

Insight 2 - The Family Constitution

Dave got to the club a little early on Monday. He wanted to do some extra stretching to ease the stiffness from a busy weekend before the group began their run. He was surprised to find Jim already there, but it quickly became apparent that Jim was hoping for an opportunity to tell Dave about his pitch to his family regarding their Family Mission Statement.

“So, how did the birthday party go?” Dave asked.

“It was great” Jim replied. “My son passed a milestone with his 35th birthday AND we had an easier then expected discussion around the dining room table about our Family Mission Statement.”

“Do tell!” Dave encouraged.

“As you suggested, I started by congratulating everyone on their personal accomplishments and then switched to the progress of the company, acknowledging that it was only through the combined efforts of the family that we are where we are today.

“I went on to say that we are a family and a company founded on strong personal values and that I believed it was important to occasionally remind ourselves of those values. And although our business principles were reflected in our corporate Mission Statement, I felt it would be worthwhile for us to have a Family Mission Statement that more specifically described the morals and ethics our family represented on a more personal level.

“I then used some of the questions you suggested as examples.”

“What was the reaction?” Dave asked.

“I was very pleased with how immediately open almost everyone was to the discussion. It was as if they had been having similar thoughts.”

“That’s quite possible,” Dave observed. “They can’t be oblivious to the same things that are causing you concern. How did it go from there?”

“We had a lively and very production discussion that lasted nearly two hours. I admit I was a bit surprised by some of the things my family had to say. It also became apparent that while we shared many values, there were differences in how some people thought those values should be applied in the real world.”

“So, were you able to get something specific in writing?” Dave asked.

“Yes, we were,” Jim answered. “It is still a work-in-progress, but can I read you our first attempt at a Family Mission Statement?”

“Sure, love to hear it!” Dave replied enthusiastically.

“We differentiated a little between individual and family values. We put family first, on the assumption that it makes more sense to align our personal principles with those of the family, rather than trying to cobble all our individual beliefs into a combined statement on behalf of the family.”

“Sounds reasonable to me,” Dave offered.

Jim pulled out his phone and read from his notes. “Here goes.”

“As a family, we promote a loving, caring and open communication atmosphere, to the best of our ability, at all times. While we have a desire to create a family business legacy for those who wish to be part of it, we also support each other’s personal innate talents and life’s goals, whether they be pursuing entrepreneurship unrelated to the family business; or simply bettering ourselves and the communities in which we live.

Recognizing that there may, occasionally, be differences of opinion, we will respect the unique personality, talents and beliefs we each bring to the table, using patience, understanding and empathy to resolve conflicts in a positive way. Within reasonable limits, this may mean placing family interests above those of individual family members.

We embrace the individual values that support our family values — kindness, honesty and integrity. We also believe in sharing our knowledge and practical experience with other family members, so we all continue to learn and grow in order to achieve a truly fulfilling life.

“Wow,” Dave replied. “This is terrific, Jim! I think it really captures who you are, and my guess is who you as a family want to continue to be.”

Just then, Alan arrived.

“What are you two up to?” he asked.

Jim responded, “Dave and I were just following up on a conversation we had last week about how to keep family relationships on solid ground in a family-owned business — more specifically, in my business.”

“Ooh, that can be a challenge,” Alan acknowledged. “My law practice has been involved in too many family businesses disputes that could have easily been avoided with just a bit of proper consideration.”

“Like what?” Jim asked.

“I like to think of them as “rules of engagement”, Alan responded. “Things like communication among family members, how decisions are made, how differences are resolved; all the way down to who gets to be part of the family business, how people are remunerated and so on.

Dave jumped in, “Jim had a family meeting over the weekend and was able to develop a pretty good Family Mission Statement that includes some of those things. Jim, do you mind sharing with Alan?”

“Not at all,” Jim answered as he passed his notes to Alan.

“Very good!” Alan congratulated him after a quick read. “A Family Mission Statement like this is a great foundation for a Family Constitution.”

“Which is...?” Jim asked.

“It is basically a document that communicates to all members of the family how life will be conducted in the family business, regardless of fate or unforeseen circumstances.”

“And people don’t object to that kind of oversight on how their business is to be managed?” Jim asked.

“Some are skeptical to be sure, but then I invite them to think about any difficult situations involving their family business, where important decisions had to be made, or disagreements occurred. That’s when I hear horror stories about the devastating impact of intra-family conflict.

