



# Business Families and Family Businesses

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The STEP Handbook for Advisers,  
Third Edition

Consulting Editor **Clare Stirzaker**

**STEP**   
ADVISING FAMILIES ACROSS GENERATIONS

# Table of contents

**About STEP** \_\_\_\_\_ 7

**Foreword** \_\_\_\_\_ 9

Clare Stirzaker

Boodle Hatfield LLP

## **Part I. Setting the scene**

**Understanding the family** \_\_\_\_\_ 11

### **business mindset: an evolutionary approach**

Justin B Craig

Tecnológico de Monterrey;

Kellogg School of Management;

Bond University

Catharina C Jecklin

Bond University

**Clarifying purpose** \_\_\_\_\_ 23

### **and values: guiding families towards meaningful goals**

Catherine Grum

Catherine Grum Consultancy Ltd

**Theories and models in** \_\_\_\_\_ 35

### **family enterprise advising**

Patricia M Annino

Rimon Law

Judy Green

Family Firm Institute Inc.

## **Part II. Stages of the family business**

**Structuring the family** \_\_\_\_\_ 51

### **business**

Toby Crooks

Katharine Haggie

Hiral Kanzaria

Rawlinson & Hunter LLP

**The value of family** \_\_\_\_\_ 67

### **governance**

Ken McCracken

MFBC Limited

**Stages of the family** \_\_\_\_\_ 77

### **business**

Yannick Archambault

KPMG Canada

Kaajal Prasad

KPMG Australia

**Advances in human** \_\_\_\_\_ 91

### **longevity and the impact upon family business transition plans**

Hayden Bailey

Boodle Hatfield LLP

**Next-generation planning** \_\_\_\_\_ 107

Matthew Fleming

Stonehage Fleming

Maria Villax

Bedrock Group

### **Part III. Succession**

#### **Preparing for transfer \_\_\_\_\_ 121 of ownership**

Dan Frosh

Family Firm Institute Inc.

Andrew P Hier

Cambridge Family Enterprise  
Group

#### **Trusts and family \_\_\_\_\_ 137 businesses: the ideal succession solution?**

Nic Arnold

Victoria Blackburn

JTC Private Office

Bryony Cove

Jennifer Ridgway

Farrer & Co LLP

#### **Extracting wealth from \_\_\_\_\_ 151 the family business**

Russell Prior

HSBC Global Private Banking

#### **Selling the family \_\_\_\_\_ 169 business**

##### **Introduction \_\_\_\_\_ 169**

Clare Stirzaker

Boodle Hatfield LLP

##### **The financial impact \_\_\_\_\_ 170 of selling the family**

**business**

Dominic Epton

Katharine Taylor

Rothschild & Co Wealth

Management

#### **The process and family \_\_\_\_\_ 176 dynamic considerations of selling the family business**

Nick Mayhew

Alembic Strategy

#### **Managing family \_\_\_\_\_ 189 dynamics: how to improve communication and deal with conflict effectively**

Tony Cohen

Alexandra Sharpe

Kinestra Partners LLP

#### **The family business \_\_\_\_\_ 205 – options for preventing and dealing with family disputes**

Guy Abrahams

Nick Jacob

Daniel Ugur

Forsters LLP

#### **Family businesses and \_\_\_\_\_ 217 divorce**

Katie O'Callaghan

Boodle Hatfield LLP

#### **Sophisticated reputation \_\_\_\_\_ 233 management for family companies**

Lily Kennett

Victoria O'Byrne

Schillings

#### **Understanding the wealth \_\_\_\_\_ 245 holder spectrum**

Matthew Braithwaite

Wedlake Bell LLP

Gina Pereira

Dāna Stewardship Advisory

**Providing advice on \_\_\_\_\_ 257**  
**philanthropy: why, when**  
**and how to raise giving with**  
**family clients**

Emma Beeston

Philanthropy adviser

Beth Breeze

Centre for Philanthropy,

University of Kent

**About the authors \_\_\_\_\_ 275**

**About Globe Law \_\_\_\_\_ 288**  
**and Business**

# Trusts and family businesses: the ideal succession solution?

Nic Arnold  
Victoria Blackburn  
JTC Private Office  
Bryony Cove  
Jennifer Ridgway  
Farrer & Co LLP

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## 1. **Setting the scene – why trusts?**

Trusts have long played a role in managing and preserving family wealth. While historically they originate from a need for medieval landowners to protect their estates in times of war and unexpected deaths, trusts have evolved to be vehicles for succession planning, protection of family and business assets as well as means of potentially saving tax.

COVID-19 exposed vulnerabilities for family businesses which highlighted the need for more robust, proactive business planning and risk management. As well as challenging the operational agility and financial robustness of family businesses, the pandemic underscored the importance of better succession planning in the wake of the sometimes unexpected death or illness of key family members. With families reevaluating their priorities, trusts can be considered as tools to generate continuity and manage the transfer of business ownership in a controlled way which avoids fragmentation and reduces the likelihood of family friction.

