Corporate Governance, family business complexity and succession

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Summary

Family businesses are more heterogeneous than are corporations listed on the stock exchange and therefore they need specific and well-tailored governance respective of the situation. Based on the complexity theorem of governance in family firms we will discuss optimal governance before and after the transfer of the family firm. As there is an optimal (corporate) governance structure for each individual family business in each point of time on one hand, and taking into consideration that succession changes the distinct qualities of the family business system on the other, a different governance structure is needed past succession.

Introduction

Corporate Governance in terms of the "organization of the management and the control of a company aiming at balancing the interests between the involved stakeholders" (Witt, 2003: 1) has attracted interest in theoretical as well as practical areas over the last years (Gillan, 2006; Benz & Frey, 2007). In addition to huge scandals such as Enron, Arthur Andersen or Parmalat, theoretical discussion about the validity of arguments (Lubatkin, 2007) or the sound theory applied (Zahra, 2007) have questioned the ubiquitous point of view.

At first, only corporations listed on the stock exchange were discussed. In the further course, family businesses (which could be businesses listed on the stock exchange as well as privately held businesses) were focussed (Andersen & Reeb, 2003; Lubatkin et al, 2005; Jaskiewicz, 2006). Accordingly well-functioning corporate governance is also – or especially – important for businesses which are significantly influenced by families. It is particularly important because of the high economic relevance of this type of business.

Family businesses dominate in almost all economies (ifera, 2003) and constitute also one of the most important pillars for the German economy (Klein, 2004). Therefore, applying the corporate governance codex on family businesses was both, timely and worthwhile (Commission Governance Codes for Family Businesses, 2004). With regard to the few data available introducing diverse corporate governance mechanisms in family businesses, we can assume that owners of family businesses remain rather reserved towards this topic (Jaskiewicz & Klein, 2007; Pieper et al, 2008).

Family businesses are more heterogeneous than publicly owned firms (Miller et al, 2007). In consequence, they only rarely share a point of view collectively. Conventional recommendations (Swiss Code of Best Practice in Corporate Governance, the German Coporate-Governance-Codex or the American Sarbanes-Oxley Act) miss out with respect to family businesses. That is attributed to the fact that recommendations are based on implicit assumptions that can only be applied to family businesses in exceptional cases. Within those recommendations, the owners are regarded as a group of anonymous shareholders. However, generally only few closely related persons are owners of family businesses. Moreover, the above-mentioned recommendations assume that shares can be traded; yet, in many family businesses this is not or not necessarily the case. The principal-agent approach which is predominant in corporate governance (Lubatkin, 2007; Zahra, 2007) has only a limited explanatory power concerning family businesses (Jaskiewicz & Klein, 2007; Klein, 2008). The assumption of the homo oeconomicus, who is short-term oriented and seeks financial advantage, is underlying the principal-agent approach; yet, it does not adequately describe the state of many family businesses. This assumption is not adequate since many family businesses have a long-term orientation comprising a goal-setting over several generations which may also be not only financially motivated (Astrachan & Jaskiewicz, 2008).

Family businesses thus need a specifically tailored corporate governance approach that allows for their particularities. To develop this approach, a systematic understanding of the organisation is needed that best fits to family businesses (Pieper & Klein, 2007). It is thereby assumed that the company's regulations for corporate governance are subject to the economic principles of costs and revenues. That is to say that the owners of a company should strive to install as many corporate governance rules as necessary (with regard to transparency, traceability and manageability). Simultaneously, they should set up as few formal corporate governance rules as possible (due to costs). It needs to be accounted for that cost of corporate governance regulations do not only arise as direct liquidity-related cost but also thoroughly arise as indirect cost. Applying the corporate governance theorem for family businesses (Klein, 2009), we can derive an optimal level of (corporate) governance mechanisms for any specific family business taking its complexity within the four sub-systems family, company, leadership, and ownership into consideration, moderated by trust.

Once succession takes place the complexity of the family business changes. The aim of the work is to apply the universally applicable theorem which in individual cases will allow for the estimation of the optimal level of corporate and family governance for a specific family business regarding cost and utilization aspects to family businesses undergoing succession. In doing so, I will put forward a concept that helps family business owners to consider potential changes in complexity and related changes needed in the governance structure prior to succession. This can lead to different paths to cope with the upcoming changes. On one hand owners could account for upcoming complexity through anticipating the incoming complexity and design prior to succession the governance structure of their family business already for the complexity they expect post succession. On the other hand they can also consider opting for a succession plan that guarantees an equal level of complexity post succession and by that does not require major changes in the governance structure.

