MARRYING CORPORATE LAW AND FAMILY BUSINESSES

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ABSTRACT

Family-owned companies are a growing part of the global economy. Although they hold a place of honor in management and finance literature, they are almost absent in law. In family-owned companies, in addition to ownership and control interests, there are also family considerations, which are not necessarily economic or rational, that positively and negatively challenge the assumptions underlying accepted corporate analysis. These issues require re-examination. This Article first seeks to lay out a conceptual and theoretical basis for a legal discussion on the complex world of private family companies. Second, the Article examines the suitability of "ordinary" corporate laws and prevailing theory as applied to family companies, particularly private companies. This Article presents the familiar agency theory—as well as the stewardship theory—which will likely have a persuasive and significant impact on the functioning and performance of family companies. Third, this Article examines the neglect and unsystematic treatment of family companies by corporate law. Fourth, the Article proposes a new, incremental model to examine the intensity of family control in companies that are subject to judicial review and suggests voluntary adoption of professional and independent counseling mechanisms to assist in company management and to minimize legal exposure. In the Authors' opinion, this model can be of use to family firms, especially those with an a priori suspicion of significant conflict of interest caused by overlapping family, business, and ownership systems. This Article's purpose is to enrich and refine the conventional discussion on corporate law and improve the theoretical and practical dialogue between ordinary companies and family companies.

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I. INTRODUCTION

As every law student learns, companies are independent legal entities that are detached from their shareholders.[1] This legal structure, whose financial and social importance cannot be overstated, is reinforced in the present era when many mundane and legal activities are carried out within the framework of companies, some of which hold greater economic power than many countries.[2] However, behind the scenes, and despite this basic

1. *See* Salomon v. Salomon & Co. [1897] AC 22 (HL) 27 (appeal taken from Eng.).

2. Vincent Trivett, *25 US Mega Corporations: Where They Rank if They Were Countries*, BUS. INSIDER (June 27, 2011), http://www.businessinsider.com/25-corporations-bigger-tan-countries-2011-6; Gary Younge, *Who's in Control—Nation States or Global Corporations?*, GUARDIAN (June 2, 2014), https://www.theguardian.com/commentisfree/2014/jun/02/control-nation-states-corporations-autonomy-neoliberalism.

legal idea of separate and independent legal entities, considerable theories and doctrines of corporate law stem from the actual structure of ownership and control of a given company.[3] In fact, this is precisely the starting point of the legal analysis that has dominated corporate law since the 1932 publication of Berle's and Means's important book, which identified the agency problem arising from the inevitable separation between ownership and control in corporate governance.[4] This starting point is based on the understanding that although each company is a separate and independent legal entity from its shareholders, the ownership structure of the company and the manner in which it is controlled and managed in practice hold considerable economic, legal, and social significance.[5]

The purpose of this Article is not to add to the considerable ink already spilled over the ideas mentioned above; rather, it is to add new insight to the legal discussion on family-owned and family-controlled companies.[6] In these companies, in addition to ownership and control interests, familial and emotional considerations also exist, which are neither economic nor rational, and challenge the assumptions underlying accepted corporate analysis.[7] These considerations are positive, as well as negative, insofar as they relate, *inter alia*, to corporate efficiency and stability, stakeholder tensions, existing and desired corporate governance mechanisms, and corporate business objectives. Surprisingly, while family companies are a special phenomenon

3. *See infra* Part III.A.

4. *See* ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 120–21, 124 (1932); *see also* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure* 3 J. FIN. ECON. 305 *passim* (1976).

5. *See infra* Part IV.A.

6. This scenario is opposed to a situation in which family representatives are not actively involved in the ongoing management of the company (passive control). As described below, a passively controlled family company is more similar to a "regular" nonfamily company with a controlling, central factor; accordingly, "family" characteristics and tendency to mix domains will be weakened.

7. Jan-Folke Siebels & Dodo zu Knyphausen-Aufseß, *A Review of Theory in Family Business Research: The Implications for Corporate Governance*, 14 INT'L J. MGMT. REVS. 280, 286 (2012). *Contra* File No. 10582/02 CA, Abu v. Hamadia Doors (Oct. 16, 2005), Nevo Legal Database (by subscription in Hebrew) (Isr.) ("Indeed, one cannot ignore the fact many Israeli companies are family companies, and we must be very careful not to discourage their incorporation. However, the approach towards them, as indicated by courts' previous decisions, is based on court experience and common sense. Thus, as far as the family structure is concerned, there is a greater chance of mixing between the good of the company and the good of the family.").

and constitute a growing layer of local and global economies—and even though management and finance academics have written much on the subject—the subject of family companies is generally absent from legal literature. This lack of proper and consistent attention adds to the misunderstanding of family companies in an already complex world of business organizations.[8]

Hence, this Article intends to stimulate discussion on this central issue; open the door to a more comprehensive legal analysis of family companies in general; point out the differences among a variety of companies; assess the suitability of applying accepted corporate theories (one of which is absent in legal literature and case law) to family companies; and examine the relationship between existing and desired laws. This analysis also reviews the question of what private family companies can learn from "ordinary" companies and vice versa. More specifically, this Article focuses on the inherent failures of private family companies and offers mechanisms to assist them in both business and legal matters, mechanisms which might help to mitigate the business, emotional, and legal tensions within family companies and improve their ability to survive and cope with potential judicial review.

This Article begins its discussion in Part II by defining family companies and describing their growing status in the business sector. Part III discusses accepted corporate theories in the managerial world (of which only one—the "agency theory"—is recognized in conventional legal analysis) and the adaptation of those theories to family companies. Part IV examines the unique characteristics of private family companies that explain their advantages over nonfamily companies but also the major failures that cloud their operation and performance. Part V examines issues from a legal standpoint and begins by surveying judicial review of family companies, highlighting the absence of a definition, legal doctrine, and legal theory for family companies. Part V then proposes a definition of family companies and parameters for judicial review on a sliding scale, both of which are based on the theories discussed therein. The conclusion of this section offers a voluntary mechanism to improve the corporate governance structure of private family companies that will mitigate some of the failures cited above, and which is discussed in length in Part IV. Part VI concludes.

8. *See* Rebecca Hirsch, *Decoding Family Businesses: Are Corporate Governance Guidelines Necessary for Family Businesses?*, 17 N.Z. BUS. L.Q. 126, 126, 132–33 (2011).

II. DEFINING A FAMILY COMPANY

Family businesses are considered one of the most ancient commercial organizations.[9] Most businesses, from small corner shops to multinational or public corporations, have many common familial elements.[10] Today, family companies constitute a significant component of the global economy, both in volume and percentage of total number of companies in the marketplace. Their high rate is a universally recognized phenomenon in many countries including the United Kingdom,[11] the United States,[12] Germany,[13] the

9. *See* Manfred F. R. Kets de Vries, Randel Carlock & Elizabeth Florent-Treacy, *Family Business*, *in* INTERNATIONAL ENCYCLOPEDIA OF ORGANIZATION STUDIES 499 (Stewart R. Clegg & James R. Bailey eds., 2008).

10. *Id.*

11. Family companies in the United Kingdom account for about two-thirds of all companies and more than a quarter of the GDP. As of 2013, there were approximately 4.8 million family businesses in the United Kingdom, of which 16,000 were medium or large companies. *About Family Business*, INST. FOR FAM. BUS., www.ifb.org.uk/knowledge-hub/about-family-business (last visited May 16, 2018). Tax revenues from these companies amounted to £149 billion in 2016, representing 21 percent of government income. *Id.* At the time, these companies employed 12.2 million workers, representing 47 percent of private sector employees. *Id.*

12. Less than one-third of the companies in the S&P 500 are family companies. *See* Åsa Björnberg, Heinz-Peter Elstrodt & Vivek Pandit, *The Family-Business Factor in Emerging Markets*, MCKINSEY & CO., https://www.mckinsey.com/global-themes/winning-in-emerging-markets/the-family-business-factor-in-emerging-markets (last visited May 22, 2018). In 2011, there were 5.5 million family businesses in the United States which accounted for 57 percent of U.S. GDP (about $8.3 trillion), employed 63 percent of the workforce, and were responsible for 78 percent of the new jobs. In 2006, 35 percent of Fortune 500 companies were family companies. *See Family Business Facts*, CORNELL U. SC JOHNSON C. OF BUS., https://www.johnson.cornell.edu/Smith-Family-Business-Initiative-at-Cornell/Resources/-Family-Business-Facts (last visited May 16, 2018).

13. Nearly 71 percent of German companies are family held and account for nearly half of the nation's gross sales, including more than 170 family-owned companies whose sales are over 1 billion Euros a year. *See* Michael Finnigan, *Infographic: German Family Businesses*, CAMPDENFB.COM (June 23, 2016), http://www.campdenfb.com/article/infographic-german-family-businesses.

European Union,[14] India,[15] Japan,[16] and China.[17] Family organizations account for approximately 19 percent of Fortune Global 500 companies,[18] with the expectation that by 2025 family companies will account for even more of this index.[19] In addition, family companies account for two-thirds of

14. Family businesses account for more than 60 percent of all European companies. *Growth: Internal Market, Industry, Entrepreneurship and SMEs*, EUROPEAN COMMISSION, https://ec.europa.eu/growth/smes/promoting-entrepreneurship/we-work-for/family-business_en (last visited May 19, 2018); *see also Facts and Figures*, EUROPEAN FAM. BUS., http://www.europeanfamilybusinesses.eu/family-businesses/facts-figures (last visited May 19, 2018) (describing the percentage of family companies from all companies in various European countries). These businesses provide more than 60 million jobs in the private sector. *See* KPMG ENTERPRISE, EUROPEAN FAMILY BUSINESS TRENDS—MODERN TIMES? 4 (2015), https://assets.kpmg.com/content/dam/kpmg/pdf/2015/12/european-family-business-trends-2015.pdf.

