abruptly and unexpectedly–for instance, when the leader of the company gets sick or dies, in which case the successors are forced to suddenly take on a position for which they may not be adequately prepared. Encouraging long-term vision and strengthening collegiate bodies–such as the family assembly, family council or partners committee–are aspects that greatly benefit the process and the maintenance of the company's value.

Planning, therefore, is a mandatory activity, in case the interest is in perpetuating the company and the family assets. Not thinking or not talking about this crossing can be a choice, but it tends to generate damage to both business and family.

To summarize the main issues to be considered in the succession process, we reproduce the strategy in 12 steps suggested by Professor Ivan Lansberg for the owners of a family business and their main stakeholders to conduct **succession planning** 🕮.

🕮 I. Lansberg, "Twelve Tasks in Succession", *Family Business Magazine*, Summer 1993. Available at: <https://www.lgassoc.com/writing/twelve-tasks-insuccession>. Accessed on: October 9th, 2019.

Box 4 - 12 Tasks for Planning

1. Decide whether you want to continue family ownership.
2. Assess whether the family can withstand the stresses that continuity planning inevitably generates.
3. Get the owner-manager(s) to agree to actively manage the development of a continuity plan and the transition in leadership to the next generation.
4. Consult and actively involve other major stakeholders in the process.
5. Set up appropriate forums for reaching consensus on key issues.
6. Develop a clear vision for the future of the business that all key family members can enthusiastically share and that spells out the role each will play.
7. Choose a successor and other candidates for the future top management team, and plan a course of training for each.
8. Help the successor build authority both in the family and in the business.
9. Design an **estate plan** ✪ that specifies how ownership of the enterprise will eventually be distributed among members of the next generation.
10. Make sure family members understand the rights and responsibilities that come with the various roles they will assume.
11. Inform important stakeholders–customers, suppliers, creditors–about the firm's continuity plan.
12. Develop a contingency succession plan, just in case.

✪ Editor's note: The subject of wills and estate plans will be debated and contextualized for the Brazilian case in Chapter 6.

3.2. Time Matters

Each family has its time, but the generation in charge must create the conditions for the next generation to legitimately occupy its space. For this, it is necessary to define the possible roles and positions that family members, heirs or family successors can occupy in the family governance system (partners, members of the family council and its committees, social leaders, among others) and in the business governance system (usually council and executive positions).

People are living longer, families are being formed later, and studies indicate that young people are less likely to have many children. As a result, families tend to be smaller and smaller. This factor can increase the age gap between parents and children and potentialize generational conflicts, since at least three generations can interact for years within the company's management. To ensure a good balance between interests and the strategic plan of the company and the individual needs of family members, it is important to define **clear roles within the company and family governance ➲**.

One thing is certain: in the company's management, there will hardly be space for everyone. It is the family governance that has, primarily, the role of integrating people and supporting their individual development and their choice of paths.

➲ According to data from IBGE, in the report *Brief Analysis of the Evolution of Mortality in Brazil*, the life expectancy of Brazilians at birth rose 18.7 years in almost half a century (1970 to 2018).

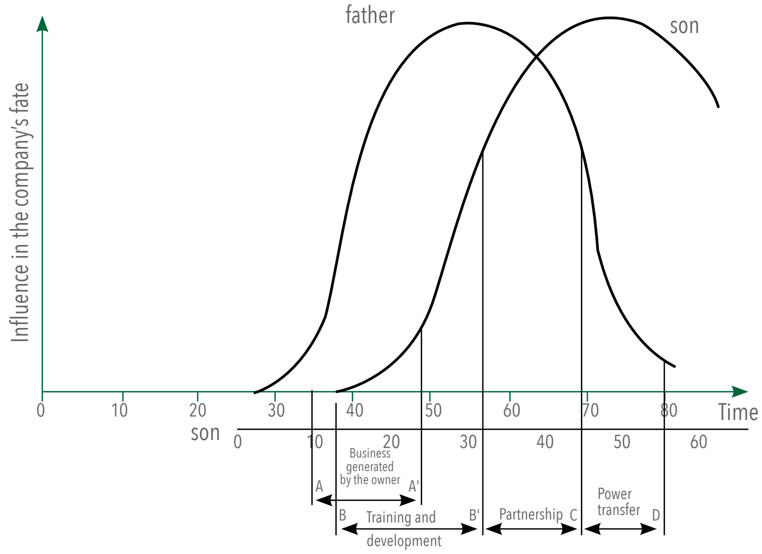
As for marriages, data from Civil Registry Statistics show that, in 1974, men and women got married, on average, at age 27. In 2018, this average rose to 30 (for men) and 28 (for women) when they considered civil marriages between spouses of different sexes, and to 34 (men) and 33 (women) when they considered spouses of the same sex. The same study indicates that, in the past 20 years, the number of mothers of up to 24 years old has dropped a lot and the number of those between 30 and 39 years old has increased.

