

Family Enterprise Governance

Assessing your board composition and the role of independent directors

Making sure you have the right directors on your board

Family businesses can benefit greatly from having an effective board of directors. To get the most out of your board, you want to make sure you have the appropriate expertise and experience as well as diversity of thought in the boardroom.

The value you wish to obtain from your board will drive the knowledge and experience you'll want on your board. A good place to start is to survey key stakeholders to identify skills and experience needed to support the company's strategic direction or expected transitions. You will also need to understand the collective skills and experience of the current board, so that you can identify gaps between existing directors and what you may need in future directors. These gaps should help inform your search for new board members. The board should repeat this process on a periodic basis to make sure it has the right skills and expertise to support the company's future strategy, as well as any anticipated transitions where it could help mentor new executives or next generation family members.

In addition to knowledge and skills, some shareholders and executives consider diversity and inclusion as important attributes to their board composition. Having diverse directors can provide broader insight into how important constituencies (for example, your customers or employees) think. However you choose to define diversity, it's helpful to consider whether your directors bring different perspectives to the table.

It is also helpful to recruit directors that have an understanding of family business dynamics to help the company and the family navigate some of the typical challenges of a family business. You want directors who can help preserve the principles, values and ethics that are essential to your family business.



An independent point of view

Oftentimes family businesses want to keep their boards restricted to family members or family members and close friends or advisors. Having this inner circle can help family businesses feel better about concerns over confidentiality and trust. However, this approach often gives families a false sense of comfort because these "insider only" directors may not be objective enough to provide meaningful feedback to support needed accountability. In addition, "insider only" board discussions can spiral into family issues unrelated to the business, which limits the board's effectiveness in strategically directing the business.

Outside directors are independent of management and the family and don't have relationships that would interfere with their ability to exercise independent judgment. This puts them in a position to challenge the ownership group in a positive way. These directors can introduce objectivity and accountability to the board. Independent directors can speak without fear of repercussion (other than being removed from the board), so they may feel freer to raise sensitive issues.

If you decide to add such directors, don't be surprised if they press for more formal board practices and policies than you're accustomed to. That said, these practices are often valuable and can help you attract other talented directors.

Role of independent directors

Independent directors can provide fresh perspectives and frank feedback, and expand networks to people and places that can benefit the business and bring credibility to the company and the family. The role of independent directors often includes:



Separating the company's needs from the family's needs: Independent directors can objectively question how the company's assets and profits are used, the appropriate level of dividends for shareholders, as well as family leaders' performance and compensation. This level of questioning without any perceived family bias is helpful to foster thoughtful decision making.



Perspectives, experiences, networks: Independent directors can leverage what they've seen elsewhere, as well as their networks, to help management address challenges or perhaps avoid them in the first place. This could include experience with new markets, technology and innovation, mergers and acquisitions, or transitions other families have navigated through.



Objectivity and accountability: Independent directors can also introduce objectivity and accountability to the board. Often a company founder or CEO is the champion for certain projects and people. Independent directors can help management make hard decisions when needed, and may be in a better position to deliver difficult but necessary messages to the CEO.



Advisor to the CEO: An important role for outside directors is often to advise the CEO. This could include acting as a trusted sounding board or helping the CEO manage through an issue.



Planning/advising on succession plans: Given family dynamics, directors who are not related to the family may be able to identify strengths as well as areas where next generation successors need coaching and development. And those younger family members may be more receptive to receiving and acting on that advice from someone outside the family.



Planning/advising on exit strategies: Sometimes passing the company down to the next generation isn't the best move to maximize shareholder value or to secure the company's future. Independent directors can provide advice to the family on whether the family should exit their ownership, which is often a very emotional decision that benefits greatly from an outside perspective directly on the board.



Oversight of board committees: As boards become more professional with the addition of independent directors, the number of board committees often increases. Audit and compensation committees, in particular, can benefit from leveraging independent and outside perspectives.

Learn more at: [pwc.com/us/familyenterprises/governance](https://www.pwc.com/us/familyenterprises/governance)

For detailed resources on professionalizing your family business board, board matching, perpetuating the family business through good governance, transitioning your board for the next generation and more.

Contact

Jonathan Flack

Private, Family Enterprises Leader, PwC US
(615) 503-2866
jonathan.flack@pwc.com

Belinda Sneddon

Private, Family Enterprises, Managing Director, PwC US
(646) 939-8616
belinda.sneddon@pwc.com