15. Family companies comprise about two-thirds of India's GDP. In addition, they are responsible for 79 percent organized private-sector jobs and 27 percent of the total number of places of employment. About 13 percent of these family companies have survived until the third generation and about 4 percent have survived until the fourth generation. *See Global Data Points*, FAM. FIRM INST., http://www.ffi.org/?page=globaldatapoints (last visited May 16, 2018) (providing general data on different countries, and among them India).

16. Japan is known as one of the countries with the most developed capital markets in the world. However, it has unique cultural characteristics; for example, family adoption vis-à-vis intergenerational management of a company is derived from economic considerations, meaning a family that owns a business or a business's assets adopts an adult person to manage the company and the adopted person then owns and/or inherits the business. Adoption is not limited to instances where there is no heir. Adoption changes the balance of considerations during intergenerational transfers. *See* Vikas Mehrotra, Randall Morck, Jungwoole Shim & Yupana Wiwattanakantang, *Adoptive Expectations: Rising Sons in Japanese Family Firms*, 108 J. FIN. ECON. 840, 841–42 (2013). Public family companies in Japan represent 40 percent of all public companies. Tai-Yuan Chen, Zhaoyang Gu, Keiichi Kubota & Hitoshi Takehara, *Accrual-Based and Real Activities Based Earnings Management Behavior of Family Firms in Japan*, 5 JAPANESE ACCT. REV. 30 (2015). In addition, some of the family companies in Japan are the oldest known companies. *See* ERNST & YOUNG GLOBAL LTD., EY FAMILY BUSINESS YEARBOOK 2014, at 138 (2014), https://familybusiness.ey-vx.com/pdfs/page-72---73.pdf.

17. More than 85 percent of businesses in China are family run. *See Global Data Points*, *supra* note 15; *see also* Xinhua, *China's Family Firms Face Succession Problem*, CHINA DAILY (Dec. 13, 2011), http://usa.chinadaily.com.cn/business/2011-12/13/content_14257381.htm (describing major data points regarding family business in China).

18. Åsa Björnberg, Ana Karina Dias & Heinz-Peter Elstrodt, *Fine-Tuning Family Businesses for a New Era*, MCKINSEY & CO., https://www.mckinsey.com/business-functions/organization/our-insights/fine-tuning-family-businesses-for-a-new-era (last visited May 22, 2018).

19. *Business in the Blood*, ECONOMIST (Nov. 1, 2014), http://www.economist.com/

all businesses in the world (both in private and in public sectors) and account for 70 to 90 percent of the Global GDP.[20] As of 2014, 50 to 80 percent of all workers, in most countries, were employed in family businesses.[21] The 500 largest family companies in the world employ approximately 21 million workers[22] and generate about $6.5 trillion annually—ranking them the third largest "economy" in the world (after the United States and China).[23] For example in Europe, about 85 percent of start-ups are built with family equity.[24] These figures speak for themselves, leaving no doubt as to the importance of family companies and their centrality in the global economy.

Consistent with the legal concept of "control"[25]—the most central concept in corporate law—a family company is defined as a company that is controlled by a family. Accordingly, two cumulative factors identify it: control and its attribution to a specific family.[26] Yet, this definition does not

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news/business/21629385-companies-controlled-founding-families-remain-surprisingly-important-and-look-set-stay (noting that analysts expect that there will be 15,000 companies worldwide with sales in excess of $1 billion, 37 percent of those will be family firms from emerging markets). In 2010, there were only 8,000 firms with such sales levels, and only 16 percent of those came from emerging market nations. *Id.*

20. *Family Business—What Starts Here Changes the World*, HRB FAM. BUS. CONSULTING (July 8, 2016), https://hrb-family-business-consulting.com/family-business-what-starts-here-changes-the-world/family-owned-business.

21. *Global Data Points*, *supra* note 15.

22. Chase Peterson-Withorn, *New Report Reveals the 500 Largest Family-Owned Companies in the World*, FORBES (Apr. 20, 2015), https://www.forbes.com/sites/chasewithorn/2015/04/20/new-report-reveals-the-500-largest-family-owned-companies-in-the-world/#4b4ce64d3602.

23. *Id.*

24. EUROPEAN FAM. BUS., EFB POSITION PAPER: FAMILY BUSINESS STATISTICS 2 (2012) (explaining the reason compilation of family business statistics would be a valuable inclusion in the European statistical programme 2013–2017), http://www.europeanfamilybusinesses.eu/uploads/Modules/Publications/pp---family-business-statisticsv2.pdf.

25. This Article adopts a fundamental definition of control that applies a substantive test to examine the existence of effective control and a real ability to influence the corporation's conduct. *See* Adolf A. Berle, Jr., *"Control" in Corporate Law*, 58 COLUM. L. REV. 1212, 1212 (1958) ("The phenomenon of 'control' is perhaps the most important single fact in the American corporate system."). "Control is a function of the corporate mechanism as it presently exists in American law. It consists of the power to choose directors, and carries with it a measure of influence over them." *Id.* at 1224; *see* 17 C.F.R. § 230.405 (2017) (defining control for the purpose of the Securities Act of 1933, 15 U.S.C. § 77a (2012)).

26. *See* EUROPEAN FAM. BUS., *supra* note 24, at 4 (listing four proposed elements of what defines a family business).

suffice for this Article's purposes since it also includes families that passively control a company but does not necessarily differentiate their behavior from that of ordinary companies with a controlling core.[27] Therefore, this Article adds a third requirement—active family control—and provides that holding a principal share of capital does not meet the third requirement. Instead, family members must also be involved in the actual management of the company and fulfill various key positions as company officers. As described in Part V, classifying control as active or passive is especially important since it has significant implications on the company's characteristics, the manner in which the family perceives the company, the family's conduct in relation to the company,[28] and the court's existing and desirable attitudes toward the family company. This requirement distinguishes family companies from other companies, and most family companies' complexities are derived from the range of active or passive control.[29]

III. FAMILY COMPANIES WITHIN CORPORATE THEORY

There are many theoretical and empirical studies in business academic literature examining the performance of family companies in relation to that of ordinary companies. Although not always consistent in their conclusions, these studies base their results on the unique characteristics of family companies as explained by the prevailing corporate theories.[30] This Article seeks to draw from this literature a coherent picture of family companies and the factors influencing their performance. For this purpose, the Article begins with the accepted theory used to justify modern corporate law, the principal–agent theory, and then examines family companies through the lens of the stewardship theory, a theory known and recognized in business literature but not in legal literature. The picture that emerges in this Part, and even more so in the next, is that unique characteristics of the family company create specific costs. Thus, family companies do not necessarily perform better than ordinary companies despite the apparent weakened principal–agent issue within family companies.

27. *See* Benjamin Maury, *Family Ownership and Firm Performance: Empirical Evidence from Western European Corporations*, 12 J. CORP. FIN. 321, 322, 339 (2006).

28. Thus, for example, studies found that passively controlled family companies do not perform differently than regularly controlled companies, while actively controlled family companies perform better. *See id.* at 339.

29. *See infra* Part V.B.

30. Kristen Madison, Daniel T. Holt, Franz W. Kellermanns & Annette L. Ranft, *Viewing Family Firm Behavior and Governance Through the Lens of Agency and Stewardship Theories*, 29 FAM. BUS. REV. 65, 65 (2016).

A. *Principal–Agent Theory*

Modern corporate legal analysis focuses on the separation between ownership and control[31] and stems from the understanding that it is both beneficial and inevitable that company shareholders delegate management powers to professionals and focus instead on administering investment risks.[32] Classic principal–agent theory identifies the failure inherent in this characteristic and describes the problems likely to arise from conflicts of interest and information gaps between minority and majority shareholders or between owners and professional management, even though the latter serve as agents of the shareholders.[33] The theory assumes that the agent, i.e., the decisionmaker, prefers to promote her personal interests over that of the owner and may occasionally act opportunistically.[34] The owner's desire to reduce any conflict of interest and improve information gaps between herself and her agents creates agency costs, including costs associated with the agent's incentive to align her interests with those of the owner (rather than with the inherent conflict-of-interest problem between them) and costs associated with the need to supervise the agent's conduct through information collection and preventive actions that preclude her from placing her personal interests first.[35] Accordingly, customary corporate law provides various tools and supervisory control mechanisms to minimize expected agency costs.[36]

Traditional corporate law refers to costs associated with the three main agency problems: (1) between shareholders and managers; (2) between shareholders and other stakeholders; and (3) between majority and minority shareholders.[37] According to the principal–agent theory, family companies experience a low occurrence of agency costs as opposed to nonfamily public

31. BERLE & MEANS, *supra* note 4, at 69; *see also* Jensen & Meckling, *supra* note 4, at 306.

32. Management of investment risks is reflected, among other things, in the diversification of their investment portfolio for spreading risk and minimizing the specific risk of each of their investments. *See* Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288, 291 (1980).

33. Jensen & Meckling, *supra* note 4, at 313 (illustrating the tension between shareholders' interests and those of the manager).

34. *See id.*

35. *See id.*

36. These include, above all, the board of directors, which is responsible for formulating the company's policy, appointing the general manager, and supervising her activities. *See id.* at 323, 351–52.

