



How to Craft your own Family Constitution: An Overview

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What is a Family Constitution?

“A family constitution is a living document.”

It is often said that successful families, especially those that jointly own a business or financial wealth together, are like “small countries” and just like countries, they need to have their own “constitution” and “rule of law” if the family members are all to live in harmony together and if the family is to continue to be successful. The family members – or their appointed representatives - make “laws” in the form of more detailed family policies and agreements, following the processes defined in their constitution. In simple terms these family policies define the “rules of the road” for the family with respect to its relationship to the family business.

Another explanation is that the successful preservation of family wealth across generations ultimately comes down to having the best possible process for joint family decision making. The essential purpose of a family constitution is that it sets out a fair process for making joint decisions together as a family. Therefore a family constitution is a decision making tool. A tool intended to help the family to stay together and to stay wealthy for more than three generations.

A third way to introduce the concept of a family constitution is to point out that all families, especially those that work together or own assets jointly together, have their own natural way of making decisions together and of communicating together; it is just that these informal, family system based rules and processes are not sufficient to deal with the increasing complexity of owning & managing a business or other wealth together successfully, especially once the family reaches the stage where not everyone who is a shareholder is involved in the management of the business. Therefore the rules of the “informal family constitution” that every family starts with need to be brought into consciousness, examined and modified and a new set of rules articulated, agreed upon, and written down.

A family constitution would typically articulate the mission vision and values of the family and important principles for working together or for governing and managing the family business.

It could also include a description of the composition and role of the “family council” – a family representative body - and how the family council makes decisions. It could include a description of the other governance structures that go to make up the family business - or the wider family enterprise if you include reference to the family foundation and the family financial investments or possibly to a “family office”. Importantly in Asia (if not everywhere) it is advisable that in addition to referring to a “family council” there should also be reference to “family elders” or a “committee of family elders”.

In summary, there is no fixed definition and there is no one way to develop a family constitution. Indeed a family constitution can best be thought of as a “living document” and one that should evolve naturally over time. For some, their “family constitution” might simply start off as comprising of a collection of key written family policies.

Before having a look at the topic of the process for crafting a family constitution, we should briefly address the question of what are the benefits of having a family constitution? There are actually two dimensions to this question. First, you should ask, what are the benefits of going through the process of creating a family constitution? Then secondly, what are the benefits of having a formal written family constitution (and family policies)?



What are the benefits of going through the process of creating a family constitution?

“The process is more important than the written work product.”

- It can be fun. It can strengthen family bonds and family unity.
- The process can help to include or involve family members or family branches that have not had a role to play or that have started to become distant from the family business. The process therefore helps to re-build “emotional commitment” to the family business.
- It usually helps to improve family communication and problem solving and conflict resolution skills.
- Ideally it should help to improve the level of individual self-awareness within individual family members.
- It makes the family members think about how they need to develop and what new skills they need to learn.
- It provides an opportunity to talk about and to plan for the future. Often without a structured platform to have such discussions, families tend to avoid such important but difficult conversations.
- It provides an opportunity to talk about the process by which the key task of succession is to be addressed.
- It helps to bring the family members who are managers, and those who are shareholders onto the same page together.
- It helps to define the different roles that exist within a family business.
- It helps to define the boundaries between family issues, ownership issues, and management issues.
- It provides an opportunity to look at the question of Board composition and leadership.
- It provides an opportunity to see if the next generation of family members will be able to learn how to work together – or not.

What are the benefits of having a formal written family constitution?

