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Trusted advisors in a family business's succession-planning process—An agency perspective

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ABSTRACT

Family business succession is a complex and challenging process, in which family members often build on the support of trusted advisors who can be seen as the most relied external source of advice and knowledge that family businesses draw on. Based on an extensive literature review, this article aims to synthesize prior research on both advisors and succession to systematically describe and analyze the role of trusted advisors during the succession-planning process. Based on arguments from agency theory, we discuss potential benefits and drawbacks associated with the involvement of trusted advisors along the four phases—trigger, preparation, selection, and training—of the succession-planning process and outline how trusted advisors can mitigate but also enhance agency costs—in particular goal divergence and information asymmetry—during each of these four phases. Subsequently, we discuss four typical constellations of advisor involvement, which vary in their agency costs and thus have different levels of bias and efficiency. We thereby outline several inefficiencies that result from the common setup in which an incumbent and a successor both rely on their own trusted advisors or a team of expert advisors and propose a balanced and efficient model of advisor involvement as a potential solution which reduces the agency costs. This conceptual article contributes to research on succession, agency theory, and trusted advisors in family firms.

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Introduction

Family business succession is a crucial and in many cases long lasting process that may absorb the attention and resources of a family for years (Cabrera-Suarez, De Saa-Perez, & Garcia-Almeida, 2001). Numerous examples around the world show that succession is also a challenging process that many businesses struggle with (Mussolino & Calabrò, 2014), in particular with defining the right timing, finding the right successor, and managing the succession process in a fortunate way (Sharma, 2004).

In light of the challenges that arise during the succession process, researchers and practitioners have recently started to point to the crucial role played by trusted advisors in the succession process (e.g., Strike, 2012). Trusted advisors are defined as the most-relied external source of business advice for members of family businesses, including, for instance, lawyers, accountants, and consultants with whom family members have enjoyed long-lasting professional relationships (LaChapelle & Barnes, 1998; Nicholson, Shepherd, & Woods, 2010). On the one hand, trusted advisors are expected to provide important capabilities such as expert knowledge and high-quality feedback and thus improve the quality of family members' decisions, the strategic planning process, and ultimately the firm's performance (Davis, Dibrell, Craig, & Green, 2013; Reay, Pearson, & Dyer, 2013; Strike, 2012). In particular, trusted advisors can improve the efficacy of the succession process by mentoring both incumbents and successors, providing new insights on the succession (Salvato & Corbetta, 2013), or acting as agents to bring different opinions together and achieve compromise solutions (Lane, Astrachan, Keyt, & McMillan, 2006; Thomas, 2002). However, trusted advisors are also associated with possible costs and drawbacks, stemming from agency costs, particularly those costs that result from divergent goals (e.g., Chrisman, Chua, & Sharma, 2004a, 2004b) and informational asymmetries (e.g., Dehlen, Zellweger, Kammerlander, & Halter, 2014) between the incumbent, the successor, and the advisor. Those drawbacks include heavy pressure on incumbents (Hilburt-Davis & Senturia, 1995), an overly task-oriented approach that neglects involved parties' emotions (Goodman, 1998; Kaye, 1996), and narrow coaching that results in a reduction in the independence of successors' actions and decisions (Lane, 1989).

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Despite recent advances in the scholarly knowledge about the influence of trusted advisors in family firms, our understanding of their role and its associated benefits and drawbacks is still superficial (see discussion in Strike, 2012). In particular, the precise benefits and disadvantages associated with trusted advisor involvement remain unclear to date. In addition, there is a lack of knowledge about the drivers of efficient and unbiased (as opposed to inefficient and biased) triadic constellations of incumbents, successors, and trusted advisors. We aim to contribute to closing this gap by integrating the abundant body of literature on the succession process (e.g., Sharma, 2004; Sharma, Chrisman, & Gersick, 2012) with the nascent research stream on family business advisors (e.g., Reay et al., 2013; Strike, 2012) and by building a conceptual model on the impact of involving a trusted advisor in a family business succession. Thereby, we consider leadership and ownership transfers to both family-internal and -external successors. Moreover, we concentrate on the "planning process" (Cabrera-Suarez et al., 2001; Sharma, Chrisman, & Chua, 2003), which is particularly determinative of the outcome of the succession process (De Massis, Chua, & Chrisman, 2008; Le Breton-Miller, Miller, & Steier, 2004; Sharma, Chrisman, & Chua, 1997) because the absence of a thorough succession plan enhances the risk of business failure (Barach, Gantisky, Carson, & Doochin, 1988; Seymour, 1993).