Understanding Complexity, Family Firms, and Corporate Governance

In the following, the underlying concepts will be presented at first. The subsections conclude with the respective definition which is applied within this work.

Understanding Complexity

The definitions of complexity are numerous; as a least common denominator, one finds three characteristics:

- Number of elements
- Heterogeneity of elements
- Interdependence and interrelatedness of elements

A system is therefore all the more complex, the more elements constitute it and the more heterogeneous those elements are (cf. Dess & Beard, 1984; Kieser, 1974; Simon, 1996; Homburg & Kebbel, 2001). Scott (1992) also distinguishes between different levels of complexity of organisations. He differentiates between the vertical referring to the different levels of hierarchy, the horizatonal as for instance the number of departments, and the spatial as for example the number of subsidiaries. This deals with the question about the number and the heterogeneity of the elements. Here, elements are all the more heterogeneous, the more diverse the organisational levels are on which they are located.

Looking at the organisation dynamically, the number of connections between the elements as well as the number of repeated actions influence the degree of complexity. Complex systems are among others characterised by nonlinear transformations of in-and output factors (Anderson, 1999). Those nonlinear transformations can naturally not be comprised sufficiently by causally justified models. We therefore conclude:

The complexity of a system is defined by the number of its constituting elements and their heterogeneity.

Understanding Family Businesses

For a long time, family businesses were classified in distinction to “non-family businesses”, anonymous business or publicly owned firms. The used definitions are built on components such as the equity share of the family, the participation in the management of the company or the intended and/or the fulfilled alternation of generations. The dichotomous classification in family and non-family businesses which underlies those approaches is artificial according to Astrachan et al (2002). In their approach of the so called F-PEC, the authors assume that the influence of one or more families on a business is rather continuous. They therefore develop a scale that makes the amount of respective influence measurable that a family has on a firm. The scale is based on three components: power, experience and culture. The initial letters simultaneously constitutes the labelling of the family influence scale.

For this article at hand, the absolute amount of family influence on the firm is of secondary importance. Single elements of the family business system can be addressed within the context of the complexity of the subsystems. For instance it can be assumed that a business which is completely owned by a single family member is significantly less complex than a business where several family members as well as non-family members have a holding (Miller et al, 2007). For the work at hand, *the existence of a significant influence of a family on a business* as a constituting element for a family business is exclusively important.

Albeit the field of family businesses is still new, there are several models that can describe and explain this species. An overview of the so far presented models is found in Pieper & Klein (2007). In this contribution, I draw on the so called *Bulleye*, a multidimensional model that is based on an open, systematic approach. This model differentiates between four levels of analysis: individual, subsystem, company and environment. Furthermore, the system of family business is constituted by the subsystems family, company in the market, ownership and management (Pieper & Klein, 2007). This model is built on the observation that a family business is made up of the two elements - *family* and *business*. Those, in turn, are interconnected through streams of factors. That, on the one hand, is capital that the family provides as owner of the business and for which the family gains more influence on and dividends of the company; on the other hand, it is the factor of labour that the family provides in the context of management and/or supervision to the company and for which the family receives a salary. These results in four subsystems: family, company in the market, ownership and management. Individuals are involved in all of those subsystems; when analyzing a specific problem such as the question of entrepreneurial orientation (Lumpkin & Dess, 1996) or succession (De Massis et al, 2008), the individual comes into focus. In other examples in the area of the strategic orientation of the company, the view is focussed on the level of the family business in its environment.

A family business is defined as an open system in which the family influences important decisions and which is constituted by the subsystems family, ownership, leadership, and business alike.

Corporate Governance of Family Firms

In the context of this work, corporate governance refers to the organization of strategic leadership and control of the business and the family. It aims at balancing the interests between the involved stakeholder groups. By means of extension of the business system around the family system, the business system becomes spotlighted by the corporate governance regulations. One of the involved stakeholder groups is explicitly the family of the business in its peculiarity as a family. The internal distribution of and the essential structures aiming to assure the predictability and responsibility of the acting persons need to be equally applied to the family members as for others that take over special tasks within the context of management. Therefore, corporate governance in family businesses comprises in addition to the classical business-governance also the family-governance as an integral part.