“The palest ink is better than the best memory.”
A Chinese saying

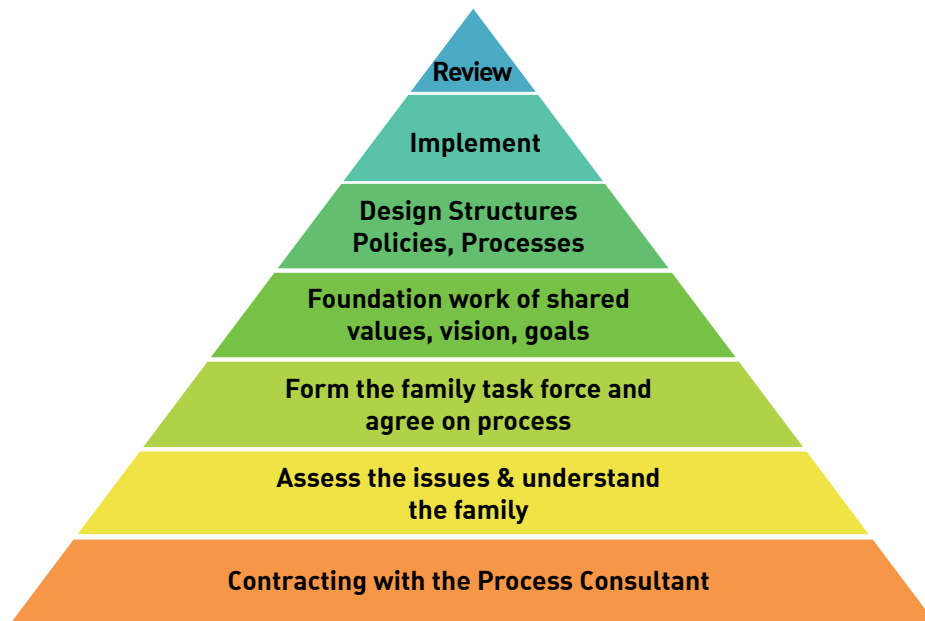
As mentioned above, the key benefit is that the constitution provides the family with a fair process for making joint decisions together, a decision making process that has gained widespread family support. In addition:

- By clarifying roles, this helps to avoid role conflicts.
- By providing forums for discussion of family and ownership issues, this prevents such issues from exploding in the wrong forum.
- By providing an “exit mechanism” this provides a way to “let off steam”.
- Having things in writing helps ensure family members are all on the same page. It prevents misunderstandings.
- The family constitution will normally include a process for dealing with family conflicts. Families that have defined their own process for managing family conflicts will have a much better chance of surviving than those that do not. Having a conflict resolution process will also ensure that when conflicts do occur, that they are raised and dealt with, rather than avoided.
- With respect to family ownership the constitution helps to keep the ownership united and to forge family commitment to the future of the business. Over time “ownership is more important than management” so defining the ownership role is a key task.
- In a family business, having a fair process is often the only pathway that enables difficult decisions to be made that the family members can accept.
- Finally it is about much more than just preserving family financial capital (or the business). If proper effort is put into the process, a family constitution helps to keep family peace and harmony, preserve family relationships, and protect family traditions.



How do you Craft your Own Family Constitution?

The purpose of this white paper is to outline a step by step conceptual process for creating a tailor made family constitution for a business owning family in Asia. The following diagram provides an overview of this process. The pyramid is used to show how later stages are built upon the foundation of the earlier stages. The starting point is at the base of the pyramid.



The following points can be noted about this conceptual process.

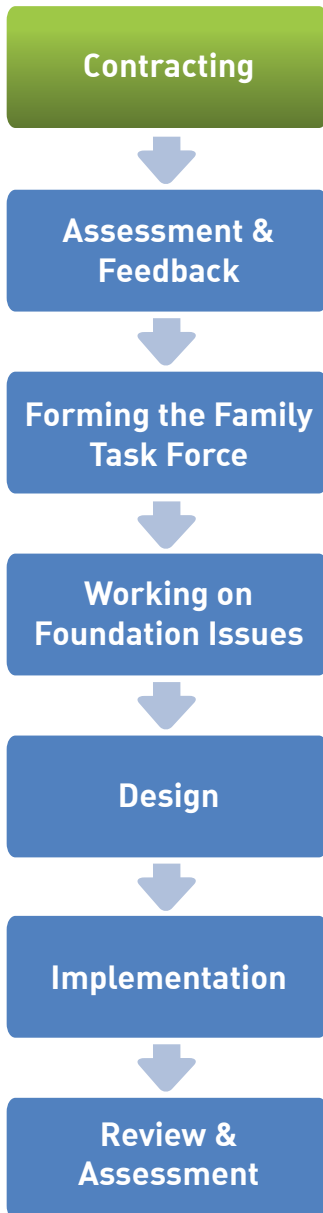
- i) With the exception of the Assessment phase described below, the main vehicle for driving this process forward is a series of family meetings, ideally with work in between family meetings being carried out by those family members who are responsible for driving the project.
- ii) There need not always be a direct correlation between the steps in this conceptual process and what is happening in “real time”.

