Parliamentary Joint Committee on Corporations and Financial Services

Family Businesses in Australia – different and significant: why they shouldn't be overlooked

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Duties of the Committee

Section 243 of the *Australian Securities and Investments Commission Act 2001* sets out the Parliamentary Committee's duties as follows:

(a) to inquire into, and report to both Houses on:

(i) activities of ASIC or the Panel, or matters connected with such activities, to which, in the Parliamentary Committee's opinion, the Parliament's attention should be directed; or

(ii) the operation of the corporations legislation (other than the excluded provisions), or of any other law of the Commonwealth, of a State or Territory or of a foreign country that appears to the Parliamentary Committee to affect significantly the operation of the corporations legislation (other than the excluded provisions); and

(b) to examine each annual report that is prepared by a body established by this Act and of which a copy has been laid before a House, and to report to both Houses on matters that appear in, or arise out of, that annual report and to which, in the Parliamentary Committee's opinion, the Parliament's attention should be directed; and

(c) to inquire into any question in connection with its duties that is referred to it by a House, and to report to that House on that question.

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Abbreviations

AAA	Agriculture Advancing Australia
ABARES	Australian Bureau of Agriculture Resource Economics and Sciences
ABS	Australian Bureau of Statistics
ADI	Authorised Deposit-taking Institution
ATO	Australian Taxation Office
BCS	Business Characteristics Survey
BLS	Business Longitudinal Survey
BLD	Business Longitudinal Database
CAFBA	Commercial Asset Finance Brokers Association
CALD	Culturally and Linguistically Diverse
CCIQ	Chamber of Commerce and Industry Queensland
CGT	Capital Gains Tax
COAG	Council of Australian Governments
Corporations Act	*Corporations Act 2001*
COSBOA	Council of Small Business of Australia
DRALGAS	Department of Regional Australia, Local Government, Arts and Sport
DIISRTE	Department of Industry, Innovation, Science, Research and Tertiary Education
DRET	Department of Resources, Energy and Tourism
EC	European Commission
EM	Explanatory Memorandum
ESS	Employee Share Scheme

EVAO	Estimated Value of Agricultural Operations
FBA	Family Business Australia
GDP	Gross Domestic Product
GFC	Global Financial Crisis
HBR	Harvard Business Review
IDC	Inter-Departmental Committee
IFERA	International Family Enterprise Research Academy
ITAA	*Income Tax Assessment Act 1997*
MGI	MGI Australasia
NFF	National Farmers' Federation
OCR	Optical Character Recognition
OECD	Organisation for Economic Co-operation and Development
PwC	PricewaterhouseCoopers
R&D	Research and Development
RBA	Reserve Bank of Australia
RDA	Regional Development Australia
RMIT	Royal Melbourne Institute of Technology
SMEs	small and medium-sized enterprises

Executive summary

On some estimates, family businesses account for 70 per cent of all Australian businesses. Although family owned and operated commercial enterprises are an established and enduring feature of the Australian economy, they have been overlooked by Australian governments. In part, the reason may be that they are seen principally as a subset of small and medium-sized enterprises (SMEs). Few government departments seemed to have awareness of the existence of large family businesses. It was apparent that government agencies have not focused on the characteristics of family businesses, the economic contribution these businesses make or the unique challenges they face.

Over the past seven months, the Parliamentary Joint Committee on Corporations and Financial Services has gathered and analysed evidence on a range of issues relating to family businesses. It makes 21 recommendations. The committee recognises that awareness and understanding of family businesses in Australia is nascent. However, it hopes that this report will begin a conversation within government that might give serious consideration to the questions: What is a family business? What contribution do these family businesses make to the economy and the community? How should family businesses be supported? What particular contribution do family businesses offer that other businesses do not? How can good public policy enable and enhance the success of the family business sector?

A lack of a definition and official data

There is no official definition of family business in Australia. Chapter 2 of this report identifies several possible definitions, noting the strengths and weaknesses of each. It also considers the key threshold questions that would need to be considered in devising an official definition: should sole traders be included; should extended family be part of a definition; should the owners have at least the intent to pass on the business; should there be a threshold based on the number of employees or annual turnover, as there is to identify small businesses?

Without an adequate definition of family business, there is no adequate data. The data that is available is from surveys by consultancy firms such as KPMG and MGI Australasia. The surveys are interesting and certainly provide talking points, but their accuracy and reliability are questionable. The data are compiled from small sample groups and, even among surveys conducted by the same consultancy firm, the methodology and the definition of 'family business' has changed over time.

The committee heard from family businesses in retail, tourism, agriculture, and hospitality, with turnover ranging from the hundreds of thousands to the billions of dollars.

The contribution and mindset of family businesses

Australian family businesses are diverse: they come in all sizes, operate in many sectors and have a range of operating structures (public companies, private companies, partnerships and trusts). Despite this diversity, family businesses have common features and traits that distinguish them from non-family enterprises. Chapter 4 of this report examines submitters' and witnesses' views that family businesses differ from non-family business in terms of their:

- risk averse, long-term approach;
- flexible decision-making;
- greater commitment to retaining staff;
- significant contribution to the community in which they operate; and
- higher labour productivity than non-family firms.

There is no reliable data that could test the strength of these attributes in family businesses and compare them to those in non-family businesses. However, the committee believes that these characteristics deserve the attention of policy makers. These traits could be measured based on the value of family businesses' balance sheet assets, their debt to equity ratios, the tenure of family business Chief Executive Officers, the average number of years of employee service in family businesses and the business' philanthropic contributions as reported to the Australian Taxation Office (recommendation 10).

There is Australian research that has found that the contribution of labour to the output of family firms was much greater than the relative contribution of labour to comparable non-family firms. The contribution of labour to output in family firms was also significantly greater than that of capital to output in these firms (chapter 4).

The possible influence that family businesses' size and governance structures have on their productivity and performance is an area of particular interest to the committee. It is a matter of obvious public policy interest if family businesses' governance structures and decision-making patterns can be shown to contribute to higher growth and productivity than non-family firms. The key would be to establish this case using official data.

The challenges unique to family businesses

Family businesses face particular challenges, key among which are the challenges of managing succession and internal conflict. For family businesses, business longevity is influenced not merely by productivity and economic factors. Family businesses must also manage family tension and conflict regarding the goals and direction of the business. These ructions can change governance practices and the willingness and capacity of family members to relinquish or assume control of a commercial enterprise.

Succession

The key issue of succession is discussed in chapter 5 of this report. The argument put by several submitters and witnesses is that a smooth transfer of family businesses is necessary to maintain a prosperous and growing economy. Successfully transitioning a family business, it is argued, maintains more jobs on average than a start-up firm.

Many argue that the challenge of passing the business on to the next generation is what distinguishes family businesses from non-family businesses. For first generation business owners, a critical stage in the process of managing succession is to recognise:

(a) that there is a viable entity to be passed on; and

(b) that the next generation is prepared to take on the role.

While there is some data that Australian family businesses have not adequately planned for succession—despite the impending retirement of their owners—the reasons for this are not clear. It is not apparent to the committee, for example, that there is inadequate information or advice on succession planning. Indeed, the committee is aware that the government's Enterprise Connect advisers and private consultants have considerable expertise in succession planning. There may be a lack of awareness on the part of some family businesses that these services are available. However, in many cases, it may simply be that the business has not yet reached a stage where the owners feel comfortable to put a plan in place.

The committee believes there could usefully be a public policy debate relating to the economic benefits of succession planning (recommendations 2(c) and 7). Government agencies may form a view that there is no broad-based economic benefit to ensuring that a family business is passed on, and that there is therefore no public policy need to encourage succession. The committee recognises that the family owners may themselves find an offer from the market to be more attractive than passing the business on to a reluctant successor. Nonetheless, the committee believes that debating these issues—both publicly and within government—is worthwhile. For sectors that are heavily based on family ownership, such as farming, tourism, trades, construction and transport, this debate will have particular currency.

The public policy debate on succession planning might also consider the ramifications of the impending retirement of the baby boomer generation on family businesses in Australia. On one estimate, 61 per cent of family business owners plan to retire between 2006 and 2016 (see chapters 3 and 5). However, the exact number of retirements and the effect it may have on the family business landscape, and the Australian economy, is unclear. Without reliable longitudinal data, the economic consequences of the baby boomers' retirement are largely unknown. The committee believes that this is an area in which government should consider collecting official data (recommendation 11).

The 50 non-employee shareholder rule

For families trading as companies, the incorporation of the family unit within the business model also presents a key challenge that is unique to the sector. Section 113 of the *Corporations Act 2001* states that a proprietary company must have no more than 50 non-employee shareholders. It must otherwise form as an unlisted public company, and comply with the disclosure obligations of public companies.

Family business representatives argued that family companies with successive generations of shareholders can exceed 50 shareholders, which unfairly forces them to relinquish family control and triggers reporting obligations. In a 2008 inquiry conducted by this committee, the FBA suggested increasing the section 113 threshold to 300 shareholders. The committee proposed an increase to 100 non-employee shareholders. However, the government made no change to section 113. Then, as now, it argued that companies with more than 50 non-employee shareholders have a sufficiently diverse ownership base to justify greater governance requirements.

The committee remains unconvinced. For successful, multi-generational family businesses, the restriction in section 113 on the number of non-employee shareholders in a proprietary company may mean that large family businesses incur additional costs. This appears to be at odds with the broader policy objective of facilitating and supporting long-term business growth.

However, it does not seem that a clear and precise case for increasing the section 113 threshold has yet been put to Treasury. Family business representatives and large family businesses themselves need to put specific cases directly to government to show that the current threshold:

- limits the expansion of family businesses beyond 50 non-employee shareholders;
- has had an adverse effect on family businesses that have passed the threshold and incorporated (see recommendation 13); or
- forces family businesses into structures that members might not otherwise choose.

In addition, the committee recommends that the Australian Bureau of Statistics (ABS) collect data on the effect of section 113 of the Corporations Act on Australian businesses, including family businesses (recommendation 17).

Family trusts

Family trusts are an established feature of the family business sector. Family businesses, and their representatives, disputed the view that family trusts are designed to minimise taxation. Family businesses can choose to adopt a trust structure for reasons that include asset protection, assisting the business to manage succession and related estate planning issues, and providing a mechanism to retain control of the business within the family unit. Within the family business sector, trusts are viewed as a legitimate means of conducting a commercial enterprise.

For family businesses trading through a discretionary trust structure, the committee heard that the existing legislative frameworks across the Commonwealth, States and Territories present various challenges. In particular, family businesses reported that the requirements in Division 6 and Division 7A of the *Income Tax Assessment Act 1936* do not appropriately recognise the operational structures of family businesses which can include multiple private commercial enterprises.

Australia's taxation requirements should achieve an appropriate balance between supporting businesses and maintaining the integrity of Australia's taxation system. There is some evidence that at present Division 6 and Division 7A may not be achieving this balance. The committee recommends that the Board of Taxation consider the evidence presented by the family business sector on the effect of Division 7A on business performance (recommendation 12). There is evidence to support the view that the current operation of the rules in Division 6 is unclear, uncertain and, accordingly, create unnecessary complexity for Australian businesses. Division 6 is currently under review. Given that the Division 6 requirements affect family businesses, the sector should be recognised, and included, in the review process (recommendation 14).

Trusts—the 80 year rule

Another legislative area of concern is the rule against perpetuities: the so-called 80 year rule. A creature of common law and State and Territory legislation, the rule limits the lifespan of the family trading trust and, by extension, family businesses operating through a trading trust structure.

While the precise number of family trading trusts that will be affected by the 80 year rule in the coming decades is presently unclear, it is clear that the rule is an example of Australia's legal system not keeping pace with developments in the business sector. The committee draws attention to concerns that the rule could stop family businesses founded on a trust structure from operating. It is essential that State and Territory governments consider whether the rule continues to be appropriate for Australia's modern economy.

The committee recommends that the Council of Australian Governments (COAG), or its relevant Ministerial Council, inquire into whether the rule against perpetuities can be abolished in each jurisdiction, or whether its scope can be limited to appropriately exclude commercial arrangements. South Australia abolished the rule in 1996. The experience of trading trusts established in South Australia since then will provide a basis for determining the likely effect of abolishing the rule. If COAG determines that it is not appropriate to abolish or amend the rule, it should actively engage with the business sector to alert trading trusts to the financial implications of the vesting requirements (recommendation 15).

Access to finance

The mindset and priorities of family businesses can influence the financial resources accessed by family enterprises. There are certainly challenges common to both family and non-family businesses, such as the lack of competition in the authorised deposit-taking institutions (ADI) market and the interest rates for business finance. However, in terms of accessing finance, family businesses appear to face particular difficulties. The conservative, family-oriented mindset of family businesses can deter them from accessing otherwise viable forms of finance, such as private equity.

An analysis of the sector's access to finance also indicates the need for greater recognition for family businesses as distinct from non-family enterprises. ADIs do not consider family businesses separately from non-family enterprises when determining the risk attached to a family business' finance application. It would seem that ADIs are failing to understand and engage with the family business sector. The committee encourages ADIs to analyse the characteristics of family businesses, as distinct from broader categories of micro, small, medium, or large businesses.

Given the prevalence of family businesses in Australia's business landscape, the Reserve Bank of Australia's (RBA) apparently limited engagement with the family business sector should also be addressed. The committee recommends that the RBA include family business representatives on its annual small business panel in each state and territory (recommendation 21).

Family businesses and the Global Financial Crisis

The contributions of, and the challenges unique to, the family business sector are of relevance to the broader business community. In part, this inquiry responded to anecdotal evidence that the family business sector proved particularly resilient in response to the Global Financial Crisis (GFC). The committee cannot conclude that the family business sector in Australia outperformed non-family businesses in response to the GFC. The anecdotal evidence and the data are inconclusive.

However, there is certainly international evidence that family businesses weathered the GFC better than non-family businesses. There is also evidence to support the conclusion that family businesses' 'patient capital' approach provides a safeguard in times of economic downturn. The sector's contribution to the Australian economy includes the promotion of the benefits of a risk adverse, long-term approach to investment and business profitability. While its effects cannot be measured on available data, the committee considers that it is an approach that the broader economy would be well-advised to consider.

Beginning the conversation within government

The main purpose of this report is to further the conversation within government about family business issues that this inquiry has started. At this early stage, it would be counterproductive for the committee to present a conclusive definition of family business to be used by policymakers in Australia. Rather, the committee recommends that an Inter-Departmental Committee (IDC) be established to consider:

(a) the issues that are particularly or uniquely relevant to family business and how these issues interconnect with distinct policy areas; and

(b) how a definition can capture these issues (recommendations 1 and 2).

To this end, the key issues that the IDC should consider are:

- identifying the number of family businesses, their location and the industries in which they operate (recommendation 2(e));
  - the need for policy makers to identify the number of family businesses that are small businesses, and if so, whether the definition of small business should be based on the threshold used for tax purposes (annual turnover of less than $2 million) or the ABS's threshold of fewer than 20 employees (recommendation 2(a));
  - the need for policy makers to identify first, second, third and later generation family businesses (recommendation 2(d));
  - the need for policy makers to identify the number of family businesses established from culturally and linguistically diverse communities (recommendation 2(f)); and
- the need for data on family businesses' contribution to Gross Domestic Product, employment and export earnings (recommendation 8);
- the importance of succession as a policy objective, and whether a definition should identify whether the owners could pass the business on, whether they intend to pass it on, whether they have a formal plan to do so (recommendation 2(c));
- the need to gather data on family businesses, should could include questions on the value of assets and balance sheets, debt-to-equity ratios, the tenure of Chief Executive Officers, the average number of years of employee service, and the sector's philanthropic contributions (recommendation 10);
- the effect of section 113 of the *Corporations Act 2001* and the need to identify the number of non-employee shareholders in family businesses (recommendation 2(g));
- the effect of Division 6 and Division 7A of the *Income Tax Assessment Act 1936* on family businesses that operate through a trust structure; and
- the effect of Division 83A of the *Income Tax Assessment Act 1997* and section 113 of the Corporations Act on family businesses trading as companies.

The committee holds that both policy makers and stakeholders have an important role to play in the creation of an official survey of family business (see recommendation 3). The joint development of a survey would then provide for the development of stronger links and understanding between government and the family business sector. With official data gathered, the dimensions and the nature of the sector will become clearer. There will then be the need for discussion between government, family businesses, consultancies and academics about what the findings mean and how, if at all, they should be acted on.

It is clear as a result of this inquiry that family businesses have been a largely unrecognised part of Australia's economy. This report records the first step towards understanding these businesses as distinct and unique contributors to the Australian economy and community. The principal purpose of this report is to begin a discussion within government about the policy need to identify a family business, which may then lead to an official definition and official data collection. The committee also argues, however, that there is an onus on the family business sector to harness the momentum generated by this inquiry to increase its engagement with government.

List of recommendations

Recommendation 1

2.92 The committee recommends that an Inter-Departmental Committee (IDC) be established to identify the policy issues facing family businesses that are not adequately captured within the existing policy framework and with existing Australian Bureau of Statistics (ABS) data collection. The IDC should include: the Department of Industry, Innovation, Science, Research and Tertiary Education; the Treasury; the Australian Taxation Office; the Australian Bureau of Agricultural Resource Economics and Sciences; the Department of Resources, Energy and Tourism, the Department of Regional Australia, Local Government, Arts and Sport; and the Department of Employment, Education and Workplace Relations. The ABS should also participate in the IDC.

Recommendation 2

2.94 The committee recommends that the initial focus of the Inter-Departmental Committee (IDC) must be on the specific public policy need for these agencies to identify a family business as distinct from a non-family business. In terms of the policy rationale for a survey (and a definition of family business), the committee recommends that the IDC carefully consider the following issues:

(a) the need for policy makers to identify the number of family businesses that are small businesses, and if so, whether the definition of small business should be based on the threshold used for tax purposes (annual turnover of less than $2 million) or the ABS's threshold of fewer than 20 employees;

(b) the extent to which a definition of family business needs to capture employment data, and the possible effect that different thresholds in the definition will have on the number employed;

(c) the importance of succession as a policy objective and the need for a definition to identify whether the owners could pass the business on, whether they intend to pass it on, whether they have a formal plan to do so;

(d) the need for policy makers to identify first, second, third and later generation family businesses;

(e) the need for policy makers to identify the industry and location of the family business;

(f) the need for policy makers to identify the number of family businesses from culturally and linguistically diverse communities;

(g) the need for policy makers to identify the number of non-employee shareholders in a family business and, therefore, the need for data on the number of family businesses that are proprietary companies as opposed to unlisted public companies; and

(h) the need for policy makers to collect data on the superannuation arrangements of family businesses, particularly the evidence that female family members do not have adequate superannuation arrangements in place.