37. *See, e.g.*, *id.* at 312–13.

and private companies which experience a high occurrence.[38] The difference between the two is based on the degree of control: in family companies, the controlling family is more likely to be actively involved in managing the company; and in private and public nonfamily companies, the controlling family is less involved.[39] The controlling family often places family members and close associates in senior managerial positions or ensures family members are significantly represented on the board of directors and various supervisory committees. Consequently, family and senior officers acting on behalf of the shareholders share the same interests; hence, there are little to no conflicts of interest between owners and management.[40] In addition, there are relatively few information gaps between owners and management. This is primarily because family members serve as company officers and information is therefore available and accessible.[41]

Similarly, the second agency problem (between shareholders and other stakeholders) is expected to be weaker in family companies than in ordinary companies, mainly because of the long-term vision that characteristically controls family companies.[42] Because of this vision, the relationships the company and its controlling shareholders have with other parties are often long-term engagement based on trust and a heightened sense of commitment.[43] This hypothesis is supported by studies that found a significant positive correlation between family companies and long-term employment, employee satisfaction, and greater employee loyalty.[44] Similarly, with respect to creditors and suppliers, family companies tend to be less leveraged than ordinary companies and repay their debts on time.[45]

38. *See* Julio Pindado & Ignacio Requejo, *Family Business Performance from a Governance Perspective: A Review of Empirical Research*, 17 INT'L J. MGMT. REVS. 279, 285–87, 290 (2015).

39. *See id.* at 285.

40. *See id.* at 287.

41. On the other hand, and as seen below, the family aspect may add a unique dimension of conflict of interest to the company. *See id.*; *see also* Carlo Osi, *Family Business Governance and Independent Directors: The Challenges Facing an Independent Family Business Board*, 12 U. PA. J. BUS L. 181, 194–95 (2009).

42. Isabelle L. Breton-Miller & Danny Miller, *Why Do Some Family Businesses Out-Compete? Governance, Long-Term Orientations, and Sustainable Capability*, 30 ENTREPRENEURSHIP THEORY & PRAC. 731, 733–35 (2006) [hereinafter Breton-Miller & Miller, *Family Businesses Out-Compete*].

43. *See, e.g.*, *id.* at 740.

44. *Id.* at 738–39.

45. *See id.* at 740–41.

This is particularly true since family companies think about long-term interests and understand the importance of good credit.[46]

Finally, the third agency problem (between majority and minority shareholders) is expected to be weaker in private companies, both family and nonfamily, than in public companies.[47] The reason for this is that private companies usually have no minority shareholders and the family (or controlling shareholder) holds a majority or all of the company's share capital.[48] Moreover, since shares in private family companies are not tradable and their acquisition is a personal transaction between the parties, most who choose to acquire minority shares generally know the associated risk and possess the necessary knowledge to protect themselves, *inter alia*, through contractual stipulations that weigh the costs of the third agency problem when proposing the share price.[49]

B. *Stewardship Theory*

Another theory, the stewardship theory (which is barely, if at all, found in legal literature on corporate law but is known in business literature) holds a different view of the various characteristics and motivations of company agents.[50] This theory not only weakens, but perhaps even eliminates, the expected negative effects of the principal–agent theory.[51] It also provides an optimistic picture of agent incentives, especially in the family company.[52] In a nutshell, the stewardship theory applies the concept of altruism within the

46. The assumption is that the long-term engagement and acquaintance between the family and its creditors (e.g., the banks) and the family's compliance with its financial obligations, as well as the mitigation of the agency problem, help the family obtain better credit terms. *See* Ronald C. Anderson, Sattar A. Mansi & David M. Reeb, *Founding Family Ownership and the Agency Cost of Debt*, 68 J. FIN. ECON. 263, 283 (2003).

47. This is considered the problem of central representation in public family companies, and there are those who claim their predicted strength is even stronger than that in ordinary public companies that have a controlling interest. Family companies add an emotional dimension that intensifies the problem's phenomena and the complexity of dealing with it. *See, e.g.*, *id.* at 266–68; *see also* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 287.

48. *See, e.g.*, Dan Weiss, *Family Business in Israel*, 1 JOSEPH KASIERER INST. FOR RES. ACCT. 5, 6 (2012).

49. *See* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 287.

50. *Id.* at 288.

51. *Id.*

52. *See id.* In addition to these central theories, the literature also mentions the resource-based theory. For practical purposes, this Article does not focus on this theory. *See id.* at 288–89.

organization-management context and investigates those situations in which an agent was motivated (without external pressure) to act in the owners' interests.[53] The theory is based on the idea that pro-organizational collective behavior will, in the long term, maximize the agents' benefits[54] and assumes that agents' qualities and considerations will lead them to adopt behavior that favors the good of the company over their own private benefits. This insight leads to a different perception of the agents' preferences compared to the principal–agent theory. In essence, this theory predicts that managers will behave responsibly and in a manner that improves the value of the asset entrusted to them, i.e., the company.[55] The theory assumes, in certain respects, agents and owners have identical interests.[56] This weakens the probability of an "agency problem," shifting the owners' focus from implementing control and supervision mechanisms to implementing a policy that expands the agents' independence and ability for self-fulfillment within the corporate framework.[57] Accordingly, the theory is based on values such as trust, responsibility, mission, and equality rather than on values such as alienation, control, restraint, deterrence, and incentive.[58] This theory presents a different and more human picture.[59] If this theory is correct, it mitigates the agency problems detailed above and negates the need to handle the problems externally.[60]

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53. James H. Davis, F. David Schoorman & Lex Donaldson, *Toward a Stewardship Theory of Management*, 22 ACAD. MGMT. REV. 20, 21 (1997); *see also* James H. Davis, Mathew R. Allen & H. Davis Hayes, *Is Blood Thicker than Water? A Study of Stewardship Perceptions in Family Business*, 34 ENTREPRENEURSHIP THEORY & PRAC. 1093, 1094 (2010).

54. Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 288.

55. Guido Corbetta & Carlo Salvato, *Self-Serving or Self-Actualizing? Models of Man and Agency Costs in Different Types of Family Firms: A Commentary on "Comparing the Agency Costs of Family and Non-Family Firms: Conceptual Issues and Exploratory Evidence"*, 28 ENTREPRENEURSHIP THEORY& PRAC. 355, 356–57 (2004).

56. *See id.* at 356.

57. *See id.* at 356, 359.

58. *See* Davis, Schoorman & Donaldson, *supra* note 53, at 28.

59. Madison, Holt, Kellermanns & Ranft, *supra* note 30, at 2 (noting the differences between the stewardship theory and the principle–manager relationship).

60. *See, e.g.*, Isabelle Le Breton-Miller & Danny Miller, *Agency vs. Stewardship in Public Family Firms: A Social Embeddedness Reconciliation*, 33 ENTREPRENEURSHIP THEORY & PRAC. 1169, 1169, 1174–75 (2009) [hereinafter Breton-Miller & Miller, *Agency vs. Stewardship*] (noting that under the stewardship theory, family-owned organizations create a "more contented and talented workforce"). It is customary to divide the influence of the goals of the theory into two. The first relates to its expected impact on personal and psychological characteristics on the agent's behavior. *Id.* For

Although this theory is used to explain management motivation in companies in general, many researchers point out that the unique characteristics of the family company, especially the blurring of boundaries between family, business, and ownership systems, make using this theory even more appropriate.[61] In this Article, these characteristics will be referred to as "unique positive characteristics," as they are expected to be reinforced by the appropriate conditions sustained by the stewardship theory, while also weakening the power of the agency problems in family companies. However, as seen in the next Part, other characteristics exist which are also mentioned in academic literature and termed "unique negative characteristics."[62] The presence of unique negative characteristics in family companies decreases the influence of unique positive characteristics and in practice does not necessarily improve the performance of family companies over nonfamily companies. Unique negative characteristics raise questions regarding the validity of the stewardship theory and challenge individuals to search for corporate mechanisms to mitigate those unique negative characteristics—even if those mechanisms originated in the principal–agent theory.[63] Such mechanisms may potentially enhance long-term advantages

example, a tendency to fulfill the demands and needs of supervisors, the existence of internal motivation, the aspiration to self-realization and fulfillment within the role, commitment to social values, and thinking of the common good are all identified as psychological mechanisms positively associated with behavior consistent with this theory. *See id.*; Davis, Schoorman & Donaldson, *supra* note 53, at 28. In other words, the theory refers to the agent's motivation in carrying out his duties and argues that, unlike under the "agent theory," the agent cannot act out of financial motivation; under the stewardship theory he is motivated by emotional, non-monetary incentives, such as a sense of success and self-fulfillment within the framework of the position. Davis, Schoorman & Donaldson, *supra* note 53, at 28. Such incentives fulfill higher order needs according to Maslow's hierarchy of needs, and therefore generate a stronger commitment and identity of interests that cannot be easily replaced, creating loyalty and making it difficult for competitors to "steal" employees. *See id.* The second goal relates to its expected impact on environmental and organizational characteristics within the company, such as the existence of a strong organizational and business culture; the existence of a promotion horizon; and the development of a personal relationships based on trust between the various company officers, the company, other claimants, and between the owners and officers. *See, e.g.*, Guido Corbetta & Carlo Salvato, *The Board of Directors in Family Firms: One Size Fits All?*, 17 FAM. BUS. REV 119, 127 (2004).

61. *See infra* Part IV.B.

62. *See infra* Part IV.B.