Besides, on IBGC's study *Governança em empresas familiares: evidências brasileiras* (2019), three generations of the family were involved in the business in nearly 30% of the participating companies; in around 6% of them, there were four generations.

To plan the succession activities in the adequate time, it is important to recognize how generations interact in the business dimension along a company's life, which is graphically represented in the following image, reproduced from an article by professors **Neil C. Churchill and Kenneth J. Hatten** 📖.

📖 N. C. Churchill and K. J. Hatten, "Non-Market-Based Transfers of Wealth and Power: A Research Framework for Family Business". *Family Business Review*, n. 10, 1997, pp. 53-67.

Figure 3. Interaction between generations during the life cycle of the business



1. **Business generated by the owner.** This stage, from point A to A', goes from the beginning of the enterprise to the formal entry of a member of the next generation into business management. In this initial phase, family considerations influence the business, but are not part of it.
2. **Training and development of the new generation.** From B to B', the second generation learns about the business. This occurs around the dining room table, from early childhood to college. Full-time involvement in the company, point A', intensifies the development of technical, interpersonal, and managerial knowledge, judgment and skills needed to lead the business in the future.
3. **Partnership between generations.** At some point, B', the offspring acquires sufficient entrepreneurial and managerial competence to receive responsibilities and begin to become involved in political decisions associated with at least part of the company. This responsibility becomes a full and shared partnership between the generations regarding operations, goals, and policy determination (point C).
4. **Transfer of power.** This is the period when operational responsibilities, policy formulation, and goal setting change from one generation to the next. The transfer begins at the last stages of the partnership, point C, and gains

speed as the founder begins the retirement process and reduces his or her active participation in the business. This can occur with or without a formal transfer of ownership.

L. B. Barnes and S. A. Hershon, "Transferring Power in the Family Business." *Harvard Business Review*, 54(4), 1976, pp. 105-114. Available at: <https://hbr.org/1976/07/transferring-power-inthe-family-business>. Accessed on: August 19th, 2019.

The intergenerational phase mentioned above is that in which family protocols that determine policies and rules on how the family relates to the company are generally developed. The family protocol records the values and purpose of the business family. Usually, the document establishes in a transparent manner the rules of entry of family members into the business, the way to elect family members for family governance positions, and, in some cases, rules of conduct and other guidelines. Some protocols detail requirements for the career of family members who want to develop as executive, director or partner.

3.3. Succession Is a Learning Process

Succession should also be seen as a learning process, that is, an opportunity to get to know the family business, its risks and opportunities, to regain purpose and, especially, to learn about oneself, relationships, and leadership

To ensure the effectiveness of this transition, the family and the company can certainly turn to outside professionals, such as consultants or mentors, who, due to their independence, knowledge, and emotional distance, can encourage the involvement and alignment of family members, in addition to supporting the design of the training plan and personal development of those involved, as well as eventually mediate potential conflicts.

The succession environment brings up intimate aspects (aspirations, fears, competition, conflict, and so on), which can make explicit issues that were previously latent but which can no longer be disregarded. It is important to recognize and understand that people react differently and at different times to the same situations. To take care of individuals in their uniqueness strengthens people, families, and businesses.

Although succession cannot be an exercise of "trial and error," we know that even exquisite planning requires adjustments when faced with reality. Therefore, making mistakes is a possibility. When this happens, it is important to quickly face the problem, learn, start again, and move on.

4

Succession in the Business Dimension

The importance of the executive president, CEO or superintendent's role and their succession processes is widely studied and documented. Literature on the subject can be found in newspapers and magazines, consulting articles, books, best practice manuals, and academic studies. Nevertheless, applying the best human resources practices of the corporate world to choose good successors does not seem to be enough for family businesses. The approach needs to be expanded and revised, because everything that happens in the succession of the business leadership reflects in the family governance and in the conduct of its members–and vice-versa.

The preparation for this change should be not only of the successor, but also of the one being succeeded. For the process to be effective, current family leaders need to feel comfortable with the role they will play during and after the process as well as with the choice of their successors. They must be confident in the next generation's skills to conduct the business, to maintain and promote family principles and values, and to pass on the legacy of previous generations. Success in the succession process is maximized when the family member to be succeeded is genuinely inclined to give up his or her place in a negotiated rite of passage.

If the successor is a member of the next generation, he or she will need to feel legitimized and comfortable with the program outlined, in addition to being supported to carry out his or her mission and assume the responsibilities delegated to him or her.

The more formalized and mature the corporate and family governance are, the greater the chances of succession in the business going smoothly. This does not mean that the delicate aspects inherent to a family business simply cease to exist if they are mature and organized. It means that the time, effort and knowledge acquired during the arduous process of implementing and improving governance systems will be used during the succession.

Box 5 - Points of Reflection

- The successor can be chosen among family members or executives outside the family. The definitive aspects should be meritocracy and professionalism.
- Having a formal protocol to choose the successor is a great help.
- The successor needs to be prepared, whether inside or outside the organization.
- The level of maturity of the family and the business may require a new set of abilities from the successor.
- The one being succeeded must develop a future life project, so their cycle of realization doesn't become extinct with the succession.

