

Family business succession planning: East versus West

Christian Stewart reflects on some of the differences between the way that overseas Chinese families in Asia tackle succession planning and family governance, and how this might differ from an 'American' approach.'



ABOUT THE AUTHOR

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This article reflects on some of the differences between the way that the overseas Chinese families here in Asia tackle succession planning and family governance, and how this might differ from an 'American' approach.

This article is necessarily an attempt at generalisation. What it ignores, of course, is that every country within Asia has its own unique culture and context and that every family is different, having a different family culture and its own unique family dynamics.

Crossing the road alone

In the US, if you were a wealthy individual, you would not walk across the road without taking your lawyer and your tax advisor and your accountant and your therapist with you!

The Chinese business family may not have any of these professional specialists. The wealthy Asian businessman will walk across the road on his own, or if he takes any one with him it is likely to be some family members or a trusted lieutenant.

One reason for a lack of professional advisors can be the desire for confidentiality. A wealthy Asian family may not want to disclose details of the family wealth to a local advisor in their home country.

It is a totally different culture in Asia in terms of the use of external professional advisors, and this must have some impact on the succession process.

Unscrambling the egg

Most Asian families do not have a family shareholders agreement or other form of 'exit plan' in place. This might be one example of the impact of a culture where there is generally an absence of professional advisors.

A more likely reason, however, is that the first generation founder might have a certain vision or dream of all of his or her children owning the business together and working together to continue the family business in the future. It might not be acceptable within the family to question the feasibility of this vision or dream, and as such any talk about shareholders agreements or the possibility of family members exiting is perceived to be too sensitive.

This is an attempt to explain the typical absence of family shareholder agreements and exit plans; it is not say that Asian families do not need these agreements. An Asian family that can talk about the need to put in place an exit plan today to provide for the future, is going to be much better off than one without such a plan.

I am a big believer that this is one 'American' approach that should be adopted in Asia.

Feeling like you are on the outside trying to look in

It is also uncommon in Asia to see the

creation of one class of voting shares in a family company, and a separate class of non-voting shares (albeit shares that still participate in dividends).

Where these arrangements are implemented in the US, the voting shares would be given to those heirs who are managing the business (the 'insiders') and the non-voting shares given to the 'outside shareholders.'

We also do not make use of 'voting trust' arrangements in Asia (essentially an agreement that vests control of the voting rights in the hands of a select committee).

A matter of trust

Also note there are differences in the way that trust structures are used in Asia, in comparison to the US. Trusts are often used in the US for specific domestic tax mitigation purposes. It is quite common in the US to make use of individuals to take on trustee roles; and even bank trustees seem to have a different take on fiduciary risk when the trust is holding domestic US assets.

In contrast, in Asia, trustees tend to be bank affiliated trustee companies and trusts tend to be set up for non-tax reasons, such as: succession planning and to ensure that there is a nest egg for the family should things go badly wrong in the home country.

If you did have a family business in Asia owned under a trust structure, while it would likely have a bank affiliated trustee company as trustee, if you looked closely at the documentation, you would see that the

trustee was not responsible for exercising the voting rights on the shares in the family company. Instead there would be a 'management committee' or a 'protectors committee' that had the right to exercise those voting rights.

So in Asia you might end up at essentially the same place: the 'insiders' controlling the decisions by being the members of the management committee; and the 'outsiders', with no direct voice in how the shareholder decisions are made, albeit able to receive distributions, through a slightly different legal mechanism.

Whatever the exact form of the legal mechanism though, there is a danger with these types of legal arrangements. A family that uses a trust structure or a class of voting shares to give legal control to the 'inside' family members is going to be less sensitive to the differing perspectives of inside versus outside 'shareholders' or 'stakeholders' and is therefore less likely to do any of the real work necessary to address these differences.

Giving the 'insiders' a way to control all of the voting rights is a dangerous strategy for a family to adopt unless the family also sets up the necessary forums and processes to give the 'outside' stakeholders a voice and to address the differing perspectives of these two groups.

'This is how my father did it and this is how I am going to do it'

Second generation Chinese family businesses in Asia are likely to have little to no formality around the process of bringing the third generation in to work for the family business. Asian families do not prepare 'family employment policies.'

If you speak to a second generation family member it is common to hear them say 'this is what our father did for us, why shouldn't we do the same for our own children?'

Having a written family employment policy is a second 'American' practice that would make a very positive difference for a Chinese family here in Asia.

A different approach should be taken for dealing with the entry of the third generation into the business. Circumstances for a member of the second generation (a child) coming and working for the founder generation (their parent) and entering a 'founder controlled business' are going to be very different from the scenario where you have a

member of the third generation coming and working for a sibling partnership.

Firstly, as they say, siblings grow up under one roof and cousins do not. Secondly, in the second generation, it is also relatively common to see all of the siblings (or all of the male siblings) working together in the business (i.e. every one in the second generation is on the 'inside'). This is unlikely to be the case for the cousins' generation.

Finally it can be very hard for a parent in the second generation to put aside their 'dad' or 'mum hat' when it comes to looking at the strengths and weaknesses of their own children as compared to their nieces and nephews.



Acting as a bridge

In a Chinese family business in Asia there is often a very large communication gap between the first generation founder (in particular the father) and the children. In practice it is very common to hear second generation family members explaining they are not able to talk to their father (or mother) about succession issues. This is a cultural factor.

In Asia, I believe that sometimes there is merit in an advisor or other third party (for example a trusted non family director) acting as a 'bridge' between the senior founder generation and the next generation, to help overcome the communication gap when it comes to succession issues. This is a way of getting things done.

An American advisor to a family would consider this to be an inappropriate way to work with a family. The advisor acting as a 'bridge' actually impedes good communication between the two generations. However, I think the gap in some Chinese families in Asia can sometimes be so large that they will never close it on their own, and either

a third party helps to facilitate, or many crucial succession questions will never get discussed.

Please don't shoot the messenger

Chinese families value privacy highly; they are often inward-looking in their orientation, and are often not keen to rely on outsiders. However, a family might ask an outside advisor to come in sometimes if they want to have a third party deliver a message to another family member. They want to maintain family harmony and avoid conflict, so the third party advisor is brought in to say what they cannot say themselves. In this case the advisor has to be very careful not to get caught in this kind of triangular situation. The advisor has to keep in mind that his or her client is the family system as a whole.

Firing the boss

I recently heard a story about an experienced US-based family business advisor who had been brought in by an American family to deliver the news that the 'old man' had to step down. The advisor's job was to tell the founder that: 'he was more of a liability than an asset to the business.' So even American families try to triangle-in their advisors. Of course this would never happen to an Asian family. In an Asian family there is no such thing as firing the founder.

Don't forget the matriarch

In the literature on succession in Chinese family firms there is a lot of talk about the power of the male Chinese business founder, both in the family and in the business. In practice though, don't forget the Chinese matriarch, especially the surviving spouse, who can also wield considerable power. The surviving wife of the business founder can often be seen to be providing the 'family glue.' In Hong Kong there was a recent, public example of the power of the matriarch. The surviving wife and mother of three sons stepped in and resolved a very public family dispute by asking the oldest son to step down.

Keeping secrets

Finally, another cultural difference between Western families and families in Asia is that in a Chinese family it is probably more acceptable to keep secrets about money and wealth from the rest of your family. To a Western family this degree of keeping secrets might be regarded as quite harmful to the family system. ■