Conflicts of Competencies between Ownership and Company Strategy, respectively between Owners and Board of Directors

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1. Summary

This essay will delve into the definitions and shaping of ownership strategy and company strategy with a focus on family firms, and explore the conflicts that can arise between them, including the tension in competencies between the owner shareholders and the board of directors.

2. Who are the Owners?

Contrary to popular belief, concentration of ownership within the company is common and most companies around the world are under the control of individual shareholders. Generally, it is assumed that 60-90 percent of all the companies in the world are family firms. The exact number of family businesses is difficult to determine because definitions vary in terms of ownership level, generation and degree of family business involvement. Among privately held companies, the number of family-owned companies is higher than among listed companies. Owners of listed companies are according to the OECD institutional investors (41% of the global market capitalization), the public sector (14%), private corporations (11%), and strategic individuals (7%). The rest is free-float (27%).

3. What is an Ownership Strategy?

Shareholders of concentrated ownership often have an ownership strategy, which is distinct from the investment strategy of minority shareholders. Minority shareholders invest their financial means in different (mostly listed) companies with a certain risk profile, such is called the investment strategy. Generally, they pursue a diversification investment strategy in order to spread the risks. Hence, minority shareholders must not care too much about the individual stock. In contrast, for anchor shareholders the company is regularly by far their greatest asset, and they keep it for the long term. Accordingly, they feel responsible for the success of the company. Often – especially with growing complexity on shareholder or company level – these anchor shareholders define precise goals for the company and establish rules for their influence.

Such is called the ownership strategy. The ownership strategy defines on the one hand financial goals regarding levels of participation, long-term growth, dividend distribution or risk tolerance. On the other hand, the ownership strategy also entails non-financial goals, such as location ties, the careful use of natural resources or the caring treatment of employees. Therewith, the ownership strategy also reflects ethical concerns and the value set of the owners. Moreover, the owner strategy says something about the ownership structure and the involvement of the owners in the company. It e.g. stipulates that ownership is held through a holding company and states how the owners are represented in the board of directors.

In family businesses, for example, the ownership strategy often defines that the family owners have the goal to pass on the family firm to the next generation and to keep it private. In state-owned companies, the ownership strategy elaborates what public utility mandate the company has and what departments are responsible to supervise this activity. Owners of start-ups may determine what percentage of the shares they want to keep and the preferred exit scenario. These are examples of the content of an ownership strategy.

With increasing complexity at the ownership or company level, for example, if there is an increasing amount of shareholders or business activities, the shareholders tend to explicitly formulate their ownership strategy. So do later generation family firms, state owned companies or start-up companies with a group of founders as shareholders.

4. Conflicts between Ownership and Company Strategy

The company strategy, on the other hand, is the plan developed by the board of directors and the executive management team to achieve the company's objectives. It encompasses decisions related to product development, market expansion, financial management, and the corporate structures. A well-defined company strategy serves as a roadmap to ensure the long-term success and sustainability of the business. The ownership strategy and company strategy can conflict: Here are two examples that family businesses have encountered frequently in the last years:

1. Sale of the original business unit: Family businesses often grow into conglomerates over time. A conglomerate is on the one hand the result of opportunity acquisitions. Family firms regularly work with other entrepreneur-managed companies or family firms and, due to the shared catalog of values, acquisitions often occur between families when the opportunity arises, for example along the vertical value chain. On the other hand conglomerations are the result of the further development of the company's products and services. Over generations, the range of the products and services of the family business deepens and broadens. Family firms in later generations therefore have often a mature corporate structure that is divided into different business areas. Over the years, it then may happen that the family's original business is no longer profitable and new business units become more attractive from a financial perspective.

   In many family businesses this leads to the controversial question of whether the original business should be divested. There are usually differing opinions among family members. Some want to hold on to the business unit because they feel a special connection to it and identify with it or because they want to preserve it due to a feeling of obligation to their ancestors. Other family members would like to sell the business unit so that family wealth is not endangered and can be passed on to the next generation. They argue that it could not have been in the spirit of the ancestors to run unprofitable businesses.

   You will rightly point out that the sale of a business unit lies in the responsibility of the board of directors and is not a decision to be taken by the owner. And this is correct. It is in the responsibility of the board of directors and executive management to consider how a sale aligns with the long-term goals and overall company strategy. They may decide to opt for a sale to focus on core competencies or acquire a new unit.