4.1. The Central Role of Those who Are Leaving

Much is said about the support needed to develop successors (potential or already chosen) and little about the care, guidance, and attention that the founders or the senior generation in power must receive to deal with the transition process. This care makes all the difference, because the founders' or senior generations' willingness to plan their succession (of ownership and management) is determinant for the success of the generational transition. Fears or discomfort to deal with the pain and uncertainty of succession should not be a justification to postpone the beginning of the process, in the expectation that some event will make it inevitable.

Difficult strategic choices are necessary, such as electing a family member to succeed at the expense of others, selecting someone in the market to fill the position or withdrawing from the business through a full or partial sale. It is also quite common in the transition to the second generation to simply do nothing, passing on decisions to be made to others in the future. Each of these options represents advantages, disadvantages, opportunities, and threats, with varying scope and impact for the company and the family. However, it is a fact that facing difficult choices generates fewer consequences than procrastinating decisions.

The reluctance to approach succession can also be attributed to a simple combination of the founder's instinctive desire to maintain control of the company and a natural aversion to planning. But the real reasons are usually much subtler and more complex, based on understandable fears and anxieties. No one likes to think about death or disability, and it is hard to make choices among children or abandon a prestigious position that can represent the work of a lifetime.

Transitions with better results tend to be those in which the founder or generation in charge is able to find meaning for the new phase of their life and have the genuine intention of leaving a greater legacy than their existence.

In many cases, one possible route to a well-crafted succession in business is to designate the one being replaced to a position on the board of directors or advisory board. With this, the senior generation gives way in the management of the company, but continues to contribute with its experience in other bodies. By participating in boards, the senior generation can guide, support, and monitor management in its decisions, with a restricted level of authority in operational matters and a more strategic and long-term view.

Later, when leaving the organization's leadership, the founder or senior generation may be involved in a membership council, family governance or philanthropic or external activities. The senior generation's transition through participation in boards and philanthropic activities is a powerful solution for them to take advantage of the experience and wisdom of previous leaders, with respect and discipline for governance and the new power structure as a premise.

4.2. Communication Is Key

Succession generates uncertainty not only within the business family, but also among suppliers, customers, employees, and other groups that relate directly and indirectly with the family business.

A good transition plan should include communication actions with stakeholders to show that the company is giving due attention to the issue, that the change is a properly managed process, and that its impacts are under control.

The communication plan should contain actions aimed at informing each audience in advance of the anticipated changes that may affect it directly or indirectly.

The messages should highlight the values of the organizational culture and need to be clear and objective, to promote transparency, ensure uniformity of speech, and avoid the dissemination of rumors.

This will help reduce the risks that the change of command in the organization will affect the perception of the brand by external audiences and the reputation of the company as an employer.

4.3. What If No Family Member Is Interested in Working in the Business? Or If There Is No Successor with a Fitting Profile?

Sometimes we may come across situations where (1) no family member, for various reasons, is interested in working in the company, whether they fit the profile or not, thinking, for example, that the most important role is to prepare to be a shareholder or even a director, instead of being in management; (2) in others, although there is interest, the profile and readiness of potential candidates are not the most appropriate, which may jeopardize the management's effectiveness.

In these cases, the search for executives in the market may be the solution, but finding the candidate with the ideal profile for the organization is not always an easy task. Besides documenting the assignments and goals of the new leader as well as his or her decision level, it is necessary to previously define the selection criteria; qualifications and accomplishments history are certainly important, but one cannot leave aside aspects such as values, principles, and psychological and behavioral profile, which will certainly have an impact on the relationship with the business family. Alignment of values and principles is a strong component for success.

Good family governance is important to attract, retain, and encourage a non-family leader, contributing substantially to good relationship dynamics and their impact on professional performance, as well as to build a healthy climate. When the company starts to be conducted by market executives, the corporate dynamic changes and so does the family dynamic. It is necessary to accept a natural loss of direct operational influence in the business and to be more rigorous with strategic guidelines and governance rituals.

The long-term vision of family companies is usually a factor of attraction for market executives, because they feel they can have more time to put their plans into practice and reap results.

It is an opportunity to perform their work close to the maximum power structure (board and partners), where decisions are faster and usually driven by patient capital (committed to the long term and not just the quarterly results).

On the other hand, the fact that the company is strongly connected with the family, the founder and its partners represents a real possibility of conflicts for the business, especially if there are gaps in the system of family and corporate governance. A strong family and corporate governance turns this weakness into strength.

This scenario may represent an intimidation factor for some of the best talent in the market and, in fact, imposes risks to the success of these managers. In order to minimize them, it is possible to adopt measures such as those highlighted in the table below.