63. Although this transcends the scope of this Article, the Authors note the inherent potential in the stewardship theory and its possible implications for nonfamily companies. The stewardship theory, which has not been sufficiently taken into consideration in the conventional corporate legal analysis, brings to the forefront the

of family companies.

The specific features of family companies are discussed in the next Part. However, presently and in order to summarize this Part, the existence of appropriate reciprocal relations between the principal–agent theory and the stewardship theory should be noted.[64] On the one hand, the principal–agent theory and the stewardship theory contradict one another, and the existence of one necessitates weakening the probability of the other, i.e., an agent cannot simultaneously be subject to the influences of both theories.[65] On the other hand, some argue these theories *can* exist simultaneously and have varying degrees of influence over the agent in different situations, both in a nonfamily company and a family company.[66] Thus, the agent may be influenced simultaneously by considerations belonging to each of the theories.[67] Our approach is consistent with the latter position, which is particularly supported by the complex and unique characteristics of the family company, some of which have a positive impact and others a negative impact on the management of a family company and the manner it performs.[68]

To conclude, traditional conflicts of interest exist less in private family companies, and this fact inherently creates more favorable conditions for the existence of the stewardship theory and its mitigating effects on the need for supervisory and deterrent mechanisms that focus on minimizing potential conflicts of interest.[69] However, family companies may include other unique

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reduction and even elimination of the costs involved in the agency problems. It is therefore interesting to examine whether, and how, regular companies can implement processes that allow the existence of this theory and its positive effects, even on regular companies and in the absence of family control. An example of such a process is the adoption and instigation of a code of ethics to strengthen the organizational and managerial culture in regular companies in a way that will increase the sense of loyalty and mission among their agents.

64. *Compare* Madison, Holt, Kellermanns & Ranft, *supra* note 30, at 66, *with* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 288.

65. Madison, Holt, Kellermanns & Ranft, *supra* note 30, at 66.

66. *See id.*

67. *See* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 288.

68. *See generally* Björnberg, Elstrodt & Pandit, *supra* note 12.

69. *See* Davis, Schoorman & Donaldson, *supra* note 53, at 24 ("Given a choice between self-serving behavior and pro-organizational behavior, a steward's behavior will not depart from the interests of his organization."); *see also* Breton-Miller & Miller, *Agency vs. Stewardship*, *supra* note 60, at 1169–70 (noting family businesses are viewed as "thriving organizations, uniquely nurtured by the stewardship of devoted family owners who pursue social and self-actualization goals to the benefit of all stakeholders").

costs related to their nature and unique conflicts of interest that are identified by the principal–agent theory.[70] As seen in the next Part, family companies do not necessarily perform better than ordinary companies with similar characteristics, particularly when considering the unique negative characteristics that operate in tandem with the unique positive characteristics and neutralize their effect.[71] In such companies, the business dimension is relatively nonexistent (for better or worse) because of emotional considerations.[72] Therefore, the principal–agent theory and the development of mechanisms designed to improve professionalism and minimize conflict of interest might provide a solution.

IV. Unique Characteristics of Family Companies

A. *Unique Positive Characteristics*

Family companies have many unique positive characteristics that give them an edge in contrast to nonfamily companies: long-term vision; reinforced matching interests between owners, management, employees, and company; and a correlation between the reputation and public image of the family and the company.[73] Family-controlled companies presume an intergenerational interest.[74] As a result, they tend to adopt a business approach that encourages long-term perspectives and examines the feasibility of alternative investments based on their overall net present value (NPV).[75] This approach causes family companies to adopt long-term investment strategies over short-term, quickly generated profits.[76] This perspective also affects the company's relationships with various entities

70. Jensen & Meckling, *supra* note 4, at 313.

71. *See infra* Part V. This insight serves readers in Part V in which this Article examines the type of inspiration family companies receive from ordinary companies that are normally analyzed using the principal–agent theory.

72. *See* Davis, Schoorman & Donaldson, *supra* note 53, at 24–25.

73. *See* Anderson, Mansi & Reeb, *supra* note 46, at 267.

74. *See id.*

75. The concept of NPV (net present value) is used to evaluate the profitability of business projects as well as investment alternatives and embodies the present value of the total cash flows expected to exit and enter the company as a result of investment in the project. As a rule, a positive NPV indicates that the project is profitable to the company. *See* Panikkos Zata Poutziouris, *The Structure and Performance of the UK Family Business PLC Economy*, *in* HANDBOOK OF RESEARCH ON FAMILY BUSINESS 555 (Panikkos Zata Poutziouris, Kosmas X. Smyrnios & Sabine B. Klein eds., 2006).

76. Anderson, Mansi & Reeb, *supra* note 46, at 286; *see also* Davis, Schoorman & Donaldson, *supra* note 53, at 41.

involved in its business activities, such as its employees.[77] In this regard, several studies have found that family-company employees usually work longer for that company than employees in nonfamily companies who accordingly have better promotional opportunities.[78] In addition, family-company employees relate better to the employer and are more attuned to its values and goals.[79] The long-term business vision of family companies, i.e., long-term family control, is based on trust and familiarity, which causes family companies to strengthen ties with various financial providers including creditors, suppliers, banks, and other claimants.[80]

A fundamental characteristic that distinguishes family companies from ordinary companies is the duplicity of roles played by family members, e.g., capital shareholders and owners, on the one hand, and management positions, e.g., CEO and comptroller, on the other.[81] The significant presence of family members in managing the company reinforces the sense of matching interests between owners, management, employees, and company. Based on the stewardship theory, the presence of family members increases selfless behavior on the part of the company officers.[82] In addition, role duplication mitigates the agency problem by reducing, and even eliminating, information gaps between the family as owners and management as their agents.[83] However, role duplication could also have negative effects, such as a lack of diversity in decision-making or independent and exclusive decision-making by a family leader—for example, when simultaneously serving as CEO or Chairman of the Board.[84]

Several studies demonstrate that over time a family's control over a company creates a correlation between the public image of the family and the company.[85] This correlation, which is in stark contrast to the separate and independent legal character of the company and the veil between the

77. *See* Breton-Miller & Miller, *Agency vs. Stewardship*, *supra* note 60, at 1175.

78. *See, e.g.*, Breton-Miller & Miller, *Family Businesses Out-Compete*, *supra* note 42, at 738–39.

79. Corbetta & Salvato, *supra* note 55, at 359.

80. Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 289.

81. *See, e.g.*, *id.* at 287.

82. *See* Breton-Miller & Miller, *Agency vs. Stewardship*, *supra* note 60, at 1174–75.

83. Hirsch, *supra* note 8, at 142–43.

84. *See id.* at 143.

85. *See, e.g.*, Alejandro Hernández-Trasobares & Carmen Galve-Górriz, *The Influence of Family Control on Decisions Regarding the Specialization and Diversification of Business Groups*, BRQ BUS. RES. Q., Oct. 2016, at 75, 75.

company and its shareholders, has social benefits for the family.[86] However, these benefits exist only as long as the company retains a positive image.[87] In addition, there are social repercussions for the family when the company's image is damaged.[88] This reciprocal relationship usually creates an incentive for the controlling family to ensure an appropriate corporate and business culture that improves the company's image and hence the family's reputation and image.[89] Indeed, findings show that in addition to the stronger organizational and managerial culture that exists in family companies, controlling families make sure their companies strive toward social and environmental activism as a means to improve the image of the company, and consequently the family.[90] These reciprocal interactions receive considerable attention within corporate social-responsibility research.[91] Many recent studies claim that a family's desire to preserve its social and economic status encourages a hyper-sensitivity to nonfamily companies.[92]

B. *Unique Negative Characteristics*

In contrast to the unique positive characteristics of family companies, family companies are not without negative characteristics—such as the plethora of family disputes, the entrenchment effect, risks associated with succession, and parental altruism. In family companies, intrafamily conflicts

86. *See id.*

87. *See id.* at 86.

88. Cristina Cruz, Martin Larraza-Kintana, Lucía Garcés-Galdeano & Pascual Berrone, *Are Family Firms Really More Socially Responsible?*, 38 ENTREPRENEURSHIP THEORY & PRAC. 1295, 1299 (2014). Studies have shown that family companies differ from ordinary companies in the manner in which they effect strategic decisions related to mergers and acquisitions and the diversity of the company's activities. Family companies are less likely than ordinary companies to expand their activities internationally, preferring to diversify their activities within their source country *inter alia* due to benefits derived from the families' identification with the company. *See generally* Luis Gomez-Mejia, Marianna Makri & Martin Larraza Kintana, *Diversification Decisions in Family-Controlled Firms*, 47 J. MGMT. STUD. 223, 243 (2010).

89. *See* Hernández-Trasobares & Galve-Górriz, *supra* note 85, at 75 (noting that family-run businesses are often risk averse for fear of diluting their brand or "socio-emotional wealth").

90. *See* Jean McGuire, Sandra Dow & Bakr Ibrahim, *All in the Family? Social Performance and Corporate Governance in the Family Firm*, 65 J. BUS. RES. 1643, 1643–44 (2012).

91. *Id.*

92. Cruz, Larraza-Kintana, Garcés-Galdeano & Berrone, *supra* note 88, at 1296.

and resolution costs are to be expected.[93] The source of these conflicts may vary, but family relationships are usually their source.[94] Thus, for example, disputes often arise over inheritance issues, inequality between family members in the distribution of company resources, and lack of uniform contribution from family members.[95] (For example, two brothers with equal shares, one is active in management and operations; the other just enjoys the company's profits.)

