

Research Assessment Exercise 2020
Impact Case Study

University: The Chinese University of Hong Kong

Unit of Assessment (UoA): 20

Title of case study: The Governance and Succession of Family Firms: Research Impacts on Large and Important Private Firms in China and Southeast Asia

(1) Summary of the impact (indicative maximum 100 words)

The great majority of business organizations in Asia are controlled by founders and their family members. Many of these business owners are seriously challenged by their succession problems. Based on the insights from his pioneering research, Joseph Fan has advised family governance, ownership design, and succession planning for firms and their owners in Asia, including very large and important Chinese private-sector companies

and collaborated with the International Financial Corporation of the World Bank Group to design and install customized ownership, governance structures, and mechanisms for companies of national-level importance in Southeast Asia. Benefiting from Fan's research insights, these companies have implemented new structures and mechanisms to cope with their leadership transition. Without these changes, the companies' productivity and continuity would be threatened - a substantial social loss given their size and importance.

(2) Underpinning research (indicative maximum 500 words)

Joseph Fan has played a leadership role in a series of pioneering studies on family firms in Asia. His research focuses on the unique roles of firm founding family members in creating, utilizing, and transferring specialized *family assets* as well as various *roadblocks* challenging the family firms' continuity. *Family assets* are specialized intangible assets contributed by founding families. For example, family members' marital decisions could facilitate creation and/or enforcement of networks that are valuable to their firms [3.3]. Although *family assets* make family firms competitive, they challenge firm sustainability. In a study on the succession of 217 Asian Chinese family firms, Joseph Fan and co-authors report that these successions are associated with an average of 56 percent value dissipation during a five-year succession period [3.5]. The dramatic value decline during the firm succession period is strongly related to the difficulty in partitioning and transferring *family assets* from the senior generation to the next generation. For example, the retirement of the senior generation is often associated with decaying relationships internally between family members, and externally with stakeholders, including professional managers, suppliers, customers, and governments. The second class of factors that challenges family ownership is *roadblocks*. *Roadblocks* refer to obstacles at family, business, market, and institutional levels. For example, inheritance laws and family conflicts often challenge family ownership, as illustrated by the case of *Formosa Plastics Group*, a Harvard Business School Case by Fan and co-authors [3.1].

These concepts and research findings are synthesized in Joseph Fan's co-authored book, *The Family Business Map* [3.4]. The book proposes that firm owners should account for *family assets* and *roadblocks* in their ownership and succession decisions. Specifically, the more a firm's competitiveness depends on *family assets*, the more founding family members should be actively involved in managing the firm. The more a firm is challenged by *roadblocks*, the more diffused the firm's family ownership and control is, and vice versa. To illustrate the framework and concepts to both academic and non academic readers, the book includes numerous original case studies from around the world.

Joseph Fan's insights of family firms have important implications to the governance of the organizational form. For example, his research demonstrates that the common business group structure and lack of transparency in family firms is importantly related to the internal sharing of resources [3.6] including intangible *family assets* that are not easily measurable by accounting numbers [3.2]. Such internal sharing is critical to bypass external markets that are typically underdeveloped in emerging economies. Therefore, the key to improving family firm governance may not be limited to the formal legal and regulatory mechanisms that work in developed countries, but also informal family governance mechanisms that cultivate and regulate family members to be responsible and collaborative managers and shareholders.

Through his research, Joseph Fan has built an expansive knowledge base to guide practice, benefiting the governance and sustainability of many family firms and their founding families.