Box 6 – Points of Attention for Non-Family Successors

- Choosing the professional profile that is most aligned to the family business characteristics (values, culture, presence of the founder/family, business momentum).
- Identifying and informing the successor of crucial, sensitive issues he or she will face.
- Adopting a solid corporate and family governance, which helps pacify the possible candidates about the existence of adequate processes and forums for solving conflicts.
- Identifying a facilitator who can give support to technical and emotional aspects.
- Choosing independent members for the board of directors.
- Instituting a transparent, continuous system of information for family members and partners.
- Defining clear, transparent rules.
- Maintaining constant communication to align expectations.

A propitious space for the generation of conflicts, succession in the business dimension, both in the management and in the relationship between partners and family members, has as key success factors the alignment of the main stakeholders (partners and family) with the strategic direction of the business, as well as the confidence in the information system and accountability of the company. Non-family executives who participate in this process are responsible for maintaining an independent, empathetic position to ensure maximum rationality in decision making.

If there are members interested in working in the business, but whose profile or competencies were not considered adequate at the time of the transition, a lot of zeal and care in communication is necessary to avoid that the internal successors not chosen for the position become obstacles or even insurmountable barriers to the trajectory of the selected external executive. Some families, in this situation, resort to coach and orientation programs, both for the chosen and the not chosen.

5

Succession in the Family Dimension

Families are groups of people with unique stories, which cannot be replicated and are generally incomprehensible for outsiders. As a social entity, the family is influenced by the macro and micro context in which it is inserted: the relationships between husband and wife, parents and children, cousins etc. This complex association between people influences and determines the way each family deals with ownership, family issues, and the business.

Relationships matter a lot to families and, more than that, they determine who the members are. A dynamic of its own, an invisible set of norms and rules organize, usually implicitly, the way people interact. Besides a hierarchy of relationships that is understood only by those who are part of the group, there are specific archetypes–such as the father or mother of a family, older sister, and youngest son–and typical behaviors: the one that complains the most, the most religious, the most studious, the most involved with the third sector, among others.

It is also common to see beliefs like "things here have always been this way and we don't know why." Throughout a family's history and experiences, myths and secrets arise that need to be discussed in order to plan the succession. The senior generation will need to make an effort to understand and respect the individuality and desires of the younger generation, even if these things do not reflect their own interests. In other words, it is something more complex than simply drawing up a checklist of actions to be taken.

Several factors can affect succession in the family dimension, among them the life cycles of its members, where succession is directly affected by events in the life of each family member, which in turn can affect business management and ownership issues.

As with any group of people, all families experience conflict and rivalry, and need to manage issues related to the tripod of love, money, and power. The important thing is to know how each family will find its own way of dealing with these issues, maintaining a certain harmony and cohesion and avoiding causing serious damage to the business. As highlighted by the Royal Bank of Canada's Succession Guide made by their wealth management branch: "Taking up one of the first principles of succession planning: for the plan to be successful, it needs to balance the needs and goals of the family and the business. Many families who don't recognize the importance of this balance end up not achieving the **expected results"** 🕮.

🕮 RBC Wealth Management, *Succeeding in Succession: A guide to keeping family harmony through your business transition*, Royal Bank of Canada, 2014, p. 3.

The family and the business are interdependent, but they operate from different perspectives and may follow conflicting orientations: the family resists change, while the business needs innovations; relationships in this family are perennial, while in business they are contractual; communication in the family is informal, in business it requires formalizations; the family seeks security, while the business needs to take risks; the family values harmony, while the business seeks profit. This tension between goals and needs of the family and the business, therefore, will always exist. The humanization of the business and the professionalization of the family must be a point of attention during the succession process.

In this section, our idea is not to cover complex intrapersonal and interpersonal issues that can affect family succession, but to highlight their relevance to the transition process and encourage their analysis and discussion.

It is essential, therefore, to ask yourself.

- How are relationships in your family?
- What is your role in the family?
- Is it the role you would like?
- Are you giving your best contribution?
- Who takes care of the emotional relationships and the maintenance of family values?
- How balanced are these relationships when it comes to the goals and needs of the family and the business?

5.1. Process Formalization

It is important that the whole family and the system where it is included know and understand the goals, principles, and rules that guide the succession process and decision making, and it is necessary to create a space to address this issue..