“Then I ask how things might have worked out if they had a document outlining how those circumstances were to be addressed in place at the time. I think you know the answer I get.”

Dave jumped back into the conversation. “Jim, earlier when I asked how the family meeting went, you used the phrase ‘almost everyone’ was immediately open to the discussion. Was there someone who was less than enthusiastic?”

“Yeah, as I mentioned in our last conversation, my in-laws, who are shareholders, have been making noise about how some aspects of the business are being managed and how they should be more involved in decision-making.”

“Is it fair to say that a Family Constitution might help to better define things for them and put everything into context? Dave asked.

“Probably, but I’m not sure they would be willing to be limited by a legal document or would feel that one was even necessary in a company like ours.”

“Actually,” Alan interjected, “a Family Constitution is not a legally binding document – it’s more like guidance than rules. Which means it can also apply to members of the extended family who may be affected by performance of the family business, without binding them to any formal agreement.”

By now, the other members of the running group were starting to arrive, so Dave quickly said, “Alan, I know that corporate governance is a speciality in your law practice. Setting aside for the moment any formal engagement, would you be willing to spend a bit more time with Jim and me talking about this?”

“Of course,” Alan responded without hesitation, “anything for my running buddies! Are you guys available later today, say 5:00 PM, to hook up for a beer?”

“I can be there.” Jim said. “Me too.” Dave added.

“OK, then, 5:00 o’clock at The Duke.” Alan said. “Now, no more talk of this. We have an hour of running ahead of us!”

By 5:05 PM, Dave, Jim and Alan were seated in the quietest corner of the pub.

“Thanks for making this time available to us, Alan,” Dave said.

“It is my pleasure,” Alan responded, “and I think it has been too long since we had a get-together other than running. However, I don’t want to create the impression that corporate governance is a quick and easy topic that we can fully address over just one beer. We can talk about some of the key considerations, but when it comes down to the actual document, Jim, you will have a fair bit of work to do.”

“And, Jim, as I mentioned last week,” Dave remarked, “I have some sample documents that I can share to get you started and I am happy to run through them with you. Perhaps, then, however, we should buy a couple hours of Alan’s time for him to review and comment.”

“Let’s not worry about buying anyone’s time at this stage,” Alan reacted. “I am happy to help out a friend, particularly one I have sweated alongside for, what is it now, 10 years!”

“So,” Alan began, “we have already talked a bit about what a Family Constitution is and what it should be designed to do. Let’s look now at the ‘why’ — why should you go to the effort of creating one? Here’s my simple take on it. You have a very successful business, Jim, that was built over time. In other words, what you know about your business is rooted in the past. You can tell me with 100% accuracy what has happened in your business since you started it.

“What you can’t tell me, however, is what is going to happen to it in the future. Yes, you have ambitions and plans, but as John Lennon wrote in a song to his son, ‘Life is what happens while you’re busy making other plans.’ So, one big benefit of a Family Constitution is that it is future oriented and provides you with a framework for dealing with unexpected contingencies that arise along the way.”

“I am already getting the feeling this is something I should have done a long time ago,” Jim admitted.

“We always recommend creating a Family Constitution as soon as possible and, ideally, before any major transitions occur in the business, so that the family has a clear idea of the goals of the business, its internal structures and the roles of family members.”

“I missed the boat on that one,” Jim confessed. “We significantly shifted our business model a couple of years ago and I can see now how we might have reduced some of the tension we are experiencing today if we had given more thought to dealing internally with the change.”

“It’s not too late.” Alan offered. “You will no doubt have other opportunities or threats in your business, so putting something in place today will serve you well when they occur. The process of creating a Family Constitution has also proven to be a good way to mend broken fences from previous disagreements.”

The conversation paused while the waiter took their orders. Dave brought it back together by saying, “I know what’s in the sample documents I have, but, what do you like to see, Alan, in a Family Constitution?”

“Again, as I said earlier today, it all starts with the Family Mission Statement that describes values and vision. You have made an excellent start on yours, Jim.

“As you might suspect from our discussions so far, processes are an important component for planning, decision making, respectfully resolving differences and overall management of the business.