Recommendation 3

2.96 The agencies represented on the Inter-Departmental Committee should periodically consult with key stakeholder groups to seek their input and feedback on the issues it is discussing. These groups should include Family Business Australia, the Australian Chamber of Commerce and Industry, the Council of Small Business of Australia and the National Farmers' Federation, and consider engaging other peak bodies that may be nominated to represent family businesses of differing sizes.

Recommendation 4

2.97 The committee recommends that the Inter-Departmental Committee report its findings to the Minister for Industry and Innovation within six months of it being established.

Recommendation 5

2.106 The committee recommends that when collecting official data based on a formal definition of family business, the Australian Bureau of Statistics should incorporate a set of clear and targeted questions into the Business Characteristics Survey. The intent must be to deliver the survey as efficiently as possible, including to limit the time taken by respondents to complete the survey.

Recommendation 6

3.11 The committee recommends that the Australian Bureau of Statistics inquire into whether the Business Longitudinal Database can be sufficiently de-identified so as to be made available for research purposes on request.

Recommendation 7

3.39 The committee recommends that as part of its deliberations, the Inter-Departmental Committee (see recommendation 1) should examine the findings on the wealth transfer survey conducted in 2012 by the accounting firm BDO Australia.

Recommendation 8

4.4 The committee recommends that in its deliberations on the specific public policy need to identify a family business, the Inter-Departmental Committee should consider the need for data on the economic contribution of family businesses. This should include the need for data on the contribution of family businesses to Gross Domestic Product, export earnings and employment, both in aggregate and by sector.

Recommendation 9

4.64 The committee recommends that the Inter-Departmental Committee consider the policy need for data on issues including the profits and growth of family businesses of different sizes, and the labour and capital productivity of these businesses.

Recommendation 10

4.68 The committee recommends that the proposed Inter-Departmental Committee assess whether data should be gathered to measure the key characteristics and behaviours of family businesses. In particular, consideration should be given to:

- the value of assets on balance sheets;
- debt to equity ratios;
- the tenure of Chief Executive Officers;
- the average number of years of employee service to the business; and
- philanthropic contributions, as reported to the Australian Taxation Office.

Recommendation 11

5.80 The committee recommends that the proposed Inter-Departmental Committee consider the need to quantify the extent to which family businesses will be transferred or closed in the coming decade as a result of the retirement of the baby boomer generation, and the policy implications for the economy.

Recommendation 12

6.54 The committee recommends that as part of its current inquiry into Division 7A of the *Income Tax Assessment Act 1936*, the Board of Taxation closely review the evidence gathered through this inquiry about the effect of Division 7A on Australia's family business sector. In considering the evidence, the Board of Taxation should consider what measures can be taken to support Australian family businesses, and by extension the Australian economy, while giving due regard to appropriate taxation obligations.

Recommendation 13

6.55 The committee recommends that the government publicly release the Board of Taxation's report into the operation of Division 7A of the *Income Tax Assessment Act 1936*.

Recommendation 14

6.66 The committee recommends that as part of the current analysis of options to reform the Division 6, Part III of the *Income Tax Assessment Act 1936* the Department of the Treasury review the evidence gathered through the committee's inquiry into family businesses in Australia and consult with representatives of the family business sector.

Recommendation 15

6.128 The committee recommends that the Council of Australian Governments, or its relevant Ministerial Council, inquire into whether the rule against perpetuities can be abolished in each jurisdiction, or whether its scope can be limited to appropriately exclude commercial arrangements. In undertaking this review, the Council should consider how many trading trusts are likely to be affected in the next two decades. It should also consider the effect that abolishing the rule against perpetuities in South Australia has had on trading trusts operating in the State.

6.129 If the Council determines that it is not appropriate to abolish or amend the rule, the committee recommends that it should actively engage with the business sector to alert trading trusts to the financial implications of the vesting requirements.

Recommendation 16

7.23 The committee recommends that the Department of the Treasury consult with representatives of the family business sector about the effect of section 113 of the *Corporations Act 2001* on large, multigenerational family businesses.

Recommendation 17

7.25 The committee recommends that the Australian Bureau of Statistics collect data on the effect of section 113 of the *Corporations Act 2001* on Australian businesses.

Recommendation 18

7.59 The committee recommends that the Department of the Treasury review the evidence gathered through the committee's inquiry into the family business sector in Australia and consider consulting the stakeholders identified through this inquiry about the sector's concerns about the effect of Division 83A of the *Income Tax Assessment Act 1997* on their capacity to engage suitably qualified executives. Treasury should advise government about whether appropriate support can be provided, whether through amendments to Division 83A or other mechanisms, to address the challenges faced.

Recommendation 19

7.72 The committee recommends that the Australian Securities and Investments Commission consult with family businesses to gauge their understanding of the *Corporations Act 2001*, in particular directors' duties and liabilities, and work with Family Business Australia and other interested organisations that represent family businesses to disseminate information through education and training. Information could also be usefully provided in plain terms on the MoneySmart website.

Recommendation 20

8.60 The committee recommends that the Australian Securities and Investments Commission review information available on the MoneySmart website about private equity investments, and design information that would assist family and non-family businesses to determine whether it is appropriate for their business to seek private equity finance.

Recommendation 21

8.64 The committee recommends that the Reserve Bank of Australia include representatives of the family business sector on its annual small business panels as an interim measure.

Chapter 1

Introduction

> *Over half the country is employed in these businesses and something like 70 per cent of this country's businesses are in private family business hands. It is extraordinary when you think about the footprint they hold. It is pretty well hidden under a bush in many respects.*[1]

> *...my point is not only are they different but they are also significant. Different and significant are necessary but not necessary in sufficient conditions to actually make them the focus of attention. They have been overlooked. They are different; they are significant and they are overlooked.*[2]

1.1 As a field of policy focus, public debate and academic inquiry in Australia, 'family business' has been relatively neglected. There are several inter-related reasons for this. There is no official definition of 'family business' and no official data collected. There is no specific public policy focus on family business: the focus is often on small and medium-sized enterprises (SMEs). And academic research in the field is nascent, with limited data available and very few Australian universities with a course on family business.

1.2 Reflecting these factors, the public debate on family business in Australia often seems limited to the stereotypes of the family corner store at one end of the spectrum, and the trucking dynasty or the media empire at the other. The media seem often to refer to businesses that are family owned and operated without using the phrase 'family business' or acknowledging that the structure and operation of the business is because of family ownership. Indeed, it seems that many businesses that are owned and operated by family members do not themselves identify as a 'family business'. Rather, they identify as a small business, a corporation, or with reference to the sector in which they operate.

1.3 This inquiry is focussed on family businesses in Australia. It is interested in how 'family business' might be defined, the contribution these businesses make to the Australian economy and their structures, mindset, resilience and sources of funding. The inquiry aims to stimulate public debate on family business in Australia. In

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1 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, Sydney, 15 November 2012, p. 25.

2 Professor Ken Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 18.

particular, it considers the case for developing a formal definition that yields regular and reliable data which is useful to policy-makers, the business community, academia and the public at large.

The referral

1.4 On 16 August 2012, the Parliamentary Joint Committee on Corporations and Financial Services ('the committee') initiated an inquiry into family business in Australia. The terms of reference for the inquiry direct the committee to examine the following matters:

(a) the definition of 'family business';

(b) the availability and reliability of information and statistics about family business in Australia;

(c) the contribution of family business to the Australian economy, in terms of financial, social, employment, innovation and sustainability outcomes;

(d) structural, cultural, organisational, technological, geographical and governance challenges facing family business;

(e) the role of family trusts in facilitating family business;

(f) access to and the cost of finance and insurance for family business; and

(g) family business responses to the challenges of the Global Financial Crisis (GFC) and post GFC resilience.

1.5 The committee set 27 February 2013 as the reporting date. The reporting date was extended to 20 March 2013 to enable tabling in both Houses on a sitting day.

Submissions to the inquiry

1.6 The committee called for written submissions by 31 October 2012. On 1 November 2012, the committee granted an extension of time for submissions until 30 November 2012.

1.7 The committee sent written invitations to make a submission to 102 individuals and organisations. This group included various lobby groups, consultancies, government departments, academics, major banks and other financial institutions. In addition, the committee sent invitations to 48 Chief Executives of Regional Development Australia.[3]

3 Regional Development Australia is a partnership between the Australian, State, Territory and Local Governments to strengthen regional communities. RDA consists of a national network of 55 committees, which are made up of local leaders who work with all levels of government, business and community groups to support the development of their regions.

1.8 The inquiry was advertised in *The Australian* newspaper on 29 August 2012, 26 September 2012, 24 October 2012 and 7 November 2012, as well as on the committee's website. The committee also requested those member organisations that were sent submission invitations publicise the inquiry among their members.

1.9 The committee received 38 submissions. Of these, 37 are publicly listed on the committee's website; one submission is confidential and another is published with the name withheld.[4]

1.10 The committee received ten submissions from consultancy, advisory and legal firms;[5] eight were from peak industry associations and institutes;[6] six submissions from government agencies and statutory authorities;[7] five from members of Family Business Australia (FBA) and the FBA itself;[8] four submissions from academics;[9] and one submission from a major bank.[10] There was only one submission from a family business that was not a member of the FBA. That submission begins: 'Hardly anyone in small business knows about this inquiry and you have missed an opportunity to hear from us all'.[11]

1.11 In some respects, the committee is disappointed with the relatively low number of submissions received during this inquiry. Considering the claims of some stakeholders about the size of the family business sector and its importance to the Australian economy, one may have expected a greater response particularly from

4 Submissions 10 and 12

5 Mr Bill Winter, *Submission 7*; MGI Australasia Ltd, *Submission 9*; PricewaterhouseCoopers, *Submission 11*; Pamela Low and Associates, *Submission 13*; Deloitte Private, *Submission 16*; Grant Thornton Australia, *Submission 18*; KPMG, *Submission 21*; Pitcher Partners Consulting Pty Ltd, *Submission 28*; Empower Business Solutions, *Submission 30*; FINH, *Submission 34*.

6 Commercial Asset Finance Brokers Association, *Submission 6*; Chamber of Commerce and Industry Queensland, *Submission 19*; Bus Association Victoria, *Submission 20*; Council of Small Business of Australia, *Submission 22*; Business SA, *Submission 23*; Institute of Chartered Accountants Australia, *Submission 25*; National Farmers Federation, *Submission 29*; Institute of Certified Bookkeepers, *Submission 36*; Agribusiness Council of Australia, *Submission 37*.

7 Australian Bureau of Statistics, *Submission 2*; Reserve Bank of Australia, *Submission 17*; Treasury, *Submission 26*; Regional Development Australia Hunter and Hunter Business Chamber, *Submission 27*; Department of Resources, Energy and Tourism, *Submission 31*; Regional Development Australia Pilbara, *Submission 33*.

8 Family Business Australia, *Submission 1*; Packer Leather Pty Ltd, *Submission 4*; Kennard Hire Pty Ltd, *Submission 5*; Kennards Self Storage, *Submission 15*; Taylor Bros, *Submission 38*.

9 Bond University, *Submission 3*; Moores Family Enterprise, *Submission 8*; Professor Mary Barrett, Dr Chris Graves and Dr Jill Thomas, *Submission 14*; Associate Professor Pi–Shen Seet, *Submission 35*.

10 Commonwealth Bank of Australia, *Submission 24*.

11 Laserforce International, *Submission 32*.

Australia's larger and better resourced family businesses. As Mr David Smorgon, himself from one of Australia's most successful family businesses, told the committee:

> …it is quite ironic, and frankly disappointing, that so many large family businesses are not here today—they are conspicuous by their absence in not giving submissions to this parliamentary enquiry. You have to ask yourself why. I don't know the reasons; I haven't asked them—perhaps it highlights the very private nature of family businesses: they do their own thing behind closed doors and are not focused on others…So it is not just the politicians; it is also the responsibility, particularly of those larger family businesses, to play their role.[12]

1.12 However, the committee does acknowledge that many family businesses are SMEs with limited time, finite resources and experience of the parliamentary process. These factors undoubtedly contributed to the lack of engagement from SMEs in this inquiry.

Public hearings

1.13 The committee held six public hearings: in Canberra on 13 November; in Melbourne on 14 November; in Sydney on 15 November; in Brisbane on 16 November 2012; in Devonport on 21 January 2013; and a further hearing in Canberra on 7 February 2013. At the Melbourne, Sydney, Brisbane and (subsequent) Canberra public hearings, the committee held a roundtable with several family businesses having the opportunity to discuss issues of importance and concern relating to the terms of reference. The second Canberra hearing was an opportunity for the committee to take further evidence from Treasury and Australian Taxation Office officials, as well as several witnesses from Perth via videoconference.

Acknowledgements

1.14 The committee thanks those who made written submissions to the inquiry and who appeared to give evidence at the public hearings. It appreciates the FBA's assistance in organising the public hearings and raising awareness of the inquiry. The committee particularly thanks those family businesses who generously gave of their time during trading hours to give evidence.

1.15 The committee also thanks the FBA for its invitation to the National Family Business Day event at Parliament House in Canberra on 19 September 2012. Committee members found this event useful in terms of meeting some of Australia's most successful family businesspeople, as well as outlining issues of key concern for the sector. The committee commends the FBA for organising this event. One of the key challenges that family businesses face is raising public awareness of their contribution to the Australian economy and the community. To this end, National

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12 See Mr David Smorgon, Generation Investments Pty Ltd., *Committee Hansard*, 14 November 2012, pp 2–3.

Family Business Day is an excellent initiative and one that the committee hopes will continue.

1.16 The committee also thanks Ms Paula Pyburne from the Law and Bills Digest Section of the Parliamentary Library for her assistance on matters relating to family trust law.

A brief historical context

1.17 Families have, of course, been central to the functioning of economies for millennia. Hunter-gatherer societies were based entirely on kinship. These societies varied in structure but were alike in that their social organisation was formed in terms of kinship.[13]

1.18 For centuries, the power and influence of royal families structured power and commerce in Europe. Succession planning was crucial to maintaining power and maintaining property. This was also important for families generally. As the Irish and English parliamentarian Edmund Burke wrote in 1790:

> The power of perpetuating our property in our families is one of the most valuable and interesting circumstances belonging to it, and that which tends the most to the perpetuation of society itself. It makes our weakness subservient to our virtue; it grafts benevolence even upon avarice. The possessors of family wealth, and of the distinction which attends hereditary possession, (as most concerned in it,) are the natural securities for this transmission.[14]

1.19 There are celebrated examples of European families without royal blood that have used the family structure to gain and maintain power and wealth. In Renaissance Italy, families used their wealth to form allegiances that led to political power. Most famously, the Medici family, which founded the Medici Bank in the 15th century, subsequently gained political power in Florence as citizens rather than monarchs.[15] In the 19th century, the five sons of Mayer Amschel Rothschild established renowned banking houses in London, Paris, Frankfurt, Naples and Vienna. The brothers were closely connected to their father and to each other and operated according to clear, defined objectives and principles.[16]

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13 See Elman Service, *The Hunters*, Englewood Cliffs, N.J., Prentice-Hall, 1966.

14 Edmund Burke, *Reflections on the Revolution in France*, 1790.

15 Richard A. Goldthwaite, 'The Medici Bank and the World of Florentine Capitalism', *Past & Present*, No. 114, February 1987, p. 6; Tim Parks, *Medici Money: Banking, Metaphysics and Art in Fifteenth Century Florence*, Profile Books, New York, 2006.

16 Rothschild, 'Our history', http://www.rothschild.com/our_history/ (accessed 3 December 2012). See also Niall Ferguson, *The House of Rothschild: Money's prophets 1798–1848*, Penguin Books, New York, 1998.

1.20 In Europe prior to the Industrial Revolution, home-based 'cottage industries' represented the main form of production.[17] Goods were home-made and families themselves sold their wares at market. During the first Industrial Revolution in England, family businesses offered stability, certainty and clear property rights.[18] In the United States, family businesses were the basis from which large economic organisations grew.[19] Well-recognised corporate brands such as Eastman Kodak, du Pont and Kellogg commenced as small family businesses in the nineteenth century.[20]

1.21 As the process of industrialisation in Western countries continued, and as businesses outgrew the family structure, the corporate form of organisation appeared. By the 1930s, with growing interest in the separation of ownership from control, historians and management specialists began differentiating family firms from other business categories.[21] The American political scientist, Francis Fukuyama described the shift from small family business to a corporate form in the following way:

> …as a business grows, its increasing scale usually outstrips the capabilities of a single family to operate it. First to fall away is family management: a single family, no matter how large, capable or well educated, can only have so many competent sons, daughters, spouses, and siblings to oversee the different parts of a rapidly ramifying enterprise. Family ownership often persists longer, but here too, growth often requires raising more capital than one family can provide. Family control is diluted first through bank borrowing, which gives the creditor some voice in running the business, and then through public equity offerings. In many cases the family gets pushed out of the business it founded, as the latter is bought out by non-family investors…The often ad hoc decision-making structure of family owned businesses gives way to a formal organization chart with structured lines of authority.[22]

1.22 There was a view that economic development required a weakening of family ties. For some time, social scientists were of the belief that there was a natural development path that led from 'family businesses based on traditional moral

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17 See Professor Mary Barrett, University of Wollongong, *Committee Hansard*, Sydney, 15 November 2012, p. 37.

18 Andrea Colli and Mary Rose, 'Family business', *The Oxford Handbook of Business History*, Geoffrey Jones and Jonathan Zeitlin (eds.), Oxford University Press, 2007, p. 198.

19 Francis Fukuyama, *Trust: The social virtues and the creation of prosperity*, Penguin Books, 1995, p. 63.

20 Alfred Chandler, *The Visible Hand: The Managerial Revolution in American Business*, Cambridge: Harvard University Press, 1977, pp 298–299.

21 Andrea Colli and Mary Rose, 'Family business', *The Oxford Handbook of Business History*, Geoffrey Jones and Jonathan Zeitlin (eds.), Oxford University Press, 2007, p. 196.