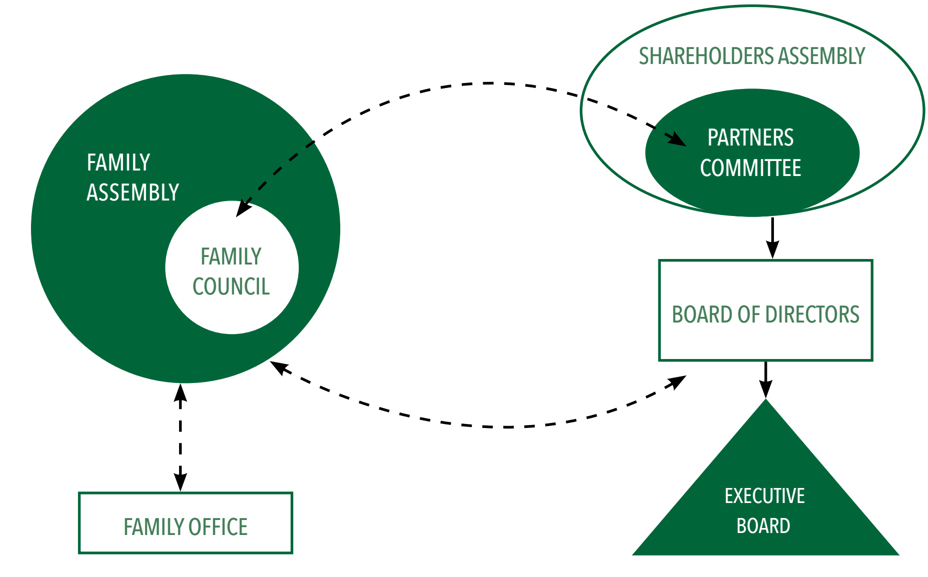
Structuring family governance so that a family council (formal or not, see item 5.2 below), or even a transitional committee, takes care of communication among family members is an important measure, which can greatly harmonize relationships in this sensitive period.

In this forum, issues relevant to a good succession can be discussed, such as:

- the family's purpose and values;
- expectations of the current and future generations;
- employability criteria;
- evaluation criteria;

- equality;
- conflict resolution;
- communication; and
- family cohesion.

Figura 4. Family governance structures



Source: Cambridge Family Enterprise Group, 2015.

Brazilian Corporate Governance Institute (IBGC), *Governança da Família Empresária: Conceitos Básicos, Desafios e Recomendações*, IBGC,São Paulo, 2016, p. 33 (Cadernos de Governança Corporativa series, n. 15). Available at: <https://conhecimento.ibgc.org.br/Paginas/Publicacao.aspx?PubId=22057>. Accessed on: October 9th, 2019.

5.2 The Role of the Family Council in Succession

Composed of family members elected by the family assembly to represent them, the family council is one of the most strategic forums of the succession process; it is the space to deal with explicit and implicit issues of the relationship between members of a family and between the family and, the business, and the ownership.

A study conducted by the IBGC pointed out that only 32.6% of the responding family businesses had a family council. The study also highlighted that the main reason for partners to leave the company was the existence of conflicts of interest. The family council can help to deal with delicate and important issues for family relations and business strategy.

IBGC, *Governança em Empresas Familiares: Evidências Brasileiras*, São Paulo, 2019 (Series IBGC Pesquisa).

In the succession from the second to the third generation and in the following ones, probably not all family members will be able or willing to work in the business. As a result, the need to develop and implement the family council to help understand and design the different roles family members can play grows.

Those interested in working in executive positions in the family business should be protagonists of their own development, relying on the support of the family governance system and mentors. To ensure the legitimacy of new leaderships, it is important to clearly define the rights, duties, and boundaries of all bodies and positions that involve governance. The family council should be responsible for leading the construction of the family agreements, which will be registered in a family protocol. Compliance with the protocol and harmonization of family relations should be encouraged by the members of this council.

In long-lasting family businesses, the family council can also play the important role of encouraging young people to have a life project, to own their own business or to make a professional choice outside the family business. This is necessary because we know that businesses tend to grow in arithmetic progression and families, in geometric progression, so there is no place available in the company for everyone who might be interested. In many successful cases, it is common for the family governance body to support the creation of individual development plans (IDP), so that each member of the generations develop their potential and skills to the maximum and can apply them inside or outside the company.

The size of the family, the size of the business, the culture of the family, the context in which the company finds itself are important factors that affect the definition of corporate governance practices and family governance to be adopted by the company. The same goes for the composition and functioning of the family council—there is no standardized model that fits all.

5.3 Engaging the Next Generation of Leaders

Families deal with the preparation of the next generations in a variety of ways. There is a myth that because they are heirs to a business, their successors make little effort. In fact, many need to prove their worth outside the family business before their ideas start being accepted in the family business circle. And, once inside the company, they need to prove again, now to managers and employees, that they really deserve the professional position they conquered.

The challenge of engaging the future generation of leaders is to find the right balance between attracting these individuals, empowering them to work in the business, and giving them the freedom to design their professional trajectory according to their own interests and vocations.

Below, we highlight some suggested actions to establish a partnership between the generations within the family organization:

Investigate and discover career expectations and examine in depth the alternatives available for each family member. Communicating and aligning these expectations is critical to the success of the succession process. Depending on the stage of each person's life, it is often necessary to help them find their vocation, which is not necessarily related to working in the family business. It is important, regardless of the size of the company, to be aware that if a family has a business and wants it to last, everyone will assume a role that encompasses rights and duties, whether as a partner, director, executive or occupying other positions in the business. Among the ways to offer support are vocational and career guidance, coaching, development programs, and integration internships in the company to forge a meaningful relationship with the business.