For example, one step in the conceptual process (say, agreeing family meeting rules) might take 2 hours to cover as part of a one day family meeting. At the other end of the spectrum, another step in the conceptual process (say, agreeing on goals and a vision for the future) might require several separate family meetings before the family are ready to move ahead.

- iii) The conceptual process that is described here is a generic framework the content or direction of which needs to be adjusted for the specific family, taking into account the issues that are important to them. There is always the key principle to follow that the family should decide on their own process, content and direction of their family constitution. The more the family “do their own work” on the constitution, the more likely they will integrate and accept the family constitution into their decision making processes.



Phase One: Contracting



Most families find that it is critical to work with a “process consultant” who can help advise on the process of creating a family constitution. This is because creating a family constitution often involves examining and changing the ways in which a family relate and work with each other. To do this the family needs to find a way to suspend their natural decision making processes. This usually requires the help of someone who is not part of the existing family & family enterprise system.

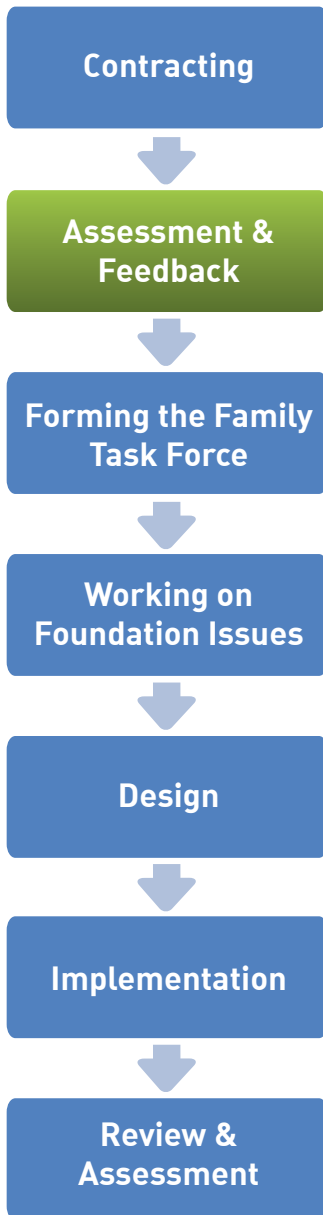
Another way of explaining this is that to make a family constitution, the family members need to be able to communicate with each other, about important and often difficult issues. Family members need to be able to “listen with empathy” to each other, and communicate directly and honestly. In a family, and especially in one that works together, family members often do not communicate exactly what is on their mind, for fear of hurting other family members’ feelings, or out of respect. Involving a neutral outside party as facilitator, makes it possible to raise difficult issues in a safe environment.

Contracting refers to the process of engaging with the external process consultant. A process consultant is different from an “expert advisor”. A process consultant will work with the family to let them understand their options for how to structure the process, but should be cautious about telling the family members “what to do”. When making a family constitution, the key factor is the discussions that the family members have, and that the solutions the family members design are their own. A process consultant will also be responsible for guiding the family members through the change process that creating a family constitution often involves.

Key issues in engaging with the process consultant will be to understand how the consultant works, the values and principles by which the consultant works, whether there is a good “chemistry” between consultant and family, and the experience and skill sets of the consultant. One critical skill set of the consultant will be the ability of the consultant to “listen with empathy” to the family members.