22 Francis Fukuyama, *Trust: The social virtues and the creation of prosperity*, Penguin Books, 1995, pp 64–65.

reciprocity' to the 'modern, impersonal, professionally managed corporation based on contract and property rights'.[23]

1.23 Business consultants writing in the 1960s and 1970s viewed a tension between the non-rational family and the rational business. The thesis of many writers was that when the family and the business components clash, the rational component—the business—is the loser. Accordingly, the recommended solution was to excise the family so as to operate firms in a more 'business-like' way.[24]

1.24 This perspective has changed as researchers have focussed in more detail on the contribution that family businesses make to different societies. Fukuyama notes that while it is possible for families in some societies to be too strong to allow the formation of modern economic organisations, in other societies the family has been important to the path of economic development. In this context, he draws parallels with family structures in central Italy and in China:

> In both cases, the family plays a central role among social structures, with a corresponding weakness of nonkinship-based organisations, and in both industrial structure consists of relatively small family businesses networked together in complex webs of interdependence….In both societies, small family businesses rely on networks to achieve what amount to economies of scale. On the other hand, neither the Italian nor the Chinese family firm has been able to break out of those sectors to which they are limited by their scale and therefore occupy similar niches within the global economy.[25]

1.25 In other countries, however, businesses based on family structures occupy a central role in key national industries. The obvious examples are the *chaebols* in South Korea which have been supported by the South Korean government for decades as part of its strategy for economic development. These conglomerates, which include Hyundai, Samsung and Lucky-Goldstar, have entrenched family control with multiple business lines. They are also important political players, with their close ties to politicians and government officials. During the 2012 Presidential campaign, both candidates campaigned to reform the *chaebols*. The winning candidate, Ms Park Geun-hye, campaigned to pursue these reforms on a more gradual basis than her

23 Francis Fukuyama, *Trust: The Social Virtues and the Creation of Prosperity*, Penguin Books, New York, 1995, p. 65.

24 Barbara Hollander and Nancy Elman, 'Family-owned businesses: An emerging field of inquiry', *Family Business Review*, Vol. 1, No. 2, Summer 1988, p. 146.

25 Francis Fukuyama, *Trust: The Social Virtues and the Creation of Prosperity*, Penguin Books, New York, 1995, p. 111.

opponent.[26] These measures aside, the challenge for the *chaebols* is to ensure the transfer of hereditary power from the second to the third generation.[27]

1.26 Family businesses provide fascinating case studies that attest to the durability, flexibility and vulnerability of the family unit. In 2007, *BusinessWeek* magazine reported on the demise of 'the world's oldest continuously operating family business'.[28] Japanese temple builder Kongo Gumi had been in operation under the founders' descendants for 14 centuries—since 578.

1.27 The *BusinessWeek* article noted four factors contributing to the longevity of Kongo Gumi. First, the industry in which it operated was highly stable: '[F]ew industries could be less flighty than Buddhist temple construction'.[29] Second, the company was flexible in selecting its leaders. Rather than automatically shifting ownership to the eldest son, Kongo Gumi chose the person 'who best exhibited the health, responsibility, and talent for the job'. On one occasion, this person was grandmother of the company's last president.[30] Third, the company adopted the practice of sons-in-law taking the family name when they joined the family firm. This practice, common in Japan, allowed the company to continue under the same name even when there were no sons in a given generation.[31] Fourth, at various times, the business had to diversify. During the 19th century Meiji restoration, for example, the business lost government subsidies and began building commercial buildings.

1.28 Succession planning is not always as smooth, as the case of the Indian conglomerate Reliance Industries attests. In 2012, Fortune Global 500 ranked Reliance Industries 99th on the list of the world's biggest corporations, with revenue for that year exceeding $US76 billion.[32] The company was founded in the late 1950s by Dhirubhai Ambani. His death in 2002 led to a long family feud between the two brothers, Anil and Mukesh, over the terms of the father's succession plan. There was

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26 'Presidential politics in South Korea: Bashing the big guys', *The Economist*, 13 October 2012, http://www.economist.com/node/21564597 (accessed 26 February 2013).

27 Cho Ji-hyun, 'Is Samsung's heir-apparent close to succession?', *The Korea Herald*, 13 December 2012, http://www.asianewsnet.net/news-40149.html (accessed 27 February 2013).

28 James Olan Hutcheson, 'End of a 1,400 year old business', *BusinessWeek*, 16 April 2007, http://www.businessweek.com/stories/2007-04-16/the-end-of-a-1-400-year-old-businessbusinessweek-business-news-stock-market-and-financial-advice (accessed 3 December 2012). In 2006, with half a billion dollars in debt, the company became a subsidiary of another company.

29 James Olan Hutcheson, 'End of a 1,400 year old business', *BusinessWeek*, 16 April 2007.

30 James Olan Hutcheson, 'End of a 1,400 year old business', *BusinessWeek*, 16 April 2007.

31 James Olan Hutcheson, 'End of a 1,400 year old business', *BusinessWeek*, 16 April 2007.

32 See CNN Money, *Global Fortune 500* http://money.cnn.com/magazines/fortune/global500/2012/countries/India.html (accessed 2 March 2013).

dispute between the brothers as to whether ownership and succession issues had been settled before the father's death. Anil left Reliance in 2005, taking the company's telecom, power and finance businesses. It was the brothers' mother, Kokilaben, who implemented the division of the Reliance empire.[33] The need for a clear succession plan is a key theme of this report.

Successful Australian family businesses

1.29 Australia has a short but proud history of successful family businesses. Some of its most iconic companies have been—and remain—family owned and operated. While there is a lack of reliable data on the family business sector, historical accounts of successful family firms give a sense of the diversity and longevity of these businesses.

1.30 In 1994, Edna Carew published a book titled *Family Business: The Story of Successful Family Companies in Australia*. It contained profiles of eight Australian family businesses, all of which were at the time at least 50 years old:

- the Brown & Hurley Group established in the 1940s;
- the funeral directors Tobin Brothers, formed in 1934;
- the Ballarat-based Selkirk Brick founded in the late 1800s;
- the transport business E Murphy and Sons established in 1858;
- G James, the glass and aluminium business which commenced operations in in 1917;
- the food processing and packaging company Ward, McKenzie which began in 1863;
- Thomas Warburton, a wholesale engineering supplier founded in 1853; and
- the packing company J L Lennard which was set up in 1879.[34]

1.31 The book notes at the outset that most family businesses never make it beyond the first generation: 'a trickle survive into the hands of a fourth generation'. The book's introduction summarises the following features common to the development of these eight businesses:

- most have confronted, and dealt with, the problem of succession;
- they have a cautious approach to borrowing;
- they have a clear business plan with an aversion to diversification for its own sake;

33 See Hamish McDonald, *Mahabharata in Polyester: The Making of the World's Richest Brothers and Their Feud*, University of New South Wales Press, Sydney, 2010.

34 Edna Carew, *Family Business: The Story of Successful Family Companies in Australia*, Focused Publishing Pty Ltd, 1994.

- they are 'loyal to family goals';
- they have a sense of having developed 'something of long-term value';
- they foster a satisfying working environment that leads to a core of long-serving employees; and
- they recognise the utility of occasionally employing 'outsiders'.[35]

1.32 A second volume was published in 1996 under the same title.[36] Again, a range of Australian family businesses were profiled including Grenda's Bus Services, the vitamin manufacturer Cenovis and de Bortoli Wines. The book's foreword is written by Professor Ken Moores (then) of the Australian Centre for Family Business at Bond University. He notes that family businesses 'have not generally attracted the attention they deserve' in part because they are in such diverse industries and locations.[37]

1.33 The second volume also has introductory pieces by the Commonwealth Bank of Australia and the Chartered Accountants Howarth & Howarth. These were aimed at explaining how family businesses can benefit from the use of their services. Notably, Howarth & Howarth's comments identified the importance of establishing a Family Constitution which set out details on the following issues:

- a clear objective—whether to sell the business or keep it in the family;
- identifying, training and installing a successor;
- the options for clear ownership;
- a policy on remuneration of family members; and
- a policy on who can join the company.[38]

1.34 In 2012, Free Run Press in conjunction with *Australia's Family Business Magazine* published an anthology of 100 Australian family businesses titled *Soul Stories*. The collection highlights the longevity and diversity of family firms in Australia. It includes stories on:

- A. H. Beard, a fifth generation Australian bedding company that began in 1899;
- Angove Family Winemakers, a fourth generation wine producer established in the 1880s;

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35 Edna Carew, *Family Business: The Story of Successful Family Companies in Australia*, Focused Publishing Pty Ltd, 1994.

36 John Arboux and James Murray, *Family Business: The Story of Successful Family Companies in Australia*, Focused Publishing Pty Ltd, 1996.

37 Professor Ken Moores, 'Foreword', in John Arboux and James Murray, *Family Business: The Story of Successful Family Companies in Australia*, Focused Publishing Pty Ltd, 1996.

38 John Arboux and James Murray, *Family Business: The Story of Successful Family Companies in Australia*, Focused Publishing Pty Ltd, 1996.

- Beerenberg, a South Australian-based farm product firm that began in 1969 by fifth generation dairy farmers;
- Coopers, the 150 year old beer brewing firm;
- Dysons Group, a family owned bus company that commenced operating in 1952;
- Haigh's Chocolate, a fourth generation firm;
- Haymes Paint, a paint-making firm that began in 1935;
- Lionel Sampson & Sons, established in 1829 in Fremantle. It purchased R. C. Sadlier (another Western Australian company) after the outbreak of World War 2; and
- Tobin Brothers Funerals.[39]

Family businesses and the BRW 200

1.35 Family businesses rank among the wealthiest in Australia. In June 2012, the *Business Review Weekly* published its annual *BRW 200 Rich List*. On that list, 29 of the 200 inherited their wealth. Most notably, the daughter of the late Lang Hancock, Gina Rinehart tops the list with an estimated personal wealth of $29.2 billion. Anthony Pratt, the son of the late Richard Pratt, is worth an estimated $5.45 billion. James Packer, the son of the late Kerry Packer, has an estimated personal wealth of $5.2 billion. Then there are first generation family business owners. Notable examples are Frank Lowy (the owner of Westfield) and Lindsay Fox (the owner of Linfox).[40]

1.36 The *BRW* Rich List distinguishes between a family in business and family businesses. While several prominent family members (some mentioned above) make the list of 'billionaires', there is also a list of the 50 richest family names. Heading this list are the Smorgon, Lieberman, Besen and Myer families, all with net wealth over $2 billion. Twenty-nine of the wealthiest 50 family businesses have property investments in their portfolios.[41]

Family businesses and migrants

1.37 Many Australian family businesses were established in the early post-WWII years by newly-arrived migrants seeking to escape economic and political turmoil in Europe. A number of the businesses on the *BRW Rich List* were established by newly-arrived European immigrants in the 1930s, 1940s and early 1950s: these include the Roth, Valmorbida, Rabinowicz, Burger and Barro families.[42] Italian migrants arrived

39 *Soul Stories: 100 Australian Family Businesses 2012*, Free Run Press, 2012.

40 Business Review Weekly, *Rich by numbers*, 24 May–27 June 2012, pp. 68–129.

41 Business Review Weekly, *Rich by numbers*, 24 May–27 June 2012, pp 122–129.

42 'Rich 50 families', *Business Review Weekly*, 24 May–27 June 2012, pp 122–129.

in Australia with a 'specific form of entrepreneurship', which resulted in many successful Italian businesses in areas such as wine making and building construction.[43]

1.38 Migrant family businesses usually had access to an informal workforce through family and spouses who were able to contribute to the business. This workforce increased as family businesses were transferred to the second generation. The requirement that children help out in the family business was often a matter of survival for many second generation Chinese families.[44] However, many second and third generation family business members were able to obtain the formal educational qualifications that their parents did not, incorporating this knowledge into the family business.[45]

1.39 The committee is interested in the contribution made by family businesses from culturally and linguistically diverse (CALD) communities. It is an area that seems largely unexplored in academic research. Unfortunately, this inquiry was unable to produce much by way of evidence in this area. The committee does make a recommendation (chapter 2) that government should consider the need for data on family businesses from CALD communities.

The Australian family farm

1.40 Australia's agricultural sector has been based on the family farm, a form of ownership that governments have assisted. Beginning in the 1860s, land reforms were introduced to create small family farms to replace the existing broad scale pastoral holdings of the wealthy squatters.[46] After World War 1 and 2, returning soldiers were thanked for their service with farmland distributed through various Settlement Schemes.[47] Chapter 3 of this report notes that today, more than 95 per cent of Australian broadacre and dairy farms are family operated and at least partly family

43 Laura Hougaz and Michela Betta, *The Business of the Family: Italian-Australian Entrepreneurs in Victoria and their Modern Dynasties*, Australian Graduate School of Entrepreneurship, Swinburne University of Technology, 2008, p. 1125 and pp 1128–1129, www.swinburne.edu.au/lib/ir/onlineconferences/.../000010.pdf (accessed 27 February).

44 Carole Tan, 'Chinese Families Down Under: The role of the family in the construction of identity amongst Chinese Australians, 1920–1960', Paper presented at the International Conference "Migrating Identities: Ethnic Minorities in Chinese Diaspora" held by the Centre for the Study of Chinese Southern Diaspora, ANU, 26–28 September 2001.

45 Laura Hougaz and Michela Betta, *The Business of the Family: Italian-Australian Entrepreneurs in Victoria and their Modern Dynasties*, Australian Graduate School of Entrepreneurship, Swinburne University of Technology, 2008, p. 1130.

46 Dr Linda Botterill, 'Rural policy in Australia: the farm family and the farm business', *Government Reformed: Values and New Political Institutions*, Ian Holland and Jenny Fleming (eds.), Ashgate, 2003.

47 Dr Linda Botterill, 'Rural policy in Australia: the farm family and the farm business', *Government Reformed: Values and New Political Institutions*, Ian Holland and Jenny Fleming (eds.), Ashgate, 2003.

owned. This type of farm accounts for 68 per cent of all Australian farms. The indications are that vegetable industry farms and irrigated farms in the Murray-Darling Basin have a similarly high proportion of family-based operations.[48]

Structure of the report

1.41 This report has 9 chapters:

- Chapter 2 looks at the fundamental issue of whether a formal definition of family business is needed and if so, the possibilities and challenges in framing a definition. It considers submitters' and witnesses' views on a range of matters relating to a definition of family business.
- Chapter 3 is concerned with the availability and reliability of data on the sector. In the absence of a formal definition and official data, several consultancies have attempted to collect and collate their own statistics. This chapter details this evidence and comments on the accuracy and reliability of these data.
- Chapter 4 summarises the committee's evidence on the characteristics and mindset of family businesses. The committee received considerable evidence that in certain key respects, family businesses have traits that are either not present in non-family businesses, or not evident to the same extent. This chapter discusses these attributes.
- Chapter 5 discusses the challenge of planning for succession.
- Chapter 6 considers the challenges to family businesses of operating a trust structure. It details the concerns raised with the effect of taxation requirements under Division 7A of the *Income Tax Assessment Act 1936*, Division 6 of the 1936 Act, and the capital gains tax provisions.
- Chapter 7 focusses on various issues of apparent concern for family businesses in current policy settings. These include the 80 year limit on trusts, the 50 member non-employee shareholder rule in section 113 of the *Corporations Act*, employee share schemes in Division 83A of the *Income Tax Assessment Act 1997* (ITAA) and the effect of Division 7A of the ITAA on the use of trust structures.
- Chapter 8 considers the capacity of family businesses to access finance. It also considers the evidence that family businesses were able to weather the Global Financial Crisis better than non-family businesses.
- Chapter 9 presents the committee's conclusions.

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48 Mr Paul Morris, Executive Director, Australian Bureau of Agricultural and Resource Economics and Sciences, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 13 November 2012, p. 39.

Chapter 2

The challenge of defining 'family business' and the needs of policy makers

Family enterprises are not officially defined, which impedes the gathering of statistical information on family businesses. Decision-makers need statistical information on family businesses to support their decisions and to assess the effects from these decisions. It is difficult to obtain statistics on family enterprises and their activities since there is no definition of family enterprise.[1]

Introduction

2.1 The first article of the terms of reference for this inquiry directs the committee to consider the definition of 'family business'. The committee deliberated on this matter in some detail: it is the crucial consideration of this inquiry. Some witnesses and submitters proposed a definition of their own; others gave broad support for one or several of these definitions; while others highlighted the difficulties in composing a definition and questioned the purpose of, and therefore the need for, a definition.

2.2 This chapter considers various aspects of a definition of 'family business' and how work on an official definition might proceed. It is divided into the following sections:

(a) the 2005 Australian Bureau of Statistics (ABS) survey question which attempted to define a family business;

(b) stakeholders' views on whether a definition is needed, the arguments for and against the development of an official definition, and whether family businesses are mainly small and medium sized enterprises;

(c) proposed definitions of 'family business';

(d) the setting of thresholds in a definition including;

- whether sole traders should be classified as a family business;
- whether there should be the possibility or intention to pass on the business; and
- whether a definition should include both small and large family businesses;

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1 Ministry of Trade and Industry, Government of Finland, 'Family Entrepreneurship: Family enterprises as the engines of continuity, renewal and growth-intensiveness', 2006 http://julkaisurekisteri.ktm.fi/ktm_jur/ktmjur.nsf/All/E7E75135A895485BC2257123003F5221/$file/jul7elo_2006_netti.pdf (accessed 12 February 2013).

(e) the public policy reasons for a definition of family business; and

(f) the committee's recommendations for how a definition of family business should be developed.

The 2004–05 Business Characteristics Survey

2.3 The first and most fundamental observation is that there is no generally accepted definition of a 'family business' either in Australia or internationally. In Australia, the ABS does not collect official data on family business.

2.4 In its submission to this inquiry, however, the ABS did note that as part of its 2004–05 Business Characteristics Survey (BCS), it asked the following question:

> As of 30 June 2005, was this business a family business?
>
> For the purpose of this survey a family business is defined as one where family members are part of the business ownership and are involved in the strategic direction of the business.[2]

2.5 The ABS found in a post-enumeration investigation that there were 'quality issues' with the data collected. It speculated that the reasons for this could have included:

- the narrow definition specifying that family members must be owners *and* involved in the strategic direction;
- the definition did not define family members, and in particular whether in-laws and those in de facto relationships are included; and
- that the answer may not be known by the person responsible for completing the survey.[3]

2.6 The ABS noted that this question (among others) was discontinued and replaced with 'questions more focused on business characteristics which demonstrated

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2 Australian Bureau of Statistics, *Submission 2*, p. 2.

The ABS describes the Business Characteristics Survey as: 'an annual ABS survey and is conducted via a mail-out/mail-back questionnaire. It is designed to collect characteristics data. It is intended that each year the survey will contain a consistent set of core questions to allow longitudinal analysis. There have been some changes to the core content of the survey in these early iterations as its purpose and scope has been refined.' Australian Bureau of Statistics, 'About the Business Longitudinal Database', http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/8168.0.55.001main+features32004-05%20to%202009-10 (accessed 1 March 2013).