Invest in education. Parents or caregivers need to assume their responsibility in the task of educating their children so that they incorporate family values, develop self-esteem, and evolve as citizens. In this process, they will have the opportunity to learn how to manage their money, business, and investments and will be able to have a vast experience before deciding whether or not to enter the family business, according to the established governance rules. If this really happens, they should be adequately prepared through individual and business development programs. Investing in education is like making a living donation, leveraging intellectual capital through family financial capital.

Encourage intergenerational work. Creating an environment that is welcoming to new generations is important for future leaders to gradually understand that they are part of a family system that holds control of a business. To follow the market's transformations, to incorporate innovative practices and new technologies, and to be open to changes is important for young people to feel interested in the company. Encouraging the activities of the new generations in accordance with the age group and personal interests is also a way of engaging them and establishing dialogue, giving them the opportunity to conquer their own space and freedom to direct their own careers.

Offer training and development opportunities. To better integrate the new generation into the business, it is important to clearly define the roles these young people can play and offer internship and trainee programs, in or outside the family business, to encourage their development. When heirs start working in the company, the objectives for each role should be clearly established and they need to receive feedback on their performance. Compensation for the work must be compatible with the market and with what any other employee would receive in the same position. In order for young people to gain credibility for their own performance in the company, it is important not to make any distinction in the compensation of family members or non-family members.

If the established governance rules allow, working in the business is only one of many career options. It is a very successful practice to encourage young heirs to start their professional life outside the company, so that, among other issues, he learns to respect hierarchies and rules, which will contribute to their maturity, self-esteem, and business vision. This experience will also help them gain the trust and respect of employees and family members in the future, should they become part of the company. It is important to define rules for family members to join the business management, making the criteria for admission–such as the requirement for external professional experience, for instance–explicit to all members of the new generation. The essential is to give equal opportunity for all young people to prepare themselves adequately to enter the company or to develop another career disconnected from the family business.

Retelling and keeping alive the history of the family and the business construction. It is very common that the story is no longer told or is lost over time.

The reasons are numerous and unique to each family. This narrative, the sequence of events, is as important for those who tell it as for those who listen. It promotes a sense of belonging and connection with family and business values. It is important that these events happen frequently and involve the whole family, as they can bring positive results for family cohesion and harmony. The older generation is recognized for its work and contribution. The younger generation has the opportunity to understand how the business started and what were the relevant participations, emblematic passages, skills developed–alas, understanding the trajectory of the family business, with all the achievements and obstacles.

5.4. The Selection of Successors within the Family

The way of choosing and ratifying a successor is decisive for their good relationship with the controllers and family members, as well as for the success of the work they will do in the company, in the family, and in the group of controllers. The family governance structure will help define the common vision and values to promote harmony among the group throughout the transition.

In the selection process, it is important to treat potential candidates equally and fairly identify who has the profile, interest, commitment, and qualification to fill the positions that need to be filled–the most important are on the family council, the board of directors, and the business leadership. Depending on family policies, spouses may be considered candidates, in the basis of meritocracy and shared values. Whatever successors are chosen in the various governance roles, positive, neutral, and negative reactions may arise, which should be properly addressed to ensure the commitment of all involved in the transition.

Thinking of the long term, one of the relevant attributions of family governance is to offer support to the professional and personal development of the family members, stimulating both individual qualification and the maintenance of good relations within the family circle. This support is as important for the success of the members of the future generation who will be directly involved in the business as it is for those who will follow different paths. It is another practice capable of encouraging healthy bonds between members of the business family over time.

> "The more inclusive and consensual the succession process is, the better. The more information, training, and interaction among family members, the better. The more everyone knows their peers, rights and duties, assets, goals, and strategies of the common business, the smoother the transition. Hence the importance of communication and interaction promoted by family governance. The institution of seminars in family meetings, with the goal of acculturation on the various aspects of governance and business moments and operations, are of great value for this process." – IBGC, *Governança da Família Empresária: Conceitos Básicos, Desafios e Recomendações* 🕮.

It is important to establish, in the governance system, minimum requisites

🕮 IBGC, *Governança em Empresas Familiares: Evidências Brasileiras*, 2019.

for jobs, related to education, professional experience, and personal profile. The competence criteria must be defined according to the family's and company's strategic goals, approved by partners and formalized in a specific document (for instance, a family protocol). The answers to the following questions, among many that can be made, help guide this process:

- What roles do we want to have in the family, the business, and the ownership?
- What personal characteristics must be present in the family council members? What about in the board of directors members?
- What leadership and management experience is needed to ensure the continuity of the family business success?
- What is the required preparation to assume the positions?
- Who are the family members with the profile and interest to occupy each of the positions?
- What are the reactions each possible choice can produce and how to deal with them?
- What are the necessary roles to manage the relationship dynamic between family and company?

6

Succession in the Ownership Dimension

The ownership structure is vital for the longevity of a family business. Through good control mechanisms and a proper structuration of net and fixed assets, the family enterprises may be successful and last longer. Planning the succession of the family assets helps to ensure it occurs smoothly and reduces the chances of court battles that may harm the family's relationships and threaten the company's health.