Phase Two: Assessment



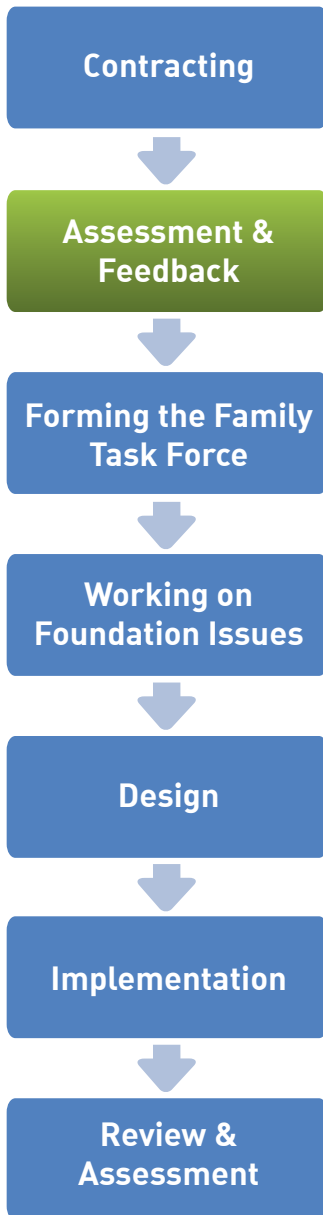
The second step in the process is the assessment and fact-finding phase. Assessment involves the external consultant having one on one interviews with the key family members. It can also be considered whether it would be advisable to talk to any senior non-family managers and /or directors. The information from these interviews is usually kept confidential by the external consultant. The purpose of each interview is to gather facts and information. Minimal advice or feedback should be given to the family members during the conduct of these confidential one on one interviews.

- i) The objective of the assessment process is to give the consultant a feel for the family system and the family culture. Given that a family owned business is one where there is a significant overlap between the family system and the business system, it is critical for the consultant to have some feel for what the family system is like. If you are a member of the family, it is very hard for you to see what the culture of the family is objectively like.
- ii) Assessing the family system will normally include looking at communication, and how decisions are made; listening for common family messages; and listening for shared family values. In some cases, the family culture might suggest taking one particular direction rather than another, as the family works together to develop the family constitution.
- iii) The one-on-one interviews helps the external consultant to appreciate the issues that are unique to the family.
- iv) The one-on-one interviews also provides the external consultant with an opportunity to identify if there are key issues that should be put on the agenda as the process moves forward.
- v) The one on one interviews provide the external consultant with an opportunity to see whether there appears to be a goal of business continuity that is shared by both the senior generation and the next generation.
- vi) The process of giving each key family member the opportunity to tell his or her own story, in a safe environment, to a neutral party who is focused solely on listening to the story teller with empathy, is actually an important step in the process of starting to improve the family teamwork and dynamics.

It is normal that every individual in a family business will have their own slightly different perspective on what the business is like and what the important issues are. When the one-on-one interviews are finished, the external consultant has to sit back and look at the totality of the information presented to form an impression of the family business system. The objective is for the external consultant to look for big picture issues and recurring themes; to see the forest not the trees.



Phase Two: Assessment



Review Basic Family & Corporate Information

During the Assessment and information gathering phase it will also be necessary for the external consultant to have a look at the basic family information (e.g. family tree) and corporate information such as the current share ownership arrangements and the current holding company structure and board role and composition.

The existing corporate governance structures and processes need to be considered. The process of creating a family constitution is not going to be a process of creating governance out of thin air. There will be existing governance arrangements in place. So it is more a question of examining the existing arrangements, and seeing if they should be continued or modified. It could be said that an important aspect of the process is making the governance arrangements explicit. It should also be considered whether there is an existing strategic planning process in place for the business and what this involves, and who is involved in it.

