

FAMILY BUSINESS REVIEW



# Research Applied: FBR Précis for *FFI* *Practitioner*

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## From *FFI Practitioner*

Thanks to Alberto Gimeno of the *FBR* Research Applied Board for his thoughtful précis of “Family Constitution and Business Performance: Moderating Factors” – an article that appears in the December 2017 issue of *FBR*. This article and the related précis draw on the actual experience of advisors and families that have instituted family constitutions and what the results have been.

### Introduction

Family constitutions are one of the most—if not the most—used instruments to manage relationships between family and business within the family business context. Essentially, as its own name indicates, family constitutions define explicitly the “rules of the game” between family and business. Family constitutions have the same impact in families as constitutions do in countries. Therefore, this entails that order is not just created by the authority of a dominant person or alliance of persons, but it also takes into account the “rule of law.”

Constitutions clarify expectations so that everyone knows what can be done and what cannot and under which conditions (e.g., access to specific post or dealing with ownership rights). Having these parameters delineated makes the behavior of family members and family businesses more predictable and, consequently, more stable.

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“A CONSTITUTION REPRESENTS AN  
IMPORTANT CHANGE IN MOST  
BUSINESS FAMILIES’ BEHAVIOR,  
BECAUSE IT SETS AN IMPORTANT  
LIMITATION IN DECISION-MAKING  
DISCRETION.”

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Constitutions can help hinder problems in the family business such as nepotism, because such behaviors become more obvious if they are not only explicit, but written. Making them explicit helps to avoid them.

Arteaga and Menéndez-Requejo, the authors of this paper, make an important contribution by studying how family constitutions affect business performance, something that has not been studied until now. To frame the research, the authors conducted interviews with six consultants who specialize in family constitutions in Spain. The section of the paper entitled Exploratory Interviews provides an interesting overview of family constitutions and the outline and process the consultants follow to establish a family constitution.



**SIDEBAR**

**Family Constitution and Business Performance: Moderating Factors**

Read the full article mentioned in this précis that analyzes the relationship between implementing a Family Constitution (Protocol) and future family business performance.

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Then, the authors rigorously studied to what extent business performance increased during the two years that followed the implementation of a family constitution, using solid statistical methods with 530 Spanish family businesses—265 firms that implemented a family constitution and 265 firms that did not.

## Findings

The results of the study show evidence regarding the following main relevant findings:

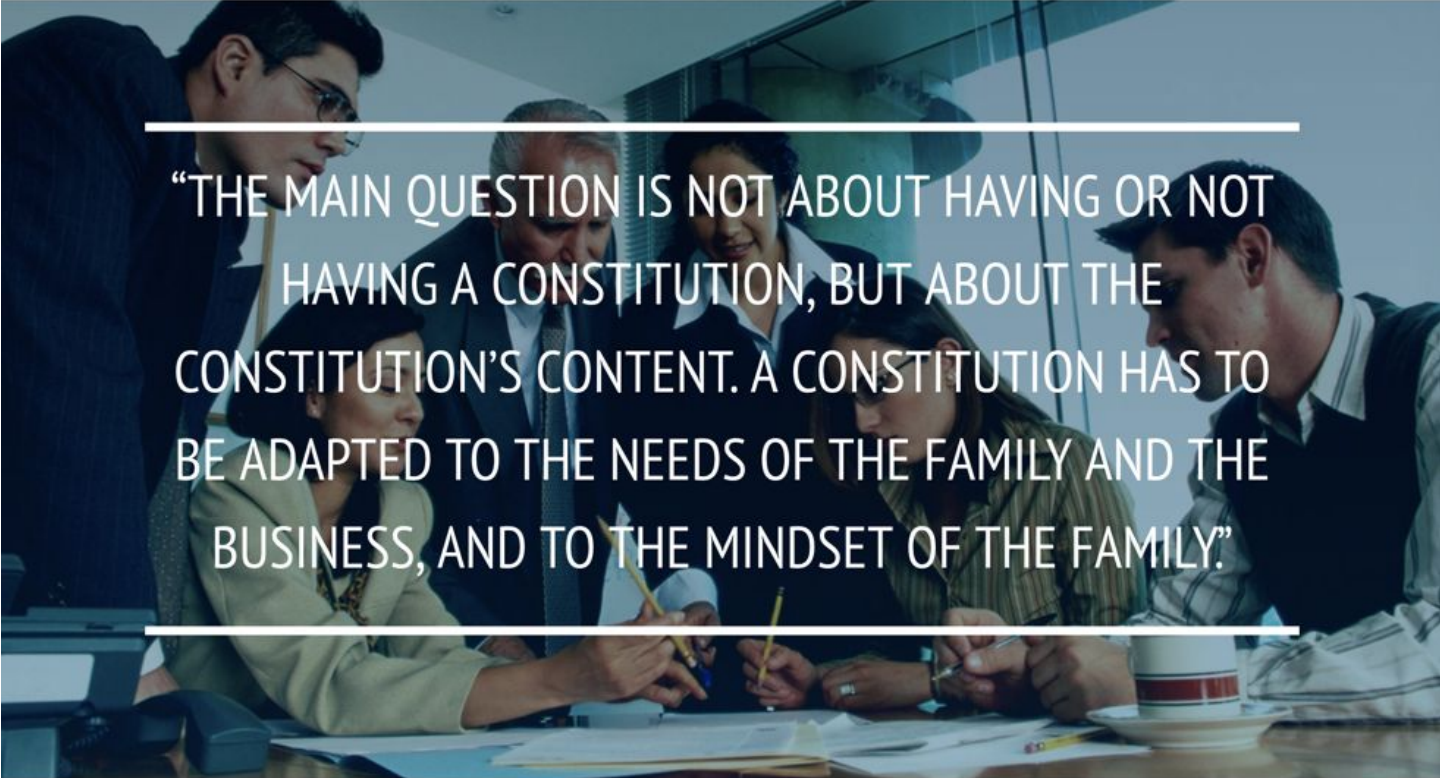
- Businesses whose owning families wrote a constitution experienced better performance than those that did not
- This increase of performance was higher in cases of higher family complexity and in cases where there was a non-family member as CEO