The basis for the corporate governance discussion in science was until recently almost only constituted by the principal-agent theory (Jensen & Meckling, 1976). This theory assumes a specific idea of man, namely that of the *homo oeconomicu*s who is acting with a short-term and opportunistic orientation while aspiring to maximise his/her personal financial utility. In particular, this last condition is increasingly questioned (Corbetta & Salvato, 2004; Lubatkin, 2007; Zahra, 2007). Benz and Frey (2007: 100) believe that the application of the principal-agent theory and its inherent excessive simplification is responsible for that the strong incentives of the "pay-for-performance" plans eventually led to that "managers [...] engage in deceitful and illegal activities". Zahra (2007: 71) suggests a different approach to corporate governance as he argues that corporate governance should be seen as a "socially constructed concept".

It is outlined that due to the heterogeneity of the type of business different explanatory approaches make sense for different family businesses. Thus, Jaskiewicz & Klein (2007) were able to show that with regard to German family businesses the size of the supervisory committee significantly differs (with equal size of enterprise) depending on the level of the goal alignment. Moreover, high goal aliment led to the acquisition of further resources and entrance possibilities to networks, following the resource-based-view (Penrose, 1959; Wernerfelt, 1984). In case of a low goal alignment, the firm adhered to the principal-agent-approach.

The a-priori goal alignment that does not need to be established by incentive and control systems constitutes a decisive variable in the context of optimal arrangement of the corporate governance. Trust and goal alignment are closely intertwined and thus inseparable. In case of a high level of trust, protagonist A assumes that he can predict the action of protagonist B and at most it is consistent with what protagonist A believes to be appropriate in this situation. Trust is defined as a basic condition so that certain procedures can be set aside that would have been necessary if the protagonists' goals would disclose huge differences. Due to the obviously high relevance of goal alignment and trust alike, the moderating variable of *trust* will be introduced in the context of this article.

Corporate governance refers to the organization of the strategic leadership and the control of the business and the family in which trust plays a pivotal role.

The Complexity Theorem: Understanding the Starting Point of Optimal Corporate Governance

The complexity theorem of corporate governance for family businesses is based on the systemic viewpoint of family businesses. A family business thus consists of the four subsystems: family, ownership, management and companies that are embedded in their common environment (see figure 1 below).

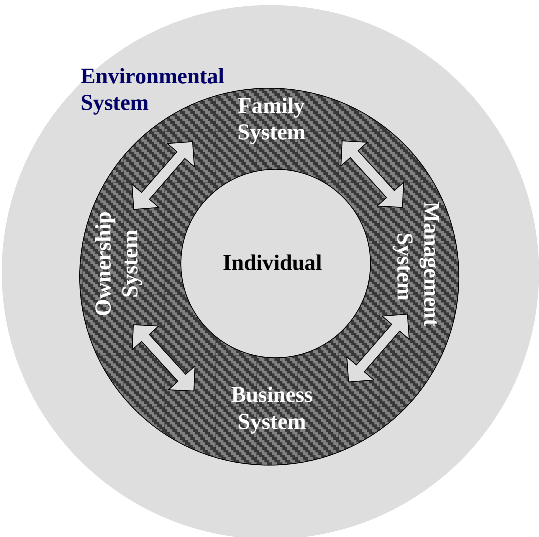

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Figure 1. The Bulleye: Open systematic approach of family businesses (Pieper & Klein, 2007: 309)

The Subsystems: Understanding how Family and Business Interact

A family business is constituted by a family and a company that are interrelated by ownership and/ or management. Here, single subsystems influence each other mutually. Individual protagonists can be members of one or several subsystems. The entrepreneur can for instance as father be a member of the family, as chairperson be a member of the management team, and as proprietor be a member of the ownership group. Simultaneously, an externally hired manager can be member of only one single subsystem as it also may be the case for a client or supplier as a member of a business subsystem. In general, it can be stated that the complexity of each subsystem increases with the increasing number of its elements (in this case of its members) and with increasing heterogeneity. In the following, the single subsystems are presented to show what determines their complexity.

Family

The elements of a family are its members. A family is consequently the more complex, the more members it has. An entrepreneurial family such as for instance the Haniel family with over 600 family members is clearly more complex than an entrepreneurial family as Henkel with less than 100 members or the family Deichmann with less than 10 members.

