



THE BOSTON CONSULTING GROUP

# A FOUNDER'S GUIDE TO PROFESSIONALIZING A FAMILY BUSINESS

By Vikram Bhalla and Christian Orglmeister

**T**HE FOUNDER OF EVERY thriving family business faces an inevitable question: How should our ways of working evolve to meet the challenges of managing a growing company? Experts typically tell founders that the answer is to professionalize, meaning that they should emulate the structures, governance, systems, and processes of a modern corporation. Yet in many cases, that approach to professionalization destroys what made the family business special in the first place. Many founders also fear, justifiably, that they will lose control of a business that is an integral part of their identity.

It doesn't have to be this way. We have a different perspective on what it means to professionalize a family business. In our view, such a business should start by determining which of its distinctive attributes—its entrepreneurial skills, its spirit, or its special strengths—have enabled the enterprise to thrive. It should then adopt the characteristics of a modern corporation that will augment those attributes and that fit with its culture. Professionalizing does

not have to mean removing the family from its role in the business. But it does mean making a deliberate choice to define clear roles for the family and for professional managers. This approach will allow the business to benefit from uniqueness where it matters and prepare for scale where it is needed.

But making this happen is easier said than done. Many family businesses struggle—often for predictable reasons—to maintain their distinctiveness as they professionalize, and some even end up worse off. Below we present a four-step approach that founders can use to overcome the challenges and position their companies to continue as high-performing enterprises for generations to come.

## When to Professionalize

In its early years, a small or midsize family business faces mainly external and market challenges: getting access to capital, defining the right strategy, and gaining a competitive advantage. Like a child, its first im-

perative is to survive and gain critical mass—that is, to grow. At this stage, a remarkable leader—a super-entrepreneur—guides the business with extraordinary passion and insight. The leader’s skills and values foster the growth of a distinctive, even a unique, business.

But successful growth comes at a cost. As the business grows in size and scale, it becomes increasingly hard for the leader to manage. When the company reaches this inflection point—its adolescence—it must focus on the internal struggles, conflicts, and challenges resulting from complexity and bureaucracy. (See Exhibit 1.)

Family businesses experience the pains of adolescence in different ways. The family leader may impede growth because he or she does not have time to make all the necessary decisions. A large number of people may be hired in response, which promotes the development of new cultures within the organization. New processes are defined, but few are actually implemented. Decision making tends to be delegated upwards, so management’s agenda gets cluttered with operational issues.

These symptoms indicate that the organization is feeling the strains of growth. They call for a close look at whether the time has come to professionalize.

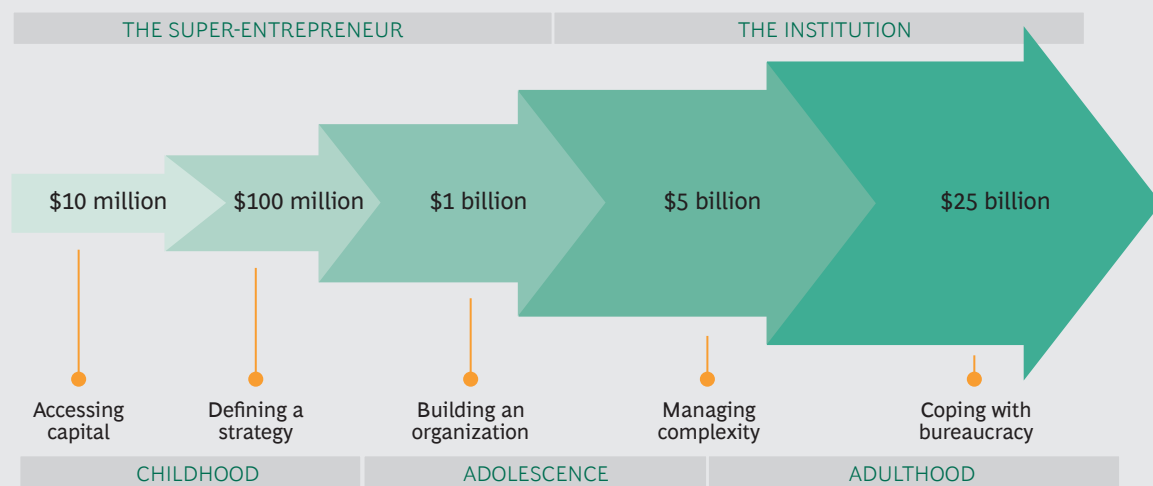
The need for professionalization may also be triggered by the family itself. Changes in its size and composition or in the interests and preferences of its members may create the impetus to reexamine roles and bring professional managers into the organization. For example, the founder may decide that the time has come to step away from the CEO’s role in order to pursue other interests. Or the company may need a cadre of professionals to prepare younger family members for leadership roles and to bridge the leadership gap until the next generation is ready.