The findings do not mean that there is a direct impact of family constitutions on performance, but that a relationship can be appreciated (correlation does not mean causality). Therefore, the results need interpretation in order to infer how they can affect practice.

Performance is the result of multiple causes and circumstances; it cannot be said that creating a constitution is automatically going to increase performance in any given specific case. Therefore, the research to find higher relationships in the case of higher family complexity and in the case of non-family CEOs becomes more relevant.

It seems quite evident that higher family complexity (various generations, more family owners, more different interests, etc.) easily generates disorder in the business. Therefore, it makes a lot of sense that a constitution will bring about order in the business and, as this research shows, in business performance as well.

More reflection is needed to understand how and why the impact of the constitution on performance is higher in the case of having a non-family CEO. Is it the CEO that makes the constitution more effective, or, on the contrary, does the constitution make the CEO more effective? Having a non-family CEO is not easy for any family business. It usually implies many changes, such as avoiding having family members in management positions, the need to control the company through the board, more analytical decision-making, etc. To make all these changes possible, family agreement and family cohesion is important; and a family constitution is a very useful tool for that end. Therefore, it seems logical to infer that the result of the family constitution supporting a non-family CEO is going to have an impact on the family business' performance.



“THE MAIN QUESTION IS NOT ABOUT HAVING OR NOT HAVING A CONSTITUTION, BUT ABOUT THE CONSTITUTION’S CONTENT. A CONSTITUTION HAS TO BE ADAPTED TO THE NEEDS OF THE FAMILY AND THE BUSINESS, AND TO THE MINDSET OF THE FAMILY.”

## Implications and Conclusions

In my opinion, this paper makes an important contribution to our field by validating that family constitutions have a positive relationship with performance. This may encourage business families to develop their family constitutions and may invite advisors to use constitutions as part of their toolkit to support business families and family business.

In order to go a step further in the interesting avenue this paper suggests, some issues may be useful to reflect upon in order to develop a constitution. I invite the reader to reflect upon three main issues:

- **Facts vs. process:** the importance of “having” a constitution vs. the importance of the process of building a family agreement about the rules. The process of how a constitution is created is even more important than its content. Rules are going to be effective when the group members feel that they are functional and fair. Every incumbent has to have a say and no one should lose face in this



process. This means that time, reflection space and, probably, someone that takes care of the process, is needed.

- **Ceremonial constitution vs. effective constitution:** the importance of dominant family members agreeing with the limits that the family agreement represents. A constitution represents an important change in most business families' behavior, because it sets an important limitation in decision-making discretion. It requires, usually, some effort for an entrepreneur. Agreeing on how relationships, decisions, obligations, and rights have to be ruled and then applying the rules is not easy for someone used to making ad-hoc decisions according to the circumstances.
- **One size doesn't fit all:** family constitutions differ according to the differences in families and businesses. The main question is not about having or not having a constitution, but about the constitution's content. A constitution has to be adapted to the needs of the family and the business, and to the mindset of the family. This means that a constitution must reflect the characteristics of the family, as well as be able to evolve according to substantial changes in the family or business.



## About the contributor

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Many thanks to all the members of the **Research Applied Board** for their thoughtful commentary on the latest *FBR* research in 2017. Special thanks to Karen Vinton, who has served as an Assistant Editor of *FBR* since 2012, overseeing the précis. An FFI Fellow and former board member, she will be stepping down from this role at the end of the year.



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