3 Australian Bureau of Statistics, *Submission 2*, p. 2. See also Ms Jacky Hodges, Regional Director, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 17.

a stronger relationship to productivity and performance'.[4] The data were used to populate the Business Longitudinal Database, initially released in October 2009.[5]

2.7 The ABS told the committee that it had recently met with representatives from Family Business Australia (FBA) and the University of Adelaide Business School to discuss the possibility of including new family business-related questions in the BCS. It noted that at this meeting, the FBA acknowledged that the question used in the 2004–05 BCS did not collect 'fit-for-purpose' information. The FBA proposed a number of questions which they believed could accurately identify family businesses. However, the ABS commented that these questions:

> …would need to be reworded and fully tested before they would be considered fit for inclusion on an ABS survey vehicle. Part of this work would require defining a 'family business' and ensuring that the definition can be understood and answered by the person completing the survey.[6]
>
> At the end of that process, they were accepting that the definitions used did have the ambiguity which caused problems and that would need to be sorted. They also accepted that in ABS we were in the business of having to balance a wide range of information requirements and that our current funding was not sufficient to do that.[7]

2.8 Treasury observed that while there is benefit in having data, there is also a cost to collecting it. In terms of the utility of a future ABS survey question on family business, Treasury agreed with the ABS that if a better question (than in the 2004–05 survey) could be designed to replace an existing question, there could be value in asking this question.[8]

Stakeholders' views on the need for a definition

2.9 The fundamental question in drafting a definition of 'family business' is to ask why a definition is needed in the first place. Interestingly, submitters and witnesses gave a range of views on this matter.

Identifying the public policy issues

2.10 In terms of the need for a definition of family business, government departments emphasised the importance of identifying the public policy issues that

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4 Australian Bureau of Statistics, *Submission 2*, p. 2.

5 Australian Bureau of Statistics, *Answer to a question on Notice*, received 10 December 2012.

6 Australian Bureau of Statistics, *Submission 2*, p. 2.

7 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, pp 23–24.

8 Mr Hector Thompson, General Manager, Small Business Tax Division, Treasury, *Committee Hansard*, 13 November 2012, p. 11.

need to be addressed. A definition of family business, they argued, might be unnecessary if the policy matter can be addressed through existing frameworks and definitions. The Department of Industry, Innovation, Science, Research and Tertiary Education (DIISRTE) told the committee:

> In essence, the role of government is to look at what the problem is that we are trying to address and to see how best to do it. In some instances, the definition may be a secondary issue to that.[9]

2.11 The committee asked DIISTRE whether in policy-making terms there was an advantage in identifying family businesses as distinct from small, medium and large businesses. It replied:

> There is nothing particularly evident other than the idea of the family structure. I guess the issue is what policy issues would need to be addressed by having a particular definition like that.
>
> …many of the issues facing small business generally—for example, there are issues relating to taxation, regulatory burden, best practice regulation, access to finance and those sorts of things—would relate equally to small family businesses as well, and so the question we would ask ourselves is: what additional factors are there at play that would require particular either data collection or definitional structures around a family business?
>
> …issues around succession are probably the main ones. Others probably relate to the more general issues facing small business.[10]

2.12 The committee asked the Department of Regional Development, Local Government, Sport and the Arts (DRALGAS) the use to which data on family businesses in regional Australia could be put. It responded:

> With that type of data we would do similar things to what we do with other industry or employment data. We would get a richer picture of what is happening in particular regions, which can support policy development across all types of areas. That would be another element of that.[11]

2.13 The ABS also emphasised that if a definition of family business is to be developed, it must reflect the public policy objective. Mr Bill Allen, Assistant Statistician at the ABS, told the committee:

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9 Mr Peter Chesworth, Acting Head, Small Business Division, Department of Industry, Innovation, Science, Research and Tertiary Education, *Committee Hansard*, 13 November 2012, p. 1.

10 Mr Peter Chesworth, Acting Head, Small Business Division, Department of Industry, Innovation, Science, Research and Tertiary Education, *Committee Hansard*, 13 November 2012, p. 2.

11 Mr Simon Atkinson, First Assistant Secretary, Regional Policy and Coordination, Department of Regional Australia, Local Government, Arts and Sport, *Committee Hansard*, 13 November 2012, p. 36.

> …we collect data based on what the information is meant to inform, so as to what the decisions and what the policies are. So it really comes down to what the policies driving those questions are. If a policy is relevant to that concept then that would be appropriate but if not it would not be.[12]

2.14 Ms Jacky Hodges of the ABS added:

> One of the considerations we would test is around people's understanding when they were filling in the survey form to make sure that the question we were asking was actually getting the information that was needed to support that policy. So there would be a lot of field testing to actually test questions before we would commit to what would or would not work in a survey.[13]

2.15 Mr Chris Lowe, a doctoral candidate examining the links between governance and performance in family businesses, also suggested that a definition must reflect the government's public policy needs.[14] He told the committee that in developing a definition, the government could approach family business industry representatives and say: 'This is what we're trying to achieve and this is why we're trying to achieve it; can you help us get this data submitted'.[15]

A definition as a heuristic tool

2.16 Some witnesses to this inquiry argued that a definition of family business is needed as a heuristic tool; that is, gathering data on the sector that could be analysed in a meaningful way would broaden the sector's understanding of itself. As Mr David Smorgon told the committee:

> Frankly, I don't care what the definition is; let's just understand and agree on one definition and let that then be the base on which all the other data can stand. Only when you have that definition can the relevant numbers be obtained. For example, how many family businesses are there? How many people do they actually employ? What is their contribution to our society? What is the wealth of the family business? How long do they survive? Most importantly, what are the key issues that they face when compared with SMEs or other businesses in our community?[16]

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12 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 19.

13 Ms Jacky Hodges, Regional Director, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 19.

14 Mr Lowe is a PhD candidate at Monash University and the Chief Executive Officer of Bus Association Victoria. His thesis will examine the links between governance and performance in family and multinational enterprises providing public transport services.

15 Mr Chris Lowe, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 13.

16 Mr David Smorgon, Generation Investments Pty Ltd, *Committee Hansard*, 14 November 2012, p. 2.

2.17 In the same vein, Mr David Hill of Deloitte Private told the committee that a definition of 'family business' should reflect the data that family businesses themselves want to know. In terms of the data that is needed, Mr Hill explained that the list is long:

> [F]undamentally, the number of family businesses. It will drive the definition of what a family business is. They are very diverse and, as we have said today, one of the most naive things to think would be that family businesses equals SMEs. That would be missing a vast component of the Australian economy. Information on the definition, the number, the employees, issues such as growth—are they experiencing growth?—and the contribution to the broader GDP of the country is very important.[17]

2.18 Professor Mary Barrett of the University of Wollongong argued that a better understanding of family businesses could assist the broader business community in Australia. She drew the committee's attention to an article published in the *Harvard Business Review* in November 2012 which compared the characteristics and the performance of family and non-family businesses. The article's finding was that while family businesses performed below their peers during upturns, they led the pack in times of crisis.[18]

2.19 Professor Barrett argued that this type of research into the dynamics of family business is important for the insights and the lessons it can provide. As she explained to the committee:

> I think there is a point in saying it is worthwhile to know what it is about the dynamic of family businesses that sets them apart from any size-based definition or any definition based on the size of loan they get in certain situations, because it gets at a mindset that has quite a lot to do with the way a certain dynamic can work in a business, for good or for bad. The point is that when you know what it is, what you have to do to make it good and how you can head off the bad you are a whole lot better off than if you had not made that segmentation.[19]

2.20 Professor Barrett took issue with the view that collecting data on the family business sector is not worthwhile as it is unlikely to be the basis of public policy and there are other factors that are more likely to predict the success of businesses generally. She argued that the operation, success and failure of family businesses is substantively different because of these family business characteristics. Accordingly,

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17 Mr David Hill, Deloitte Private, National Managing Partner, *Committee Hansard*, 14 November 2012, p. 3.

18 Nicolas Kachaner, George Stalk and Alain Bloch, 'What you can learn from family business', *Harvard Business Review*, November 2012, p. 104.

19 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 36.

Professor Barrett emphasised that proper data collection and analysis is 'absolutely vital'.[20]

2.21 In terms of the ABS's 2004–2005 BCS family business question, Professor Barrett suggested that a few amendments could be made. She argued that instead of asking 'do you regard this business as a family business?' and then 'why?' (for those that ticked 'yes'):

> I would just have them separately: 'Do you regard this business as a family business?' Then I would have those questions, but not with a 'why' connection to the first one. They would just say: 'Do you do this? Do you do that?' Then we would catch the people who self-identify, and then we would still have all the other data, with which we can slice and dice as other people have said. I would be delighted, and I think just about every academic in the country would love the opportunity, to do a bit of head scratching with the ABS over that one.
>
> For my own part, I would basically be happy to see the two main conceptual issues in the literature captured in a definition of family business which had something to do with control and, as I say, one to two people, members of the same family. Yes, there is a problem about family, but what I liked about the original definition was that the family themselves could define how they thought of their family.[21]

Doubt on the need for a definition

2.22 Some stakeholders were sceptical that a definition of 'family business' and the subsequent collection of data are necessary. Mr Peter Strong, Executive Director of the Council of Small Business of Australia (COSBOA), told the committee that in considering a submission to this inquiry, the feedback from members was that the issue of a definition of family business is not important. He explained:

> As I was looking at writing this report…I thought, 'It's obviously important enough for people to be looking at it.' So I rang a few people, and the same thing happened across the council. It does not come up for us, and it has never really come up in the whole time that I have been around COSBOA, which is since 1996. It comes up from technicians who need to define small business for technical purposes. Family Business Australia have their head around this.
>
> The impression I get is that it is for the wealthier people. So it is the family businesses that have money, not mum and dad down the road who are

20 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 36.

21 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 36. See the discussion in chapter 3 of this report on the ABS' Business Longitudinal Survey. This survey used a similar format to that proposed by Professor Barrett.

> running a little shop. They are very different, even though I would define them as a business. You can hear that I get quite confused about where I am going with this whole family business thing. When I talk small business, I am very comfortable. I do not see the difference quite often.[22]

2.23 He emphasised COSBOA's view that the first priority should be to establish a clear definition of a small business:

> In all the time that I have been around I have never heard of anybody in COSBOA asking for a family business definition. It is not a big issue for us. A definition of small business is a much bigger issue. If we bring the family into that I am comfortable with it, but let us get a definition of what a small business is first. Otherwise, my experience is that we will end up concentrating on the people who have the money to be concentrated on. That is always the way.[23]

2.24 Indeed, COSBOA argued that efforts to refine the definition of a small business will assist in identifying and addressing family business issues. Mr Strong told the committee:

> …at the beginning of this year, we ran a roundtable with the tax institute on the definition of small business, so getting back to the definition of what a small business is—and that has its own problems and I am sure you are aware there is any number of definitions depending on how you look at it. By the way, I do not think we will ever get one definition. I think that is a bridge too far. But we can cut it all down to not many definitions. That is an area we can work on. I think it will then impact upon the family business issues if we can say, 'Okay, we can define a business this way and the owners of the business can be structured shareholders or it can also be about the people who have put a lot of time and effort into it and are part of a family structure.' That will take solicitors and lawyers some time to work out but I think that is the way we have got to go.[24]

2.25 Other witnesses, while not rejecting the need for a definition, noted that they had not required data on family businesses. For example, the Queensland Chamber of Commerce and Industry told the committee:

> The chamber predominantly deals with issues that impact on all business, so we have never had the need to differentiate between family-run business and non-family-run business. We often find that the issues that are important to large businesses are equally important to small businesses. The issues important to those businesses in South East Queensland are equally

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22 Mr Peter Strong, Executive Director, Council of Small Business of Australia, *Committee Hansard*, 13 November 2012, p. 29.

23 Mr Peter Strong, Executive Director, Council of Small Business of Australia, *Committee Hansard*, 13 November 2012, p. 29.

24 Mr Peter Strong, Executive Director, Council of Small Business of Australia, *Committee Hansard*, 13 November 2012, p. 26.

important to those businesses operating in regional Queensland. The issues relevant to some industry sectors are relevant to other industry sectors.[25]

Are family businesses mainly small and medium-sized enterprises?

2.26 A point of some discussion during this inquiry was the extent to which family businesses are small and medium-sized businesses. Witnesses such as COSBOA argued that policy-makers' focus on small business will also address the concerns of family businesses. Other witnesses strongly rejected this argument. They claimed that not only do family businesses come in all sizes, but that their issues are distinctive to those of other small and medium sized businesses.

2.27 Table 2.1 (below) shows that 96 per cent of all businesses in Australia are small businesses, employing less than 20 employees. Among family businesses, 64 per cent employ less than 20 employees; 32 per cent are medium-sized firms employing between 20 and 199 employees; and four per cent are large businesses, employing 200 or more employees.[26]

Table 2.1: Businesses by size (employees)

	All businesses	Family businesses
Small (0–19 employees)	96	64
Medium (20–199 employees)	*	32
Large (more than 200 employees)	*	4

Source: The figure for all businesses is taken from the Australian Bureau of Statistics, *Counts of Australian Businesses, Including Entries and Exits, June 2007 to June 2011*, Cat No. 8165.0, released 31 January 2012, p. 2. The data for family businesses is taken from the MGI Australian Family and Private Business Survey 2010, p. 13.

2.28 Table 2.2 shows data on businesses by annual turnover. The first two columns are taken from ABS data. It shows that as of June 2011, roughly a third of all Australian businesses fell in each of the ranges of less than $50,000 annual turnover, from $50,000 to less than $200,000, and from $200,000 to less than $2 million. Only six per cent of Australian businesses have an annual turnover of more than $2 million. Therefore, on the ATO and Treasury's definition of small business (less than $2 million in annual turnover), 94 per cent of all businesses are classified as small businesses.

25 Mr Nick Behrens, General Manager, Advocacy, Queensland Chamber of Commerce and Industry, *Committee Hansard*, 16 November 2012, p. 9.

26 Australian Bureau of Statistics, *Counts of Australian Businesses, Including Entries and Exits, June 2007 to June 2011*, Cat No. 8165.0, released 31 January 2012, p. 2; MGI Australian Family and Private Business Survey 2010, p. 13. http://www.mgiaust-survey.com/sites/default/files/fpbs_report_0.pdf

2.29 Table 2.2 contrasts this data with the findings of the 2009 KPMG and FBA Survey of Australian Family Businesses. 648 businesses were surveyed, of which 70.6 per cent self-identified as a family business. This survey found that 36 per cent of respondents reported the annual turnover of their business between $1 million and $5 million, and a further 36 per cent of respondents reported annual turnover at more $5 million.

2.30 Assuming respondents gave correct responses, the sample of businesses used in the 2009 KPMG survey was unrepresentative of the business community at large. Their annual turnover is far in excess of what the official data would indicate was a representative sample. Either the respondents gave inaccurate responses or the businesses surveyed were disproportionately medium and large businesses. Chapter 3 comments on the broader issue of the reliability of the consultancies' survey data.

Table 2.2: Businesses by size (turnover)

	% of all businesses ABS data		**% of businesses (648) (71% family businesses) KPMG/FBA data**
Less than $50K	29	Less than $500K	17
$50K – $200K	35	$500K to less than $1 million	12
$200K – less than $2 million	31	$1 million to less than $5 million	36
More than $2 million	6	$5 million to less than $10 million	10.3
		More than $10 million	25.4

Source: Australian Bureau of Statistics, *Counts of Australian Businesses, Including Entries and Exits, June 2007 to June 2011*, Cat No. 8165.0, released 31 January 2012, p. 11; Australian Centre for Family Business, *KPMG and Family Business Australia Survey of Family Businesses 2009*, 2009. Note: Numbers have been rounded up.

2.31 DIISTRE confirmed for the committee its view that most family businesses are small businesses.[27] Its engagement with family businesses is mainly through its dealings with small businesses. As it told the committee:

> What we tend to do is focus on the idea of small business and definitions around small business—of which there are more than one across government as well for a range of policy and legacy reasons as well. Our

27 Mr Peter Chesworth, Acting Head, Small Business Division, Department of Industry, Innovation, Science, Research and Tertiary Education, *Committee Hansard*, 13 November 2012, p. 3.

interactions with family businesses tend to be, I guess, through that small business prism.[28]

2.32 DIISTRE argued that from a policy perspective, the issues that some claim to be particular to the family business sector may best be handled within a broader policy rubric applying to small and medium-sized enterprises (SMEs). It explained:

> Coming from the policy perspective, I just reiterate, it has been suggested in the past that there are some family businesses whereby the succession can be an issue. From a policy perspective, we would see that in the broader issue of management capability. It has been demonstrated over a number of years that that is a challenge for Australian businesses: management capability and capacity. That might be one of the issues that could fall under that.[29]

2.33 The Reserve Bank of Australia (RBA) put a similar view:

> On family businesses, the thing that is striking there is that small and medium seem to collect a large proportion of family businesses, but there are family businesses that are extremely large as well. But you are probably picking up quite a bit in that small and medium-sized category.[30]

2.34 The RBA added further context to the parallel between small and family businesses by noting the similarities between small business decisions and those of households. As Mr Aylmer told the committee:

> …there is an interesting characteristic of small businesses…that to a large extent they look more like households, because family businesses' decisions are actually household decisions. They are not necessarily scaled down versions of very large businesses. Once you get to a certain size, you will have people who will manage all of your financials. You start to specialise when you get very large. In family businesses, particularly the smaller ones, quite often decisions on whether or not they want to grow are basically decisions about their households and whether or not, as a family, they want to expand and get bigger and take on the additional pressures of being a larger business.[31]

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28 Mr Peter Chesworth, Department of Industry, Innovation, Science, Research and Tertiary Education, *Committee Hansard*, 13 November 2012, p. 1.

29 Mr Peter Chesworth, Department of Industry, Innovation, Science, Research and Tertiary Education, *Committee Hansard*, 13 November 2012, p. 1.

30 Mr Christopher Aylmer, Head, Domestic Markets Department, Reserve Bank of Australia, *Committee Hansard*, 15 November 2012, p. 1.

31 Mr Christopher Aylmer, Head, Domestic Markets Department, Reserve Bank of Australia, *Committee Hansard*, 15 November 2012, p. 1.