Succession in ownership encompasses all of the family's assets: companies, moveable assets, real estate, and net assets. The assets conveyancing may occur while the owner is alive, in full or partially, or be bound to the owner passing, although planned. This process is key in the preservation of the family legacy and, often, brings the gain of ensuring the continuity of assets within the family.

Therefore, it is an essential topic to promote the perpetuity and leadership of the business family. As times goes by, the family expands, the relationships change, and, if these changes are not well calculated in the ownership structure, they may affect the control and, consequently, the family businesses.

Ideally, the first step towards a planned succession must be built through the family governance. This is what supports the succession process so that it does not concentrate only in the company management or assets conveyancing. The family governance will also be responsible for conveying the legacy and values to support the involvement of next generations and strengthen a mindset that takes into account the different roles of family members, partners, and executives.

The business and ownership succession are complementary processes. Possibly, the first concern will be to identify and prepare a new leader for the company, although ownership issues also are pivotal. The company's control, preferably established by a shareholders agreement, is determinant for the company management and for the relationship among partners.

Often, complementary tools–such as wills or paid or gratuitous contract arrangements–may be required to ensure that principles defined in the succession planning are fulfilled and that the heir rights are respected, and the assets conveyed in under the terms and conditions required to the efficient control of the company. These components, as well as decisions on wealth conveyancing, composing of the partnership votes and dividend distribution, are pivotal topics.

Commonly, the business succession happens and the senior generation who holds the control still follows and deliberates on relevant issues without an immediate succession in ownership. This transitional period alternative in succession may be a good path for developing a successor and for the gradual exit of the former leadership. In many successful histories of succession, the family members who had left still supported the business and the business family as a sort of "knowledge asset."

The new generation needs to be prepared to make decisions obeying to power skills, and both generations need to develop in order to feel comfortable in their roles before and after the transition. It is important to have in mind that this transition must not be extended beyond its required time. To end it, the senior partners must rest assured that the next generation will have the abilities and the commitment to effectively hold voting power. Another partner concern on ownership transference often is loss in income. However, there are legal instruments to avoid or mitigate those effects.

6.1. The Importance of the Shareholders Agreement and of Legal Instruments

The shareholders agreement ✪ is a legal instrument that seeks to regulate the partners' relationship as shareholders of the company's. The document defines rights and obligations, rules of corporate governance, exercise of voting rights, purchase and sale of shares (quotas or participation), and strategies to exit the company, among other matters. Therefore, it is an important pre-requisite of the patrimonial succession plan.

✪ In some companies, the shareholders agreement is known as partners agreement.

For a planned transfer of assets, it is vital to have a shareholders agreement that makes clear how the partnership's most critical aspects will be managed, reducing the potential for conflicts between partners. Other documents developed by family governance–such as a protocol, a family constitution, and a code of conduct–can also help in succession processes. Often, the work of drafting these documents helps understand the roles and responsibilities of each family member. Working well on corporate relations and communication, preparing a group of partners to analyze the business with the vision of the business family, and knowing how to make the choices that need to be made are important aspects to support the directions that the partnership and the company should take.

Still within the planning of succession, it is recommended that the owners of the property use appropriate legal instruments or make a will–in case they prefer that the asset transfer occurs after their death–to dispose of their assets. In this way, they will indicate which heirs will receive which assets, who should manage the heritage left to the underage heirs, and, also, they will make the testamentary dispositions compatible with the guidelines outlined by the shareholders agreement. Thinking about succession is important for all generations and family members, regardless of age or position in the company and family.

A shareholders agreement can also define decision-making levels, an essential issue to avoid conflicts and, therefore, one of the priorities in the design of the corporate governance model. It is up to the partners to define which decisions they want to keep for themselves, which other decisions will be delegated to a board of directors and what level of autonomy the executives will have. In addition to those already defined by the applicable legislation for each corporate type, the others need to be clearly stated in the shareholders agreement, in the by-laws/contract, and in the board of directors' internal regulations.

It is also important to consider that, in succession or in the donation of assets, there are costs and incidence of taxes, which may result in large expenses. Planning the transfer or donation of assets over time and having resources available to support the transfer of property is something vital that needs to be defined with legal support. Some types of planning only produce effects after the owner's death, while others have immediate repercussions–while he or she is still alive.

6.2 The Transfer of Control

The succession in the ownership dimension will, in fact, occur when the shareholding control is transferred to the beneficiaries. One way to work on this family transition process is to establish a partners committee, in which the controlling group discusses, through its representatives, topics related to ownership or that exclusively concern the partners 🕮 – for a clear distinction between topics related to the interests of the company and those of the controlling shareholders.

In some cases, the interests of the family may be different from the needs of the company, and these issues need to be addressed by the controlling shareholders. In these cases, the committee may analyze specific issues and propose solutions.