(3) References to the research (indicative maximum of six references)

- [3.1] "Formosa Plastics Group: Business Continuity Forever", Joseph P.H. Fan, Li Jin, and Winnie S.C. Leung, *Harvard Business School Case* (N9-210-026), 2010.
- [3.2] "Founder Succession and Accounting Properties", Joseph P.H. Fan, T.J. Wong, and Tianyu Zhang, *Contemporary Accounting Research*, 29(1), 2012, 283-311.
- [3.3] "The Value of Marriage to Family Firms", Pramuan Bunkanwanicha, Joseph P.H. Fan, and Yupana Wiwattanakantang, *Journal of Financial & Quantitative Analysis*, 48(2), 2013, 611-636.
- [3.4] *The Family Business Map: Assets and Roadblocks in Long Term Planning*, Morten Bennesen and Joseph P. H. Fan, Palgrave Macmillan, July 2014.
- [3.5] "The Family Business Map: Framework, Selective Survey, and Evidence from Chinese Family Firm Succession", Morten Bennesen, Joseph P.H. Fan, Ming Jian, and Yin-Hua Yeh, *Journal of Corporate Finance*, 33, 2015, 212-226.
- [3.6] "Revisiting the Bright and Dark Sides of Capital Flows in Business Groups", Joseph P. H. Fan, Li Jin, and Guojian Zheng, *Journal of Business Ethics*, 134 (4), 2016, 509-528.

(4) Details of the impact (indicative maximum 750 words)

Overview. Through practical workshops and consulting projects, Joseph Fan's family firm research has deeply impacted leadership succession, ownership structure, founding family governance and corporate governance decisions of private sector firms in China and Southeast Asia. With Joseph Fan's guidance, firms and their founding families have successfully designed and implemented their new governance mechanisms for family and business continuity. Below is a list of Joseph Fan's 12 impact activities. For illustration purposes, 3 representative cases marked with asterisks are further described in detail and supported by key person's statements.

Workshops on family governance and ownership design:

Anonymous Company, a 2nd generation family firm and the largest consumer good retailing group in Myanmar*; *Anonymous Company*, a 3rd generation family firm and major men's clothing manufacturer based in Hong Kong; *Anonymous Company*, a 1st generation leading real estate development group in central China; *Anonymous Company*, a 2nd generation family firm, the largest manufacturer of consumer products accounting for almost 70% of market share of its kind in Indonesia.

Consulting projects on succession planning, family governance, and ownership design:

Anonymous Company, a bed manufacturer based in Hong Kong with a history of over 50 years and a famous brand; *Anonymous Company*, a 3rd generation family firm and a leading publicly traded company of down products in Taiwan; *Anonymous Company*, a 1st generation resort/property developer in northern China; *Anonymous Company*, a 1st generation top publicly traded manufacturer of bedding and textile products in China; *Anonymous Company*, a 1st generation leading publicly traded manufacturer and designer of fashionable clothes in China; [REDACTED] manufacturing group in China*.

Consulting projects on leadership succession and corporate governance:

Anonymous Company, a publicly traded firm and a dominant leader of transportation vehicles of its kind in China; [REDACTED] equipment company in China*.

Impact Case (1): IFC Family Governance and Ownership Design Workshops.

As corroborated in its Testimony [5.1], the International Financial Corporation, the investment arm of the World Bank, engaged Joseph Fan to conduct workshops for their investment clients in Southeast Asia. In 2017, a family owning the largest consumer good retailing business with dominant market position in Myanmar gathered almost 20 family members spanning 3 generations to plan for their business succession and family governance. With respect to the workshop, Fan conducted a questionnaire survey about the family's key *family assets* and *roadblocks* [3.4; 3.5], then benchmarked the results against a large set of data that he and his collaborator collected from prior questionnaire surveys. The benchmarking analysis found that the family members shared values and relationships and that the firm enjoyed market leadership more than other comparable business families, and therefore transferring ownership and management within the family would be a feasible succession goal according to *The Family Business Map* model [3.5]. Accordingly, Joseph Fan guided the family in designing mechanisms to make joint decisions, share family goals, values, and relationships, all of which would help enforce long-term family collaboration as required of a closely held family firm.

After the first workshop, the 2nd generation family head wrote to Fan: "On behalf of our family, we would like to express our sincere thanks for conducting the Family Governance workshop for us. Everyone that attended enjoyed the workshop and realised the value of the workshop and completing the family governance constitution. We are very glad to have this workshop done at this time which will pave the way to sustain the business, family harmony and legacy for the long term." A first generation senior member wrote to Fan: "It was a great two days making our family members understand how important it is to entrench the philosophy of family constitution... I am very happy having the opportunity to learn and share so many valuables which is intangible from you and the team."