2.35 COSBOA noted that for its purposes, 'family business' and 'small business' are essentially interchangeable. As Mr Peter Strong, the Executive Director of COSBOA, told the committee:

> …in the main we are all family businesses, so the definitional stuff becomes confusing for a lot of our members because they say, 'Small business or family business; it's really much the same sort of thing, isn't it?'[32]

2.36 Mr Graham Henderson, a board member of Family Business Australia and a part-owner of a third-generation family business, told the committee that the majority of small businesses (those with a turnover of less than $2 million) are family businesses. However, he argued that the $2 million threshold used by the ATO to identify small businesses was not necessarily a useful point of reference to identify family businesses:

> The segment of business that is family business, whether it be the Stillwell Motor Group of $400-plus million or our business of about $17 million or the small hardware store of $2 million, is a segment that is very different to what we perceive as big business…In terms of family business and small business, or if you want to call them one and the same thing because it is really the sector we are talking about, there are so many things that are very different in our sector of the business than in larger business and the considerations we talked about regarding capital gains tax, shareholder rulings, education et cetera are all relevant to family business. So my response to you would be to say that, rather than have a minister for small business, I would very much favour a ministry for family business, which would then cover off a lot of the things we are talking about.[33]

2.37 Some witnesses strongly disagreed with the characterisation of family business as simply small business. Mr Bill Noye of KPMG, for example, told the committee:

> From a definitional point of view, I need to stress that it is very important that 'family business' is not just seen as 'small business'. I think to do so is a poor misconception and provides a misguided view of the sector and its needs. It is wrong. Family businesses are unique. They are not necessarily small. They have unique issues that impact on them. In our view, it is that uniqueness that this committee should focus on. We are inclined to support the European view. We do support the FBA view of the definition of family

32 Mr Peter Strong, Executive Director, Council of Small Businesses of Australia, *Committee Hansard*, 13 November 2012, p. 26.

33 Mr Graham Henderson, Board Member Family Business Australia, *Committee Hansard*, 14 November 2012, p. 38.

> business, but we would like to extend that somewhat further to be consistent with the European Commission definition.[34]

2.38 Mr David Smorgon, whose family's business interests exceed $2.5 billion in value, also rejected the idea that family businesses are simply small and medium-sized businesses. As he put it:

> We also know that family businesses are not necessarily SMEs. I know we are always branded as SMEs, but there are some very large family businesses that would abhor to think that they are classified as a small business enterprise.[35]

Possible definitions of a family business

2.39 The following section looks at three possible definitions: one proposed by Family Business Australia (FBA) in its submission to this inquiry; another used by MGI Australasia in a 2010 survey; and a third used by the European Commission in 2009. These definitions were the basis of considerable comment during this inquiry. A key point of stakeholder focus—common to all three definitions—was the requirement that a family member or members have control (and ownership) of the business.

Family Business Australia's definition

2.40 In its submission to this inquiry, the FBA proposed the following definition of family business:

> a family business is comprised of two or more members of the same family involved in the business with one or more related members having a controlling interest.[36]

2.41 The ABS foresaw that the FBA definition may encounter some of the problems that beset the 2004–05 BCS question. As it told the committee:

> Our initial response is that the definition is expected to come up with some of the same conceptual issues that we expressed in 2004-05, particularly around issues such as the definition and interpretation of a family—so does it include immediate family, extended family and de facto relationships and the like—the nature of the involvement—is it a legal involvement in the business or an operational involvement?—what we mean by controlling interest—is it financial, strategic direction or ownership?—and the availability of the information to the provider of the data. An example

34 Mr Bill Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 10.

35 Mr David Smorgon, Generation Investments Pty Ltd, *Committee Hansard*, 14 November 2012, p. 2.

36 Family Business Australia, *Submission 1*, p. 1.

> would be that in many of our surveys, particularly those of a financial nature, it might be referred to the tax agent who may not be on top of the specific ownership implications.[37]

2.42 However, other witnesses appeared to support the FBA's approach and in particular, the focus on family members having a controlling interest. Mr Andy Kennard of Kennards Hire, for example, told the committee that a definition of family business:

> …has to include the aspect of ownership and control. There are many public companies that are controlled by families, so it does not have to be 100 per cent ownership, but ownership and control are a key factor, and I think they are the two things. I do not think the number of generations matters. The size certainly does not matter; it is across all sectors.[38]

2.43 However, he added:

> I do not know why you have to have two or more involved. You can have multiple people owning it but only one person working in it…I think the numbers do not matter. I still think it comes back to who owns it. Many family businesses do not actually have family working in them.[39]

2.44 Professor Barrett also seemed to support the FBA's definition. She argued that a definition essentially needs to refer to the involvement of family members and the control of these members over the business. Professor Barrett noted that she was comfortable with a definition that left it open to respondents to determine whether they were family members. The threshold of 'control' would be satisfied where two people are 'actively involved in the management and/or working in the firm'.[40]

MGI Australasia's definition

2.45 Another definition of family business was used in the MGI Australasia 2010 *Australian Family and Private Business Survey*, conducted in conjunction with Royal Melbourne Institute of Technology (RMIT).[41] This definition was as follows:

> A business is a family business when it involves two or more related individuals who work together (or are otherwise associated) in a commercial enterprise that is controlled by one or more of them.[42]

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37 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 19.

38 Mr Andy Kennard, Owner, Kennards Hire, *Committee Hansard*, 15 November 2012, p. 48.

39 Mr Andy Kennard, Owner, Kennards Hire, *Committee Hansard*, 15 November 2012, p. 48.

40 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 36.

41 See http://www.mgiaust-survey.com/key-findings (accessed 13 December 2012).

42 MGI Australasia, *Submission 9*, p. 2.

2.46 The committee questioned MGI about various components of this definition. In terms of what constitutes 'related individuals', Mr Desmond Caulfield, a Director of MGI Australasia, responded:

> I would define 'related' in the same manner as it is currently defined in the *Income Tax Assessment Act*. Related parties are clearly defined in various sections of the *Income Tax Assessment Act*. I believe they are also defined in the corporations law and the company law similarly. It covers situations of spouses, children, cousins, associates of those people who would be spouses of cousins et cetera, so it is a fairly wide definition.[43]

2.47 The *Corporations Act 2001* and the *Income Tax Assessment Act 1997* (ITAA) define 'relative' and 'related' broadly. Section 9 of the Corporations Act defines 'relative' as 'the spouse, parent or remoter lineal ancestor, child or remoter issue, or brother or sister of the person'. Section 995-1 of the ITAA defines 'related' as:

> a) the person's spouse; or
>
> b) the parent, grandparent, brother, sister, uncle, aunt, nephew, niece, lineal descendent or *adopted child of that person, or of that person's spouse; or
>
> c) the spouse of a person referred to in paragraph (b).

2.48 Mr Caulfield told the committee that a 'commercial enterprise' is not necessarily a full-time business, but it must be a business that is established to make a profit. In terms of the reference in the definition to 'controlled', Mr Caulfield explained:

> Control is generally ownership, and ownership means that if you own more than half of something you are considered to control it—you may not, but you are considered to control it if you own more than half of it. There are various definitions in the corporations law about what 'control' means. For significantly large public companies sometimes as little as 15 per cent can be considered to be some form of control, but what we are talking about here in our submission is that for it to be control more than 50 per cent must be owned by a family group.[44]

Other suggested definitions focused on ownership and control

2.49 In the academic literature over the past thirty-five years, several proposed definitions of a family business have been based on the conditions of family control and/or ownership. Bernard (1975) referred to 'an enterprise which, in practice, is

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43 Mr Desmond Caulfield, Director, MGI Australasia, *Committee Hansard*, 14 November 2012, p. 23.

44 Mr Desmond Caulfield, Director, MGI Australasia, *Committee Hansard*, 14 November 2012, p. 24.

controlled by the members of a single family';[45] Barnes and Hershon (1976) to 'controlling ownership';[46] Davis (1983) referred to 'significant influence by one or more family units…through ownership and sometimes the participation of family members in management';[47] and Holland and Oliver (1992) propose 'any business in which decisions regarding its ownership or management are influenced by a relationship to a family or families'.[48]

2.50 Mr Francesco Barbera, a researcher at the Australian Centre for Family Business at Bond University, referred in his submission to a 'structural based classification' of family businesses: where family firms are defined as those which are owned, controlled and/or managed by a family unit. He noted that this definition allows for a wide range of family firms given that the degree of family ownership, control and management can differ among individual firms.[49]

2.51 Several consultancy firms also emphasised that a definition of family business must be based on family members being both the owners and managers of a business. For example, Mr Robert Powell of Grant Thornton Australia proposed a definition of family business where there are at least two family members involved in management and the family controls the business through voting rights.[50] Similarly, KPMG recommended a formal definition of family business that recognises 'the unique characteristic of family business owners as both the owners of equity/capital and managers of the business'.[51] Mr Paul Brassil, a partner at PricewaterhouseCoopers, proposed a definition where the family has 'a significant percentage of ownership of the business' and where 'the family is predominantly in control of the direction of the business'.[52]

2.52 Deloitte Private also argued that a definition of family business should be based on recognition of family ownership and control of the business. In its submission, Deloitte contrasted 'private business' from public corporations. It noted

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45 B. Bernard, 'The development of organization structure in the family firm', *Journal of General Management*, Autumn, 1975, p. 42.

46 L. B. Barnes and S. A. Hershon, 'Transferring power in the family business', *Harvard Business Review*, 54(4), 1976, p. 106.

47 P. Davis, 'Realising the potential of the family business', *Organizational dynamics, 12(1)*, 1983, p. 47.

48 P. G. Holland and J. E. Oliver, 'An empirical examination of stages of development of family business', *Journal of Business and Entrepreneurship*, 4(3), 1992, p. 27.

49 Mr Francesco Barbera, *Submission 3*, p. 3.

50 Mr Robert Powell, Partner, Grant Thornton Australia, *Committee Hansard*, 15 November 2012, p. 12.

51 KPMG, *Submission 21*, p. 6.

52 Mr Paul Brassil, Partner, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 26.

that in the case of public corporations, ownership is offered to the public and decision-making and management is outsourced to employees overseen by a board of directors appointed by shareholders. In private companies and family businesses, by contrast, every decision 'directly affects the welfare and wealth of the family or families who own the business and the ability of the business to support the family members now and in future generations'.[53]

2.53 Deloitte noted the broad scope of this definition. Mr David Hill, a partner at the firm, stated that a definition based on family involvement in both the ownership and management of a business:

> …could extend right through to listed companies where the family either controls the business through their shareholding or controls the composition of the board. That could go from the corner deli through to very large listed companies which remain under the control of the broader family either in terms of the composition of the board or via their voting rights or their shareholding. I think any attempt to come up with a common agreed definition needs to recognise that that is the reality of the breadth of family business in Australia.[54]

2.54 KPMG made essentially the same point. While the lack of separation of ownership and management is a defining characteristic of a family business (compared to a publicly owned business), a family business may become publicly owned with the family maintaining a controlling interest. KPMG argued that in these cases, the family may still see its involvement as being part of the family business despite outside shareholder influence. It added:

> It may be necessary to contemplate the continuation of the 'family business' as both a closely held 'private' entity and also a more widely 'held' public entity providing the organisation can demonstrate that there exists a significant level of family influence.[55]

The European Commission's definition of family businesses in company form

2.55 The committee is also aware of a definition of family business first proposed in 2006 by the Family Entrepreneurship Working Group, which was established by the Finnish Ministry of Trade and Industry in 2004.[56] In November 2009, the

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53 Deloitte Private, *Submission 16*, p. 3.

54 Mr David Hill, National Managing Partner, Deloitte Private, *Committee Hansard,* 14 November 2012, p. 6.

55 KPMG, *Submission 21*, p. 5.

56 Ministry of Trade and Industry, Government of Finland, 'Family Entrepreneurship: Family enterprises as the engines of continuity, renewal and growth-intensiveness', 2006, http://julkaisurekisteri.ktm.fi/ktm_jur/ktmjur.nsf/All/E7E75135A895485BC2257123003F5221/$file/jul7elo_2006_netti.pdf (accessed 12 February 2013).

European Commission's (EC) Expert Group on Family Business endorsed the Finnish Working Group's definition. The definition is as follows:

> A firm, of any size, is a family business if:
>
> 1. the majority of decision-making rights is in the possession of the natural person(s) who established the firm, or in the possession of the natural person(s) who has/have acquired the share capital of the firm, or in the possession of their spouses, parents, child or children's direct heirs.
> 2. The majority of decision-making rights are indirect or direct.
> 3. At least one representative of the family or kin is formally involved in the governance of the firm.
> 4. Listed companies meet the definition of family enterprise if the person who established or acquired the firm (share capital) or their families or descendants possess 25 percent of the decision-making rights mandated by their share capital.
>
> This definition includes family firms which have not yet gone through the first generational transfer. It also covers sole proprietors and the self-employed (providing there is a legal entity which can be transferred).[57]

2.56 This definition differs from the FBA's and MGI Australasia's in several respects. First and significantly, it explicitly notes that a family business can be a firm 'of any size'. Second, instead of a broad reference to a 'controlling interest', it refers to 'the majority of decision-making rights'. Third, there is an explicit reference to one member being involved in the 'governance' of the firm. Fourth, in keeping with the definition of a 'firm of any size', there is reference to a family business being a listed company provided the founder or their descendants have at least a quarter of decision-making rights. And finally, unlike the other definitions, there is the reference to sole proprietors and the self-employed being family businesses, and to firms 'that have not yet gone through the first generational transfer'.

2.57 It would seem that the detail in the EC's definition is its obvious strength. It clarifies some of the issues that are essentially left open to interpretation in the FBA's and MGI Australasia's definitions. The EC's definition explicitly acknowledges the diversity of family businesses' size and structure. As the remainder of this chapter emphasises, this issue of the sector's diversity is important to many stakeholders.

2.58 In this context, another observation is that many of the ABS' concerns with the lack of detail in the FBA's definition seem to be addressed by the EC's definition:[58]

57 First published in the *Final Report of the Family Business Expert Group to the European Commission: Overview of family-business-relevant issues: research, networks, policy measures and existing studies*, November 2009, http://ec.europa.eu/enterprise/policies/sme/promoting-entrepreneurship/family-business/family_business_expert_group_report_en.pdf (accessed 1 March 2013). See KPMG, *Submission 21*, p. 6.

- The ABS queried whether the FBA's reference to 'involved in the business' was to legal involvement or operational involvement. The EC's definition makes explicit reference to 'governance of the firm'.
- The ABS was concerned with whether 'family members' refers to immediate family or extended family. The EC's definition makes clear reference to 'spouses, parents, child or children's direct heirs'.
- The ABS questioned the meaning of 'controlling interest' in the FBA's definition and whether this referred to the financial stake, the strategic direction or the ownership of the firm. The EC's definition clearly states that the family must have a majority of decision-making rights or at least a quarter of these rights if it is a listed company.

2.59 While the EC's definition is detailed, it relates only to family businesses in company form. The committee draws attention to the thresholds set in the EC's definition. If the EC's definition is to be used as a guide in the Australian context, these thresholds will need to be carefully considered: should the decision-making rights thresholds be set at these levels; should the 'majority of decision-making rights' threshold extend more broadly than to 'spouses, parents, child or children's direct heirs'; and should sole traders be included?

Are sole traders family businesses?

2.60 Another issue relevant to the question of a definition is whether sole traders should be considered a family business. While the sole trader is the business owner and trades in their own name, he or she often employ their own staff which can include family members. Sole traders account for a sizeable portion of all Australian businesses. ABS data indicates that 33 per cent of all Australian businesses are companies, 29 per cent are sole proprietors, 22 per cent are trusts and 16 per cent are partnerships.[59] The Australian Bureau of Agricultural Resource Economics and Sciences (ABARES) told the committee that roughly one in five family farms are operated as sole traders, a higher proportion than family farms run by trusts and

58 See Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 19.

59 Australian Bureau of Statistics, *Counts of Australian Businesses, Including Entries and Exits, June 2007 to June 2011*, Cat No. 8165.0, released 31 January 2012, p. 7.

corporate structures.[60] Partnerships are the dominant form for family farms in Australia.[61]

2.61 There does appear to be a case for including sole traders in a definition of family business to recognise those businesses with a single owner but with a family member or members working in the business. Regional Development Australia (RDA) told the committee:

> …if information were collected, depending on the definition that you use…you could have someone who is effectively a sole trader who has a family and has all the other characteristics associated with what you would want to know in a region.
>
> So just getting family owned businesses where you might have several members of that family involved does not necessarily mean that you should not also be looking at, for example, sole traders, because they could also have family, children, social engagement and all those other things.[62]

2.62 The ABS similarly raised the inclusion of sole traders in a definition of family business as a possibility. Mr Allen told the committee:

> We are not saying they [sole traders] need to be included. They just need to be considered and whether it is appropriate for their inclusion depending on the information needs. We have had instances where a family can be a family of one. We are not prejudging. We are just making sure that the policy implications are considered with that group in mind.[63]

2.63 Mr Matthew Power, a family business owner based in Canberra, claimed that the issue of including sole traders as family businesses is a matter of perception. He told the committee that:

> …when we speak to sole operators they forget about the fact that their wives, children and cousins are involved in what they do. Probably the only ones I can think of are the one-person consultancies, where they literally go

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60 Mr Peter Martin, Policy Officer, Australian Bureau of Agricultural and Resource Economics and Sciences, *Committee Hansard*, 13 November 2012, p. 40. The National Farmers Federation noted that as farm businesses become more complex in operation and larger in size, there has been a gradual shift in operating structures from sole trader and partnership, to more operating in a trust or company structure. *Submission 29*, p. 9.

61 Mr Peter Martin, Policy Officer, Australian Bureau of Agricultural and Resource Economics and Sciences, *Committee Hansard*, 13 November 2012, p. 40.

62 Mr Shane Bennett, Assistant Secretary, Economic and Infrastructure Policy, Department of Regional Australia, Local Government, Arts and Sport, *Committee Hansard*, 13 November 2012, p. 35.

63 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 20.

> in, write a report and leave. But even then, you sit at home in your study, your wife brings you a cup of tea, she's the one answering the phone—[64]

Committee view

2.64 The committee is interested to receive from the ABS an estimate of how many sole traders would be likely to fall within a definition of family business based on 'at least one family member' working in and owning the legal entity. It also seeks advice from the ABS on how this number would be likely to change if a definition required:

- at least two family members working/involved in the business, with ownership of the entity by at least one family member (as per the FBA and MGI definitions).

2.65 Including or excluding sole traders in a definition can significantly alter the number of family business that are identified. The committee draws attention to comments made in the 2006 study by the Finnish Ministry of Trade and Industry, with reference to a 2002 survey of Finnish businesses:

> If estimated using a structural and a subjective indicator, a significantly higher proportion of Finnish enterprises are family enterprises compared to the estimates using a functional or a generational-transfer indicator. A closer examination of the material shows that the difference is mainly caused by sole-proprietor businesses, which comprise approximately 40 per cent of Finnish enterprises (number of personnel in companies in 2003). It is also difficult regarding the definition if family members are involved in the sole proprietor’s business activities as wage-earners or as owners.[65]

The possibility or the intention to pass on the business

2.66 Another possible element of a definition of family business is the potential and/or the intention of the family to pass the business on to the next generation. This is a complex issue. In evidence to the committee, Mr Barbera reflected on this complexity:

> I am lecturing a class here at Bond that is called 'Understanding the family enterprise', and in the first week we deal with this issue of definition. Technically, according to Poza, the textbook that we are using, the family firm does not become a family firm until the next generation, the children of the founders, are somehow involved; then you can call it a family business. What I am suggesting is that just the intention alone to involve your children, whether or not they are currently involved, would constitute your business to be a potential family business. Of course, those intentions

64 Mr Matthew Power, ACT Chairman, Family Business Australia, *Committee Hansard*, 13 November 2012, p. 49.

65 Ministry of Trade and Industry, Government of Finland, *Family Entrepreneurship: Family enterprises as the engines of continuity, renewal and growth-intensiveness*, 2006, p. 23.

