

Conflicts and Disputes in Family Businesses

how best to avoid them to maintain harmony within the family?

Many family businesses are faced with the same challenges as other businesses. However, in a family business where there exist personal relationships between members, different considerations apply when things go wrong.



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Key Points	<p>What is the issue? Conflicts and disputes in family business can arise in different sub-systems of a family business system ("FBS").</p>
	<p>What does it mean for me? Each sub-system of the FBS is different and have different priorities competing for limited resources, which contributes to family conflicts.</p>
	<p>What is Key take away? Conflicts in the FBS must be handled with care and ways to improve family relationship to minimise tension and/or conflicts.</p>

Where there is a conflict in a family business, relationship will always be at stake. As Irish-American novelist **F. Scott Fitzgerald** said, "Family quarrels are bitter things". Also, as the saying goes, it is complicated enough when people bring 'work' problems home, or 'home' problems to work, but in a family business, the two worlds are often interconnected, so that what happens in each sub-system would potentially affect the other.

For this reason, if conflicts in a family business are not handled with care, it can create long lasting harm for the family as members (unlike outsiders) in dispute cannot simply walk away even after it is purportedly resolved because of the familial relationship and other ties that bind them, e.g., ownership stakes or careers in the family business.

Before one delves deeper into the subject of family conflicts, it may be useful to appreciate the concept of the *Three-Circle Model of a Family Business System* ("FBS") which was developed by **Renato Tagiuri and John Davis at Harvard Business School** in 1978. In their findings, they described the Three-Circle Model (the "Model") of the FBS being constituted by 3 sub-systems, i.e., Family, Ownership and Business sub-system as depicted in the diagram below.

From the Model, it is apparent that every individual in a family business can be placed in any one of the seven segments of the Model and understanding this helps to better appreciate their perspective on key issues affecting the family business, and even predict

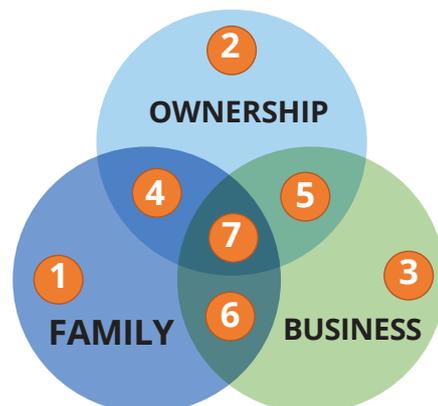


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their motivations, fears and expectations. This in turn goes a long way to help avoid family conflicts or disputes and preserve family harmony.

Conflicts in family businesses are sometimes hard-wired into the FBS as they are inherent realities of working in a family business. Alternatively, conflicts of interest can arise when people in the FBS are expected to perform various roles in the system. People in each sub-system have different priorities that may compete for limited resources, e.g., time, money and jobs, which are always finite. For this reason, it is inevitable that conflicts between competing interests in the overall FBS will arise. Examples of typical family conflicts

Three-Circle Model of the Family Business System



Legend for Three-Circle Model of the Family Business System		
Segment No	Description of segment	Concerns/Motivation
1	Family members (do not work in family business and with no equity)	Lifestyle, family legacy and family reputation.
2	External Investors (do not work in family business and not family member)	Return on investment, business exit and information flow.
3	Management and employees (neither owner nor family member)	Career prospects, job security and nepotism.
4	Non-working family owners (family member with equity but do not work in family business)	Financial expectation, sense of duty to support business and seek control (depending on size of stake).
5	Employee owners (non-family member with equity given as part of remuneration)	Career development, return on investment or cash out on termination.
6	Family employees (family member work in family business but no equity)	Career development and prospects of ownership through transfers from parents in future.
7	Working family owners (family member with equity and work in family business)	Profitability and success of business, wear multiple hats and succession issues.

(non-exhaustive) that can arise in a family business and proposed solutions are set out below for illustration:

Case 1

If there is only one person to be appointed the next CEO and the family has three (3) siblings who would like the job in the family business, then the manner in which this role is allocated could potentially lead to a conflict. The question of who takes over as the next business leader first centres upon whether it be a non-family member, e.g., employees (Segment 3) or a family member (Segment 1)? There is no question that the family would choose someone among them, except that if all three siblings are equally capable, this surely presents fertile ground for conflict!