Family officers often become entrenched in their positions, regardless of their contribution to the company's success.[96] The entrenchment effect describes situations in which relatives continue to hold various positions within the company even though the economic benefits derived from their services are less than the costs of their employment.[97] Moreover, the desire to prevent recurring intrafamily disputes keeps these unproductive family members on the payroll.[98] A common manifestation of this phenomenon is family members who serve as company directors but are in fact puppet rulers.[99] This effect can be extracted from the observation that the average number of board members in a family cooperation is greater than that in nonfamily companies.[100]

Succession is unique in family companies, and some believe it is a far more impactful decision than it is in nonfamily companies.[101] This process is a combination of several considerations and obstacles.[102] In view of its crucial importance to the dominant family and the future of the company, many families invest great resources in its meticulous and careful planning.[103] The

93. *See* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 287.

94. *See, e.g.*, Hirsch, *supra* note 8, at 143.

95. *See generally id.*; *see also* Madison, Holt, Kellermanns & Ranft, *supra* note 30, at 81.

96. *See* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 287.

97. *See id.*

98. *See id.* at 286.

99. *See id.* at 287.

100. *See id.* at 286–87; Anderson, Mansi & Reeb, *supra* note 46, at 1304.

101. Ruth V. Aguilera & Rafel Crespi-Cladera, *Firm Family Firms: Current Debates of Corporate Governance in Family Firms*, 3 J. FAM. BUS. STRATEGY 66, 67 (2012); *see also* Brian Luster, *Five Ways to Keep a Family-Owned Business 'In the Family' for Generations*, FORBES (Dec. 15, 2015), https://www.forbes.com/sites/brianluster/2015/12/15/five-ways-to-keep-a-family-owned-business-in-the-family-for-generations/#8e5a4046759f.

102. *See* Aguilera & Crespi-Cladera, *supra* note 101, at 67–68.

103. *See* Wendy C. Handler, *Succession in Family Business: A Review of the*

risks that succession causes to the family company's prosperity are not insignificant. Even though most of the oldest companies known began as family companies,[104] studies show that most family companies—approximately 70 percent—do not survive the first succession transfer.[105] In addition, with second and third transfers, the failure rate increases (rising to about 90 percent).[106] Finally, increased involvement in this process costs the company and includes high consulting costs to plan for transition and information-dissemination costs to explain the often-made decision to appoint an inexperienced descendant as heir.[107]

Beyond the survival risk, this process also impacts the company's performance. Several studies have found that appointing a descendent to the position of CEO could have a negative impact on the company's performance as well as its value in the eyes of investors (as reflected in the company's market value).[108] Furthermore, appointing an outside professional creates a positive relationship, improves management, and increases the company's value.[109] One explanation for this is that investors perceive appointing a family member as proof of faulty management and corporate governance principles.[110]

Research, 7 FAM. BUS. REV. 133, 133–34 (1994). In addition, a study published by one of the world's four largest accounting firms (The Big 4) shows that the process of inheritance is one of the most important factors in a family business. *Cf., e.g.*, GRANT WALSH, KPMG ENTERPRISE, FAMILY BUSINESS SUCCESSION: MANAGING THE ALL-IMPORTANT FAMILY COMPONENT 9–10 (2011) (listing succession as a benefit of family business), https://assets.kpmg.com/content/dam/kpmg/pdf/2015/07/3468-succession.pdf.

104. *The World's Oldest Companies: The Business of Survival*, ECONOMIST (Dec. 16, 2004), https://www.economist.com/node/3490684.

105. George Stalk & Henry Foley, *Avoid the Traps that Can Destroy Family Businesses*, HARV. BUS. REV., Jan.–Feb. 2012, at 25, 25.

106. Danny Miller, Lloyd Steier & Isabelle Le Breton-Miller, *Lost in Time: Intergenerational Succession, Change and Failure in Family Business*, *in* HANDBOOK OF RESEARCH ON FAMILY BUSINESS 371–72 (Panikkos Zata Poutziouris, Kosmas X. Smyrnios & Sabine B. Klein eds., 2006); *Succession Planning*, FAM. BUS. INST., https://www.familybusinessinstitute.com/consulting/succession-planning (last visited Apr. 24, 2018).

107. *See, e.g.*, Stalk & Foley, *supra* note 105, at 26; *Succession Planning*, *supra* note 106.

108. Francisco Pérez-González, *Inherited Control and Firm Performance*, 96 AM. ECON. REV. 1559, 1585 (2006).

109. *See id.*; *see also* Alex Stewart & Michael A. Hitt, *Why Can't a Family Business Be More like a Nonfamily Business? Modes of Professionalization in Family Firms*, 25 FAM. BUS. REV. 58, 61 (2012).

110. *See* Pindado & Requejo, *supra* note 38, at 291.

Parental altruism is also an aspect unique to family companies. In this framework, parents tend to promote their own children within the family company—for example, by appointing them to key and senior management positions even when they are inexperienced and unsuitable for the positions—and often create significant costs for the company, directly through mismanagement and indirectly through fallout by disgruntled employees.[111]

In sum, family ownership and control of a company is not without its cost. The greater the family control, the more positive and negative characteristics have a significant impact on the management, performance, and survivability of the company. Although, at first glance the unique characteristics of a family company are expected to diminish the agency problem and increase the prevalence of pro-organizational and collective behaviors, which are consistent with the stewardship theory. With that, it is important to recognize other unique characteristics exist that could neutralize the positive influence of family control and the unique strengths of the family company. The next Part examines these notions using descriptive and normative aspects of the law.

V. FAMILY COMPANIES IN THE EYES OF THE LAW

A. *The Hidden Assumption: Commingling of Affairs and a Broad Definition*

Existing legal discourse on private family corporations assumes significant commingling between the family and the company. This, in turn, justifies the court's increased judicial review of company matters and its increased tendency to pierce the corporate veil.[112] In view of the intuitive assumption regarding the link between family members as company shareholders and family members as officers, courts tend to apply the

111. Michael H. Lubatkin, William S. Schulze, Yan Ling & Richard N. Dino, *The Effects of Parental Altruism on the Governance of Family-Managed Firms*, 26 J. ORGANIZATIONAL BEHAV. 313, 320 (2005); *see also* James J. Chrisman, Jess H. Chua & Reginald A. Litz, *Comparing the Agency Costs of Family and Non-Family Firms: Conceptual Issues and Exploratory Evidence*, 28 ENTREPRENEURSHIP THEORY & PRAC. 335, 338 (2004); William S. Schulze, Michael H. Lubatkin & Richard N. Dino, *Toward a Theory of Agency and Altruism in Family Firms*, 18 J. BUS. VENTURING 473, 473–90 (2003); Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 286.

112. *See* Deborah L. Murphy & J. Edward Murphy, *Protecting the Limited Liability Feature of Your Family Business: Evidence from the U.S. Court System*, 14 FAM. BUS. REV. 325, 330–33 (2001).

"instrumentality" and "alter ego" doctrines—two of the main justifications for piercing the corporate veil—to these companies.[113]

Clearly, the court gives weight to the uniqueness of the family company vis-à-vis piercing the corporate veil and is prepared to adapt the law on a case-to-case basis.[114] However, it appears that in so doing, the court does not dwell on the uniqueness of the family company in its entirety (including its potentially positive uniqueness), both regarding the definition of a family company and the scope of judicial review.[115] This Article suggests a more precise and systematic judicial approach to review the piercing of the corporate veil in family companies to improve both corporate governance and legal certainty: first, examine the extent of the commingling of spheres in each family company, according to a systematic definition of the concept of the family company; and second, use a scaled definition of family company.

B. *The Family Company: Proposing a Scaled Definition*

This Article proposes a tiered scope of judicial review ranging from lax to stringent, which depends on the level of separation between the family and the family company. Accordingly, courts should examine several points on a continuum, measuring the predicted intensity of commingling between the family and the company and examining whether there are existing objective and independent monitoring mechanisms that neutralize commingling. Only after calculating these two factors should courts determine the appropriate judicial review in each circumstance.[116] For this purpose, this Article proposes a three-staged review: First, identify the type of family company; second, determine the actual family involvement in

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113. Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1054–57, 1064 (1991); *see* Birbara v. Locke, 99 F.3d 1233, 1238 (1st Cir. 1996) ("The key Massachusetts cases on piercing the corporate veil have all involved close, family-owned defendant corporations.").

114. *See* Thompson, *supra* note 113, at 1063–64 ("The seeming indeterminacy of veil-piercing law reflects not just the conclusory language frequently used by the courts but also the broad range of reasons proffered when the courts attempt to explain their conclusions. As one commentator has noted, the same reasons seem to appear in cases which pierce the veil and those decisions which do not.").

115. *See id.* at 1064 ("These results suggest that courts are looking beyond the formal overlap of shareholders, directors, and officers to see if businesses show other signs of intertwining between the corporation and the shareholder.").

116. The conceptual ladder used here draws inspiration from Berle's article on control. *See* Berle, *supra* note 25, at 1212.

company management; and third, examine the company's independent and professional controls and supervisory mechanisms.

Stage 1: Determining the Type of Company

The type of family company is determined according to its affiliation with one of the following quarters: (I) a passively controlled family, public company; (II) an actively controlled family, public company; (III) a passively controlled family, private company; and (IV) an actively controlled family, private company. For this Article's purposes, active control has three cumulative components: (1) family control of the company's shared capital, (2) family members' direct involvement as company officers, and (3) family members' active involvement in company decision-making.[117] Under the active-control model, the family seeks to maximize its benefits derived from the company through optimal management by family representatives and associates, whereas passive control is expressed by family control in the company's shared capital alone.