Further, geopolitical influences, such as the war in the Ukraine, US/China trade tensions, global inflation and even the departure of the United Kingdom from the European Union, will impact the decisions made by family business owners in an increasingly interconnected and unpredictable world.

This chapter looks at how families can use trusts to protect their family business from such external threats and even, it might be said, from the biggest potential threat: the family itself. As family dynamics and needs change, the impact of just one family member's actions can have extremely negative impacts on the long-term family wealth preservation and success of the business.

It should be noted that this chapter does not seek to replace detailed legal and tax analysis, nor the exact advice which may be given on a jurisdiction-by-jurisdiction, and family-by-family, basis. This chapter does, however, provide useful guiding principles and examples which should assist the practitioner.

We shed light on the advantages, and disadvantages, of passing ownership

of the family business to trustees (individuals or professional trustees) to oversee the family's future interaction with the family business, and consumption of the family wealth.

We look at some of the challenges which may occur where families do not appreciate the role that a trust plays in their lives, where trust deeds may have been drafted too rigidly to meet evolving family needs, or where beneficiaries' expectations are not aligned with those of the trustees and/or other family members. Such challenges can give rise to disagreements, and case law provides important guidelines for dispute resolution. Trusts have also faced challenges as tax legislation continues to evolve across the globe, but despite this, it is rare to see the mass collapsing of trust structures due to tax law changes.

## **2. Trust principles – the basics**

Trusts are known within common law jurisdictions for their ability to provide control and flexibility over family wealth beyond the founding generation. Families have found a powerful mechanism by which to manage the family business ownership. In simple terms, the trustee is able to act as a single and often sole shareholder and decision maker who is able to hold a macro view of the family business. This is a position that can be held in perpetuity while the beneficial class(es) who may have either an active or a passive engagement in the family business, evolve over time and through the generations. While other types of structures in civil law jurisdictions may seek to achieve a similar result, trusts have a particular ability to provide meaningful long-term safeguarding of wealth in a way that embodies the values and desires of the wealth creators. This is perhaps especially true when used to protect family businesses, as trustees can play a central role in the long-term relationship between family members and the family business.

In technical terms, most trust law is spread across three sources: common law principles, statute and case law. Each jurisdiction's trust law has evolved differently, and we will seek to illustrate examples through this chapter from key jurisdictions, including England and Wales, which is arguably the original trust law jurisdiction.

The role of trustees and their interaction with beneficiaries will be governed by all three sources and requires careful navigation. Indeed, in order to fulfil their fiduciary duties, professional trustees will usually require regular and ongoing input from professional advisers in their capacity as trustees separate from, and in addition to, professional advice taken by the trust beneficiaries.

In each jurisdiction, trustees will be informed by local statute setting out the nature and extent of their powers and duties (eg, the Trustee Act 2000 under English law in relation to investment powers). Typically, however, case law will also need to be considered across different trust jurisdictions when exercising those powers, and each trustee should bring their own experience to bear.

While the courts may be consulted in relation to larger decisions, often referred to as ‘momentous decisions’ (per *Public Trustee v Cooper*<sup>1</sup>) – such as the appointment of a large shareholding on a new trust, or to a particular beneficiary, or the decision to sell the long-held family business – the general principle is that trustees must make decisions based on their knowledge of the trust assets, the beneficiaries and the surrounding context.

Trustees will need to review the appropriateness of the decisions they take by appraising all relevant considerations (which includes the settlor’s wishes) but disregarding irrelevant considerations (per *Hastings Bass (deceased)*<sup>2</sup>). We look further at this later in the chapter.

A statement or letter of wishes, while not legally binding, is an important reference point for trustees to follow when executing their fiduciary duties. Where most effective, this document should provide guidance to trustees about the settlor’s personal preferences for the management and distribution of a trust’s assets.

In many cases, additional checks and balances are achieved through the appointment of a protector. While the trustees will typically focus on the day-to-day management and administration of the trust, the protector provides an oversight role, ensuring the trustees are acting appropriately and reasonably, and typically their role is to see that the trust continues to align with the settlor’s intentions and the needs of the beneficiary class, albeit within the present context. The protector may have powers of veto (their consent is required for certain trustee decisions) or may have the power to appoint or remove trustees, with powers to add to or exclude individuals from the beneficiary class.

Settlors may also reserve certain powers to themselves. This often includes investment powers, the power to remove and appoint trustees or, sometimes, dispositive powers or vetoes. Such powers may support a bond of trust between the settlor and the trustees, or alternatively may drive a wedge between them. Care is needed. Utilising the skills of the settlor in the first few years can be of benefit, but a plan for succession to the powers held by the settlor should be included to ensure longevity and give the trustees the space to appropriately perform their duties.

Trustees need to be conscious of any limitations on the exercise of their powers, but in the context of a family business, where powers held outside the trustee body (by non-trustee power holders, like a protector) are managed well alongside the trustee role, this will provide an opportunity for good governance and family communication. This is explored further later in the chapter.