Furthermore, complexity comes with different age of the family members, with geographic distance between them, and finally with their goals and how important these respective goals are for each family member. As a simple example, age could range from 0 to >100 years. Within a family in which the parents are in their mid 40s and their both two children are in their mid 20s, there are no grandchildren yet, and the grandparents have passed away, the range of age, so to say the heterogeneity with regard to age is relatively low. In comparison, the range within the same family is significantly bigger if the grandparents are still alive in the end of their 60s and, on top, there is still a great-grandmother in the mid of her 90s as well as offspring that is two years old. Next to the absolute range of age the average difference of age between family members is a possibility to capture the heterogeneity due to the different ages. The resulting bigger heterogeneity increases the complexity of the family system and necessitates further communication structures to prevent destructive conflicts (and thus further costs).

Furthermore, geographic distance of the family members among each other (family in one location, family in Germany, in Europe, in the world) increases complexity. Concerning the goal setting, the more single utility functions of family members differ, the higher is heterogeneity and thus also complexity as well as in the subjective importance of the goal setting (Picot & Fiedler, 2002). The expected net benefit for the individual follows from the utility function that, on the one hand, reflects the goal setting and, on the other, shows the subjective importance of these goals. That, in turn, defines the magnitude with which the individual pursuits his/her goals even if it is against the interests of other family members.

The complexity of the family results of the following elements: the number of family members, the range of age of those members, the geographic distance, the difference between the individual goals, and the subjective relevance of those goals.

Depending on the level of complexity, the essential degree of family governance regulations can be estimated for the respective family. Here, mechanisms such as informal family meeting, formal, frequent, several times per year occurring meetings or even so called family councils and also family constitutions can be introduced. Pieper (2007) developed an interesting approach that depicts the solidarity of a big entrepreneurial family in a multi-dimensional concept with corresponding measures to fortify the different dimensions. He also differentiates with regard to the cohesion of single family members to the business family. He notes that cohesion can be financially but also emotionally motivated. The cohesion of the family towards the business also can be both, financially and emotionally motivated. Out of that emerges the dimensions of “family emotional cohesion”, “family financial cohesion”, “business financial cohesion”, and “business emotional cohesion”. A high degree of cohesion among the entrepreneurial family in long-term can also be observed where all four dimensions are be supported actively. That may, for example, be effected through rituals within the family (birthdays, common athletic or cultural activities), through financial cohesion to the family (financing of education, direct payment for an activity for the family), through rituals in the context of the business (meeting of the next generation, retiree dinner, gala dinner after the shareholders’ meeting), and through financial benefits (dividends, individual financial advantages, fringe benefits for shareholders).

Management

The entrepreneurial family influences the business through management and ownership (Pieper & Klein, 2007). The organization of management can reduce complexity; however, since it originates from corporate governance regulations such as internal rules of procedures for the advisory body and the executive board or the basic organisation of the company, it is not seen as the cause for complexity but rather as a possibility to handle it.

Regarding number and heterogeneity of elements as the relevant variables for complexity, for the executive board it means that the complexity of management is defined by the number of executive board members as well as its heterogeneity. The more executive board members the company has, the more complex are processes that are needed for coordination and communication. The heterogeneity of executive board members consists of different elements. Qualification here is important and in particular the differences between the respective qualifications and experiences play a major role. Whereas members of similar occupation groups usually speak a common language and hence have a mutual basis for communication, this basis still needs to be established for members of different occupation groups.

Moreover, the differences of particular origin of the directors are important. In an extreme case all directors come from the family business family. In other cases, directors from abroad or directors who before they entered the business have worked for considerable different companies (e.g. in a huge corporation) are found next to family members. Those differences in education, experiences and national mentality increase the complexity of management. The underlying idea of man also plays an important role in the area of management (Davis, Schoormann & Donaldson, 1997). The resulting subjective goals of single directors and their subjectively perceived relevance are important indicators for complexity. In case those goals of the members of the executive board are diverging and that they are also perceived to be highly relevant, the complexity and thus the necessity of regulating increase.

The complexity of the management system hence stems from the following elements: the number of directors, the difference between the particular qualifications, the difference of personal origin and life experience, the difference of the respective goals and their subjective relevance for the individuals.

Ownership

The complexity of the ownership system mainly stems from the number of perceived roles of owners as well as from the differences between share sizes. From the perceived roles and share size implicitly result the respective goal settings and their subjective relevance. This is also why they do not need to be separately mentioned in the area of ownership system.