I (Public, Passive)	II (Public, Active)
III (Private, Passive)	IV (Private, Active)

Quarter I companies (public, passive) should be treated as ordinary companies, since statutory provisions require public companies (ordinary and family alike) to establish objective, professional governance mechanisms (such as advisory boards) and there is no enhanced fear of commingling and agency costs.[118] Quarter II companies (public, active), despite existing regulation, have active control by family management which could exacerbate the agency problems vis-à-vis a nonfamily minority and dispersed shareholders.[119] This justifies applying a higher standard of fiduciary duties to company officers. In this context, integrating an advisory

117. Active control can also occur indirectly through family agents who are not family members. For example, a family can appoint a professional CFO with long-term ties to the family, thus achieving a similar effect.

118. *See* Sarbanes-Oxley Act of 2002 § 404, 15 U.S.C. § 7262 (2012).

119. *See* Siebels & zu Knyphausen-Aufseß, *supra* note 7, at 286–87.

committee as described below may prevent, or at least mitigate, this potential conflict of interest.[120] Quarter III companies (private, passive) should be treated as ordinary private companies (as is the case with Quarter I companies), since neither unique externalization nor commingling are expected. However, within Quarter IV companies (private, active), there is a reasonable fear of commingling (both negative and positive). Since regulation and compulsory corporate governance are generally not required by corporate and securities law, a legal vacuum exists, making special consideration required.[121]

Stage 2: Determining Family Involvement in Company Management

Naturally, the greater the family involvement, the greater the chance of commingling family and company affairs. However, this in itself does not automatically justify increased judicial review. Clearly, there is a variety in the degree of overlap between the three circles (family, management, and ownership).[122] Therefore, this Article refers to four degrees of familial management that determine the family's "hold" over the company based on four key positions in the company—CEO, board of directors, chairperson of the board of directors, and senior management. When family members hold these key positions, the intensity of commingling is expected to rise. In general, a correlation exists between the number of family members serving in each of these positions and the potential for commingling.[123]

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120. CATHERINE BROMILOW & JOHN MORROW, PWC, FAMILY BUSINESS CORPORATE GOVERNANCE SERIES: WHAT IS A BOARD'S ROLE IN A FAMILY BUSINESS? 2–3 (2014) (describing additional benefits family companies may derive from the integration of independent and objective entities in their activity), https://www.pwc.com/us/en/corporate-governance/publications/assets/corporate-governance-role-in-family-business.pdf.

121. Stephen Giove & Robert Treuhold, *Corporate Governance and Directors' Duties in the United States: Overview*, THOMPSON REUTERS PRAC. LAW (Feb. 1, 2013), https://content.next.westlaw.com/Document/Id4af1a411cb511e38578f7ccc38dcbee/view/FullText.html?contextData=(sc.Default)&transitionType=Default&firstPage=true&bhcp=1 (explaining the United States has not adopted a corporate governance code and indicating much of this oversight is left to the states and excludes many privately held companies from most federal corporate laws and regulations).

122. Renato Tagiuri & John Davis, *Bivalent Attributes of the Family Firm*, 9 FAM. BUS. REV. 199, 201 (1996) (suggesting a three-circles model to describe family businesses).

123. *See* Osi, *supra* note 41, at 187–88 (detailing the many pitfalls of maintaining a family-run company and how family members, by wearing "various corporate hats," can impair both professional and personal relationships, as well as steer family-held companies into trouble with the Sarbanes-Oxley Act).

A very high degree of familial management is classified by those companies in which family members function in the four key positions, and in such companies, family control and commingling of affairs is extremely high and objective decision-making is likely to be limited.[124] Moreover, any attempt to force pure business considerations on the company against the family's will is likely to encounter fierce resistance.[125] Accordingly, increased judicial review should be expected in a company that does not maintain voluntary objective and independent oversight mechanisms, and less weight should be given to the corporate veil.[126]

A high degree of familial management is classified by those companies in which family members are board chairpersons, members of the board of directors, and senior managers, but the CEO is staffed by an external, nonfamily professional. Although the family's control is still strong, the presence of an external CEO is expected to moderate and bring objective business considerations into the decision-making process.[127] In this case, the court should examine the CEO's degree of independence and her actual ability to influence the company's decision-making process. Insofar as the court determines that the family respects the CEO's independence and allows her to implement best practice business measures, the standard of judicial review should be reduced. In contrast, if the court concludes that the family blocked the CEO's ability to manage the business based on impartial, professional decision-making, the court should increase the level of the judicial standard and ignore the corporate legal veil.

A medium degree of familial management is classified by those companies in which family members serve as board members and in senior management positions. In these companies, the CEO and chairperson of the board are professional, nonfamily members. While the family's ability to influence the company's affairs is expected, its effective control is predicted to significantly decrease because the CEO and chairperson are "outsiders" and their objective, professional decision-making and lack of family influence should allow the court to ease the judicial-review standard and

124. *See id.* at 200.

125. *See id.*

126. Thompson, *supra* note 113, at 1054–56.

127. *See* William Mullins & Antoinette Schoar, *How Do CEOs See Their Roles? Management Philosophies and Styles in Family and Non-Family Firms*, 119 J. FIN. ECON. 24, 39 (2016). A possible explanation for this is that the CEO competes with other CEOs in the professional labor market based on professional parameters. The CEO therefore will act to prevent unrelated, emotional considerations to hamper the family business.

respect the corporate veil.[128]

A low degree of familial management is classified by those companies in which family members only hold board positions. Thus, the family's ability to influence the company's daily management decreases. Albeit, the family still can influence company policy through the board of directors and the shareholders' general meeting. Boards with a majority of family members, or members closely affiliated to the family, indicate strong family influence. However, if this influence remains limited to the control of the board of directors and business policy, then the court should not increase the standard of judicial review and should maintain the corporate veil.

Stage 3: The Existence of Objective Independent Monitoring and Supervision Mechanisms

The use of objective and independent monitoring and supervision mechanisms, such as an advisory board (which is discussed below), expert committees, and external professional consultants is expected to reduce the potential for negative commingling of affairs and to reduce family involvement.[129] Here too, courts should examine these mechanisms and determine the quality of their activities and ability to influence decision-making processes. Elements of the court's examination should consider: who is part of the monitoring and supervision mechanism (family or external); the members' experience and level of professionalism and expertise; the manner in which members were chosen (nepotism or impartial); intensity of the mechanism's operation (number and timing of annual and periodical meetings); the mechanism's independence (quantity and type of information available to its members); the members' authority to consult with external professionals; tenure of the members; and the weight of the mechanism's recommendation (whether the family can ignore recommendations). Courts should respect the corporate veil in those cases where the mechanisms truly function and family involvement is limited. Hence, courts will look for a balance between family involvement and objective business measures. For example, a court will ease its judicial review of a company with extreme family involvement if it has effective monitoring and supervision mechanisms (as determined above). The company then will be protected against court intervention in its affairs and family assets.

The analysis proposed above is inspired by the approach that prefers

128. *See id.*

129. BROMILOW & MORROW, *supra* note 120, at 2–4.

objective, professional, and independent factors, which are the same factors increasingly accepted today by nonfamily companies.[130] Use of these factors, such as the mechanism developed below, will minimize the risk of commingling of company and family affairs and legally protect the company, its shareholders, and those acting on its behalf.[131] Moreover, and this is beyond the scope of this Article, the proposed objective, professional, and independent governance mechanism will likely improve the management, performance, and survivability of the family company.

C. *Toward Improved Corporate Governance: The Advisory Committee*

1. *Legislative and Case Law Trends*

Corporate law consolidates corporate governance provisions, whether recommended or mandated, to alleviate the agency problem, especially in public companies. While corporate governance provisions are not mandatory for private family companies, this Article suggests their voluntary implementation, albeit with changes. This approach is likely to be even more effective, as the modern judicial approach encourages the use of preventive restraint mechanisms that strengthen the professionalism and independence of companies' directors and officers and also minimizes judicial review of companies.[132]

Companies can mitigate the agency problems by promoting objectivity among company directors and officers. Corporate law assists in this process by regulating the characteristics of public company directors.[133] For example, the rules of registration with various stock exchanges require public companies to appoint directors who meet detailed criteria of independence.[134] At the same time, stock exchange rules stipulate that public companies must establish a special directorial committee including an audit,

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130. *See* Corwin v. KKR Financial Holdings, 125 A.3d 304, 308–14, 311 n.24 (Del. 2015); Kahn v. M & F Worldwide Corp., 88 A.3d 635 *passim* (Del. 2014); *In re* Books-A-Million, Inc. Stockholders Litigation, C.A. No. 11343-VCL, 2016 WL 5874974 *passim* (Del. Ch. Oct. 10, 2016) (confirming and clarifying the *Kahn* and *Corwin* cases' analyses).

131. Murphy & Murphy, *supra* note 112, at 333–34.

132. *Id.* at 326–28, 330 (noting there is an upward trend of courts being willing to pierce the veil of corporate entities, family run or not).

133. *See, e.g.*, DEL. CODE ANN. tit. 8, § 141 (West 2016).