“From required processes comes the need for structure. Who’s the ultimate boss? Even if you have a very collaborative family group, it is usually important that you have a final authority to break deadlocks, should they occur. What roles and responsibilities are needed? What are the qualifications for those roles? How are family members to be compensated – for their work in the firm and for their participation or ownership as family members? How do you deal with underperformance?”

“A prosperous family business also often brings community involvement with it. What is the guidance around things like public behavior, lifestyle, political interests, charity, media attention and the like?”

“As children age or families expand, what are the rules of entry and participation for additional members in the business?”

“We already have some documents — shareholder agreements, confidentiality agreements and the like. Does the Family Constitution include those?” Jim asked.

“It doesn’t specifically include them, but it builds on their intent.” Alan answered. “Those legal structures, and clearly defined rights and responsibilities, are crucial to good management of the family business. However, sometimes the speed with which they can adapt to changes in the family dynamic or their lack of flexibility in how things are to be handled, can’t adequately address the problems that can unexpectedly arise in a family business.

“For example, I can think of a recent case where one of the directors and shareholders of a family-owned company died; and her husband insisted that he take her place on the Board. Her rationale was that he had to ‘protect the shares’ he would inherit as a result of his spouses’ death. Unfortunately, he had no business experience whatsoever, had never been involved in any of the company affairs and had a strained relationship with the other family members. Should he have automatically assumed all the rights of his spouse?”

“In another situation in which we were involved, a husband and wife who both worked in a family business, went through a nasty divorce. Should they both be allowed to continue working in the family business? How would the inevitable bitterness be handled? What happens when it comes to paying dividends – should they both receive the same amount?”

“Fortunately, we had previously put a Family Constitution in place in both firms, with stated principles and protocols to facilitate swift settlement of these unexpected issues.

“Wow – good lessons,” Jim said. “From those examples, can I assume that, like the Family Mission Statement, everyone should be involved in crafting our Family Constitution – so no one can claim ignorance or try to circumvent what we all agreed to?” Jim asked.

“Yes, you want anyone in the family affected by the document and who is capable of understanding its purpose to participate. We also recommend that the Constitution be formally ratified by most, if not all, those family members, so they feel included.”

Jim sat silent for a moment until Dave spoke.

“Jim, clearly, the development of a Family Constitution is a much bigger job than creating a Family Mission Statement, so why don’t we approach it this way — you and I will review the sample documents I have, picking out clauses that you feel apply to your family and your business. Then, we will engage Alan to review and comment on what we have decided was appropriate for your situation and prepare a draft to present to your family.

“Does that make sense to you?”

“It does,” Jim replied with a far away look in his eyes that said he was already thinking about what he would like to include in the document to address what was already happening in his business.

TOOLBOX

SAMPLE

FAMILY CONSTITUTION ISSUES FOR DISCUSSIONS

Managing Succession

- How to identify the next president?
- When does the presidential transition take place (timing)?
- How do the current CEO and successor share planning and decision-making responsibilities during the transition?
- How to evaluate the next president's performance and plan for his or her replacement?
- What non-business interests will keep the senior generation fulfilled during retirement?

Family Business Careers

- How to decide which family members can join the family business?
- How to plan management development experiences?
- What preparation or experience, if any, is required?
- How to evaluate performance and reward achievement?
- What if a family employee does not perform?
- How to encourage the contributions of non-family employees?
- What if a family member chooses to leave the business?
- Whether to permit spouses, partners or other non-blood relatives to work full or part time in the business?
- Whether to allow the next generation's children to enter the business? Under what circumstances?

Compensation

- How to evaluate and compensate family members?
- How are bonuses determined?
- Who participates in stock option programs?

Ownership and Governance

- How to assure the senior generation of financial security?
- Who can own stock in the business?
- What returns and rewards do shareholders get?
- Whether to pay dividends?



FAMILY CONSTITUTION ISSUES FOR DISCUSSION CONTINUED

- How to redeem stock to provide liquidity for shareholders?
- Does all stock have the same voting rights?
- How are members of the board of directors selected?

Family Relationships

- How to deal with conflicts between generations?
- How to deal with sibling or cousin conflict?
- How to teach young members and in-laws the business and also family traditions?
- How to share the family activities and customs with the next generation?
- How to develop and revise family agreements?
- How are family meetings and activities planned?
- How to create a process for family planning and decision-making?
- When to formalize the family governance by organizing a family council?

