Family Businesses: The pioneers of Sustainable Corporate Governance

European Family Businesses (EFB) is a federation of 15 national family business organisations. European Family Businesses strives to make political decision makers aware of the contribution of family businesses to society and to promote policies that are conducive to long term responsible entrepreneurship. Our members represent a turnover in excess of one Trillion euro, and over 9% of European GDP.

Sustainable Corporate Governance is at the heart of any good family business, as it is with many companies. Because of a culture of responsible and generational ownership, sustainability is built into family businesses and is propelled through the values that guide them. Whilst European Family Businesses fully supports initiatives that would encourage all companies to adopt more sustainable practices and supports the need for effective corporate governance, EFB believes that the European Commission needs to adopt a cautious approach to regulating corporate governance. A prescriptive and overreaching proposal would make life more difficult for long-term orientated, responsible businesses.

1. Varying Ownership Models: Businesses across Europe tend to favour concentrated ownership business models as opposed to dispersed ownership. Inside these concentrated models, values drive the business, and these instill responsibility.

2. Responsible Ownership: Family Business owners instill family values throughout a company and ensure that it is ready to pass onto the next generation. Therefore, family ownership is, by essence, responsible and plays a fundamental role in sustainability practices and the guidance of a company's strategy.

3. Overcoming Short-Termism: Short-term thinking in a business can have an adverse effect on sustainability and the perception of companies. One of the clear advantages of family companies is their long-term approach, meaning sustainability is already built into the fabric of these enterprises.

4. Regulatory burden: The European Commission has committed itself to lessening the regulatory burden on companies. However, increased reporting

requirements from additional Corporate Governance provisions could place an unnecessary burden on businesses which they could certainly do without in the current economic climate.

5. Education rather than obligations: Instead of imposing restrictive, formulaic, provisions on a company's corporate governance, the European Commission should focus on promoting responsible business owners and directors. Europe should showcase its leaders in sustainable business and provide best case examples for EU businesses and the rest of the world to follow.

Sustainable Corporate Governance is at the heart of any family business, as it is with many other companies. EFB believe that Sustainable Corporate Governance is a key element to delivering the European Commission's Green Deal programme, which EFB fully supports. Whilst EFB welcomes the introduction of a proposal on Sustainable Corporate Governance from the European Commission and agrees that changes need to be made in business, EFB believes that any future proposals must take into account the nature and diversity of the different types of companies in Europe, not only regarding the size but also the structure of its ownership.

1. Varying Ownership Models

Corporate governance measures are based on the principle that management and owners are different individuals with different interests, something that can often be the case in listed companies with dispersed ownership.

However, it is incorrect to assume that the dispersed ownership model is the case for all businesses across Europe. In fact, most businesses in the EU have concentrated ownership structures, vs the Anglo- Saxon model of more dispersed ownership, with the most effective of these models being via concentrated ownership via a family.

The majority of family businesses have concentrated ownership models, even if they are listed. In fact, the latest statistics from the Netherlands tell us that 93% of family businesses are owned by 1 family, and of the top 500 performing businesses in the Netherlands, half of these are owned by families or single owners.[1])

In a family business, as with many businesses, an owner can often be the manager or there is often a closer alignment of interests between the owners and the management through internal structures such as family councils and family members sitting on the Board of Directors.

[1] CBS, Rapportage Familiebedrijven in Nederland 2015-2018, October 2020.

This creates an air of responsible business through the family values that drive the business: concentrated ownership creates responsible businesses. Belgian company SIPEF are an example of this as despite being listed on Euronext Brussels, they are still run-in part by the Bracht family and remain pioneers of sustainability, featuring a sustainability department and a longstanding sustainability commitment since 2004.

2. Responsible ownership

Family business owners act as the stewards of the company ensuring that it is left in a better state compared to when they found it. Therefore, owners and directors of family businesses have a duty of care and genuine emotional links to the business. They aim to strengthen company purpose and resilience for all stakeholders.

Therefore, generational ownership drives sustainability as this is the only way to ensure survival to the next generation. This is not only sustainability at an environmental level but also at a social level (commitment to the community they live in) and business level (companies need to be profitable to be sustainable). Sustainable Corporate Governance is built into family businesses because it is instilled through the family values that guide these businesses. They are sustainable by nature.