The legal form of the company moderates the potential configurations of corporate governance regulations. The stricter legal regulations and standards with respect to the legal form, the less freedom exists with regard to corporate governance regulations.

The number of elements with regard to the ownership system refers to the owners. The more shareholders exist, the more complex communication and coordination becomes. Moreover, a higher role diversity of the individual protagonists also augments the complexity. A shareholder who simultaneously is a father/ mother, uncle/aunt, or a nephew/niece and may also be a director of the business compared to a sole owner has different interests. If also non-family, third party shareholders are involved, the degree of complexity rises again since it is assumed that the goals of the involved persons differ even more.

A further interest conflict which has been discussed many times in classical corporate governance literature exists between majority and minority shareholders (Shleifer & Visny, 1997). Those interest conflicts also increase the complexity in family businesses. A family business which, in the subsystem of ownership, has several shareholders holding an equal portion of shares is significantly less complex and therefore needs different regulations compared to one in which minority shareholders face majority shareholders.

The complexity of the ownership system hence results from the number of owners, the differences of their perceived roles as well as the differences of the different share sizes.

According to the complexity of the ownership system, classical corporate governance mechanisms such as the introduction of a supervisory committees or regulations under the company law can be found. Here, as will be shown, trust between the involved persons plays a major role. The deeper the trust between the protagonists, the lower is the necessity for formal regulations at a comparable level of complexity. Trust operates as a moderating variable. In consequence, family businesses with high goal alignment between owners and management have significantly less often supervisory committees; in case, supervisory committees are set up, those are significantly smaller and rather consist of non-family third parties than of family members (Jaskiewicz & Klein, 2007).

The Company in the Market

Interestingly, the company itself is often not mentioned in discussions about the appropriate corporate governance regulations. That might be due to the fact that the classical corporate governance literature refers to big, listed companies that are more similar to each other than are family businesses. Usually, those are stock corporations that are settled in different markets, often globally. Moreover, those companies are often connected among themselves through diverse relations, e.g. through a board interlock, through joint ventures abroad.

Family businesses are much more heterogeneous when looking at their respective positions in the markets. The spectrum ranges from companies with only one relevant product (ALDI) with most diverse procurement markets and sales markets in different countries, conglomerates with many very different products (Dr. Oetker) to small companies with only very few procurement markets, one product, and one major purchaser (Howe, Ulm). Here from, relevant requirements for respective corporate governance regulations results.

The structure of (external) financing also may increase or decrease the complexity regarding the company. In certain fields, family businesses are found to have a very low equity ratio and most diverse elements of external financing; others, however, depict an equity ratio of up to 100%. Corporate governance in terms of transparency for stakeholders was naturally geared to the number and structure of those stakeholders in the field of financing.

Hence, the relevant complexity of family businesses in the market results from the elements: number of sales markets, number of products, and number of procurement markets and the complexity of the external financing structure.

The complexity of the business subsystem needs to be reflected in the regulations of corporate governance. It can, in terms of access to networks, be reasonable to appoint a representative of relevant markets to a supervisory committee. On one side, the external financing structure, as far as a choice exists, needs to be accounted for. This can for instance be done by integrating stakeholders with a critical position into the work of the committees. One the other hand, in a business that is only acting in one market and on top of that is equity financed, it increases costs without increasing transparency to set up a supervisory board.

Complexity Theorem for Corporate Governance in Family Businesses

The complexity theorem for corporate governance in family businesses states that the complexity of corporate governance regulations has to reflect the complexity of the family business and its subsystems. If corporate governance is more complex than the structure of the family business, additional costs are incurred; being less complex leads to potential costs of conflicts (in terms of specific transaction costs of family businesses) and hence it results in a not optimal outcome.

$$\mathbf{C}_{\mathbf{FB,\,I}} = \mathbf{C}_{\mathbf{CG,\,i}}$$

The complexity $C_{FB,\,I}$ of the family business i consists of those elements

(1) $C_{FB,\,I} = \{C_{Fam,\,I}, C_{Man,\,I}, C_{Own,\,I}\ , C_{Com,\,i}\}$

($C_{Fam,\,I}$ Complexity of family system, $C_{Man,\,I}$ Complexity of management system, $C_{Own,\,I}$ Complexity of ownership system, $C_{Com,\,I}$ Complexity of company in the market)

and the complexity of the corporate governance system $C_{CG,\,I}$ needs to reflect it.