Responsibilities and Code of Conduct

- How to help family members with financial, personal, or career difficulties?
- What responsibilities does one family member have to others?
- What if there is a divorce?
- What if a family member breaks the law or acts in a seriously irresponsible manner?
- How much financial information to share? With whom?
- How to support family members' new business venture ideas?
- How to cope with the visibility and the public's expectations of successful families?
- What responsibility does the family have to the community?
- How to share credit for family achievements?

Source: R. Carlock & J. Ward, 2001. Strategy planning for the family business: parallel planning to unify the family and business, Palgrave, London.



FAMILY CONSTITUTION TEMPLATE

FAMILY CONSTITUTION

<p>Vision and values</p>	<ol style="list-style-type: none"> 1. What are our hopes for the family, for the business? 2. Where do we want to be? 3. Does the family want to continue to own the business and what role does it want? 4. What are the business/family values?
<p>Process</p>	<ol style="list-style-type: none"> 1. How will we make decisions? 2. How will we manage differences? 3. How will we treat each other?
<p>Structure</p>	<ol style="list-style-type: none"> 1. How will we organize ourselves? 2. What are the policies and procedures for the family and for its relationship with the business? (Lifestyle? media? remuneration? family jobs? family bank? Political interests?)
<p>Participation</p>	<ol style="list-style-type: none"> 1. How will we select and train people to be governors? 2. What are the "rules of entry" to work in the business? 3. How will we ensure ongoing participation and communication with expanding family?
<p>Education</p>	<ol style="list-style-type: none"> 1. How will we educate the next generation about ownership, the business and family governance? 2. Who will take part and when?

SAMPLE FAMILY CONSTITUTION

From: <https://www.credit-suisse.com/media/assets/apac/docs/cs-family-governance-white-paper.pdf>

Family Constitution (Template)

1 Introduction

1.1 Objective

This Family Constitution has been established to serve as a reference point for relationships between family members and the business during the next 10 to 15 years, a period in which we foresee the change from the second to the third generation taking place. We, the members of the **Smith Family**, recognize our common bonds and assume the responsibility for carrying on the legacy, through **ABC Manufacturing**, into the next generation.

1.2 Mission

It is necessary to bear in mind that the Family Constitution

- Clarifies what **ABC Manufacturing** and the **Smith Family** want to be and thus outlines the form and content of the main points of the relationships between the business and the family.
- Highlights ways of increasing unity and commitment, essential components of the family enterprise.
- Can never be contrary to what is stated in the laws governing the corporation or in the company bylaws.

1.3 Approval and Modification of the Family Constitution

The Family Board is the competent body for the approval and, when necessary, the modification of the present Constitution.

2 Guiding Principles of the Family Constitution

2.1 About the Founders

2.2 Values to Be Passed On

In the same way, we members of the **second** generation wish to pass on other values that form the basis of the work done during these years.

2.2.1 *Work ethic and a sense of accountability.* These are the best vehicles for the continuation of the entrepreneurial idea of the founders. Hard work reflected in products that are highest in relative quality is the reason for our success.

2.2.2 *Understanding, unity, harmony, and a bond among the shareholders.* These have played fundamental roles in the continuity of the company. They also continue to play a key role in the life of the extended **Smith Family**.

2.2.3 *Stewardship of the brand.* As stockholders, we must always keep in mind the consequences that our actions may have for the Company, the rest of the shareholders, and our family's reputation.

2.2.4 *Ethical conduct.* As evidenced by discretion, honesty, and humility, it works in favor of the common good.

2.2.5 *Dedication and commitment to the attainment of company objectives.*

- 2.2.6 *Confidence in the governing bodies of the company*, including respect for the people who today carry out the managerial, family and family wealth responsibilities and those who may do so in the future.
- 2.2.7 *Partnerships with customers and suppliers*. Continuously working on enhancing the value of the relationship for the **partners in the supply chain**.
- 2.2.8 *Love and concern for family and the family enterprise*. As a result of his/her ownership role, the family shareholder or board member should not enjoy any special treatment in his/her professional career within **ABC Manufacturing** by the mere fact that he/she is a member of the family. In this sense, family members who are active in management will have the same rights and responsibilities that the rest of the nonfamily employees have (salary, working days, promotions, vacations, etc.).
- 2.2.9 *Philanthropy*. Tithing and other community and cause-based gifting will continue to be carried out by the **Smith Family** through its family foundation, with oversight by the Family Board.