> can change at any given moment; in fact, depending on when you ask them, those intentions may be different. So that relates back to the trickiness of it, the complexity of it.
>
> There are multiple ways of doing it. As I said, typically, what we would do is take a structural based approach and look at who is holding the equity; is it a controlling ownership stake; and, subsequent to that, are there intentions to either increase or decrease the family relatedness or inter-relatedness in this particular firm across multiple generations. So, yes, I agree it is a problem. It has always been a problem in this discipline and it is one that I do not think is going to be solved any time soon.[66]

2.67 A 1987 article in the *American Journal of Small Business* defined a family business as one that had either already been passed on to the next generation, or anticipated to do so:

> What is usually meant by family business is either the occurrence or the anticipation that a younger family member has or will assume control of the business from the elder.[67]

2.68 In a 1988 book, Professor John Ward defined all family firms specifically as those that will be 'passed on for the family's next generation to manage and control'.[68] The same year, an article published by Ivan Lansberg, Edith Perrow and Sharon Rogolsky suggested that the key to defining a family business was the potential for inter-generational transfer.[69] They proposed the following definition:

> A family business is a business in which related family members control the ownership, vision and direction and which is potentially sustainable across generations of the family.[70]

2.69 In his evidence to the committee, Professor Kenneth Moores of Moores Family Enterprise, emphasised the need for a definition of family business to be based on the issue of succession. He argued that a definition of family business must recognise:

> …their essence, and that is their intention to maintain this across generations over the longer term. Until you have crossed that particular

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66 Mr Francesco Barbera, *Committee Hansard*, 16 November 2012, p. 37.

67 N. C. Churchill and K. J. Hatten, 'Non-market based transfers of wealth and power. A research framework for family businesses', *American Journal of Small Business,* vol. 11, no. 3, 1987, pp 51–64.

68 John Ward, *Keeping the Family Business Healthy*, San Francisco, Jossey-Bass, 1987. John Ward, 'The Special Role of Strategic Planning for Family Businesses', *Family Business Review*, vol. 1, no. 2, 1988, pp 105–117.

69 Mr Francesco Barbera, *Submission 3,* p. 1.

70 Family Business Australia, *Submission 1*, p. 2; I. Lansberg, E. L. Perrow and S. Rogolsky, 'Family Business as an Emerging Field', *Family Business Review*, vol. 12, no. 1, 1988, pp 39–46.

> rubicon, I do not think you actually are a family business. If you are a family in business and have a lot of people working in the business, you have many of the issues. But when the penny drops and you say, 'We want to keep this,' there intrude many more of the issues that highlight the difference of this sector of the economy.[71]

2.70 The FBA and MGI Australasia definitions are silent on this issue of the capacity or the intent to pass on the business to the next generation. The EC's definition mentions that it applies to firms that have not gone through the first generational transfer. On the other hand, a proposed definition by the German Wittener Institute fur Familienunternehmenas, emphasised:

> The transgenerational aspect is essential to a family business. For this reason, it is strictly speaking only correct to refer to a company as a family business if the family is planning to hand down the company to its next generation. Start-ups and owner-managed companies are therefore not yet family businesses in their own right.[72]

2.71 Some submitters to this inquiry also argued that a definition should refer to the transgenerational nature of family businesses. Mr Lowe, for example, told the committee:

> I think there is a need to reference in some way the transgenerational nature of the family business…I would think the intention of having sustainability and tenure is a core objective of both family and non-family firms, but it is the handing down and passing on of the business to continue the IP and give the family firm a competitive advantage that needs referencing in a formal definition.[73]

2.72 However, the FBA disagreed that an intention to pass on the business should be part of a definition. Ms Taylor described this aspect as an 'unnecessary complication'. She told the committee:

> I do not believe it should be included. I do think that when a family business starts and maybe is into its first decade of business, the intention to continue as a family business might not be there. You might also find that the founders and owners do not at that stage have children who have indicated that they are ready, willing and able. But that can change as time goes on. We have found within our family business community that family businesses have come to our conferences and been inspired by what has been achieved by second, third and fourth generation businesses and have turned their thinking around. They subliminally, maybe, have thought that

71 Professor Kenneth Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 17.

72 Cited in KPMG, *Submission 21*, p. 5. See http://www.wifu.de/en/research/definition-of-family-business/ (accessed 1 March 2013).

73 Mr Chris Lowe, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 14.

> they might sell the business once they have made enough money to survive on it and they have then changed their thinking.[74]

Committee view

2.73 Whether a definition of 'family business' should be framed around the intention, or the event, of passing the business on to the next generation is an important but difficult question. Clearly, without a definitional requirement of intending to pass the business on, there will be many 'families in business' classed as a 'family business'. On the other hand, if a definition requires that the business has at least been transferred to the second generation, there will be comparatively few businesses in Australia classed as a family business. As the 2006 study by the Finnish Ministry of Trade and Industry observed: '[T]he stricter a definition of a family enterprise is used, the older a family enterprise often is'.[75]

2.74 Between these extremes, there are other possibilities to consider. If a family business is to be defined as one that could be passed on to the next generation, there will be many businesses captured by the definition that may in fact never reach the hands of a second generation. The same is true if a definition is based on the intent to pass the business on.

2.75 In both these cases, the definition of a family business would rely on the businesses themselves 'self-identifying'. In terms of official data collection, this seems unsatisfactory. If a survey simply asked respondents whether they could, or intended to, pass on the business, and if on this basis they are classified as a family business, one might expect many respondents to do so. This would particularly be true if respondents thought there would be some public policy benefit from self-identifying.

2.76 Short of restricting the definition of a family business to second and later generation businesses, a definition could require that the business have in place a succession plan. In other words, the intention alone is not enough; there needs to be a formal plan in place for the business to be classed as a family business.

2.77 This requirement is certainly a higher threshold than merely the possibility or the vague intention of passing the business on. As discussed later in this chapter, the committee believes that a formal definition of 'family business' in Australia must carefully consider the public policy rationale for a definition. If the policy rationale is

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74 Mrs Philippa Taylor, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 32.

75 Ministry of Trade and Industry, Government of Finland, *Family Entrepreneurship: Family enterprises as the engines of continuity, renewal and growth-intensiveness*, 2006, p. 23. The study referred to a 2003 paper which found that only 18 per cent of firms surveyed had been transferred from one generation to the next. J. Heinonen and J. Toivonen, Perheyritykset suomalaisessa yhteiskunnassa. Teoksessa Heinonen, J. (toim.) Quo Vadis, suomalainen perheyritys? Turun kauppakorkeakoulu, PK-Instituutti, 2003.

to assist businesses that have made clear and concrete plans to succeed, the committee believes that a definition should require evidence of a succession plan.

Should a definition include small and large family businesses?

2.78 Another matter considered by the committee in terms of defining a family business is whether a threshold is needed to distinguish between small family businesses on the one hand and large family-based corporations on the other. Some submitters noted that without a threshold—however framed—a definition of family business would be too broad and untargeted for public policy purposes. DIISTRE told the committee:

> …family businesses can be across all ranges of structures. They can be small or they can be multinational. So it is difficult to see how a definition of a family business could apply equally to a corporation like Westfield, for example, and to a family business located in the suburbs...[76]

2.79 Treasury was asked whether in its view, a local corner store and a multi-billion corporation have common traits where they are both family-owned entities. It responded:

> I could make the comment—and this is purely from a tax perspective—that the tax issues that a large globally competitive company is likely to face are significantly different from the tax issues that I imagine a small partnership in a suburb is likely to face. I guess that is from the perspective of the business; I imagine they are going to have a very different set of preferences around their interaction with the tax system and a very different set of capacities to engage with it.[77]

Committee view

2.80 The committee recognises that the question of whether to set a definitional threshold based on numbers employed or annual turnover has polarised opinion during this inquiry. While it may be true that most family businesses are SMEs, a definition without a size threshold would also find many large companies that are family businesses. These businesses are often highly successful and have gone through intergenerational transfer. There is an argument that it is these large businesses that embody what a family business is, and there should therefore be no size threshold within the definition. On the other hand, as the following section of this chapter emphasises, the setting of a threshold in an official definition of family business

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76 Mr Peter Chesworth, Acting Head, Small Business Division, Department of Industry, Innovation, Science, Research and Tertiary Education, *Committee Hansard*, 13 November 2012, p. 2.

77 Mr Hector Thompson, General Manager of the Small Business Tax Division, Treasury, *Committee Hansard*, 13 November 2012, p. 13.

should be based on how policy makers intend to use the data. If their focus is only to be on SMEs, there may be a case for a definition with a size threshold.

2.81 The committee does recognise that policy makers' use for data must acknowledge stakeholders' concerns and needs. Government agencies need to be aware of the extent to which family business issues differ between medium and large sized businesses and small businesses. To some extent, this will require consultation with these businesses.

Public policy reasons for a definition of family business

2.82 There is already a policy framework and statistical basis upon which to consider the needs of small and medium sized enterprises (SMEs) and large corporations. The key issue, therefore, is to identify the particular public policy needs of family businesses.

2.83 This issue was considered by the EC Expert Group in its November 2009 report. It noted the following six areas of policy interest:

- there is limited awareness among policymakers of the contribution that family businesses make to the economy and society. A commonly recognised definition of family business 'would significantly help overcome this challenge';
- family businesses face specific financial challenges related to succession and the choice of financing method. It noted that national governments may consider issuing regulations to grant access to finance for family enterprises, without threatening decision-making powers within the company;
- family businesses must prepare for succession which is widely viewed as the most important issue facing family businesses. The EC report argued that the main issue to enable succession is to raise awareness of the importance of early preparation and to make training available for the transfer. It claimed that this type of initiative is best undertaken at a local level or by private sector organisations;
- family firms require a 'special type of management' which minimises potential tensions between the family and business aspects. The report argued that governments need to raise awareness of these governance issues and the tools that are currently available;
- there is a need to improve the image of family businesses in the labour market to overcome perceptions that they are nepotistic, paternalistic and fail to offer career opportunities; and

- national governments need to develop family business-specific courses as part of existing curricula or as new curricula.[78]

2.84 In a 2010 article, Dr Linda Glassop of Deakin University gave an Australian context to these areas of policy interest.[79] She argued that establishing the significance of family businesses to the Australian economy requires an operational definition of family business and data on the number of businesses by legal status, industry, region, revenue size and employment size. She noted that only then can research be conducted on the extent to which owner relationships affect business practices (including governance, employment, operations, risk-taking and innovation).[80]

2.85 The committee recognises that the EC's list is by no means comprehensive. There will be other areas of policy interest as well as several elements within the six mentioned above that deserve closer attention from policy makers.

2.86 For example, there is a useful discussion that Australian government agencies could have on the economic benefits of succession. Several witnesses to this inquiry have argued the need for this discussion.[81] The committee suspects that Australian policy makers have not given adequate consideration to the possible benefits of succession to the economy. The view could be that whether business owners pass on to the next generation or sell to the highest bidder is a matter of judgment for the business owners. As Treasury told the committee:

> …if they have a succession plan or not, many businesses will simply hit a point whereby they enter into negotiations for sale. They will sell the business as an ongoing concern to someone else. The point from a productivity perspective is that this may result in a possible loss of corporate knowledge. That is going to be heavily dependent on the transition between the new buyers and the existing sellers. From an economy-wide perspective, if you make the assumption that these businesses are viable, then, arguably, they should be being sold and you should have a smooth transition. Having said that, and speaking from a personal perspective, I think it would be good business practice to have transition plans in place.[82]

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78 First published in the *Final Report of the Family Business Expert Group to the European Commission: Overview of family-business-relevant issues: research, networks, policy measures and existing studies*, European Commission, November 2009, pp 11–18.

79 Dr Linda Glassop, *Family owned businesses: Perspectives on Australian policy*, http://dro.deakin.edu.au/eserv/DU:30031227/glassop-familyownedbusinesses-2010.pdf (accessed 1 March 2013).

80 Dr Linda Glassop, *Family owned businesses: Perspectives on Australian policy*, p. 4.

81 See for example, Mr Yasser El-Ansary, General Manager, Leadership and Quality, Institute of Chartered Accountants, *Committee Hansard*, 14 November 2012, p. 21.

82 Mr Michael Wilson, Analyst, Small Business Tax Entities Unit, Treasury, *Committee Hansard*, 13 November 2012, p. 11.

2.87 This type of comment suggests to the committee that government agencies would benefit from focused discussion on the economic benefits of succession planning, particularly within sectors such as farming. It may well be that government agencies form a view that there is no discernible economic benefit from ensuring that a family business is passed on. It may well be that a business can survive and perform better in the hands of an unrelated buyer, rather than a reluctant successor. Nonetheless, the committee believes that based on the discussions during this inquiry, it is worthwhile for policy makers to have this debate.

The committee's conclusions on an Australian definition of family business

2.88 The committee believes there is merit in scoping an official definition of family business in Australia. The case for this view is developed throughout this report, noting as it does the unique characteristics of these businesses and their contribution to economic activity. As the following chapter outlines, these characteristics and contributions have not been reliably measured to date. However, a definition of family business should not be developed merely to satisfy curiosity—the committee stresses that any effort to develop a formal definition of family business and devise survey questions must be principally based on clear policy objectives.

2.89 In conducting this inquiry, however, the committee has observed that consideration of how family businesses fit within the broad policy framework is generally not as well-advanced as it is for other groups, such as small businesses. While family businesses have certainly not been ignored, this inquiry has perhaps been the first occasion that multiple government departments and agencies have been required to directly turn their attention to family business issues. This has allowed a preliminary discussion on policy implications; however, there is a need for this to be continued.

2.90 Given the committee's view that a formal definition of family business needs to be linked to policy objectives, the committee believes that there is a need for officials to further consider the policy areas that are particularly relevant to family businesses. Following this, a clear definition of family business and ABS survey questions that are useful for policy development can then be framed. Accordingly, the final part of this chapter considers the process through which an official definition of family business should be developed. The committee acknowledges the complexity of this task, and argues the need for a systematic process of consultation and analysis.

An Inter-Departmental Committee

2.91 The committee recommends that a formal definition of family business should be based on a collaborative process involving key government agencies. This should take the form of an Inter-Departmental Committee (IDC). The agencies on the IDC should include—but should not be restricted to—the Treasury, DRALGAS, the Australian Taxation Office, DIISTRE, the Department of Resources, Energy and

Tourism, the Department of Education, Employment and Workplace Relations and ABARES. The ABS should be an active participant on the IDC throughout.[83]

Recommendation 1

2.92 The committee recommends that an Inter-Departmental Committee (IDC) be established to identify the policy issues facing family businesses that are not adequately captured within the existing policy framework and with existing Australian Bureau of Statistics (ABS) data collection. The IDC should include: the Department of Industry, Innovation, Science, Research and Tertiary Education; the Treasury; the Australian Taxation Office; the Australian Bureau of Agricultural Resource Economics and Sciences; the Department of Resources, Energy and Tourism, the Department of Regional Australia, Local Government, Arts and Sport; and the Department of Employment, Education and Workplace Relations. The ABS should also participate in the IDC.

The first phase—the policy need for data

2.93 The IDC's principal objective must be to identify the public policy need for data relating specifically to 'family businesses'. Each agency on the IDC should address the following questions:

(i) what has been the agency's *past* need for—or interest in—data relating specifically to businesses that are owned and operated by a family?

(ii) to what extent has the particular need/interest for family business data related specifically to:

- the economic contribution of family businesses;
- their contribution to employment;
- workplace relations issues;
- the productivity of family businesses;
- taxation and trust matters;
- governance structures (such as the presence of a succession plan);
- superannuation arrangements, particularly for women involved in family businesses;
- technological innovation;
- rural and regional policy; and

83 The committee thanks the ABS for its explanation as to how it approaches the task of forming a national definition for government clients. *Correspondence received 27 February 2013*.

- behavioural considerations (such as the propensity to reinvest profits, levels of indebtedness)?

(iii) to what extent is there international data on family business based on these indicators that the agencies find useful, and to what extent is it important that there is consistency with the format of this international data?

(iv) to what extent have agencies shared a need for, or interest in, information based on these indicators?

(v) to what extent could the agency find *future* use for data on family businesses based on these indicators, and what is the shared need/interest for this information?

(vi) has there been, or could there be, a need for the agency to distinguish between small, medium and large family businesses?

(vii) what is, or what could be, the specific public policy need to distinguish between small, medium and large family businesses?

Recommendation 2

2.94 The committee recommends that the initial focus of the Inter-Departmental Committee (IDC) must be on the specific public policy need for these agencies to identify a family business as distinct from a non-family business. In terms of the policy rationale for a survey (and a definition of family business), the committee recommends that the IDC carefully consider the following issues:

(a) the need for policy makers to identify the number of family businesses that are small businesses, and if so, whether the definition of small business should be based on the threshold used for tax purposes (annual turnover of less than $2 million) or the ABS's threshold of fewer than 20 employees;

(b) the extent to which a definition of family business needs to capture employment data, and the possible effect that different thresholds in the definition will have on the number employed;

(c) the importance of succession as a policy objective and the need for a definition to identify whether the owners could pass the business on, whether they intend to pass it on, whether they have a formal plan to do so;

(d) the need for policy makers to identify first, second, third and later generation family businesses;

(e) the need for policy makers to identify the industry and location of the family business;

(f) the need for policy makers to identify the number of family businesses from culturally and linguistically diverse communities;

(g) the need for policy makers to identify the number of non-employee shareholders in a family business and, therefore, the need for data on the number of family businesses that are proprietary companies as opposed to unlisted public companies; and

(h) the need for policy makers to collect data on the superannuation arrangements of family businesses, particularly the evidence that female family members do not have adequate superannuation arrangements in place.

2.95 While the committee emphasises the key role of the IDC as a mechanism for policy discussion on all these issues, it is also important that stakeholders have a voice in this process. The IDC should periodically consult with key stakeholder groups to ensure that the IDC registers and considers their views. A good example of the need for consultation is in relation to recommendation 2(g) (above). As Chapter 7 of this report discusses, this issue of the number of non-employee shareholders and how this affects the business' legal structure, is an issue of stakeholder concern. Consultation with stakeholders should occur within the IDC process.