### Professionalization and Its Pitfalls

The professionalization of a family business typically comprises three phases. (See Exhibit 2.)

- **New Ways, Same Company.** Initially, the company brings in a few new recruits at various levels and institutes a few new processes, typically in HR. But the company’s operations and culture remain largely unchanged.
- **Two Worlds.** This second phase is the most complex. The company hires external talent for important positions and defines and implements several critical new business processes. But it

#### EXHIBIT 1 | Inflection Points for a Family Business



Source: BCG analysis.

grapples with the need to reconcile the old and the new. Many companies give up on professionalization at this point and never see its benefits.

- **A High-Performing Enterprise.** Companies that reach this phase have succeeded in retaining the family’s “special sauce,” even as they attract top talent for positions throughout the organization. They use processes and systems to deal with scale effectively.

Although companies on the journey to professionalization can falter for many reasons, they most commonly fall into at least one of these traps:

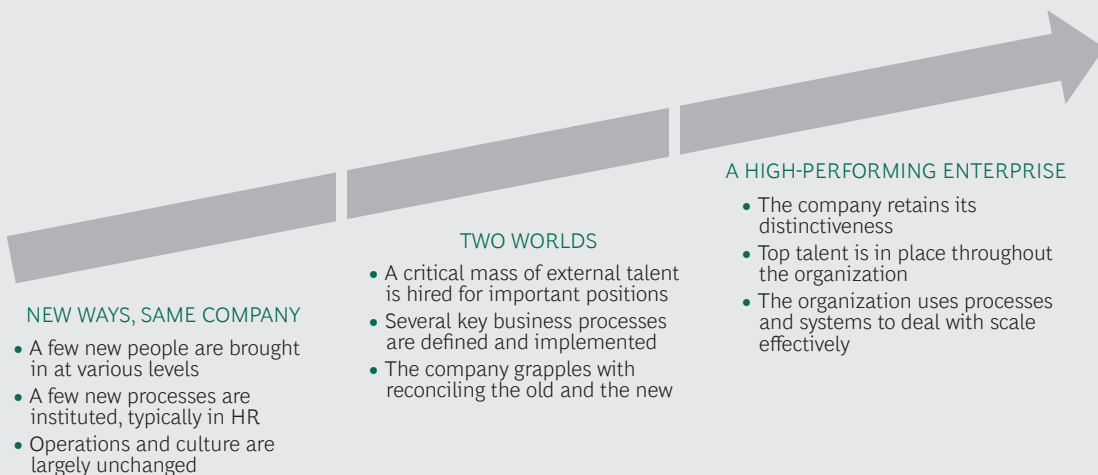
- **People Potpourri.** Professionalization requires hiring numerous new employees from a variety of backgrounds and corporate cultures. Integrating new hires and long-serving employees into a single, cohesive company culture can be difficult. If the integration is not managed properly, clashes and tensions can occur at all levels. With the deterioration of collaboration and effectiveness, the company loses its edge.
- **Paper Processes.** Family businesses often establish far too many processes in their effort to emulate modern corporations. Moreover, nonfamily executives may craft these processes

without considering what the family’s role should be or its style of working. Worse, they sometimes design them with the goal of circumventing family members rather than ensuring their healthy participation in decision making. In many cases, the organization ignores the new processes and adheres to the old ways of working. The processes end up existing only on paper, leading to confusion and frustration on the part of employees.