Complexity and Trust

In addition to the “simple” complexity, trust also plays a decisive role. Since the beginning of the corporate governance discussion based on the principal-agent theory, we know that the lacking goal alignment between principle and agent result in that the agent acts differently to what the principle perceives to be desirable for achieving his own goals (Jensen & Meckling, 1976). Davis, Schoorman and Donaldson (1997) established the Stewardship-theory as an alternative theory to the principle-agent theory. That theory is based on an idea of man diametrically facing a *homo oeconomicus* which can be traced back to Argyris (1964). The Steward is motivated to convert his principle’s goals into his own ones and acts accordingly. The relationship of the protagonists is marked by trust and thus follows different legalities than the relationship of two *homo oeconomici* which is marked by distrust.

The Role of Trust in Terms of Corporate Governance

The level of trust moderates the connection between business complexity and complexity of the corporate governance system in a company. Trust is defined as the probability that A assumes that B operates in way x and not in way y which is perceived as “wrong”. Hereby, a benefit arises when acting in way x; when acting in way y, loss is generated. The more intensely A trust in B that B will prefer action x, the lower is the necessity of A to ensure that B acts as A wants him to by means of regulations of any kind. A trusts in that B will do the what A perceives to be correct.

Trust is established through experience. If A and B have cooperated for years, A will have often experienced how B decides. A therefore trusts in B’s consistency of action believing that he is able to relatively reliably predict B's preferences. If A and B share the same value systems and goals, no or almost no deviation of goals occurs. A hence does not need to check whether B really follows A's goals since both, A an B's goals are similar.

That kind of goal alignment can among other things result from common value systems that stem from a very similar (or almost similar) socialisation. Values in terms of central concepts on a very high abstraction level can be found on the breaking point of the individual and society. Those are independent of time and situation and as far as possible are formed through socialisation in the early years (von Rosenstiel, 2007). It is therefore assumable that in entrepreneurial families a higher goal alignment is possible due to common value systems compared to groups of individuals that do not meet each other until adulthood. Moreover, the mechanisms of choice for non-family third parties as for instance for the occupancy of director positions can, besides the classical criteria for choice, also be strongly oriented on "soft factors" (Klein & Bell, 2007) to ensure a match of values.

It is to be stated that trust among individuals involved in a family business moderates the necessary complexity of the corporate governance system at a given complexity of the family business system based on common fundamental values.

Due to the long-term mutual acquaintance of family members and a possible high match of their values, an especially high level of trust is possible particularly in family businesses. The relationship between members of the family business system that are not family members as for example non-family directors or employees is also often of a long-term duration and marked by high trust. In cases where a high level of trust exists, the CG system can also be less formalized in complex family businesses in a following step.

Succession and Complexity

Succession in family firms is described as the transfer of ownership and management to the next generation. There are several possibilities how complexity of the family business system is influenced through succession. Gersick and colleagues (1997) distinguish between stable, evolutionary, and devolutionary successions in terms of complexity. In other words, complexity can stay the same, if, e.g., the eldest son inherits all shares his father owned and takes over the CEO position the father filled earlier. In terms of the management of complexity and with the goal to avoid changes in the level of complexity, this rather oldfashioned way of organizing inheritance and hence succession turns out to be favourable. Usually, there are changes in complexity during succession. A parent who divides his/her shares among several children will augment past succession complexity in the ownership subsystem accordingly. An incoming owner who appoints younger and more diverse managers to the board of directors does so, too. The question remains how to deal with changes in complexity during succession from a corporate and family governance point of view. Let's employ the complexity theorem for a more formal discussion.

The complexity theorem for corporate governance in family businesses

(1) $C_{FB,\,i} = C_{CG,i}$

allows for four different possibilities of influence to set up an optimal balance of complexity of the family business system and the corporate governance regulations. That four possibilities result consistently from the theorem itself.

If

(2) $C_{FB,\,i} \neq (1\text{-}T_i) * C_{CG,\,i}$ holds, either

(3) $C_{FB,\,i} \prec (1\text{-}T_i) * C_{CG,\,i}$ or

(4) $C_{FB,\,i} \succ (1\text{-}T_i) * C_{CG,\,i}$ is true.