2.3 Other Values

The members of the first generation dedicate themselves to ensuring that the following values become gradually known and appreciated by the second generation.

- 2.3.1 *A balance between dedication to work and dedication to family*, in order that, over time, the healthy development of the next generation, unity and an appropriate commitment of service to the company may be maintained.
- 2.3.2 *Focused differentiation in niches and custom solutions*. Always seeking opportunities to compete Based on unique capabilities, customization and novel ways of doing business. These shield us from commoditization and price competition.
- 2.3.3 *A sense of history that informs family members of their legacy* and firmly positions the family and the business for a promising future.
- 2.3.4 *The hope to form part of an important business* that should continue to be able to compete advantageously. A family member's motivation should be found in the opportunity offered to him/her to be able to collaborate and contribute to the growth and continuity of the family business.
- 2.3.5 *Respect for all people: family, employees, customers, suppliers, competitors*.
- 2.3.6 *An understanding of the obligations and responsibilities of the shareholders* of a family business, among which stand out the need to seek out the best resources for the company and to collaborate positively for the good of the other shareholders.
- 2.3.7 *An understanding that participation as a shareholder of the family business is a privilege bequeathed by our ancestors*, and as part of our legacy, we must use the capital responsibly to increase it, insofar as it is possible, and to pass it on to the following generation.
- 2.3.8 *The hope to pass on to future generations a company whose brand and customer service capability stands out in its field*.
- 2.3.9 *A commitment to search for solutions for liquidity and peaceful separation* (in agreement with the established procedures) with shareholders who don't want to continue participating in the business as patient capitalists or who don't share the aforementioned values.
- 2.3.10 *A commitment to wealth and opportunity creation for family members and employees alike*.

3 The Type of Company We Want to Be

- 3.1 *A business in which the families*, as represented on the Family Board and the Board of Directors, *retain controlling ownership*.
- 3.2 *A company that is among the leaders in its field* and among the best in the industry.

- 3.3** *A business that is a leader in technology, forward-looking and technology driven. Always seeking process improvements and product innovations that will keep **OEMs considering ABC Manufacturing a preferred partner.***
- 3.4** *A business that continues to grow, providing a livelihood and opportunities for personal and professional growth.*
- 3.5** *A business that continues, from generation to generation, as a professionally managed family owned company with members of the family on the Board of Directors and/or on the Executive Team. Because of this,*
- Job positions cannot be indiscriminately offered to any family member.
 - Family members working in the business should do so in leadership positions. Such positions, in order to be executed successfully, demand a person with a vision of unity, the ability to lead people, and advanced technical and managerial skills.
 - Within the bounds of respect for personal freedom, the development of family members toward positions of company leadership is deemed a priority.
- 3.5** *A business with an organizational structure designed to offer both family and nonfamily managers exciting career opportunities and the ability to act with autonomy, supported by the latest in professional management.*

4 What Can ABC Manufacturing Expect from its Shareholders

- 4.1** *A long term investment horizon that gives the family business the patient capital it needs to deploy unique competitive strategies.*
- 4.2** *Support for the development of intellectual capital in the business.*
- 4.3** *Support for product development and new markets development.*
- 4.4** *Significant industry and operations experience from any owner who chooses to work in the business.*
- 4.5** *Commitment to family business continuity across generations.*
- 4.6** *Respect for the very different roles and responsibilities of owners, managers and family members that form part of this family business.*
- 4.7** *Ethical and responsible behavior that enhances the reputation of ABC Manufacturing Industries.*

5 What Can Shareholders Expect from Our Family Business

- 5.1** *Growth in the size of operations, notwithstanding existing competition and the evolution of markets.*
- 5.2** *Growth in the value of the estate, increased shareholder value, by aiming for higher profitability and growth than the average in the industry. This will be accomplished via the following strategic commitments from top management:*
- Gaining client loyalty by offering the best product and/or service value available.
 - Developing new products and services.
 - Entering promising new segments and markets and abandoning those that are less so.
 - Achieving the lowest costs by economies of scale, integration, and continuing vigilance against bureaucracy.
 - Reinvesting 30% or more of annual earnings in the business
 - Procuring and developing subsidiaries and joint ventures.