- **Diluted Distinctiveness.** When companies push too hard to institute new processes and systems, they risk losing track of what made them special in the first place. They sacrifice the uniqueness that helped them succeed and wind up becoming like any other company. This scenario typically occurs in companies whose founding family steps away from the business before its values have been embedded in the professionalized organization.

For an example of how a family business can make choices that allow it to retain its distinctiveness, consider this company in the rental car business. The founder and CEO decided it was time to step back and move into a supervisory role as chairman of the board. In accordance with corporate-governance best practices, he would become much less involved

## EXHIBIT 2 | Professionalization Comprises Three Phases



Source: BCG analysis.

in making executive decisions. As CEO, however, the founder had been personally responsible for the company's most critical executive activity: negotiating with manufacturers to purchase cars. In moving to the chairman's role, he would have to give up this important value-generating function. Instead, while relinquishing other key roles, he decided to stay involved in these negotiations for 18 to 24 months, helping other executives prepare to eventually assume the purchasing role.

## Four Steps to Professionalization

So what should family businesses do to get professionalization right? We believe they need to take four crucial steps.

### 1. DEFINE THE FAMILY'S ROLE

First, family members must agree on the need to professionalize and clarify their vision for the company's future. They must align their aspirations for the business and for themselves.

Defining each generation's specific role is essential. It is often hard for older family members to step away from a business that has been the central focus of their lives and identities. And in some cases, their continuing involvement can be advantageous to the business, if it is properly managed. Rather than trying to circumvent the senior generation, the company should identify ways to make the best use of its skills. For younger family members, the challenge is to increase their involvement in ways that are appropriate given their skills and readiness for leadership.

One family-led automotive company addressed this generational challenge in an interesting way. The chairman, who wanted to hand leadership over to the next generation and to professional managers, was anxious about separating from the business and losing control. Through a process of counseling and guided self-discovery, he realized that he enjoyed leading design and technology initiatives more than being involved in the daily oversight of the busi-

ness. In fact, his contributions to design and technology were part of what made the business special. The company therefore created a specific function for new-product and technology development under the chairman's leadership, and he ceded all his other functions. He continued to contribute his insights through this formal role, while younger family members and professional managers took charge of other aspects of growing the business.

To clearly define its role, the family must articulate the sources of the company's distinctiveness and success. It should then identify which elements of that distinctiveness must be retained in order to ensure continuing competitiveness. One family, for instance, had an instinct for knowing when to buy and sell a specific type of large capital equipment. Such valuable skills must not be lost in the course of professionalizing.

### 2. STRENGTHEN GOVERNANCE

Governance should be addressed at four levels, each of which must be clearly defined and consistent with the others.

**The Family.** The family must decide how it will be governed and how it will manage its relationship with the business. Some families undertake a comprehensive family governance exercise, while others seek to address only the core issues—that is, the family's role in the business and how it will make decisions related to the business. Other elements of family governance, such as those relating to wealth management and philanthropy, are important but can be addressed separately. (See "Governance for Family Businesses: Sustaining the 'Magic' for Generations to Come," BCG article, October 2014.)

Most families address the question of governance through two bodies: the family assembly, which deals with a broad set of family alignment issues, and the family council, a smaller body that deals with the family's relations with the business. To insulate professional managers from family disagreements, the family council should meet privately to agree on key issues that affect the family and the business. It is im-

portant to delineate which types of issues the family council will consider and the family's decision rights on those issues.

**The Board of Directors.** By inviting nonfamily members to join its board of directors, a family business gains access to executives and specialists who can provide valuable insights that support decision making. Many countries have statutory requirements relating to the governance of the board of directors. Family businesses that are private companies and not subject to these requirements should nonetheless establish governance mechanisms. To clarify the mandates of family and nonfamily members, it is important to define the board's role in relation to the family, the business, and other entities.

**The Corporate Center.** Many family businesses, especially those that are diversified, create a "corporate center" as another level of governance. The corporate center supports the family in running the business and helps the various business units achieve their objectives. Corporate centers can take many forms, ranging from "light" centers that only set and review targets to "heavy" centers that also seek to drive performance, operational decisions, and synergies across business units. (See *Designing the Corporate Center: How to Turn Strategy into Structure*, BCG Focus, May 2013.) The business should clarify the objectives of the corporate center and appoint people with the right expertise and mindset to achieve them. It is also critical to delineate the corporate center's decision rights and responsibilities relative to those of the business units.

