

10 WARNING SIGNS your family governance is stuck in defense mode

Don't focus your governance on avoiding problems at the expense of promoting purpose-driven outcomes.

BY MATT ALLEN AND ROB LACHENAUER

“**O**ffense sells tickets, but defense wins championships,” iconic college football coach Bear Bryant famously said, putting his own spin on the old sports adage, “The best offense is a good defense.”

The maxim applies well beyond athletics, and there's a good reason for that: humans tend to be risk-averse, as psychologists Daniel Kahneman and Amos Tversky documented in a series of well-known experiments around hypothetical bets. In many cases, we work harder to avoid negative results than to pursue positive outcomes, and dwell on failure more than we celebrate success.

But a defense-first approach is not always the best prescription. In fact, contrary to Coach Bryant's assertion, strong offense has been found to be a much better predictor of success in football, including a team's likelihood of making it to the Super Bowl. Sometimes, it turns out, the best offense is a good offense.

This is also true in settings far from the field or court, including in family business governance. In our experience, family businesses that default to “defense mode” for their governance — more or less trying to not screw up what the senior generations have built — create a different type of risk: disengaging the family owners, especially the next generation.

This article examines the problem of overly defensive governance in family enterprises. We offer 10 signs showing your family may already suffer from it — and what to do to turn that around.



Matt Allen



Rob Lachenauer

WHY DEFENSIVE GOVERNANCE IS DETRIMENTAL

Defensive governance is what happens when families in business focus all or most of their governance efforts on avoiding problems and thus ignore opportunities to use governance systems, rules and processes to promote purpose-driven outcomes.

For example, in crafting a family employment policy, families might create strict rules to make it difficult — or nearly impossible — for members to work for the business, such as requiring multiple degrees or a decade of outside work experience. But these policies only seek to avoid a negative outcome — such as an unprepared or less capable family member entering the business — rather than preparing and encouraging members to join and contribute to their family business.

Similarly, a family's buy-sell agreement may be focused largely on restricting the sale of shares in the business, rather than considering the full range of possible scenarios in which selling may make sense for a member or branch — and, ultimately, for the broader family.

This defensive posture can be far from ideal for the family. For one, it prevents future situations from which the family may benefit, such as having an ostensibly less qualified but high-potential member join the business or board — someone who could bring creativity and fresh thinking to discussions and initiatives. Equally important, defensive governance creates a culture of constraint,

scarcity and fear, where members are more likely to either withhold their ideas and contributions or take them elsewhere, to the detriment of both individual and collective.

In many families, defensive governance is the norm, to the point that those who've developed and enforce it no longer even recognize this reality. It's like the David Foster Wallace joke: An older fish passes by two younger fish and asks, "How's the water?" The younger fish swim on for a bit before one turns to the other and says, "What's water?" You don't know it when you're in it.

10 SIGNS OF OVERLY DEFENSIVE FAMILY GOVERNANCE

1. **A family employment policy focused on keeping people out, rather than encouraging contributions**, such as through strict requirements for education or experience. Some policies even explicitly pay family members below-market wages.
2. **Secretive and opaque communication in the family about the business and ownership**, such as information related to the financial performance of the business, succession or director selection, with small, cabal-like groups in charge of decision-making and rationales rarely offered.
3. **Buy/sell terms in a shareholder agreement that preclude family owners from selling their shares** (why members can't sell, whom they can't sell to) versus a recognition that selling may be beneficial in certain circumstances.
4. **Exclusionary policies related to married-ins**, such as prohibition

from holding shares, joining the business or board, or even from taking part in discussions.

5. **An approach to conflict designed to drive disagreement to zero, stifling healthy debate.** This approach fosters as "go along to get along," overly consensus-focused mentality and culture or, worse, a "you're either with us or against us" philosophy.
6. **An approach to business growth that is all about protecting the "golden goose" in the short term**, with little consideration of taking calculated risks for longer-term success. Here, a defensive posture may result in more than 50% of your sales being derived from products or services more than 10 years old.
7. **A board of directors full of family, close friends or company management.** These boards tend to act more as a rubber-stamp than a true overseer of, and thought partner for, the executive team, with little internal debate or willingness to challenge management on strategy and tactics.
8. **Engagement of the next generation is treated as a test.** Instead of offering a helping hand to the next generation, the current generation puts up a stop signal. Members of the rising cohort are expected prove themselves to the senior generation before being given meaningful engagement opportunities.
9. **Trusts that remove all agency in ownership decision-making from next-generation beneficiaries.** Beneficiaries become passive recipients of their

distributions with no-to-limited voice on matters of ownership.