The partners committee brings together representatives of the controlling groups or the different family branches, as appropriate, and can be composed of several generations. The attributions and composition of the shareholders council will be more or less comprehensive, depending on the size of the company and the number and diversity of

🕮 Brazilian Corporate Governance Institute (IBGC), *Governança da Família Empresária: Conceitos Básicos, Desafios e Recomendações*, IBGC, São Paulo, 2016, p. 33 (Cadernos de Governança Corporativa series, n. 15). Available at: <https://conhecimento.ibgc.org.br/Paginas/Publicacao.aspx?PubId=22057>. Accessed on: October 9th, 2019.

partners. The body will have an advisory or decision-making role.

The membership committee tends to be an important instrument, when combined with the membership agreement, and can play an essential role in the analysis and alignment of relevant issues that will be deliberated at the membership meeting. If the membership committee has only an advisory character, it will become an appropriate forum for the development of future members by working on the relevant issues that will be debated at a membership meeting or other appropriate body.

Box 7 – Questions to Move Forward with Succession

- **Leadership** – Who can lead the business from now on? Who should nominate this person? Is the current leader ready to transfer leadership?
- **Ownership** – How will the business be controlled? Should owners always be involved with the company? How will owners be secured after leadership is transferred? What about control?
- **Legacy and value** – What are the family's values? Do current owners trust that the next generation will honor those values?
- **Wealth transmission** – Are there plans about how wealth will be defined among family members (participations in the company and other assets), whether in life or after passing?

7

Final Considerations

The business challenges in a family firm are similar to those of many other companies–small, large, listed or not–in which the permanent agenda involves answering questions such as: What should we do to ensure competitiveness, differentiation, and innovation over time? How to achieve consistent economic and financial results? How to have an engaged and motivated team that makes a difference? How to build customer loyalty? The systemic approach to these challenges is done mainly through corporate governance.

However, in the family business, an immense number of emotions and interpersonal relationships between shareholders, heirs, family members, and business managers are added. Throughout its life cycle, an extremely sensitive and neuralgic link is the succession process–understood as every change in the range of relationship, power, and control structure between shareholders, heirs and other corporate governance bodies, involving the dimensions of family, ownership, and business.

As we have seen, succession is not an event, but a process that requires organization, planning, care, affection, and, above all, time. Traditionally, founders may tend to postpone the start of this process, which should happen while they are still in full physical and intellectual vigor, enabling them to outline the future of the company and the family as well as to adequately prepare successors, tracing fiscal strategies and renegotiating the governance of the family and the business.

Succession in family firms is primarily about people. Although there is logic and technical guidance for succession, people (family members and others impacted) react in a unique way to the processes of change, in their own time and with their peculiar perception. Therefore, we emphasize the need to integrate technical and legal aspects to the socioemotional aspects in order to reach a good conclusion.

We talk about preparing new leaders for the rite of passing the baton, which involves emotions, aspirations, fears, competition, and another myriad of feelings that cannot necessarily be overcome by logic and rationality.

We emphasized the importance of planning and highlighted some of the main challenges to conduct the process in the dimensions of family, ownership, and business–both from a technical and inter-relational point of view (family-family; family-ownership, and family-business).

We explained some of the facilitating pillars of the process, such as the definition of the family's aspiration for the future with the business and what role the family will play and the relationship it aspires to have with the business and society, in its attributions as shareholder-citizen.

To have a long-lasting family business the family needs to be united and aligned around what is essential. This alignment can be strengthened with the creation of a family council, with a family protocol, with the formalization of a shareholder agreement, and with the definition of the family's vision of the future and the relationships it aspires to have between the family itself and with the business, among others.

People who build a family business legacy have a rare type of competence and sense of entrepreneurship, and may even have the aspiration to transcend, which, if conducted well, can create long-lasting value not only for the family but also for society.

Finally, the generation that is in charge of the business needs to be very clear about whether they want to just pass on an asset or leave a legacy. Many leave the heritage as the greatest asset; others go further: they leave for future generations the lesson and the missions of a lifetime. This subtle difference can determine how far each business family will go over time.

8

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Like the Moiras, who created the destiny of gods and humans, the family must unite and weave its own rules of succession, organizing and planning the lines of its resources in order to promote the preservation of the family's emotional and material assets, avoiding disagreements and dissatisfactions.

The Moiras were always respected by all mortals and even by the gods, because it was believed that if a god dared to transgress their laws, this would disturb the cosmic harmony. Scholars say that this myth justified the need to strengthen the character and individuality of people, because when the three sisters determined the destiny of an individual, it was up to that individual to accept it and face it as a means of developing his or her character. Otherwise, it would weaken their spirit. In the same way, it is hoped that the lines drawn in the succession planning will maintain the family's balance and, consequently, the family business, strengthening the character and individuality of its members.

Awareness, mediation, and alignment of family members to debate succession, as well as implement and monitor good practices of corporate and family governance are the basis of the processes carried out by our office to promote the convergence of family members and the perpetuity of their emotional and material assets.

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