- Making acquisitions that ramp up the organic growth represented by the above approaches.
- 5.3 *Growth that is balanced*, without taking undue risks, engaging in speculation or threatening the low debt to equity ratio that is essential to continued independence.
 - 5.4 *Growth financed primarily out of internal cash flows*. Only in cases where the opportunity is unusually compelling, should the company rely on external debt.
 - 5.5 *A market-sensitive dividend policy* that respects the company's needs for continued reinvestment and acknowledges shareholder needs and preferences.
 - 5.6 *Extensive factual information provided to shareholders* about the status of the business and its markets. Through periodic shareholder meetings and Family Board meetings, shareholders will be briefed on financials, competitive conditions and the overall state of the business.
 - 5.7 *The continued use of best practices and the selection and retention of best practitioners, family or nonfamily*.
 - 5.8 *First among equals for a top management job whenever a family member is deemed apt and capable* by the President or Board of Directors for a top management position that he/she desires. A qualified family member will be preferred for the job over a similarly qualified nonfamily candidate.
 - 5.9 *Professional advice on ownership transfer and succession*, so that the behavior and actions of individuals and the predictable challenges facing families in business do not create problems for the whole.
 - 5.10 *To have **ABC Manufacturing** be a continued source of pride for the **Smith Family***.

6 Working in the Family Business: Family Employment Policy

It is important that family members be informed of the unique responsibilities and challenges of employment in **ABC Manufacturing**. They should be advised that in most cases they will be held to a higher standard of conduct and performance than other employees. We support an internship program to introduce future generations to the company.

6.1 General Conditions

- 6.1.1 Family members must meet the same criteria for hire/fire as nonfamily applicants.
- 6.1.2 Family members are subject to the same performance review as nonfamily members.
- 6.1.3 Compensation for family members will be at "fair market value" for the position held, the same as for nonfamily members.
- 6.1.4 Promotions and career opportunities for family members will be based on individual performance and company needs, the same as for nonfamily members.
- 6.1.5 Family members may be eligible for career-launching internships. This temporary employment will be limited to any one unit of employment for a predetermined time period. Family members may be encouraged to participate in internship programs with other companies with which **ABC Manufacturing** could reciprocate.
- 6.1.6 Family members will participate in summer employment opportunities when it represents a win-win for the family and the business.
- 6.1.7 No family member will be employed in a permanent internship or entry-level position; an entry-level position is defined as one requiring no previous experience or training outside **ABC Manufacturing**.
- 6.1.8 Family members seeking permanent employment must have at least three years' work experience outside **ABC Manufacturing**. During those three years with the employer, there must have been at least two positive reviews or promotions to rising levels of performance,

competence, responsibility, and trust. It is our view that if a family member is not a valued employee elsewhere first, it is likely that that family member will be neither happy nor productive at ABC Manufacturing.

6.1.9 Graduate degrees in management, engineering, and other disciplines related to the knowledge base that is essential to the success of **ABC Manufacturing** are encouraged. A family career-development committee will be developed for the next generation's entry. It will be responsible for interviewing, coaching, and guiding interested family members to the HR Department and other appropriate company representatives, where the ultimate employment decisions will be made. This committee will comprise family top management team members and two independents.

6.1.10 No spouses will be considered for permanent employment at **ABC Manufacturing**.

7 Ownership of the Family Business

7.1 Ownership of the Shares

Direct descendants of **Gary W. Smith** should retain controlling ownership of the shares.

7.2 Recommendations for the Owners

While enjoying the most profound respect for their freedom and individual needs and aspirations, the owners should:

- Always consider the repercussions that decisions about passing on shares through estate planning will have on the business and the rest of the owners. In this sense, the desirable course of action would be always to look for ways that would most clearly facilitate the unity of the family business and the commitment of the shareholders to its continuity.
- In the most prudent fashion, make it possible for capable members of the third generation to attend, as informed and responsible shareholders, the Annual Shareholders' Meeting.

7.3 Shareholder Liquidity

In order to facilitate liquidity for the shareholders, the company will do everything in its power to pay dividends and also endow a Liquidity Fund. The object of the Fund will be to provide a buyer (namely, the family business) for the shares. The Liquidity Fund will complement the existing buy-sell agreement between shareholders. The intent is to guarantee liquidity in small quantities, following the spirit of the statutes and the Family Constitution. (The specifics of the Liquidity Fund and its tax implications need to be developed.)