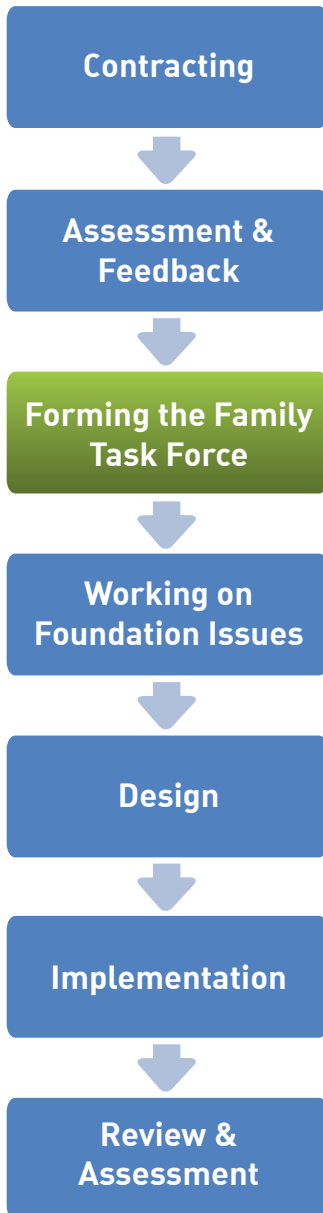
Feedback After The Assessment

There are several alternatives for making use of the information from the Assessment and fact finding phase. A process consultant will discuss the exact way for handling the feedback with the senior generation of the family:

- i) First, the information from the assessment phase will be important information for the external consultant to understand when working with the family. In this case the information is just used as background information for the consultant so he / she has an idea of the unique family system.
- ii) Second, the information gathered can be used by the external consultant as the basis for preparing the agenda for the family meetings that follow. In this way the issues raised by the family members are then discussed by the family members at a series of family meetings.
- iii) Third, the feedback could be sent to all of the family members and then presented for discussion as part of the first family meeting. This is a common approach. In many cases once a written feedback report is delivered to a family, it starts the family members discussing issues among themselves and can be the catalyst for helping the family to resolve issues that they may previously have been struggling with.
- iv) The final alternative is for the information to be presented as a written report which is only given to the senior generation of the family. However this last option is unlikely to be as effective as the case where the feedback report is provided to all of the family members.



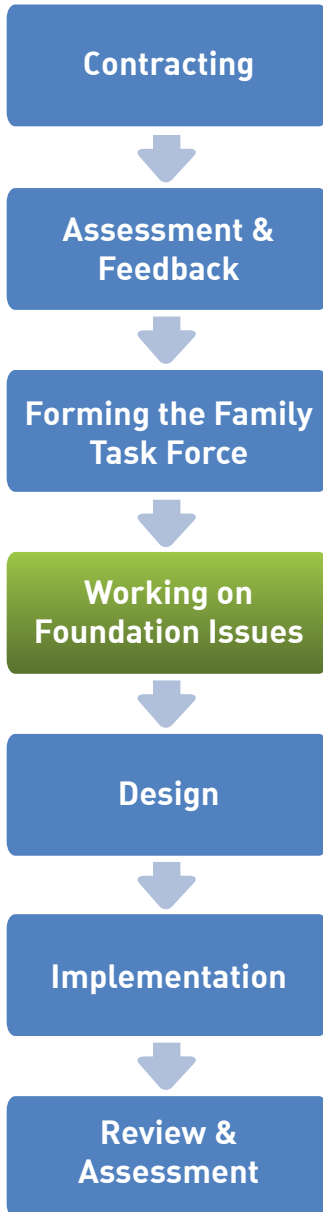
Phase Three: Forming The Family Task Force



Conceptually there is a step of forming the family task force and agreeing how the family task force is going to proceed and make decisions. This involves deciding and agreeing on the process for the family meetings that will follow. In practice it is well worth it to invest the time on forming the working group (task force) and on process issues before getting into the substance of the work.