Recommendation 3

2.96 The agencies represented on the Inter-Departmental Committee should periodically consult with key stakeholder groups to seek their input and feedback on the issues it is discussing. These groups should include Family Business Australia, the Australian Chamber of Commerce and Industry, the Council of Small Business of Australia and the National Farmers' Federation, and consider engaging other peak bodies that may be nominated to represent family businesses of differing sizes.

Recommendation 4

2.97 The committee recommends that the Inter-Departmental Committee report its findings to the Minister for Industry and Innovation within six months of it being established.

The second phase—scoping a survey

2.98 If the agencies do identify sufficient need to collect and use official data on the family business sector, the next task of the IDC should be to discuss these outputs or measures with the ABS.[84] In correspondence to the committee, the ABS explained its process for identifying these outputs:

84 The committee understands that the ABS often convenes a 'reference group' to discuss with key agencies the possibilities of a definition and a survey. The committee believes that if the proposed IDC does agree that there is a specific policy need to proceed with a survey, the IDC should fulfil the role that the reference group normally would. The committee also suggests that when the IDC reaches the stage of discussing the type of survey questions, it would be useful for key academics to be involved in these discussions.

> When considering whether a particular survey vehicle is appropriate to consider asking a new question, firstly there has to be an understanding of what outputs or measures are required. This includes whether the survey vehicle has the scope and coverage for the desired outputs to be at the required level of disaggregation. This includes whether the scope of the survey covers the population of interest and whether the coverage provides for the data to be available by industry, business size, geography (e.g. state, regional) for what is required by the end users.[85]

2.99 Having identified the agencies' use for the data, the ABS then determines what questions would best yield these results. As the ABS explained:

> Does the data need to only provide high level metrics of information or is further detail needed, for example, with family businesses is it just a raw count that is required or is information needed on the business structure and management, inter-generational involvement or future intentions of the business?
>
> …
>
> The ABS then develops appropriate questions (and response options) that will inform these policy areas. This includes seeking advice from internal experts on form design and methodology to reduce the potential of non-sampling error, such as poor layout, ambiguous or offensive questions, inadequate instructions and so on. Expert ABS areas provide the survey area with formal feedback on every survey form, with particular focus on new questions being tested.[86]

2.100 The committee suggests that the format of a survey to identify and gather information on family businesses needs to use two sets of questions:

- those that are fundamental to determining whether a respondent is a family business; and
- those that further inform policy makers (as distinct from defining whether the respondent is a family business).

2.101 Table 2.3 presents a range of issues according to this division of 'definitional issues' that are fundamental to determining whether the respondent is a family business (column 2). The key definitional issues relate to the size and composition of the business and its governance structure. There are also several information issues relating to size/composition and governance of the business that the IDC and the ABS may want to consider (column 3).

2.102 A key area of discussion for participants on the IDC will be how the thresholds set on the various definitional issues will impact the data set. Including sole

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85 Australian Bureau of Statistics, *Correspondence received 27 February 2013*.

86 Australian Bureau of Statistics, *Correspondence received 27 February 2013*.

traders will inflate the number of family businesses, as will a broad interpretation of 'family members'.

2.103 The committee recognises the expertise of the ABS in devising survey questions and definitions based on its clients' intended use for the information, and with an eye to international data and definitions.

2.104 In its evidence to the committee, the ABS commented on some of the practicalities in collecting official data on family businesses. It made the following points:

- first, the ABS noted that if a question on family business was to be included in the BCS, existing questions would need to be cut;[87]
- second, the ABS noted that there is more interest among key stakeholders, such as DIISTRE and Treasury, in many of the existing questions in the BCS than in data on family businesses;[88]
- third, and relatedly, the ABS told the committee that in terms of eliciting responses on family business, there would need to be 'quite a few questions to draw out the concept properly';[89] and
- fourth, if the family business questions could not be included in the BCS, the ABS noted that it would need to look at additional funding options.[90]

2.105 The committee believes that if the government does proceed with the formal collection of ABS data based on a definition of family business recommended by the IDC, this process should be incorporated into the existing BCS. It is important that the process be as efficient as possible, both from the perspective of public administration and respondents' time. There should be a set of clear and targeted questions which reflect the policy need for the data, and which are most likely to present policymakers with evidence for possible action.

Recommendation 5

2.106 The committee recommends that when collecting official data based on a formal definition of family business, the ABS should incorporate a set of clear and targeted questions into the Business Characteristics Survey. The intent must be to deliver the survey as efficiently as possible, including to limit the time taken by respondents to complete the survey.

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87 Australian Bureau of Statistics, *Submission 2*, p. 2.

88 Ms Jacky Hodges, Regional Director, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 18.

89 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 18.

90 Ms Jacky Hodges, Regional Director, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 18.

Issue	*Definitional issues (critical)*	*Information issues (useful)*
Size and composition	the **number of family members** employed in the business (should a definition include sole traders if there are family members informally employed in the business?); the **definition of 'family'** and whether 'family' should include de facto members and extended family (should it be consistent with definitions of 'related' in the Income Tax Assessment Act?)	the number of family and non-family members employed in the business; whether the survey should ask: 1. if the business is small, medium or large with reference to the existing ABS definitions of these terms 2. if the business is a public company (more than 50 non-employee shareholders) 3. if the business has an annual turnover of more than $2 million
Governance	whether the definition of 'family business' should refer to **'control'** and if so: 1. whether this term needs to be consistent with existing definitions in Australian statute (section 50AA of the Corporations Act); 2. whether a definition should refer to a 'controlling interest by one or more related members (FBA and MGI Australasia) whether the definition of 'family business' needs to refer to **'owned'** and if so, whether to refer in the survey to having a majority of the equity whether the definition of 'family business' should also refer to **'managed'**, and if so, how should this be measured (eg: majority of decision-making rights; working in the business) whether the definition should require at least one representative of the family is formally involved in the governance of the firm among first generation owners, whether they **intend to pass the business on** to the next generation	whether the business is owned by the first, second, or later generation whether the business has a Board of Directors presence of a formal Strategic Plan establish and annually review a succession plan superannuation arrangements and whether all family members have superannuation arrangements in place whether female family members are involved in the governance of the business
Finance		reliance on equity rather than debt capital
Performance		the productivity and profitability of the business
Location and sector		the principal industry/sector and region in which the business operates

2.107 The ABS informed the committee that the final stage of the survey development process involves field testing the questions:

> These new questions are then field tested on a range of business types, size and industry groups. The measures for determining whether a new question will be included on the next iteration of the BCS are:
>
> - the data needs of users;
> - the level of accuracy needed, the availability of the data from the respondent, the language appropriate for respondents, data item definitions, standard question wordings and any other relevant information e.g. accounting standards, ABS classifications;
> - the office processing system you are using, including editors, data entry staff, OCR [Optical Character Recognition] etc;
> - the sequencing, or order of questions; and
> - the answer space required for each question.[91]

Final comment

2.108 The committee's key recommendation is that an IDC be established to discuss the public policy need for data relating to family businesses in Australia, which will inform a definition of family business. The committee hopes that the evidence it has gathered during the course of this inquiry will be a useful reference point in the IDC's deliberations.

2.109 The committee recognises that there are key threshold questions relating to the definition of family business on which the IDC—in discussion with the ABS—should form a view. Including sole traders and extended family in a definition will increase the number of businesses that are family businesses. Requiring at least the intent to pass the business on, and limiting the definition to under a certain employee or turnover threshold, will reduce the number of businesses defined as a 'family business'. These are potentially very complex considerations. The committee emphasises that in making these decisions, agencies need to consider carefully their need for the data, how it will be used and whether it should be in a form that matches available international data.

91 Australian Bureau of Statistics, *Correspondence received 27 February 2013*.

Chapter 3

The availability and reliability of information and statistics on family business

I am nervous about all of these numbers because I think the only really reliable statistics are those that come from the ABS.[1]

For targeted policy on family businesses…if that were the intention, the collection of consistent, reliable data on family businesses would be very important.[2]

The availability of reliable information is essential to make policy makers…aware of the importance of the family business sector, and to advocate favourable action.[3]

Introduction

3.1 The second article of the terms of reference draws the committee's attention to the availability and reliability of information and statistics about family business in Australia. This chapter considers the data that is available on Australian family businesses and makes some observations about the dependability of these survey findings. Consistent with the recommendations in chapter 2, the committee does not seek to define what official data should be available: this is a matter for government.

3.2 The lack of reliable data is not unsurprising given there is no official definition of family business. In the absence of a formal definition and official data, consultancy and advisory firms have undertaken their own research and analysis. The analysis of family business in Australia has therefore developed in a fragmented way, through surveys that have produced interesting but questionable findings.

3.3 This chapter has two parts:

- the first presents the findings of various consultancies' surveys and some limited data from the Australian Bureau of Statistics (ABS); and

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1 Professor Ken Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 20.

2 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 13 November 2012, p. 22.

3 European Commission, *Final Report of the Family Business Expert Group to the European Commission: Overview of family-business-relevant issues: research, networks, policy measures and existing studies*, November 2009, http://ec.europa.eu/enterprise/policies/sme/promoting-entrepreneurship/family-business/family_business_expert_group_report_en.pdf

- the second part presents submitters' and witnesses' views on the reliability and accuracy of this research and their opinion as to whether, and if so what, official data is needed.

A patchwork of surveys

3.4 Over the past 20 years, an assortment of unrelated surveys has been conducted into various aspects of family businesses in Australia. Even among surveys conducted by the same research organisation, the methodology and even the definition of 'family business' has changed over time; the questions have changed from one survey to the next; the sample sizes have often been low; and some of the data is quite dated while the newer official data has restricted access. These factors compromise the reliability and utility of the findings.

3.5 Nonetheless, the committee believes it is useful to sketch in this report some of the key findings of these surveys. The committee recognises that while the reliability of the findings can be questioned, they do highlight the areas that might interest and inform policy makers (see chapter 2). The following section presents selected findings from:

- the ABS' Business Longitudinal Survey (BLS) and Business Longitudinal Database (BLD);
- the MGI Australian Family and Private Business Surveys, conducted by Professor Kosmas Smyrnios of the Royal Melbourne Institute of Technology (RMIT);
- the Family Business Australia (FBA) surveys, conducted by Deakin University and KPMG; and
- the 2012 PricewaterhouseCoopers (PwC) private clients family business survey.

The Business Longitudinal Database and the Business Longitudinal Survey

3.6 The ABS's BLS data was gathered for the years 1994–95, 1995–96, 1996–97, and 1997–98 under the title of Business Growth and Performance Surveys. The BLD was introduced in 2005 and has two independent samples or Panels:

- Panel One contains five reference periods of data (2004–05, 2005–06, 2006–07, 2007–08 and 2008–09) for 2,732 business records; and
- Panel Two also contains five reference periods of data (2005–06, 2006–07, 2007–08, 2008–09 and 2009–10) for 3,432 business records.[4]

4 Australian Bureau of Statistics, *Business Longitudinal Database—Introduction*, http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/8168.0.55.001main+features22004-05%20to%202009-10 (accessed 22 February 2013).

The ABS states the aim of the BLD is to increase understanding of the activities or factors that are relevant to business performance and the associated business characteristics.[5]

3.7 In his submission to this inquiry, Mr Frank Barbera, a doctoral student at the Australian Centre for Family Business at Bond University, noted that the ABS's BLS and BLD both contained the following questions:

1) *Do you consider the business to be a family business? Yes/No*

2) *If yes, why do you consider this a family business? Family members are:*

   i) *Working directors or proprietors. Yes/No*
   ii) *Employed in the business. Yes/No*
   iii) *Not working, but contribute to decisions. Yes/No*
   iv) *Business acquired from parents. Yes/No*
   v) *Close working relationship between management and staff. Yes/No*
   vi) *Other. Yes/No* [6]

3.8 Mr Barbera noted that of the family firms responding to question 2 (above) in the 1994–95 to 1997–98 BLS and the 2004–05 to 2009–10 BLD:

> 34.91 percent selected i only; 27.45 percent selected both i and ii; 11.79 percent selected i, ii and v; 4.39 percent selected i and v; 3.18 percent selected i, ii, iv and v; and 3.18 percent selected i, ii and iv. Based on this, and out of 64 possible permutations, nearly 95 percent of all family firms at least selected i, which is understandable since we would expect small to medium sized family firms to have a more operational classification; however, not excluding these, approximately 37 percent also selected iv and v, which is associated with the essence based classification of a family firm.[7]

3.9 Mr Barbera also expressed frustration that the options listed under question 2 are not mutually exclusive, which makes intra-firm differences across family businesses difficult. He argued that in order to better understand the economic impact of family ownership in Australia:

> …more effort must be directed towards collecting data which distinguishes the intra-firm differences across family owned firms. In other words, the

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5 Australian Bureau of Statistics, *Business Longitudinal Database—Introduction*, http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/8168.0.55.001main+features22004-05%20to%202009-10 (accessed 22 February 2013).

6 Mr Frank Barbera on behalf of the Australian Centre for Family Business, Bond University, *Submission 3*, p. 5. The family business questions were asked of all businesses in 1995–96 and only those new to the study in 1996–97 and 1997–1998. See Australian Bureau of Statistics, http://www.abs.gov.au/websitedbs/D3310114.nsf/0/f7739966adba7636ca2572030016614c/$FILE/1994-95%20to%201997-98%20CURF%20docoV2.pdf (accessed 1 March 2013).

7 Mr Frank Barbera, on behalf of the Australian Centre for Family Business, Bond University, *Submission 3*, p. 5.

> current state of family business research necessitates a move towards viewing family firms as a heterogeneous group. Information specifically related to the structural, intentions, and family sub-system definitional approaches will help in this regard.[8]

3.10 Mr Frank Barbera also drew the committee's attention to restrictions with the availability of the BLD data. Unlike the BLS, he noted that the BLD is 'subject to rigid confidentiality restrictions' with access only via the ABS's Remote Access Data Laboratory. He argued that the confidentiality of the BLD data could be retained by removing reference to specific respondents while releasing the dataset to sanctioned individuals.[9]

Recommendation 6

3.11 The committee recommends that the Australian Bureau of Statistics inquire into whether the Business Longitudinal Database can be sufficiently de-identified so as to be made available for research purposes on request.

3.12 Noting the difficulty in accessing data from the BLD, the submission presented a table showing 'a representative SME sample from the older BLS data'. It shows that:

> …just over half [the firms] are family owned. Further, family firms employ more than 40 percent of all full-time equivalent employees, own nearly 30 percent of all assets, and contribute nearly 32 percent towards total output in all sectors.[10]

3.13 The committee notes that the earliest data on which the table is based (1994–95) is now nearly 20 years old. Further, the table contains no information on the representation of family businesses in the agricultural sector. The committee was informed that the BLS does not include information on this sector.[11]

MGI Australian Family and Private Business Survey

3.14 Since the early 1990s, Professor Kosmas Smyrnios of RMIT has completed seven surveys into family business in Australia. The surveys were conducted in 1994,

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8 Mr Frank Barbera on behalf of the Australian Centre for Family Business, Bond University, *Submission 3*, p. 5.

9 Mr Frank Barbera, on behalf of the Australian Centre for Family Business, Bond University, *Submission 3*, p. 5.

10 Mr Frank Barbera, on behalf of the Australian Centre for Family Business, Bond University, *Submission 3*, p. 9.

11 See the discussion, *Committee Hansard*, 16 November 2012, p. 39.

1997, 1999, 2000, 2003, 2006 and 2010.[12] The last three of these surveys, commissioned and sponsored by MGI Australasia, are called the MGI Australian Family and Private Business Survey. In its submission to this inquiry, MGI described the surveys as 'the most comprehensive longitudinal study of family businesses available in Australia'. [13] It believed that the data is reliable but the committee notes that the sample size is small and the definition of 'family business' changed between surveys.

3.15 The key findings of the 2010 MGI Australasia survey are as follows:

- 80 per cent of businesses surveyed had a private company structure (up from 73 per cent in 2006) while 12 per cent operated a family trust structure (down from 19 per cent in 2006);
- the proportion of family business owners who 'would seriously consider' selling their business if approached decreased from 75 per cent in 2006 to 61 per cent in 2010;
- the proportion of family business owners who planned to sell their business fell from 53 per cent in 2006 to 44 per cent in 2010:
    - of the 44 per cent who planned to sell their business, 20 per cent stated they wanted to retire while nine per cent said there was a lack of a family successor. The percentage of respondents giving these reasons was quite significantly down from the 2006 survey response;[14]
- in 2006 only 17 per cent of family business owners stated they did not have an adequately funded retirement program—this increased to 31 per cent in 2010;
- the average (mean) number of employees in the family businesses surveyed was 37 in 2010, 39 in 2006 and 31 in 2003;

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12 Kosmas Smyrnios and Claudio Romano, *The Pricewaterhouse/Commonwealth Bank Family Business Survey 1994*, 1994, http://www.mgiaust-survey.com/sites/default/files/1994_Report.pdf
Kosmas Smyrnios and George Tanewski, *The Australian & Private Family Business Survey: 1997*, 1997, http://www.mgiaust-survey.com/sites/default/files/1997_Report.pdf
Kosmas Smyrnios, Claudio Romano and George Tanewski, *The 1999 Australian Family Business Lifestyle Audit*, 1999;
Claudio Romano, Kosmas Smyrnios and Lucio Dana, *Succession Matters: The Australian Family Business Survey 2000*, 2000;
Kosmas Smyrnios and Rhett Walker, *The Australian & Private Family Business: 2003*, 2003, http://www.mgiaust-survey.com/sites/default/files/2003_Report.pdf
Kosmas Syrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2006*, 2006, http://www.mgiaust.com/publications/MGI%20Survey%20book.pdf
Kosmas Smyrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2010*, 2010, http://www.mgiaust-survey.com/ All documents were accessed on 25 February 2013.

13 MGI Australasia, *Submission 9*, p. 2.

14 Respondents could identify more than one reason.

- the average age of the family business owner is 55 years, which is very consistent across the three surveys;
- the average age of the family businesses surveyed was 32 years, compared to 28 years in the 2006 survey;
- only 11 per cent of family business owners are female, up from 10 per cent in 2003 and 4 per cent in 2006;
- in the 2010 survey, 35 per cent of family businesses surveyed noted that a spouse was involved in the day-to-day running of the business. The same percentage noted that a son is involved in the day-to-day running of the business;
- in all three MGI surveys, the majority of family businesses were first generation businesses (58 per cent in 2010), roughly one-quarter were second generation businesses (31 per cent in 2010) and a smallest proportion were third generation business (11 per cent in 2003);
- in the 2010 survey, 47 per cent of family business owners were tertiary qualified, compared to 52 per cent in 2006; and
- the 2010 survey was perhaps most notable for the results to the question on respondents concerns for the future. Fifty-four per cent of the family businesses surveyed indicated their concern with the 'financial performance of the business', compared to only 31 per cent in the 2006 survey. Thirty-eight per cent of respondents identified the particular industry in which they operated as a concern, up from 21 per cent in 2006 and 15 per cent in 2003. Twenty per cent of family businesses surveyed identified 'funding for growth' as a concern, compared with only six per cent in the 2006 survey.[15]

3.16 Notably, the 2010 MGI survey does not contain an estimate of the wealth of family businesses in Australia. The 2003 and 2006 surveys estimated this wealth at $3.5 trillion and $4.3 trillion respectively. Apart from questions about the reliability of these figures, they are also now dated. The FBA relied on the 2006 estimate in a September 2012 Media Release.[16]

3.17 The committee also notes that the definition of 'family business' varies across the seven MGI surveys. For the 1994 and 1997 surveys, 'family business' was defined as an enterprise for which:

- more than 50 per cent of the ownership is held by a single family or more than one family;

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15 See Kosmas Smyrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2010*, 2010, p. 8.