In particular, we aim to answer the following research questions: *(1) How can agency theory elucidate the specific benefits and drawbacks associated with trusted advisor involvement along the different phases of a family firm's succession-planning process? and (2) Based on those theoretical deductions, what constellations of the roles and relationships of incumbents, successors, and trusted advisors are likely to maximize or minimize agency costs during the succession process?* After a brief overview of the extant research on trusted advisors, succession planning, and agency theory in family firms, we focus on how trusted advisors either increase or decrease important agency costs throughout the four phases of the succession-planning process. Subsequently, we discuss four commonly observed constellations of the relationship between incumbents, successors, and trusted advisors and analyze the costs and benefits associated with those constellations. We argue that a constellation with two or more instead of one trusted advisors is not only inefficient, but also increases agency costs. Furthermore, we discuss that lack of bias (i.e. when the trusted advisor does not favor either party) is a crucial prerequisite for agency costs being minimized rather than maximized through advisor involvement in family firms.

Our article contributes to the literature in several ways. First, we advance the research on trusted advisors in family businesses by building on agency theory to systematically investigate the advantages and disadvantages stemming from trusted advisor involvement. Most extant studies on family firm advisors are characterized by a focus on anecdotal evidence and lack of theoretical rigor (see critique by Jaffe & Lane, 2004; Strike, 2012; Swartz, 1989; Upton, Vinton, Seaman, & Moore, 1993). Second, we further extend the literature on family business succession by systematically integrating the role played by trusted advisors and his or her impact on agency costs. Instead of the dyadic relationship between an incumbent and a successor (Handler, 1994), we move to the triadic relationship between incumbents, successors, and trusted advisors, which alleviates several agency costs but gives rise to other agency costs. Thereby, we focus in particular on agency costs in form of goal divergence and information asymmetry and outline in detail how trusted advisors on the one hand mitigate and on the other hand increase those costs. Third, we discuss several constellations of trusted advisor involvement commonly observed in practice—such as relying on advice from several consultants or engaging a close accountant to manage the succession process—and identify their related agency costs. After the identification and an extensive discussion of the positive and negative effects of trusted advisors on agency cost, we synthesize a proposition of a balanced and efficient model that reduces those agency costs. Fourth, we also advance research on agency theory. Although there is a large body of research on agency costs in family businesses, most of this research focuses on classical owner–manager relations. This manuscript extends this predominant view by including the trusted advisor as a further actor that, while neither being owner nor manager of the firm, can affect the level of agency conflicts in the firm. Doing so provides a more nuanced picture of agency costs in family firms that is not restricted to dyadic relationships but considers a triadic relationship.

Theoretical background and key concepts

The succession-planning process

Succession in family business is widely seen as the process that transfers ownership and leadership from an incumbent to a next-generation successor, who may or may not be a family member (Sharma, 2004; Steier & Miller, 2010). Researchers agree that succession is one of the most important processes of a family business's life cycle due to its substantive effect on the firm's strategy, culture, and also its survivability (Ahlers, Hack, & Kellermanns, 2014; Cater III & Kidwell, 2014; Handler, 1994). The succession-planning process, which is the focus of this paper, is the first and one of the most important parts of the overall succession process and has two main goals: first, the selection of the successor, which includes setting criteria or defining a pool of possible candidates (Le Breton-Miller et al., 2004); and, second, preparation for the transfer of management control as well as ownership shares from an older to a younger generation (Sharma et al., 2003). Because the planning process embraces every succession-related activity from the incumbent's first consideration of his or her exit to the actual transfer of leadership and ownership, it is determinant of the outcome of the entire succession process and thus, is particularly worthy of study (Chittoor & Das, 2007; Sharma et al., 1997). Based on an extensive review of prior literature on family firm succession, we synthesize four important phases of the succession planning process: the *trigger phase*, the *preparation phase*, the *selection phase*, and the *training phase* (Brockhaus, 2004; De Massis et al., 2008; Murray, 2003; Le Breton-Miller et al., 2004). Those phases can differ in length and can either occur consecutive or (partly) in parallel.[2] Table 1 provides an overview of ten important, previously published studies that investigated the succession planning process in detail and links their findings to the four phases applied in this manuscript.

The first step in succession planning is an incumbent's readiness to hand over the business, which is often initiated by a *trigger* (Murray, 2003). The trigger to consider one's own exit from a business can be a result of developmental pressures such as age or health, internal forces such as family, a predestined succession candidate, company management, or external pressure for a change, for example, from accountants or customers (Gersick, Lansberg, Desjardins, & Dunn, 1999). One important aspect of succession readiness is an incumbent's willingness to hand over the business (Brun de Pontet, Worsch, & Gagne, 2007): While owner-managers of family firms typically possess the general

[2] At times those phases might have unclear starting and ending points, in particular the first phases can even occur rather unconsciously and/or in an unplanned, unsystematic way. As this article focuses on the impact of trusted advisors in each of the four phases, we henceforth assume a conscious and rather defined nature of all four phases.

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