134. *See, e.g.*, NYSE LISTED COMPANY MANUAL § 303 (2018), http://wallstreet.cch.com/LCMTools/PlatformViewer.asp?selectednode=chp_1_4&manual=%2Flcm%2Fsections%2Flcm-sections%2F.

compensation, and nomination committee.[135] A majority of the members of the special directorial committee must be independent directors; after which, selected board powers are then transferred to this committee.[136] The stock exchange listing rules dictate the percentage of directors on the board and committees in public companies and assign them specific functions (such as chairman of the audit committee).[137] In this manner, corporate law (and stock market regulations) augment the assessment of business decisions, especially those already tainted with conflicts of interest.[138]

A similar trend can be discerned in court decisions on rules of intervention created by courts to review companies' business decisions. In the past, the "nonintervention rule," today known as the "business judgment rule," governed, and courts were more hesitant to second guess companies' business decisions.[139] Under the nonintervention rule, courts focused on the process that led to the business approval and not the substantive content of the decision.[140] However, in the mid-1980s, courts changed their position, especially in cases concerning conflicts of interest.[141] This trend brought about significant deviation from the nonintervention rule (the business judgment rule); and instead, in conflict-of-interest cases, courts began to prefer to examine the content and practicality of each business decision on its own merits.[142] This examination is now carried out under the auspices of the "enhanced business judgment rule," "enhanced scrutiny," or "entire fairness doctrines."[143]

135. Julie Hembrock Daum, *Building a Balanced Board*, *in* NYSE: CORPORATE GOVERNANCE GUIDE 75–76 (Steven A. Rosenblum et al. eds., 2014).

136. *See* NYSE LISTED COMPANY MANUAL, *supra* note 134, at § 303A.

137. *See id.*

138. *See, e.g.*, Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 949 (Del. 1985).

139. Douglas M. Branson, *The Rule that Isn't a Rule—The Business Judgment Rule*, 36 VAL. U. L. REV. 631, 634–35 (2002).

140. *Id.* at 635–36.

141. *See* King Fung Tsang, *The Elephant in the Room: An Empirical Study of Piercing the Corporate Veil in the Jurisdictional Context*, 12 HASTINGS BUS. L.J. 185, 186–87, 207 (2016).

142. Murphy & Murphy, *supra* note 112, at 333–34.

143. *See Unocal Corp.*, 493 A.2d at 954; *see also* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 180 (Del. 1986). Keep in mind, the business judgment rule is the norm; while the "enhanced business judgment rule," "enhanced scrutiny," or "entire fairness doctrines" are used for specific treatment of unique issues. Thus, for example, the enhanced security standard is applied to hostile purchases of public shares in companies with dispersed control, and the entire fairness standard is applied to transactions involving serious conflict of interest, such as "going-private"

This Article does not intend to discuss these rules of intervention which were developed in case law. However, recent case law expresses a clear tightening of the monitoring of board of directors and its members to ensure that they better protect shareholders as well as the company's overall activity.[144] In practice, legal oversight in the context of more stringent doctrines of enhanced scrutiny and entire fairness (especially due to the controlling party's personal interests and reduced assumption of objectivity in the decision-making process) seeks to determine whether decision-making was based on professional and objective considerations that embody maximum economic benefit to all shareholders.[145]

In this context, it is also worth noting legal developments regarding independent committees formed to encourage corporate policing and preventative mechanisms. An example of this is a requirement mandating the establishment of a designated subcommittee of board of directors, which answers a predefined criterion of independence, as a procedural and substantive condition for rebutting the severe judicial-review standard of entire fairness or, alternatively, to grant immunity to a transaction using the business judgment rule.[146]

This points to a clear trend supporting the establishment of independent committees advocating fair and optimal management, which in turn greatly aids the company and officers in corporate governance. This Article adopts this concept through the advisory committee mechanism among private family companies, as proposed in the next subsection.

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transactions in which the company's controlling shareholder makes a purchase of minority shares in order to turn the company from a public company into a private one. *See, e.g.*, *Revlon, Inc.*, 506 A.2d at 184–85.

144. *See, e.g.*, Kahn v. M & F Worldwide Corp., 88 A.3d 635 (Del. 2014) (discussing corporate policing in the form of approval from an independent subcommittee and an informed vote from the majority of minority shareholders).

145. *See id.*

146. Thus, according to the ruling, beyond the approval of the transaction by a majority of the minority shareholders, the company is required to establish a special committee, all of whose members will be independent of the controlling shareholder, who will negotiate the terms of the transaction in a manner as similar as possible to negotiations under market conditions between independent parties with the aim of obtaining the best deal for the company and its shareholders. *See id. passim*.

2. *In Praise of Adopting Objective, Professional, and Independent Mechanisms*

Legislation and case law developments mainly apply to public companies with acute agency problems.[147] However, they can be applied to private family corporations as well.[148] To clarify, this Article does not propose a mandatory approach in private family corporations.[149] A contractual approach to corporate law avoids a paternalistic and coercive approach, as well as the significant burden and transaction costs associated with establishing and maintaining multiple corporate governance mechanisms.[150] On the contrary, contractual freedom should be preserved, especially in the context of private companies since it helps maintain the positive characteristics of family companies.[151] However, in the Authors' opinion, family companies will benefit from considerable economic and emotional benefits by using objective, professional, and independent mechanisms within internal corporate governance, especially since family companies often suffer from internal family conflicts that overflow into the company and affect their performance and survivability.[152]

Family disputes are often brought to court to settle them ex post, using unsophisticated legal tools such as corporate laws prohibiting oppression of minority shareholders. Moreover, in a family company, it is almost impossible to prevent conflict from spilling into the business sphere, which then overshadows the company's business activities and sabotages and impedes its normal functioning.[153] Placing objective, professional, and independent bodies as gatekeepers may protect the company from such spillage.

Family companies have other interests that cannot be ignored. For instance, a family company may want to preserve the family characteristics of a business—which may at times mean employing a family member or

147. *See, e.g.*, Thompson, *supra* note 113, at 1043, 1056, 1063.

148. Murphy & Murphy, *supra* note 112, at 333–34.

149. *See* Lucian Arye Bebchuk, Forward, *The Debate on Contractual Freedom in Corporate Law*, 89 COLUM. L. REV. 1395, 1396 (1989) (discussing the contractual freedom in corporate law).

150. *See* Benjamin Means, *Contractual Freedom and Family Business*, *in* RESEARCH HANDBOOK IN PARTNERSHIPS, LLCS AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS 40–41 (Robert W. Hillman & Mark J. Lowenstein eds., 2015).

151. *See id.*

152. *See supra* Part III.B.

153. *E.g.*, Hirsch, *supra* note 8, at 131.

preserving conduct that is economically inefficient—even at the risk of harming long-term company performance. The negative phenomenon can be mitigated by introducing objective, professional, and independent elements to management—especially transparency, full disclosure, and professional assistance in planning, hiring, promoting, and intergenerational transfer processes.[154]

Intergenerational transfer is a critical stage in the life cycle of a family company as well.[155] Literature discussing the process strongly recommends early planning and consulting with external agents to introduce objective and professional considerations, thereby neutralizing negative psychological effects on family members.[156] In addition, it may be easier for consultants to persuade family members to consider appointing a professional external successor as opposed to an unprepared family member.[157]

Finally, parental altruism describes situations in which parents promote their offspring's well-being, even at the expense of the company's good.[158] Here too, objective professionals can mediate between these two interests and impress unbiased decision-making on family members.[159] This argument is especially true when trust and esteem exist between the family members and objective professionals. Another way to bypass ticking bombs is to create specific corporate provisions in company bylaws that mandate objective and professional approval mechanisms for decisions relating to nepotism or promotion of family members. [160]

3. *Advisory Committee*

a. *Purpose and function*. To build trust within and outside the family,[161]

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154. *See* Osi, *supra* note 41, at 192–93 (discussing how objective, professional, and independent agents can serve as intermediaries during the intergenerational transfer process).

155. Claudio Fernández-Aráoz, Sonny Iqbal & Jörg Ritter, *Leadership Lessons from Great Family Businesses*, HARV. BUS. REV., Apr. 2015, at 82, 87–88.

156. *Id.*

157. *See* BROMILOW & MORROW, *supra* note 120, at 2–4.

158. Lubatkin, Schulze, Ling & Dino, *supra* note 111, at 319–20 (linking the parents' well-being with that of their children's and noting any improvement in the children's well-being positively affects the parents' well-being).

159. *See* BROMILOW & MORROW, *supra* note 120, at 2–4.

160. *See* Osi, *supra* note 41, at 206 (illustrating how incorporating independent directors can help check against substantive hires or promotions that reek of nepotism).

161. BROMILOW & MORROW, *supra* note 120, at i.

this Article suggests family companies voluntarily create an independent, advisory committee. In doing so, companies introduce objective and professional considerations into their processes and assist the shareholders, management, and board of directors in improving company performance and managerial components.[162] The advisory committee will balance positive family elements with harmful family elements and integrate positive family characteristics into the business and organizational systems often used in nonfamily companies.[163] In addition, the advisory committee will arbitrate and mediate family disputes.[164] These roles clearly indicate that advisory committee members must have appropriate business and personal qualifications.[165]

b. *Organizational hierarchy*. The location of the advisory committee in the organizational hierarchy depends on the company's unique characteristics. That is especially true when considering the voluntary format this Article proposes. Therefore, the exact location of the advisory committee in the corporate hierarchy should be determined in accordance with its primary goal—to improve the company's performance by advancing the functioning of relevant components in a given corporation. While the advisory committee should be akin to a supervisory board of directors, it is important that it is independent from the company and recognized as a separate entity from the company's traditional power structures. This distinction is advantageous and enables it to remain neutral, leading through agreement and trust and not by command (an authority reserved for the board of directors).