C=Complexity; FB=Family Business; CG=Corporate Governance; T=Trust

In the case that $C_{FB,\,i} \prec (1\text{-}T_i) *C_{CG,i}$, complexity of the corporate governance system can be lowered to the point where $C_{FB,\,i} = (1\text{-}T_i) * C_{CG,\,i}$ holds. Cost reduction can hence be achieved without endangering the necessary transparency and accountability. Situations where the corporate governance system is more complex than it needs to be can evolve for instance because stakeholders due to their well-understood concerns transfer their experience from anonymous businesses to family businesses. Those situation can also occur since creditors, in particular banks, have a much higher necessity for transparency (to protect the bank's position, but also to safeguard the own career) than is reasonable for the company.

This type of disequilibrium only rarely occurs in the succession situation. If the corporate governance system is way too complex prior to succession it might pose problems for the successor(s) past succession as the corporate governance system itself is not easy to understand and to handle. This situation opens potential avenues for non-family members to act in their own favour and should therefore be avoided prior succession.

More often we find the case of $C_{FB,\,i} \succ (1\text{-}T_i) * C_{CG,\,i,}$. The complexity of the family business system outruns the complexity of the corporate governance system which was designed for the complexity prior to succession. In this case, there are several possibilities to react. On the one hand, the complexity of the corporate governance system can be adapted to the complexity of the family business system. That is often necessary when the complexity of family increased significantly due to an alteration of generations; yet, none or only insufficient systems in the area of corporate governance of the family subsystem are present. For instance, whereas it had been possible to bring together all family members in order to personally discuss important question, this is not possible if the number of family members increases by three times. Therefore, here for example formal meetings need to be introduced that by the help of trainings prepare the adolescent generation for their tasks as owners, etc.

Furthermore, one alternative – which can admittedly only be implemented in long-term – is to increase trust in the family business system. On the basis of common shared values a family can significantly increase the level of trust among the involved persons through education and communication in long-term, e.g. by opportunities of intense meetings. An example from the praxis is a huge entrepreneurial family that sustains a holiday camp for the adolescent generation (with suitable activities as swimming, fishing, paddling, soccer, night walks, etc). The members of this generation being in the age between 8 and 18 years old can get to know each other and build trust among each other due to common experiences. Yet, this example also outlines that this strategy can only be implemented with a very long-term orientation and with certain effort.

Thirdly, it is also possible to react to the disequilibrium by attempting to reduce the complexity of the family business system. Each reduction of the number of involved persons reduces complexity. For instance, a buyout of shareholders can restore the capacity to act without increasing the corporate governance complexity e.g. by the inauguration of an advisory board/supervisory board. A division of the company also significantly lowers the complexity of both, the family and the business system. This decision would generate independent family subsystems and business subsystems for instance as in case of Bahlsen to solve a conflict between protagonists after succession.

Discussion and Outlook

Corporate governance which ensures the transparency and accountability for all stakeholders is also decisive for family businesses. However, especially family businesses have to pay attention to implement only those measures that are necessary in the context of their company size and complexity. All implemented measures on top of that increase costs and hence decrease competitiveness. In the article at hand, the assumption was raised that the complexity of the corporate governance system needs to match the complexity of the family business system and the complexity of its subsystems family, management, ownership and company in the market. This will ensure optimal governance in the context of a cost-benefit ratio. This relation is moderated by the trust among stakeholders.

This paper aims to help family business owners to better understand how complexity and governance are intertwined and by that to design governance structures that meet the requirements of their businesses without raising cost above what is necessary. Furthermore, this papers provides a guideline to understand how complexity and by that the requirements for the governance structure alter through various types of succession. Knowing this, family business incumbents can anticipate the level of complexity past succession and implement prior succession an adequate governance structure that will match the requirement past succession. By that, incumbents reduce the potential conflict cost past succession.

However, a work like the one presented here also has its limits. First of all, this work solely presents a conceptual work that still needs to be empirically proven. Moreover, it will not be an easy task to carry out exactly this empirical verification since this work is built on a systematic understanding that generally struggles with the issue of how to operationalize. For research, the question will be raised whether and in how far the empirical examination of the complexity theorem will succeed.

In total, it is to be stated that the given complexity theorem of corporate governance in family businesses constitutes a first beginning to meet the particularities of heterogeneous groups of family businesses and hence to contribute to an optimal arrangement of control mechanisms in family businesses.

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