

Should We Separate the Chair and CEO Roles in our Family Business?

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In family businesses, it is common for a single individual to hold both the CEO and Chair of the Board positions generation after generation. This combined role is usually a result of a board needing a Chairperson and finding no reason to look beyond the well-qualified leader of the business. The business's performance benefits as operational and governance functions more easily align to efficiently support business agility. We see many family firms default to a combined function as generations and business circumstances change without questioning the arrangement, unless there is a significant leadership change such as the appointment of the first non-family CEO.

Yet, when the CEO position is held by a family member, is a combined CEO/Chair function always the right structure? The answer becomes complicated in later generations, for bigger families, for those with more complex businesses and when governance is formalized. The opportunity to challenge tradition is while you are planning a leadership change or making significant changes to the board, such as increasing formality as with the addition of independent directors. It should also be a key question in your emergency succession plan.

When to Separate and When to Combine

We have no hard and fast rules for when to separate the roles of Chair and CEO and when to keep them combined. However, one of the most common reasons to split the roles is to increase the confidence of

shareholders to provide greater alignment between owners and management. We see this when trust has fallen below a threshold and also with larger families who are geographically dispersed or disconnected from the business. A single family member holding both positions can understandably appear like a conflict of interest to non-operating shareholders. They reason that since a key purpose of the board is to ensure effective management, it becomes more difficult to hold a CEO accountable if that person is also leading the board of directors.

Further, in situations where shareholders are concerned with business performance and the two roles are combined, there will often be a push for non-operating shareholder participation on the board. The result may be an ineffective board, especially if non-operating shareholders have little business experience or lack the governance skills the business needs. Many consider it a waste of a resource if the board primarily becomes a management oversight function. By splitting the roles, many have found that the Chair can focus on good governance, including utilizing independent directors, and populating the board with those who most add value to business success, while providing management oversight.

So in general, should small shareholder groups combine the roles and large groups seriously consider splitting them? Maybe, in general, but consider two counterintuitive examples:

Case #1: The Team of Four Brothers

Typically, the founder of a successful business built a board with independent directors. And more typically, he became Chairman while retaining the CEO role. Tradition continued when one of his four children was identified as the successor leader and was appointed President and the founder retained the Chairman/CEO title. The four siblings were thoughtful and envisioned their future board structure for the period after when their father transferred to them his controlling interest. Would the President adopt both the Chairman and CEO roles? Surprising many around them, the four brothers decided to transfer the Chair position from their father to a non-family, independent Chair.

Why? The brothers reasoned that separating the CEO and Chair in their generation would lessen the status differences already in place by one sibling owner as CEO, who would be the only brother to have a board seat. Further, they concluded a non-family, independent director Chair of the Board would make CEO oversight by the board more formal and allow the four brothers to be more equal as shareholders. Each brother owned a considerable percentage of the business and felt pressure to make it successful. They all benefited from CEO accountability to a board led by an independent Chair.

After several years, the brothers have not questioned their decision. They have a “bundle of sticks” team strength as shareholders and business operators. None are concerned about the balance of the board’s influence versus shareholder influence, and they highly respect the value of independent objectivity from their board.

Case #2: Moving from Third- to Fourth-Generation Cousins

Three generations of decidedly passive shareholders reaped strong dividends from great business results and a “trust us” inference from management. When many of the fourth generation emerged into their mid-30s, the business leadership was being passed on to a fourth-generation member at the same time. It became clear that the shareholders should not and would not remain passive if they were to continue as a unified and committed family-owned business.

The “operationally-oriented” board configuration dominated by family management members from the third generation would no longer be supported by the younger shareholders who desired more involvement. There was a strong movement to place non-operating shareholders on the board to oversee the new leader. After a long process involving research, communication and back and forth between the family managers and non-operating shareholders, they decided to keep the combined CEO/Chairman role in the fourth generation. It was also decided to not include outside shareholders on their board. Everyone was in full support.

Why? They reasoned that a small operationally-responsive board had served them very well in the past with business results exceeding all industry benchmarks. Instead of adding shareholders to the board and encumbering management with oversight-oriented directors, they opted for independent directors instead for strategic purposes, who would also provide sufficient oversight. Non-operating shareholders would be involved in the nominating and compensation committees of the board, but would not have seats. The CEO/Chair would keep the board and management aligned and retain their market responsiveness competitive advantage.

After several years, business results are still leading the industry. Over 40 shareholders personally know the three independent directors currently serving on their board and a very active family council keeps increasing the variety and options for shareholder engagement with the business.

What do These Cases Tell Us?

Following in the footsteps of a founder, most sibling business families tend to opt for a single CEO/Chair. However, the four sibling brothers most wanted a strong unified bond between themselves and they worried about their ability to do so if one brother was CEO, the Chairman and the only shareholder on the board. They also wanted objective input on key business decisions and strategy. They considered board membership inappropriate for the three who worked in the business and reported to their brother the CEO. Their decision to appoint an independent as Chair allowed them to keep their trust of one another high and to focus on their roles as a team of shareholders and managers in the business, and worry less about monitoring the CEO.

In the second case, the cousins would be expected to separate the Chair and CEO roles in order to fully assure shareholders that their assets were being put to the best use by management, and as a compromise for not including shareholders on the board. Further, it is reasonable to expect the vigilant cousins, adding independent directors to their board for the first time, would opt for a Chair who would concentrate on the new governance function. It might be too much and too distracting to a CEO's job of running the business. However, the family shareholders had experienced high trust in management for three generations and they fully supported an efficient governance/management relationship, which would also provide oversight. Thus, they opted to preserve as much of the governance and management structure that had worked in the past, knowing it would be significantly enhanced with the addition of independent directors, which would further add to high trust in the fourth generation.

Both firms looked at their unique circumstances and chose what would work best for them rather than adopting for what might be traditional or would work for another business family.

Conclusions

In summary, family firms who are led by a family member might consider the following when deciding to combine or separate the roles of CEO and Chairman:

- Deliberately question it. Don't blindly follow tradition and adopt for what worked in the previous generation. Each transition is an opportunity to evaluate both options.
- If shareholders need more confidence and it will help increase trust and alignment, consider the potential of separating the roles so that a Chair can focus on the effectiveness of the board and the CEO can focus on the business.
- If a business's agility can be enhanced by an individual who can skillfully perform the duties of CEO and Chair while maintaining shareholder trust, consider taking advantage of the combined roles.
- Don't adopt the "best practice" or "good corporate governance" solution for your circumstances too quickly without a challenge. A counterintuitive solution may be the best practice for your business family.

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