**The Executive and Management Committee.** The family must clarify the roles of the company's leadership team and how it will make decisions. This typically involves creating an executive and management committee. To be effective, the committee must focus on strategic and policy issues and avoid cluttering its agenda with operational issues.

### 3. STRENGTHEN THE COMPANY

Professionalization requires strengthening the company itself. Several elements are

especially critical to a high-performing enterprise.

**The Leadership Team.** The family must decide who will lead the company, determine the leadership team's structure and composition, and set forth the expectations for the team's performance. In addition, the family must arrange for the active support and coaching of the leadership team for at least a year (two to three years in many cases). This is essential to ensuring that the new leaders have the time they need to build their capabilities.

Some families choose to hire an executive who will eventually become the CEO. Selecting the future CEO is a complex and momentous task. The best candidates are those who are not only competent but also a good fit with the family and the business. Successful transitions are achieved gradually. Some companies initially hire an executive to serve as the COO, giving him or her time to settle in and understand the business and its culture. Then, in six-month phases, they assign decision rights to the new executive, transferring additional responsibilities as he or she demonstrates high performance and a strong grasp of the business. The complete transition to CEO generally takes more than a year, although in rare situations it can be accomplished in three months.

Some family businesses bring in a temporary CEO to facilitate the transition from family leadership to a professional governance model. This is a person with the experience to lead the company but no aspiration to serve as CEO in the long term. Over a defined period, usually three years, the temporary CEO fosters trust and transparency by building bridges between family members and professional executives. After this transition period, a new CEO takes the helm and, in some cases, the temporary CEO joins the board of directors and serves as an independent advisor to the family.

**The Organization Structure.** In their effort to professionalize, some companies overcomplicate the organization's structure,

stifling its effectiveness. The structure should support the company's growth goals over three to five years rather than its projected needs ten years out. The structure should also reflect the company's culture and history. To ensure successful collaboration, role mandates within the structure should be clearly delineated and communicated.

**Business and Support Processes.** Rather than creating manuals for every organizational process, companies should focus on defining cross-functional and critical business processes as well as key support processes. New processes should take into account the organization's culture and the family leader's preferences so that they retain and protect, rather than dilute, the company's distinctiveness. For example, processes related to innovation, investments, procurement, and operational improvement must capture the strengths that the family and company culture bring to the business.

**Control Systems.** Leaders and family members are more willing to relinquish some involvement in the business when they believe they will continue to have visibility into, or even control over, the company's performance. Strong control systems (such as management information systems) give family members confidence that when they delegate decision making, they will still be able to keep informed about performance.

#### **4. DEFINE THE COMPANY WAY**

In addition to the "hardwiring" described above, institutionalizing the company's culture, values, and leadership behaviors is essential to successful professionalization.

The leaders of the business must clearly and explicitly articulate their culture and values and then take steps to communicate and institutionalize them, with the goal of preserving them as guiding lights into the future. Workshops and communication tools are valuable, but the company must also share stories about what makes the family business special, the people who embody the culture, and the organizational elements that reinforce it.

The company should also set out behavioral expectations for its leaders, top managers, and employees throughout the organization. In addition to encouraging high performance on the part of current leaders, clearly defined expectations help potential future leaders understand the requirements for success at the company. To establish behavioral expectations, many companies create a leadership behavior charter that articulates clear dos and don'ts, which are sometimes integrated into the appraisal process for executives.

**A**T SOME POINT in the life cycle of every successful family business, it becomes imperative to professionalize. This can mean a period of turmoil for both the family and the business. Navigating through the turbulence requires leadership by the family, patience and perseverance, and careful planning and implementation. Most important, the family must never lose sight of the distinctiveness that made the business the success that it is today. Businesses that strengthen their family-built institution using the right supporting elements of a modern corporation will create a high-performing enterprise that will thrive for generations to come.

## About the Authors

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