

SAVED BY THE BOARD

In an era of increased focus on the independence of corporate boards, **Dennis Jaffe** looks at how the family business can benefit from outside advice. It's not all about losing control – an effective board could spell the difference between success and failure



Irwin Jacobs, a visionary engineer who created the internal workings for many of today's cell phone networks, founded Qualcomm in 1985. It has since grown to be a public company with US\$5.7 billion in annual revenue. Irwin's equally brilliant son Paul, now 42, joined the company in 1990, after earning his PhD in robotics with the clear expectation

of becoming his successor. After a mixed career in various entities within the company, this year he was named by the Board as CEO.

Sounds like a familiar family business succession path, with a predictable outcome. But the family owns only 3% of the company, and it was the board, not Irwin, who appointed him. Eyebrows can still be raised, as an image of the board as 'friends of Irwin' comes to mind. But in an era of increased focus on the independence of corporate boards, the choice of Paul can be considered an informed one. Of course they took into account the continuity of passing from father to son, but they also spent years overseeing Paul's performance, and also looked at other candidates. It cannot be considered a rubber stamp, and the board will now carefully monitor his performance.

A few years ago, at a similar family company – Motorola – the board reluctantly decided to remove third generation heir Chris Galvin from the leadership after some severe business reversals, and gave the reins to Ed Zander, a talented Silicon Valley executive. While both boards were keenly aware and respectful of the family's heritage and leadership of the company, by their behaviour, they acted judiciously and came between the family and the business, to do what was right for the company.

Such behaviour should be expected at every publicly-held family business, with independent directors exercising oversight over the wishes of family members. But what is the role of the board at a closely-held family business, where there is no requirement for outside directors? Increasingly, an independent board is

being seen as a resource for a family, not a burden. A good board can help the family let go of residual bad habits due to family needs taking precedence over business realities, and allow the company to grow and develop.

The emergence of a board can be viewed as a key developmental stage of a family business. In its first iteration, the board consists of the family managers. They may even include a family member who doesn't formally work in the business – say the spouse of the founder – but who is deeply engaged in business decisions. As the second generation of a business approaches, or as a business grows and thrives, the family owners may not see the need for a board. Since they have all the control, why do they need one, or why should they want someone to look over their shoulders? They are doing just fine.

There are several reasons to think about creating a board when the business is successful. First, differences emerge within the family. There may not be a single potential successor, but rather more than one sibling, and even some non-family candidates. Family members may see the business as a prize to be fought for and won. Family politics can turn to infighting with attention being taken off the business and its environment.

Second, every management team develops blind spots and bad habits. The tenure of a CEO is usually shorter than the CEO would like. The founder may not be interested in envisioning succession in his lifetime, and the next generation certainly can't bring up this issue without seeming disloyal. Or, the next generation family managers may not really be able or willing to do their jobs, and nobody within the company can give them feedback. A culture of mediocrity or self-satisfaction may mask business challenges.

A board consisting of the family members most attuned to the environment, with several independent members, can become 'the voice of the business' and challenge the family, in a tactful and respectful way that can achieve results. A board has the potential of coming between the family and the business, and between family members and generations, and mediating challenges that would otherwise not be addressed. A good board, with wise independent members, may form a 'neutral zone' where family members can face their differences, look at challenges and make difficult decisions.

A GOOD BOARD IS A PRICELESS SOURCE OF VALUE FOR A FAMILY COMPANY AS IT GROWS AND DEVELOPS



Sailing ahead: Motorola's non-family Ed Zander was a wise board decision

A board asks the business leaders to stand back and define and clarify their strategy and reflect on major choice points. It looks at financial results, asks probing questions and challenges thinking. As we saw above, it makes selections of key leaders, holds them accountable, and defines their compensation. In most family businesses, these are very tendentious areas. And finally, there are informal things that board members can do. They can mentor young family members as they move into leadership, and even sometimes counsel them out. They can talk to dissident family members and help them understand the limits of their power as a family owner, or the wisdom of their policies. They can mediate conflicts between different family factions. Only a board that has the requisite gravitas and standing with the family can do this.

The devil is in the details, and while families see the virtue of having such an entity, they tend to find it hard to set up. The first person who must accept the need is the founder/owner/leader who wonders why he or she should give up their total control? The way to convince them is to suggest that while the board can challenge the company and the family, in fact, the board is appointed by the family. If there is a crisis and the family owners feel a board member is not effective, they can remove that director. So, when planning to install a board, the owner/manager does not lose formal control. What he gains, is good counsel.

A second issue is how to initiate the shift from a family only board. A first step is to look for potential independent members, who are usually elders in the community – people who have run their own family business, or who are prominent in the industry. While family advisors sometimes are thought of as potential

board members, it may be best that they remain as advisors. After all, the family already purchases their advice, so it would be redundant to make them directors. Potential advisors should be knowledgeable about areas of business relevant to where the business wants to go (for example, from a larger company that the family envisions becoming in the future), who have the time, and are willing to do the work. It is helpful for the family to start not with one but with a pair of outside advisors. A good board for a large family business should have a narrow majority of non-family directors.

A related issue is that of family representation. The family may be used to having most if not all family owners on the board. Over time, this can become unwieldy. Some family members, though owners, just don't take the time, or have the capability, to be directors. The family should transition to a process where the family selects a group of family members who represent the whole family. The family board members, sometimes also with the independent members, should then schedule periodic joint meetings with the family owners, to hear their concerns and share information. These are much like the annual shareholders meeting of a public company, but hopefully more informative, open and collaborative.

Having a good board is just a first step toward using it wisely. Board meetings should be frequent enough that they can keep their eye on relevant changes, but not so frequent that they become quasi-managers. Sometimes a family business board can become over-involved and not allow the management team enough autonomy. Meetings can be quarterly, or twice a year, in most cases, unless there is a major crisis or transition.

Recent writings on boards have noted that the mere presence of a board doesn't do much for a company. The board must be a forum for debate and exchange about the relevant issues. The board members have to arrange to spend some non-meeting time with the company leaders, and become informed in key areas. The meetings have to be arranged so that the family leaders take the time to assemble the relevant data in time for the board members to look at it, and then take the time in the meeting to talk about issues, not have a lecture by the family leader. In many boards the exercise of making a case for the board, and gathering data, is a deep learning experience for young family executives.

A good board is a priceless source of value for a family company as it grows and develops. It serves as a buffer to help the family – who may avoid the most difficult issues – to address what is important. It brings in business knowledge from experienced people who could not be hired as consultants. It helps the family leader see his or her blind spots, and begin to make plans for the next generation. While a family business can succeed without such a resource, as a business faces the dual challenges of separating from the family, and thriving in a complex business environment, developing a board of directors can spell the difference between success and failure. It becomes an open window, bringing fresh air into the family enterprise. ■

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