Phase Four: Foundation Issues



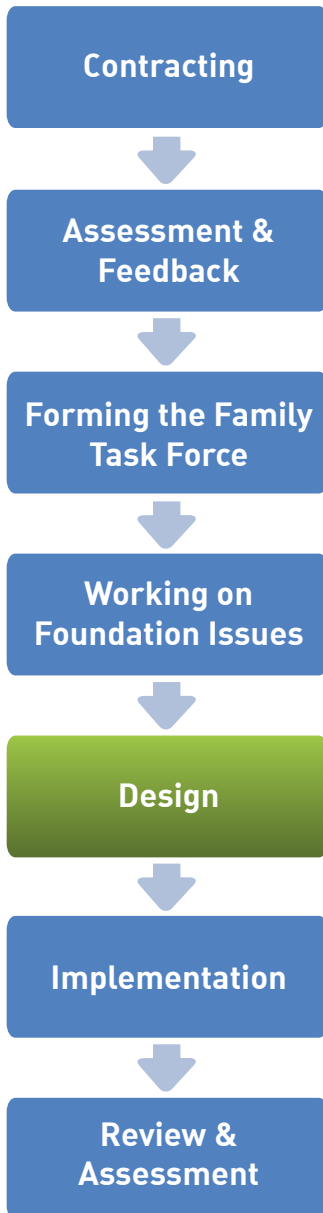
“Would you tell me, please, which way I ought to go from here?”
“That depends a good deal on where you want to get to,” said the cat.
“I don’t much care where,” said Alice.
“Then it doesn’t much matter which way you go,” said the Cat.
Lewis Carroll, Alice’s Adventures in Wonderland, 1865

The next phase in the process is to spend time on “foundation work”.

There needs to be a clear sense of what the shared goals and direction of the family are before it embarks on the process of designing its family governance arrangements and its family constitution.



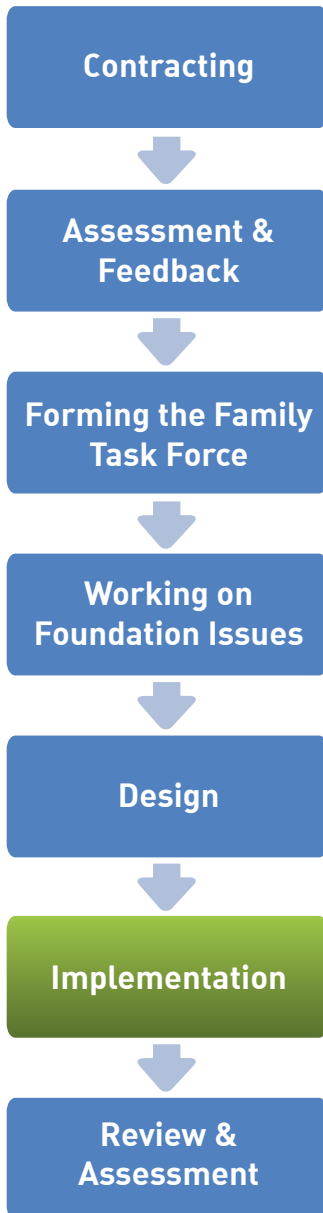
Phase Five: Design



When it comes to the Design Phase, the goal is for the family task force to decide on what is to go into their family constitution and what type of governance arrangements should be in place for their family business. The key philosophy is that the family should make their own rules. There are various different ways of designing a family constitution.