Liquidity bylaw's key points:

- *The maximum amount* offered for purchase yearly will be up to 1% of the total shares of the company, depending on the funds available.
- *The value of the family business* will be calculated annually, in agreement with a formula proposed by valuation experts and approved by the Board of Directors. In the aforementioned formula, the different values of the totality of the shares, whether majority or minority, must be kept in mind. The values determined by the valuation process will be made known to the shareholders.
- *Purchase-sale:* In the situation in which a shareholder would want to sell and other shareholders would want to buy at a value higher than that offered by the Fund, or in the case that the Fund

may not be able to buy, the Board of Directors will authorize the purchase-sale in accordance with the rules set forth in the Shareholder Buy–Sell Agreement.

8 Governing Bodies

In a family business that has the intent to strengthen the participation of the shareholders in the knowledge of the business, there are two types of governing bodies:

- Those responsible for the management of the company—that is to say, those established in the bylaws, the Annual Shareholders’ Meeting and the Board of Directors. Others may be established by the Board of Directors and the Management Team, as necessary.
- The Family Board, responsible for shareholder education, communication, and developing and implementing the Family Constitution.

8.1 Annual Shareholders’ Meeting

During the regular Annual Shareholders’ Meeting, extensive information will be offered with the purpose of enabling the shareholders to be very familiar with the family business. Family members agree to refrain from using this information indiscriminately, given its confidential nature. One of the two Family Board meetings for the year will immediately follow this Annual Shareholders’ Meeting.

8.2 The Board of Directors

The Board of Directors is the highest governing body of the company after the Annual Shareholders’ Meeting. The Top Management Team is supervised and held accountable by the Board of Directors.

The functions of the Board, detailed in the corresponding bylaw, include:

- Reviewing and approving the business’s strategy.
- Reviewing the financial performance of the company and holding top management accountable for such performance.
- Ensuring the ethical conduct of management and the corporation.
- Promoting the development of the managerial resources of the company.

8.3 Rules and Regulations for Board of Directors’ Operations

- The election of board members is regulated by state laws and company statutes.
- There will always be a minimum of three high-influence independent outsiders serving on the Board of Directors.
- There will be two at-large representatives of the Gary W. Smith family serving on the Board of Directors.
- Meetings should take place on a quarterly basis and be scheduled at least one year in advance.

8.4 Family Board

The main purpose of the Family Board is to foster a strong understanding of the business, the family, and the relationship between business and family among the family members/shareholders. Its responsibilities include:

- Informing and educating the family about the business.
- Facilitating the relationships of the family with the business.
- Educating the family about the legacy, disseminating the contents of the Family Constitution and keeping it a living document.
- Proposing to all family members those changes in the Family Constitution that, based on their judgment, can help foster a greater understanding among the family members/stockholders and better relationships between owners and managers of the company.

All family members over the age of 16 will be considered members of the Family Board until they are retired and have tendered their stock. As the family grows beyond 12 members, the Family Board will be made up of two members of each of the branches in that generation. Representative members are selected by the branches. One family member serving on the Board of Directors will also serve on the Family Board and represent a point of linkage between these two governing bodies. Total membership of the Family Board will therefore be limited to 12. Family Board meetings will sometimes be facilitated by an outside expert on family business.

8.5 Family Board's Problem-Solving and Conflict Resolution Committee

The primary mission of the Problem-Solving and Conflict Resolution Committee is on behalf of the Family Board, to prevent and ultimately resolve any conflict that may threaten the owning family's unity and commitment to the family's business. Its members will be selected by Family Board members and include family members and a minimum of two independent outsiders, at least one of which should be well versed in mediation and conflict resolution approaches. As a duly constituted committee it will be ready to meet only on an as needed basis after formulating its procedures and mode of operation. This Committee will also be responsible for proposing principles and approaches for the prevention of similar situations in the future.

8.6 Family Assembly

The Family Assembly, made up of all the blood members and their spouses, will meet once a year with the purpose of:

- Promoting greater knowledge and understanding of each other.
- Promoting greater knowledge and understanding of the business.
- Promoting greater knowledge and understanding of the estate and family trusts.
- Having fun and promoting extended family bonds.