There will always be advantages and disadvantages of owning a family business within a trust structure. Key to this will be the care with which the

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1 [2001] WTLR 901.  
2 [1975] Ch 25 (CA).

trust is set up, the experience and quality of the trustees overseeing the family wealth, and the degree to which it is recognised that a trust structure used to protect a family business should be treated as an integrated part of the working mechanics of the family with strong beneficiary communication and education.

### **3. Control – when it works and when it doesn't**

The most common concern that families have when contemplating settling their family business into trust, is about passing shareholder ownership of the business to the custody of decision makers who are not family members and giving up the control they have been used to over many years.

In the context of a family business, concerns can legitimately arise that the trust will distance the family from their business, particularly where professional trustees exert a high degree of governance through the processes and procedures they employ to protect the family wealth.

These concerns can be managed via what is now a classic ownership model whereby the trustees are the shareholders owning a holding company, which in turn owns the trading business(es). This effectively separates ownership, oversight and management of the business. Family members routinely sit on holdings boards with senior executives and have a say in their composition, whether by formal veto, via a family protector or a formal consultation requirement (with these powers or processes typically set out in the relevant corporate governance documentation). The business itself is then run by an executive board for the trading entities which sit below the holding company.

In addition, for larger trusts with complex assets including family businesses, the protector may be a committee rather than an individual, and this can help with issues of protector succession, particularly where the idea of acting on the committee for a set term is introduced.

This idea is exemplified in the case of a second generation £1 billion family business which was held through a Jersey trust. The trust, settled by the deceased patriarch, was discretionary in nature, with wide trustee powers. The business was very successful and was driven by full-time involvement from all members of the second generation. However, it was becoming clear that the nature and level of family input would need to adapt to accommodate the increased number of third-generation family members who represented a wide range of ages and degree of business involvement. The protector provisions were used to implement a family-led protector committee operating on set terms and replacing the role of one person with family members from all branches of the family. Consent is now required from the committee for major trustee decisions, including significant disposals, sale of shares in the business, and the power to remove and appoint trustees. This innovation will play a key role within the family business governance as the number of trust beneficiaries gets larger and the overall family involvement in the business is reduced.

In the case of an elderly shipping magnate who had spent his life making the major decisions to create and run his business empire, the challenge was that, despite the different talents and responsibilities of his descendants, there was no individual who could replace him in the role he had created. There was a real concern that everything he worked so hard to create and the stability this provided for his family would collapse after his death. The decision was taken to put the family business into trust, and with the support of the trustees, the settlor built an advisory committee comprised of key family and business members whose roles and responsibilities were enshrined in a family charter linking in with the operating side of the business. As a result of this careful planning, the talents of the next generation were utilised in a meaningful way alongside the introduction of the trust structure to protect the family business for the long term.

In situations where family members are able to exert power over the day-to-day running of the business outside the role of an employee or consultant, the addition of trustees as stewards and legal owners can formalise roles and responsibilities, and enhance the skills and reflect the goals of the family individually and collectively.

In the case of a settlor who had passed away many years before, the burden of wealth was a real concern for the patriarch's six children. The new patriarch, the eldest son, was intimidated by the responsibility imposed on him, demotivated by having so much wealth and the business quickly declined, as did his focus in life. Using the trust structure as a tool, and with the input from the trustees and other key advisers, a strategy was developed that allowed him to generate a new focus and to appoint people better able to manage the family business. He stepped down as CEO and built an impressive philanthropic side to the trust, which helped him find a renewed purpose and sense of fulfilment.

This is an extract from the chapter 'Trusts and family businesses: the ideal succession solution?' by Nic Arnold, Victoria Blackburn, Bryony Cove and Jennifer Ridgway in *Business Families and Family Businesses: A STEP Handbook for Advisers, Third Edition*, published by Globe Law and Business.

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# Business Families and Family Businesses

The STEP Handbook for Advisers, Third Edition

## **Business Families and Family Businesses: The STEP Handbook for Advisers, Third Edition**

Since the publication of the last edition in 2018, the world has experienced significant change. COVID-19, war, economic downturn and a more urgent focus on climate change are just some of the key events that have led to increased geopolitical risk.

This third edition, co-published with STEP, looks at developments within the approach to family business advising since 2018, taking account of the current geopolitical backdrop and the shift in attitude in a growing number of clients towards succession, philanthropy and investments.

However, for those new to the field there remains ongoing guidance on:

- how to understand the unique nature of family businesses;
- typical family dynamics that impact succession;
- the power of governance in supporting good ownership and management;
- the typical stages of the family business and the key risks that will invariably arise; and
- the different legal and non-legal approaches to tackling such problems.

Featuring contributions from leading practitioners in the field (including the Family Firm Institute, Cambridge Family Enterprise Group, KPMG, Rawlinson & Hunter, JTC Private Office, Boodle Hatfield, Forsters, Farrer & Co, Wedlake Bell, Schillings, HSBC Global Private Banking, Stonehage Fleming and Rothschild & Co), this comprehensive handbook makes essential reading for all practitioners who advise business families, including lawyers, accountants, financial advisers and wider family business advisers.

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