For example, Van Wijhe Verf, a paint producing family business from the Netherlands were able to invest in a 2-year R&D programme to find a natural way of producing their paint from starch as opposed to the oil-based resins that have long been a key component of paint. This R&D project created a greener product which ensured that the business was ahead of the sustainability challenge and in a great place for when the time arrives for it to be transferred.

There are many family and privately-owned businesses who have developed effective governance structures for decades. They not only include independent boards of directors but also ownership bodies like family councils, owners' councils, family assemblies and documents like a family constitution or family charter. In fact, in recent times, we have seen a trend in these businesses to establish specific sustainability committees that ensure businesses comply with targets and can explain why they act in certain ways.

In 2014, Dutch family business Bavaria created a family manifesto in which they challenged themselves to achieve ambitious sustainability goals including generating at least 50% of energy by sustainable sources and achieving 10% savings on energy, water, wastewater, waste and packaging per year from 2016 to 2020. Following the establishment of their manifesto, in 2016, Bavaria began publishing an integrated report detailing both their financial reports but also their sustainability efforts.

3. Overcoming Short-Termism

EFB recognises that Sustainable Corporate Governance can be an effective solution to the problem of short-termism which is found in a small number of businesses.

The majority of private businesses that remain unlisted are not under pressure from market-based forces to increase their quarterly earnings and can be driven by long-term shareholders and projects. These long-term investors often have restricted stock. It is therefore essential that policy makers understand that accountability to the owners is at the heart of the formulation of good corporate governance. In other words, the ownership structure of a company will have a decisive impact for the governance structure. This should be recognised by the Commission as the assumption that listed companies have inherent short-termism is not the reality since many are run with family values.

EFB is of the belief that the most effective way to combat short-termism is to better incentivise long- term investor behaviour. Shareholders who make a long-term commitment to businesses and who play an active role in the strategic direction of a company, should be rewarded through fiscal incentives.

EFB welcomes the fact that the European Parliament Report on Sustainable Corporate Governance clearly recognises the importance of retained earnings for the long-term performance of companies. 2Member States should realise that any fiscal burdens on ownership as such (in the form of net wealth, gift or inheritance taxes) form a threat to long-term responsible ownership, as they inevitably drain the retained earnings.

4. Regulatory Burden

With the recent publication on the new SME strategy, the European Commission made it clear that they intend to, where possible, decrease the regulatory burden on SMEs and Family Businesses. There is a risk that new provisions under the Sustainable Corporate Governance strategy could have the reverse effect on facilitating SME Listing as established in the Capital Markets Union, but also could increase Non-Financial Reporting obligations for businesses; an increase in red tape that companies can

[2] https://www.europarl.europa.eu/doceo/document/A-9-2020-0240_EN.pdf

scarcely afford at the moment and has been prominent in recent non-financial reporting directives[3] [4]

In fact, these new regulations would make life harder for our European businesses. If they have to worry further about legal liability, stakeholder interference and greater regulatory burden, they will become more risk averse, less agile and less competitive and this will slow the progress of the much-needed green transition. Whilst the initiative argues that this will not be the case for SMEs, it is difficult to see a world where this increased administrative burden would not impact all types of businesses.

Furthermore, the European Commission should also revise the impact of red-tape not only for SMEs but for our medium-sized businesses across Europe. EFB recognises that the non-financial reporting directive and sustainable corporate governance are intertwined; however, EFB does not endorse this position. EFB believes that the European Parliament's call for the enlargement "of the scope of the NFRD to cover all listed and non-listed large undertakings established in EU territory, as defined in Article 3(4) of the Accounting Directive;"5 is damaging for businesses, especially as they class large undertakings to be companies that employ 500 employees or more.

Our medium-sized businesses should not be burdened with the same legislation as large businesses. Our medium-sized businesses are often regional champions and have significantly fewer resources than our large, often multinational, businesses. They should be protected and encouraged to grow sustainably; thus, administrative burden should be lessened also for them.