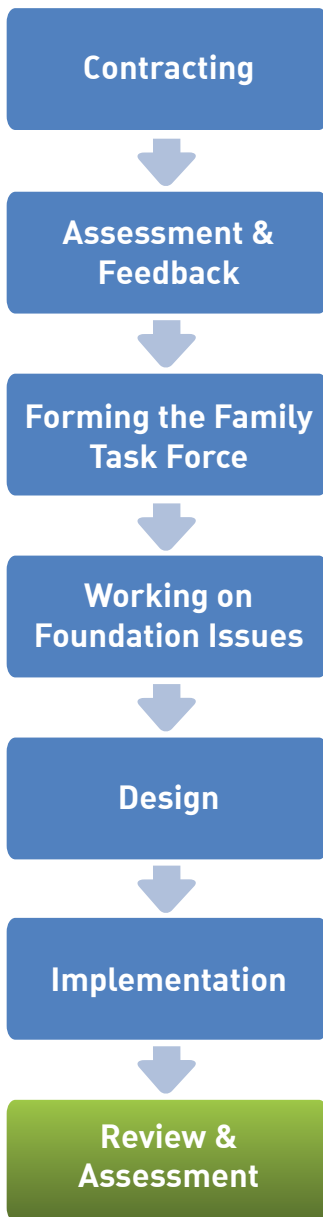
Phase Six: Implementation & Establishing Ongoing Processes



Once the Design phase is completed, the Implementation Phase refers to putting into practice the ongoing governance structures, processes and policies that have been agreed upon. At its simplest this might be a question of starting to schedule and hold family council and/or ownership council meetings.



Phase Seven: Ongoing Review & Assessment: The Annual Family Meeting



The final phase is for the family council to institute the practice of holding an annual family meeting where they review (i) the effectiveness of the family governance arrangements and objectives, (ii) how the family rank themselves against “best practices” and (iii) how the family is going in terms of completing any tasks that it had set out to work on during the year.

This annual review and assessment practice frames the work on the family constitution as an ongoing process for the family. It is important to appreciate that to have effective family governance, “there is no finish line”.



About Christian Stewart



Originally a tax and trust lawyer from South Australia, Christian moved to Hong Kong in 1994. In July 2008, he formed Family Legacy Asia to provide independent advice to Asian families on family governance. In this role he acts as a process consultant to help family businesses in Asia work together, through facilitating family meetings and helping the family to prepare their own family policies and constitution. He also advises several Asian Family Offices on trust and succession matters. He acts as an advisor on several Private Trust Company structures.

Prior to founding Family Legacy Asia Christian was a Managing Director and the Head of Wealth Advisory in Asia for JPMorgan Private Bank for 6 years. In this capacity he was responsible for representing JPMorgan's trust business in Asia.

Prior to joining JPMorgan, Christian was with Pricewaterhouse Coopers in Hong Kong for 7 ½ years. At PwC he became a Partner in their Tax Practice specializing in Hong Kong estate duty planning and trust structuring, and he ran their Trust & Private Client team.

Acknowledgements

Much of this white paper relies upon the work of Barbara R. Hauser (author of International Family Governance, by Mesatop Press) on family constitutions and of James E. Hughes Jr. (author of Family Wealth; Keeping it in the Family, Family, the Compact Among Generations, and co-author of The Cycle of the Gift, all published by Bloomberg Press) on family governance in general.



About Family Legacy Asia

We work with successful Asian families to help them establish communication platforms and decision making structures for both the family and the family enterprise.

We facilitate family meetings to help the family talk about their vision and values and the relationship between the family and the family enterprise. We help them to create the “rules of the road” so that family members know what to expect in the future.

We believe that the key to passing on a successful family enterprise that will flourish for at least five generations comes down to the way in which the family members make joint decisions together, and this is called family governance.

While our approach is tailored for every family, we often use the process of creating a family council and family constitution to help build the “family team”, to strengthen family unity, and to help the family resolve the specific issues that they have been unable to resolve on their own.

The process of creating family governance is a problem solving process.

Our process can help simplify the challenges of planning for family succession.

One of the benefits of our process is that it helps to build a bridge between the older generation of the family and the next generation.

Another benefit is that we help create tools for the family to balance doing what is good for the family with doing what is good for the business.

In many family controlled enterprises, family conflicts arise because of confusion between family roles and values on the one hand, and business roles and values on the other hand. We help families avoid these kinds of conflicts.





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