From a purely legal perspective, the family members do not have to agree to a sale of a business unit, since it is not the shareholders who are selling part of their stock, but rather the company as a legal entity is selling part of its assets. Although the initial situation is legally clear, ownership strategy and business strategy overlap here. In such a situation, there is a need for owners and company to coordinate their strategies. If this alignment does not take place, there is a great potential for conflict, which in the worst-case results in an open conflict between family, respectively their representatives on the board of directors and the non-family board members. Such a conflict is neither in the interest of the family nor the company.

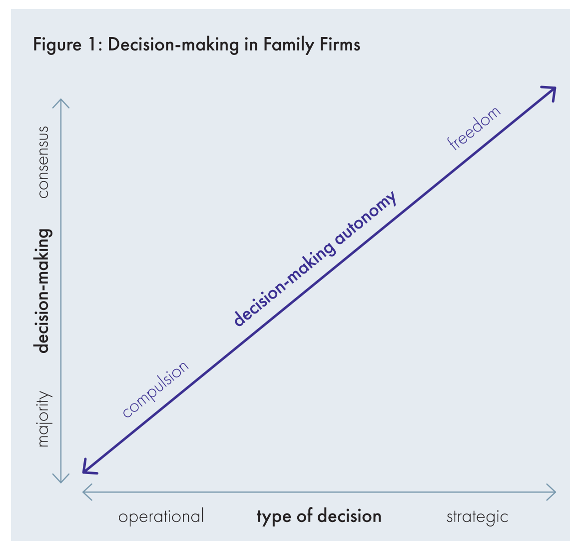
2. Definition of sustainability goals: A second issue that has repeatedly led to conflict in recent years is the definition of the sustainability strategy. Family businesses are praised for the fact that their management is strongly value oriented. This value orientation supports intra-family succession because it gives the next generation the opportunity to use their human and financial resources meaningful. The values are the glue between the generations. In succession processes a value discussion hence regularly takes place. Family members talk about what values their ancestors followed in their entrepreneurial activities and what values should guide the family members into the future. The results of this discussion can be found in the ownership strategy which families formulate in their family constitutions. Mostly this part of the constitution is the part family members cheer the most.

   In our time, this discussion of values within a generational change happens to coincide with the zeitgeist of sustainability. In many family firms, we can therefore observe that the next generation has specific environmental concerns and demands that the company strategy aligns with these values, even if it entails added costs. The board, however, refers to the division of competences and rejects such demands because of broader financial considerations.

5. Decision Making and Solution Finding

How should family members and board members react to such conflicting strategies? In these cases, decisions by the board of directors referring to the division of competences as well as majority decisions in the board of directors are neither useful nor sustainable. Strategic decisions are questions of identity – one cannot disagree and move on. Strategic decisions therefore require the support of all involved parties and the alignment of ownership and company strategy.

Figure 1: Decision-making in Family Firms



In the first example, the sale of the original unit, the family representative and the chairperson on the board of directors as well as the family chair, if available, play a key role. It is up to them to ensure that, on the one hand, the family members come to a common opinion and, on the other hand, that communication between the family and the company is fruitful. That means first, that the family knows about the entrepreneurial challenges and understands them. So that the family is not surprised when important decisions come up. Second, that also the company knows about the concerns and interests of the different family members.

Such communication is not established overnight but needs constant engagement by the parties. Ideally, a constant, regular, and timely communication ensures that the question of a sale of a business unit, is then not a disruptive one. Governance structures, such as a family council or a family speaker, a thoughtful representation of the family in the board of directors support the establishment of a fruitful communication.

In the second case – the definition of sustainability goals – boards should see the engagement of the next generation as opportunity to pass the company on to a next generation of committed, long-term thinking family members. But in order that the blessing does not become a curse, the board of directors should first educate the next generation about their role as owners and then set clear guidelines as to how the next generation, or the whole family, will be involved in the topic of sustainability. Whether they are simply informed, whether they are listened to or whether they are even allowed to have a say on certain issues.

6. Conclusion

In conclusion, the conflict between ownership strategy and company strategy is an inherent challenge in family firms or other companies with an anchor shareholder. Finding an alignment between these strategies is crucial to ensure the long-term success of the company. Effective communication, education and discussion of roles and responsibilities can help mitigate conflicts and enable shareholders and the board of directors to work in harmony.