Through its Non-Financial Reporting declaration, the Commission has already increased the burden upon business owners and boards, therefore EFB strongly advises the Commission to carefully remember its commitment to reducing red-tape for businesses and wishes to warn about the risks of excess red tape that could easily lead citizens and companies in the Member states to become frustrated with the EU and its' institutions.

Finally, if new mandatory regulations in the field of sustainable corporate governance were to be considered at an EU level, European Family Business calls for any potential impact assessment to take into account the importance of company ownership and family businesses. For example, the SME test was created to take into account the

[3] https://www.europarl.europa.eu/doceo/document/A-9-2020-0155_EN.html

[4] https://ec.europa.eu/info/business-economy-euro/banking-and-finance/financial-markets/securities-markets/sme-listing-public- markets_en

[5] https://www.europarl.europa.eu/doceo/document/A-9-2020-0240_EN.pdf

specific needs of SMEs, the European Commission should apply the same concept to family companies by creating "the family business test".

5. Education rather than Obligations

Instead of creating more obligations on businesses through increasing red tape and administrative burden, the Commission should present plans to increase awareness of effective Sustainable Corporate Governance practices in Europe. EFB believes that instead of imposing restrictive, formulaic provisions, on a company's governance, the European Commission should formulate guidance and educate board members on how to integrate sustainability into their business plans and how to set these as genuine business objectives to ensure a commitment to developing sustainability within a business. Europe should showcase its leaders in sustainable business and provide an example for the rest of the world. EFB would be willing to help the Commission with this process.

This guidance should include the sharing of best practices so that other businesses can learn from what other, sometimes similar, businesses have done and take lessons from these. As suggested by EcoDa, EFB agrees that the establishment of a Commission Advisory Group on Sustainable Corporate Governance to identify good practices on stakeholder engagement and involvement would be an effective way of doing this as long as the differences in terms of Corporate Governance models are taken into consideration.6 Promoting the exchange of best practices could be a useful exercise for many unlisted companies, of which most are family businesses, to organise their governance as well as responsibilities to their stakeholders.

Moreover, for entrepreneurs and start-ups, this education should include support and education alongside their financing and obligations to improve their commitment to sustainability. They should be educated in how to set up an effective board and have to set up boards that are able to give a clear sustainable business direction whilst also being dutybound to give clear explanations for strategic choices. Responsible family business owners could provide the much-needed expertise to policy makers and a way of doing this could be as part of the Commission Advisory Group.

Educating business owners on how to adapt to the sustainability trend is more productive for businesses and directors alike and can help Europe to become global leaders in the sustainable business challenge. Through educating business owners in

[6] https://ecoda.org/wp-content/uploads/2019/08/20201002-EC-Impact-assessment-on-Directors-duties-ecoDas-Response- FINAL.pdf

sustainability rather than providing them with restrictive obligations, directors and business owners can be free to create their own governance structures involving sustainability at their heart that take into account the cultural specificities of a family business and provide examples and case studies for businesses across the world in the global effort to increase the focus on sustainable business.

Concluding Remarks

As such, whilst EFB is favourable to the European Commission's proposal to promote the practice of Sustainable Corporate Governance, EFB notes that the Commission must be cautious in its approach. EFB believes that any future proposal must not be too wide-reaching and burdensome on companies, particularly for those who are long-term orientated, because of "systemic short-termism" in some companies.

Therefore, any future requirements should be encouraged on a voluntary basis only and targeted towards those businesses that must adopt more sustainable practices and where responsible ownership is not present.

In furthering the legitimate and important sustainability goals of the EU, companies remain very much part of the solution: they innovate, they invest, they look for new ways of reducing their environmental impact, they employ, they pay taxes, and they fulfil the needs of customers. They are doing all this primarily because it is vital for their competitiveness, success and long-term survival, not because they are forced to do so by laws and regulations. This basic fact must not be overlooked in any discussion on sustainable corporate governance. The potential or perceived positive impact of company-related regulatory measures on other stakeholders should therefore not be overemphasized, nor should the negative impact on companies themselves be taken too lightly: if companies are put to suffer, then they will simply be in a weaker position to contribute to society.

FEBRUARY 2021

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