In addition, determining the location of an advisory committee in the organization's hierarchy should be based on the unique characteristics of a given family company and its stage within the business life cycle, i.e., a new company or an established company.[166] In a company's early stages, an advisory committee should only have a few members and focus on assisting

162. *Id.* at 2–4.

163. *Id.*

164. *Id.*

165. *See* Osi, *supra* note 41, at 206 (noting how an independent advisory committee mechanism "can serve as an informal 'court of first resort'").

166. Kimberly A. Eddleston, Franz W. Kellermanns, Steven W. Floyd, Victoria L. Crittenden & William F. Crittenden, *Planning for Growth: Life Stage Differences in Family Firms*, 37 ENTREPRENEURSHIP THEORY & PRAC. 1177, 1193 (2013).

the company's executive functions, such as aiding the CEO in making operational business decisions, including selecting suppliers and finding investors.[167] Whereas, in an operational company, an advisory committee should assist the company by overcoming normal operational difficulties and issues relating to its continued growth. As the company progresses and develops, an advisory committee should gradually shift from operational functions to policy making; and as the company furthers advances, the committee can turn to issues related to maintaining the family character of the company.

c. *Composition*. The advisory committee's composition is critical and, of course, influenced by the identity of the family company in question. It is particularly important to consider the voluntary status of the committee and its informal authority, as well as family members' ability to block or ignore its decisions or even demand that it disband.[168] Accordingly, members of the committee must have a variety of characteristics, including:

i. *Expertise*. Clearly, advisory committee members must have some expertise in the area the company operates. Furthermore, it is recommended, at least in the company's early stages of activity, that committee members also hold expertise in areas other than those of family members; this would assist them in making decisions in these areas.[169] Similarly, it is desirable that committee members' areas of expertise be as varied as possible to add a variety of views and improve the decision-making processes.[170] Above all, committee members must be sensitive and recognize

167. *See, e.g.*, Hedda T. Schupak, *A Small Company with BIG Plans*, FAM. BUS., July–Aug. 2014, at 36, 38.

168. *See* THOUGHT LEADERSHIP COUNCIL, WOMEN CORP. DIRECTORS, KPMG ENTERPRISE, ENDURING ACROSS GENERATIONS: HOW FAMILY BOARDS DRIVE VALUE IN FAMILY-ORIENTED BUSINESSES 3–5 (2015); Russ Alan Prince, Editorial, *Are Family Business Advisory Boards Worthwhile?*, FORBES (Nov. 23, 2015), https://www.forbes.com/sites/russalanprince/2015/11/23/are-family-business-advisory-boards-worthwhile/#210a3dcb6539 (noting many of the failings of advisory boards are a result of poor planning or staffing but acknowledging that these failings do not discount the concept of an advisory board itself).

169. *See* Osi, *supra* note 41, at 197–98; Emma Su & Junsheng Dou, *How Does Knowledge Sharing Among Advisors from Different Disciplines Affect the Quality of the Services Provided to the Family Business Client? An Investigation from the Family Business Advisor's Perspective*, 26 FAM. BUS. REV. 256, 258–59 (2013).

170. *See* Su & Dou, *supra* note 169, at 263 (noting that the evolving challenges of the business world can require skills or knowledge that are "beyond the capabilities" of any single advisor).

the complex nature of family companies and understand their unique dynamics.

ii. *Professionalism*. Unlike expertise, professionalism relates to the ongoing conduct of committee members in performing their duties.[171] For example, a person could have great expertise in his field but treat his position in the company in such an offhand manner that he lacks all professionalism. Professionalism includes a number of important characteristics and attributes: commitment to the position; use of proper decision-making processes; fact-based and evidence-based advice; proactive management that is not affected by the controlling family; ongoing professional updates; transfer of relevant materials to committee meetings; use of external consultants; and more.[172] Committee members must possess and act according to appropriate values, principles, and professional ethics.[173]

iii. *Independence and autonomy*. Independence is primarily the duty to exercise autonomous discretion. This obligation is directed at the absence of a priori dependence on a party with an interest of one kind or another that may affect members' discretion.[174] Parenthetically, in early stages of the family company, committee members need to be less independent.[175] Thus, even those who meet the definition of "grey director" can be appointed as committee members.[176] At this stage, the family is building the business; thus, the family fabric must be protected. Moreover, as the company is still young, the committee must avoid arousing the suspicions of family members against independent "strangers" who may be perceived as trying to manage the family's every move.[177]

iv. *Status*. As a voluntary entity, the advisory committee's success depends on the legitimacy it receives from family members and senior

171. *See* Stewart & Hitt, *supra* note 109, at 61.

172. *See id.* at 61–62.

173. Eli Bukspan & Asa Kasher, *Ethics in Business Corporations: Legal and Moral Considerations*, 2 L. & BUS. 159 *passim* (2005) (in Hebrew).

174. Osi, *supra* note 41, at 195.

175. *Id.* at 196.

176. "Grey director" describes directors who were once independent and autonomous. However, since they have worked with the company for many years, they have developed a business or personal dependence on it or its owners. Grey directors can be clients, suppliers, bankers, professional advisors (such as an attorney or an accountant), or others in the industry. *See id.* at 194–95.

177. *Id.* at 219.

company officers.[178] Legitimacy is based on the family members' trust in the committee.[179] Selecting a committee member who is recognized in her field increases her chances of winning the family's trust and gaining legitimacy.[180] Appointing a committee member with status can contribute to strengthening the company's image and public standing and increases the company's network—both inside and outside the industry. Such a committee member may, in addition, assist the company in the intergenerational transfer process and serve as a mentor to the younger generation in its early years of leadership.[181]

v. *Authority*. As a voluntary body, and as the name implies, the advisory committee does not have given legal authority to govern. Its influence is derived from the recognition of family members and company officers. Accordingly, tasks and authority are given to the advisory committee as allowed by the company's bylaws; generally, its decisions constitute nonbinding recommendations. However, the controlling family and company can adopt the advisory committee's decisions and grant them binding status. This point is derived, inter alia, from the essential differences between an advisory committee and a board of directors.[182]

VI. CONCLUSION

This Article lays a conceptual and theoretical foundation for a legal discussion of the complex and unique arena of family companies and examines whether family companies can suitably adapt to nonfamily corporate governance provisions. This task is important and necessary due to the prevalence of family companies and their significant contribution to the global economy, as well as to courts' a priori and superficial perception of family companies as ones that commingle affairs. Moreover, until now, legislation, case law, and legal literature have not systematically addressed this issue. To this end, this Article begins by establishing a definition for family companies, noting its social and economic importance, and describing family companies within corporate theories. In this framework, in addition to the familiar principal–agent theory, this Article also presents the stewardship theory. The latter is recognized in academic management

178. *Id.* at 202.

179. *See id.*

180. *See id.*

181. Carlo Salvato & Guido Corbetta, *Transitional Leadership of Advisors as a Facilitator of Successors' Leadership Construction*, 26 FAM. BUS. REV. 235, 235–36 (2013).

182. Osi, *supra* note 41, at 207–09.

literature but not in conventional corporate legal writing. As this Article shows, the stewardship theory is expected to have a significant impact on the functioning and performance of family companies and even has useful insights to the analysis of ordinary companies as well. This Article then identifies the family company's unique characteristics, which integrate both business and emotional characteristics. This investigation leads to the conclusion that while family companies are endowed with unique qualities that are likely to afford them economic advantages—qualities consistent with the stewardship theory and long-term thinking—it cannot be unequivocally determined that family companies' performances will outshine that of regular companies. In addition, these characteristics could also affect the manner in which family companies interact with the legal world. The reason, in this Article's assessment and evident in its survey of management literature, is that alongside positive characteristics, family companies inherently carry negative characteristics that overshadow and moderate the effect of positive characteristics. The Authors' assumption is that the overlap between the family circle and the business circle, and the possible spillover of emotional considerations onto business decisions, stimulates negative characteristics.

This insight pushes us to look for mechanisms to mitigate the predicted power of the negative characteristics and tip the scale in favor of the positive characteristics, thus improving the legal status of family companies, their performance, and survivability. Accordingly, this Article proposes criteria to determine those instances where the commingling of business and family affairs is high versus those where it is relatively weak. This will allow courts to treat each family company on an individual basis and not in one general and intuitive or prejudicial manner. This Article also suggests that private family companies, especially those with active family control, adopt an objectively independent, professional mechanism that borrows traditional corporate analysis from the principal–agent theory. While the traditional agency problem is usually weaker in private family companies, an objective, independent, and professional voluntary mechanism would integrate the business and family vectors in a creative, effective, and trusting manner. Even though the advisory committee is based on the principal–agency theory, which assumes alienation between those in control of the company and its shareholders, this Article proposes its use even in family companies with no such separation. Voluntary adoption and effective assimilation of an advisory committee are consistent with the enabling philosophy of company law. Therefore, the objectives, functions, organizational hierarchy, and powers of an advisory committee will be determined in accordance with the characteristics of each family company. As this mechanism is inspired by corporate legislative changes and trends, this may decrease the court's suspicion and scrutiny of the private family corporation. Moreover, it has potential to neutralize the company's unique negative characteristics while preserving its unique positive characteristics.

In other words, the dialogue this Article proposes between family companies and ordinary companies should inspire benefits that companies of the first type can gain from companies of the second. In the same breath, accepted corporate analysis of ordinary companies can benefit from knowledge of the world of family companies and the stewardship theory, but this will remain the subject of an additional article.