The consequences of each decision are clear, the risk of losing a capable member of staff or possible family discord.

Case 2

In the ownership sub-system, there could be inherent conflict between family owners (Segment 4) who would like an increased dividend to maintain certain lifestyle, but the Board would like to retain profits or invest in capital expenditures for the business (a desire among family employees (Segment 6)) so how funds are allocated to meet the conflicting demands of the different stakeholders could cause friction or conflicts between different sub-systems in the FBS.

The consequences of no retention of profits for investment/expansion could lead to stifling business growth which should be weighed against no distribution, and hence non-working family owners cannot depend on distribution as a source of income to finance their lifestyle.

Case 3

Where family members have to perform different roles or wear different hats, this could cause positions of conflict, e.g., an individual family shareholder may serve as director of the company (Segment 7), and simultaneously is trustee of a family trust created for the benefit of certain family beneficiaries. Inevitably, this could create positions of conflict for the individual as he has different duties as director of the company and as trustee of the family trust, and interests of the parties may not necessarily be aligned.

The consequence of this is that the individual with conflicting roles would find it difficult to reconcile his thoughts and feelings with the duties and responsibilities expected of the position bestowed upon him by the family business.

Solutions

Looking at the facts of each case against the backdrop of the Model, it requires sensitivity to handle the diverse individual needs across different segments of the Model so that conflicts of interest and potential disputes in each instance may be avoided or mitigated:

In **Case 1**, if the family has a written Constitution which provides for their shared purpose and a family mission statement, including a statement of family values and beliefs and an outline of family business principles articulated, for example, on the following principles:

- Only the best person for the business can be CEO.
- A business must have only one leader (not co-CEOs) akin to a ship must have only one captain.

- The roles of CEO and Chairman must be separate and where possible, assumed by family member(s).

then having defined the principles of how business succession is to be adopted, this could be used as a guide when appointing CEO for the family business.

In **Case 2**, if the family company has a dividend policy (which is transparent to shareholders) which allocates amount set aside to align with company's goals (e.g., capital expenditure budget) and amount available for distribution to shareholders, this would enable family members to know in advance to what extent they can depend on dividends to support their lifestyle.

In **Case 3**, if the Settlor setting up the trust at the outset has provided the trustee with a clear letter of wishes how the Trust is to operate and circumstances under which distributions are made, this would provide clarity to the individual acting as trustee while holding the position of director at the same time.

Observations/recommendations for mitigating family conflicts

- 1) Since conflicts in business emanate from anxieties inherent in the FBS, it is always advisable to face up to them and deal with the underlying issues that cause the anxieties.
- 2) Families sometimes employ the technique of sustaining apparent disputes to avoid or delay a bigger discussion, e.g., succession in family. They believe this approach is more tolerable and better than trying to unpack the bigger issues which can turn out to be a can of worms.
- 3) There is a popular myth that, if something is not talked about, the family will be stronger because there are no fights. However, the reality is that when families have the ability to agree to disagree on important issues and they are resolute to employ tools to resolve their conflicts, they develop far more trusting relationship.
- 4) An adversarial approach to resolving family conflicts/disputes, no matter how good one's intention, can accelerate a system's descent into costly litigation that may also compromise or destroy personal relationship among family members.
- 5) Always remember the cliché "Don't wash your dirty linen in public", the Chinese equivalent proverb (家丑不可外扬) (in Hanyu Pinyin "Jiā chǒu bù kě wài yáng") as this would make public family conflicts/disputes which can be embarrassing for the family (reputational harm), and the negative publicity could potentially cause disruption to the family business. Hence, the important lesson is always to nib a problem in the bud before it develops into a bigger problem!
- 6) Some of the ways to improve family relationship to minimise tension and/or conflicts:
 - Develop empathy for each other.
 - Work on communication skills, try to be a good listener.
 - Always have the best interests of the business at heart.
 - Allocate family time to connect just for fun where no business talk allowed.
 - Harness relationship built on trust, love and care for each other.
 - Develop a family code on how family members should treat each other.
 - Develop a process for resolution of family conflicts/disputes.
 - Don't be afraid to reach out for outside help (advisors) in the face of any adversities. ■