10. Leadership that has aged out.

Family members who are in senior managements have average age is well into their 60s or older or your controlling owners are in their 80s and 90s, both of which squeeze out opportunities for your next generation of leaders.

BALANCE DEFENSE AND OFFENSE

If many of the signs above sound familiar, your family enterprise is likely operating with overly defensive governance.

So, what can you do about it? It starts with defining and understanding your enterprise *purpose* fully: providing for the next generation, being a leader in the sector, supporting the broader community through philanthropy or some combination of those (or something else altogether). That North Star will help you set or reset your mission and hoped-for outcomes, then you can work backward to the governance measures that serve those best — moving from preventative and risk-averse to inclusive and opportunistic.

Here are 10 practical ways to make that happen.

1. **Govern for recruitment and development of family.** Make engaging with and learning about the business easier for the next generation. Facilitate early interactions of family, to gauge interest, fit and development needs. Defensive policies, meanwhile, should be restricted to leadership/top management positions or other high-stakes areas.
2. **Build more transparency in appropriate places**, such as a

family council representative of generations, branches and in-laws, which enables greater contribution, engagement, connection and, ultimately, trust. For example, we worked in one system who had never shared even their annual revenue figures with their beneficiaries. Now, they have annual CEO “look backs” and “look forwards” to share their business performance and future strategies with family members.

3. **Adjust buy/sell agreements.** Provide opportunities for family members to divest shares or “cash out” some equity for their personal needs, such as education, housing or debt consolidation. The goal is to have engaged, grateful shareholders, not captive, fearful owners. Every multigenerational family business should have an exit policy. Paradoxically, we find that systems with exit policies have more committed and aligned shareholders.
4. **Get to know married-ins’ capabilities and interests** and match those to roles and opportunities across the entire enterprise, including in the business, on the board, in the ownership group and in family governance. Protect assets as needed with prenuptial agreements but err on the side of inclusiveness. Engaging spouses well doubles the talent pool of the family.
5. **Move beyond “fake harmony.”** Don’t default to prioritizing zero conflict. Consider assigning family members or leaders to play devil’s advocate with key decisions at the business, ownership or board level,

to see multiple sides and explore alternative approaches. Some families use a “Candor-o-Meter.” If a conversation is operating in “fake harmony,” everyone has permission to ask how candid people feel the conversation is from one (zero candor) to five (“talking turkey”). People who rank candor low — at one or two — during that exercise inevitability end up sharing what’s really on their minds.

6. **Consider evolving your portfolio.** Instead of treating the core business as the only investment opportunity, think about growth in other areas as well. For example, one family has created four investment types: income generators, core wealth creators, moonshots and a “hurricane fund”, which have differing levels of risk/reward. That approach helped the owners think beyond their legacy business and increased both diversity of returns and family engagement.
7. **Create a board that is linked to capabilities needed to deliver on its purpose.** All boards have important work to do during the upcoming years of their tenure. Recruit your directors according to their ability to help solve specific problems, be they family members or non-family members. Remember not to devalue the long-term perspective that only family board members bring.
8. **Create opportunities for NextGens to engage.** Don’t just wait for them to say they’re ready to contribute or to prove it. Develop relationships with the rising cohort, including internships, early employment to

board observer roles and NextGen-only discussion forums.

9. **Demystify your trusts.** While useful for tax and liability reasons, trusts can create passive next-generation beneficiaries. Help your beneficiaries get to know their trustees and develop a collective voice to their trustees on issues such as their owner goals.

10. **Balance term limits with NextGen engagement.** Focus on when the next generation should come in rather than only on how long the leading generation can stay. Guide this decision more by market dynamics, organizational needs and personal performance than inertia and the desire for leadership to stay where they are.

All teams play both offense and defense, including family enterprises. But, along with being careful stewards of their shared assets, top family businesses tend to:

- Foster a welcoming, learning and nurturing environment for the next generation.
 - Build agency for family owners to influence their outcomes.
 - Value the unique voice of the family owners in the owner, family and boardrooms, and sometimes in the management room.

In the long term, both offense and defense are needed to win..” **FB**

Matt Allen is the John L. Ward Clinical Professor of Family Enterprises and Executive Director of the Ward Center for Family Enterprises at the Kellogg School of Management. **Rob Lachenauer** is a co-founder and partner at Banyan Global.