In a follow-up workshop, Joseph Fan guided the family in designing a family holding company structure to consolidate dispersed family assets and ownership shares based on principles and guidelines derived from his research [3.4; 3.5]. He further guided the family in designing ownership transfers and board mechanisms to consolidate family control, induce family incentives, facilitate firm productivity, and ultimately achieve the family succession goal suggested by the *Family Business Map* analysis [3.4; 3.5].

As acknowledged in the Testimony [5.1], the workshops resulted in two important documents: a *Family Constitution* [4.1] and a *Family Holding Company Shareholding and Governance Policy* [4.2], incorporating the family's succession goal, as well as ownership and family governance mechanisms. Since then the family has been implementing these mechanisms, and achieving significant improvement in family governance and corporate governance according to feedback from the family head in 2019.

Impact Case (2): Succession and Governance of the founding family of [REDACTED] Group (China).

[REDACTED] The founder of the group is one of the most senior and successful entrepreneurs in China. Through his colleagues' recommendation, he read and became familiar with Joseph Fan's research [3.5] and professional writings. In 2015, He invited Fan as an expert consultant to plan for his business ownership succession and family governance. As corroborated in his personal statement [5.2], in the following three years, Fan guided

the founder and his family in completing a *Family Constitution* [4.3] detailing various family governance topics, including family goals, values, decision rules, business venturing, charity projects; and a *Family Succession Agreement* [4.4] detailing family business succession, ownership structure and associated decisions, along with transfer and payout mechanisms. Accordingly, the family has been educating family members and implementing the governance mechanisms since then, making smooth advancement according to the founder.

Impact Case (3): Governance and Leadership Succession of [REDACTED] Company (China). [REDACTED]

In 2014, Joseph Fan was invited by the secretary of the board of directors of [REDACTED] as an expert advisor on designing the governance structure and mechanisms associated with the company's foreseeable leadership succession. As corroborated in the board secretary's statement [5.3], in the following three years, Fan conducted a series of workshops in which he presented analyses and cases from *The Family Business Map* [3.4] and his other research, and guided the discussion of various relevant topics.

[REDACTED] it is clear from this project that it benefits from family firms' wisdom and practices. In particular, family firms are sustainable because they have family governance mechanisms to share *family assets* among family members [REDACTED], they engage ownership mechanisms to delegate decision rights to capable and responsible family leaders [REDACTED], and they customize corporate governance mechanisms to create healthy check and balance.

In 2018, as an outcome of the workshop series, [REDACTED] created a new *Corporate Governance Charter* [4.5] incorporating the governance framework and detailed mechanisms for the new leadership era, including new decision bodies and rules to ensure effective decision making, new monitoring bodies and rules to enhance check and balance, new ownership and incentive mechanisms to induce collaboration and productivity, and new mechanisms to cultivate and transfer corporate values. The Company has been in the process of implementing and fine tuning the new governance design and progress has been good according to the board secretary.

References:

- [4.1] *The (anonymous) Family Constitution*, 2017
- [4.2] *The (anonymous) Family Holding Company Shareholding and Governance Policy*, 2018
- [4.3] *The [REDACTED] Family Constitution*, 2017
- [4.4] *The [REDACTED] Family Succession Agreement*, 2016
- [4.5] *Corporate Governance Charter*, [REDACTED] Company, 2018

(5) Sources to corroborate the impact (indicative maximum of 10 references)

For proprietary reasons, the aforementioned documents associated with the cases are not available. However, the key persons of these cases have provided their testimonies ([5.1], [5.2], [5.3] as attached) that corroborate the impacts stated in this report.

[5.1] Statement of Mr. J. Chris Razook, Corporate Governance Lead, EAP, IFC-World Bank Group, Hong Kong SAR, China

[5.2] Statement of Mr. [REDACTED], Founder of [REDACTED], China

[5.3] Statement of Mr. [REDACTED], Chief Secretary of the Board of Directors, [REDACTED], China