16 Family Business Australia, 'Is government overlooking the interests of family business?', *Media release*, September 2012. http://www.fambiz.org.au/documents/MediaRelease-FamilyBusinessMinister.pdf (accessed 25 February 2013).

- a single family group is effectively controlling the business; or
- a majority of the senior management is from the same family.[17]

3.18 In the 2003 survey, participants could self-identify as a family business, while in the 2006 survey, the definition was not provided in the survey report. In 2010, 'family business' was defined as an enterprise involving two or more related individuals working together, or otherwise associated, in a commercial enterprise that is controlled by one or more of those individuals (see chapter 2).[18]

3.19 Clearly, the changing definition of 'family business' limits the utility and accuracy of the longitudinal data. There is also the small number of businesses surveyed. As the FBA noted of both its surveys and the MGI surveys, 'the reliability of the data in each case is limited by their relatively small sample size'.[19] In the 2010 MGI survey, only 5000 Australian family businesses were surveyed from a sample:

> …based on location by state, industry, number of employees, and sales turnover [from]…selected companies in the proportions found in the Australian population of employing small-to-medium enterprises (SMEs).[20]

3.20 With the relatively small sample size as a caveat, the surveys do contain some notable findings. Most obvious is the respondents' concern about the financial performance of their business and the adequacy of their retirement program. These concerns are not surprising given the impact of the Global Financial Crisis (GFC). The GFC occurred between the 2006 and 2010 surveys. As the report stated:

> The survey reveals a less confident family business sector post-GFC than pre-GFC – with family business owners more reliant on the continuity of their business to fund their retirement and more concerned over the future of their business.[21]

3.21 The capacity of family businesses to save adequately for retirement is an issue of some concern for the committee. Although it has received little by way of concrete evidence on retirement plans and superannuation savings, the committee suspects there is significant under-investment in this area with many family businesses opting instead to hold equity in assets rather than through superannuation funds. The

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17 Kosmas Smyrnios and Claudio Romano, *The Pricewaterhouse/Commonwealth Bank Family Business Survey 1994*, 1994, p. 2; K. Smyrnios, C. Romano and G. A. Tanewski, *The Australian & Private Family Business Survey: 1997*, 1997, p. 2.

18 Lucio Dana and Kosmas Smyrnios, *The MGI Australian Family and Private Business Survey 2010*, RMIT University, July 2010, p. 9.

19 Family Business Australia, *Submission 1*, p. 2.

20 MGI Australasia, *The MGI Australian Family and Private Business Survey 2010*, http://www.mgiaust-survey.com/sites/default/files/fpbs_report_0.pdf (accessed 20 December 2012)

21 MGI Australasia, *The MGI Australian Family and Private Business Survey 2010*, p. 4.

committee notes that government policy settings can encourage family businesses to shift equity into superannuation funds.

3.22 Another point of interest in the 2010 MGI survey is that the average number of employees is 37. In light of the discussion in chapter 2 of this report, the figure seems high. If most family businesses are small business, and small businesses employ under 20 employees, one would have expected the average to be less than 20 employees. However, MGI used the mean rather than the median to calculate this figure. The committee suggests that the mean is not an appropriate measure of central tendency. If data on the number of employees is collected, the ABS should consider a modal class to assess the midpoint.[22]

The Family Business Australia surveys

3.23 The FBA noted in its submission to this inquiry that it has commissioned six annual surveys of the family business sector. The surveys were sponsored by KPMG. The 2005, 2006, 2007 and 2008 surveys were undertaken by Deakin University.[23] The Australian Centre for Family Business conducted a further FBA survey in 2009.[24] In 2011, the FBA and KPMG conducted and released the findings of a survey described as a 'biennial survey'.[25]

3.24 In its submission to this inquiry, MGI Australasia noted that the FBA surveys have extracted data 'from a limited sample size and therefore could be considered as not significantly reliable'.[26]

3.25 Intriguingly, the FBA's submission contained only one reference to any of these published surveys' findings. Perhaps this was intended so as not to cloud the

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22 A modal class would indicate the number of businesses employing 0–4 employees, 5–9 employees, 10 to 14 employees, 15–19 employees, etc.

23 Linda Glassop, Yuen Ching Ho and Dianne Waddell, *KPMG and Family Business Australia survey of family business needs*, KPMG, 2005, http://peak.fambiz.org.au/documents/item/243; Linda Glassop, Pauline Hagel and Dianne Waddell, *KPMG and Family Business Australia survey of family business needs*, KPMG, Canberra, 2006, http://peak.fambiz.org.au/documents/item/245; Linda Glassop, Pauline Hagel and Dianne Waddell, *KPMG and Family Business Australia survey of family business needs 2007*, KPMG, 2007, http://peak.fambiz.org.au/documents/item/246; Linda Glassop, Pauline Hagel and Dianne Waddell, *KPMG and Family Business Australia survey of family businesses 2008*, Deakin University, Melbourne, Australia, 2008, http://peak.fambiz.org.au/documents/item/247 (all documents accessed 1 March 2013).

24 Australian Centre for Family Business, *KPMG and Family Business Australia Survey of Family Businesses 2009*, 2009, http://peak.fambiz.org.au/documents/item/250 (accessed 1 March 2013).

25 KPMG and Family Business Australia, *Stewards: Moving forward: moving onwards*, 2011, http://www.kpmg.com/au/en/issuesandinsights/articlespublications/documents/family-business-survey-2011.pdf (accessed 1 March 2013).

26 MGI Australasia, *Submission 9*, p. 2.

FBA's central message that official, reliable data needs to be collected.[27] It certainly is striking that having commissioned no fewer than six surveys in a six year period, the FBA should be essentially silent on the findings. Instead, the submission made several references to the findings of the 2006 MGI survey.

The 2011 FBA survey

3.26 There are some findings of note in the most recent FBA–KPMG survey in 2011. The survey's focus was on 'internal dynamics of a representative cross section of Australian family businesses'. 658 businesses were surveyed.[28] Some of the key findings were:

- more than 60 per cent of respondents identified retaining control of the family business as an issue of high or very high importance;
- nearly 60 per cent of respondents identified preparing and training a successor before succession takes place as an issue of high or very high importance;
    - 51 per cent of respondents identified that selling the business to an independent third party was a possible exit strategy in the next 12 months, compared with only 13 per cent who identified passing the business on to the next generation;
    - 42 per cent of respondents identified that selling the business to an independent third party was a possible exit strategy in the next three years, compared with 17 per cent who identified passing the business on to the next generation;
    - 34 per cent of respondents identified that selling the business to an independent third party was a possible exit strategy in the next five years, compared with 24 per cent who identified passing the business on to the next generation;
- 48 per cent of respondents identified experience outside the business as a 'very important' attribute of a potential successor; 34 per cent of respondents identified the attainment of formal business qualifications as a 'very important' attribute of a successor;
- 57 per cent of respondents identified distributing ownership among family members as a low or very low issue of importance;
- 54 per cent of respondents identified establishing a family constitution or code of conduct as a low or very low priority;

27 Family Business Australia, *Submission 1*, p. 4.

28 50.5 per cent of these respondents employed fewer than 21 employees; 36.5 per cent employed from 21 to 100 employees; and the remaining 13 per cent employed more than 100 employees.

- 20 per cent of respondents identified the future strategy of the business as the most common cause of conflict in the family business; only 10.5 per cent of respondents identified succession as the most common cause of conflict;
- 32 per cent of respondents had no formal mechanisms to resolve family conflict; and
- 61 per cent of respondents said the family members in the business were paid the same as non-family members; 25 per cent noted that family members were paid more than non-family members; while 14 per cent indicated that family members were paid less than non-family members.

61 per cent of family businesses to transition between 2006 and 2016

3.27 The FBA submission's single reference to a finding from a survey that it had commissioned was to the 2006 survey undertaken by Deakin University. Specifically, the survey found that:[29]

> More than half the survey respondents (61%) noted that they plan to retire in less than ten years. This is not surprising given that around half (58%) are aged over fifty years. However, with the majority of family businesses having no formal succession plan (78%) and not yet chosen a successor (62%), these family businesses would appear to be at high risk. The question of succession appears ambiguous given that the same number of respondents indicate that their exit plan is to either pass the business to the next generation or sell it (60%). With around a quarter (26%) of family businesses indicating that they have a succession plan for the CEO and other senior positions held by family members (23%), longevity of these family businesses appears doubtful.[30]

3.28 This finding was a key reference point for the committee throughout this inquiry. The committee sought comment from various stakeholders as to whether they believed the figure was accurate and if so, what trends it could explain. In particular, the committee asked whether the figure reflected the imminent retirement of baby boomers who own family businesses.[31]

3.29 The committee notes that the 2008 KPMG survey found that 34 per cent of family business CEOs are likely to step down within five years, and 27 per cent between five and ten years. KPMG noted that this finding is 'consistent with the fact that forty-three percent have been in the role for more than twenty years'.[32] KPMG

29 Family Business Australia, *Submission 1*, p. 7.

30 Linda Glassop, Pauline Hagel and Dianne Waddell, *KPMG and Family Business Australia survey of family business needs*, KPMG, Canberra, 2006, http://peak.fambiz.org.au/documents/item/245

31 *Committee Hansard*, 15 November 2012, p. 3.

32 Linda Glassop, Pauline Hagel and Dianne Waddell, *KPMG and Family Business Australia survey of family businesses 2008*, Deakin University, Australia, 2008, p. 11.

also drew attention to the age of respondents: 32 per cent were aged between 46 and 55; and, 31 per cent aged between 56 and 65.[33]

3.30 Reflecting on its finding, KPMG told the committee that while the 2006 figure of 61 per cent of respondents planning to retire within ten years had 'shrunk a little post GFC', the figure partly reflects the fact that the next generation does not want to take over the business. As Mr Des Caulfield told the committee:

> …there is a change of the attitudes in the community or perhaps in the younger generations. Once it was almost assumed that if mum and dad had a business, the children would take over. That has certainly changed due to a number of things including the fact that business has changed so much now. The traditional business, the local supermarket or whatever, was never much different. All of a sudden there are all these other things out there now so people are finding that the next generation does not necessarily want to take on mum and dad's business. That is the main reason I think there are more people wanting to get out.[34]

3.31 KPMG also recognised that demographic factors are at play:

> The situation is there is a whole heap of people in that age category, between late 50s and late 60s, who are now finding that their children do not necessarily want to succeed them in the business. They probably should have known longer ago than now that that was going to happen but also probably did not accept it because they thought, 'I have had the business and my kids are going to take it on.' There is a bulge there of businesses that will have to close or go on market if they cannot find a successor. That is going to have an impact on the value of those businesses because the more businesses that are available, the lower the price is likely to be. I do not know if there is anything we can do about it but it is reality.[35]

3.32 The committee asked both the Reserve Bank of Australia and Treasury if they could comment on the figure of 61 per cent of family businesses facing transition between 2006 and 2016. Treasury recognised that the figure could reflect the play of market forces, rather than a demographic trigger:

> ...many businesses will simply hit a point whereby they enter into negotiations for sale. They will sell the business as an ongoing concern to someone else. The point from a productivity perspective is that this may result in a possible loss of corporate knowledge. That is going to be heavily dependent on the transition between the new buyers and the existing sellers. From an economy-wide perspective, if you make the assumption that these

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33 Linda Glassop, Pauline Hagel and Dianne Waddell, *KPMG and Family Business Australia survey of family businesses 2008*, Deakin University, Australia, 2008, p. 3.

34 Mr Des Caulfield, Director, MGI Australasia Ltd, *Committee Hansard*, 14 November 2012, p. 25.

35 Mr Des Caulfield, Director, MGI Australasia Ltd, *Committee Hansard*, 14 November 2012, p. 25.

businesses are viable, then, arguably, they should be being sold and you should have a smooth transition.[36]

3.33 Treasury did point out that an accurate picture of the number of Australian family businesses facing transition requires official longitudinal data. It told the committee:

> It goes back to the broader data question: the advantage of an ABS time series or some RBA data is that you can look at it through time. In the family business context a succession plan would normally revolve around a family member taking over the running of that business. I do not know whether or not it would be normal that within the next 10 years most family businesses do not have a formal succession plan with respect to a particular family member. I do not think there would be any data on it on a time series basis.[37]

3.34 In its submission, KPMG also noted that an estimated $3.5 trillion in wealth held by family businesses is likely to be transferred over the next 10 years. Professor Ken Moores queried the reliability of both the 61 per cent and the $3.5 trillion estimates. He agreed that it is not possible to know whether the figures are accurate or not, adding:

> I am nervous about all of these numbers because I think the only really reliable statistics are those that come from the ABS…My centre, KPMG and FBA have produced these [surveys] and had 600 respondents and things like that, and we have interpolated from there, but I am always a little wary as to making big, bold statements. Certainly, with 61 per cent, where is the error in those sorts of things?[38]

Committee view

3.35 The committee shares Professor Moores's doubts about the reliability of the 2006 KPMG survey's finding on the transition of Australian family businesses. It may be that when interviewed in the 2006 and 2008 KPMG surveys, roughly two in three family business respondents planned to retire (or step down) within the decade. However, the sample sizes in these surveys were relatively small and there is ambiguity around whether the respondent wanted or needed to sell the business, or whether they wanted to pass it on. The committee agrees with Professor Moores that only ABS data can provide the requisite breadth and depth of data. It is concerned that Treasury does not have any data on the succession plans of Australian family

36 Mr Michael Wilson, Analyst, Small Business Tax Unit, Treasury, *Committee Hansard*, 13 November 2012, p. 11.

37 Mr Hector Thompson, General Manager, Small Business Tax Division, Treasury, *Committee Hansard*, 13 November 2012, p. 11.

38 Professor Ken Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, pp 20–21.

businesses over the next decade. These issues of succession intentions are raised in chapter 5 of this report.

BDO Australia's Wealth Transfer Survey

3.36 The Australian Centre for Family Business told the committee that it is currently working with the accounting firm BDO Australia on what it called a 'wealth transfer survey'. Mr Barbera explained that the survey relates to the transfer of ownership (rather than management) and will include issues such as:

> How is it going to be done? What are the tax implications? What are the intentions of the owners: for example, are they needing this money to retire, are they interested in maintaining the wealth of the family as a whole or are they interested in selling and distributing that money amongst the family and then have some sort of investment vehicle that continues to generate wealth? There are all these sorts of questions as far as the modes of wealth transfer, what are the motivations behind wealth transfer and when do they expect to do this transfer of wealth? That is what we looking at right now.[39]

3.37 There were 320 respondents to the survey. BDO Australia has published some preliminary findings from the survey. These include:

- 93 per cent intend to transfer business wealth within the family—seven per cent outside the family; and
- 39 per cent have a complete succession plan that nominates a CEO successor.[40]

3.38 At the time of writing, the final report on the wealth transfer survey had not been made publicly available. The committee understands that the final report is expected to be released in March 2013. It believes the findings will be useful to stimulate discussion about the possible public policy objectives on succession-related matters.

Recommendation 7

3.39 The committee recommends that as part of its deliberations, the Inter-Departmental Committee (see recommendation 1) should examine the findings on the wealth transfer survey conducted in 2012 by the accounting firm BDO Australia.

39 Mr Francesco Barbera, *Committee Hansard*, 16 November 2012, p. 40.

40 BDO Australia, *Family business wealth transfer survey*, December 2012, http://www.bdo.com.au/resources/newsletters/growth-matters/Growth-Matters,-December-2012/family-business-news/family-business-wealth-transfer-survey (accessed 1 March 2013).

The PricewaterhouseCoopers private clients family business survey

3.40 In its submission to this inquiry, PricewaterhouseCoopers (PwC) gave a summary of its findings from an international survey of family businesses conducted in July and August 2012.[41] Fewer than 2000 businesses were surveyed of which only 50 were Australian.

3.41 PwC claimed that the results of the survey 'can be recommended as a timely and accurate snapshot of family businesses in Australia'. The survey found that:

- almost 40 per cent of Australian respondents intend to pass on management to the next generation. The remaining businesses are 'twice as likely to sell or float than to pass down but employ non-family management';[42]
- 58 per cent of Australian respondents indicated that they have non-family members on the board, while 28 per cent of Australian respondents indicated that they have non-family staff who have shares in the company;[43]
- in terms of the perceived challenges faced by the business in the next five years, only 30 per cent of Australian respondents identified company succession planning as a challenge;[44]
- 56 per cent of Australian respondents agreed that 'government should make it easier for family businesses to access finance';[45]
- Australian respondents ranked 19th out of 28 countries in terms of the perception of government in recognising the importance of family business;
- 82 per cent of Australian respondents agreed with the statement that family businesses 'do all you can to retain staff, even in the bad times';
- 78 per cent of Australian respondents agreed with the statement that family businesses have a 'sense of responsibility to support employment in areas where you operate';
- 68 per cent of Australian respondents agreed with the statement that 'the culture/values tend to be stronger than in other types of businesses';
- 62 per cent of Australian respondents agreed with the statement that there is a 'sense of responsibility to support community initiatives in your area';[46] and

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41 PricewaterhouseCoopers, *Private clients family business survey*, http://www.pwc.com.au/private-clients/assets/family-business-survey/Australia-Family-Business-Survey-Oct12.pdf (accessed 1 March 2013).

42 PricewaterhouseCoopers, *Submission 11*, p. 1. PricewaterhouseCoopers, *Private clients family business survey*, p. 22.

43 PricewaterhouseCoopers, *Private clients family business survey*, p. 18.

44 PricewaterhouseCoopers, *Private clients family business survey*, p. 12.

45 PricewaterhouseCoopers, *Private clients family business survey*, p. 24.

46 PricewaterhouseCoopers, *Private clients family business survey*, p. 26.

- roughly equal proportions of Australian respondents agreed as disagreed with the statements that family businesses:
  - 'take a longer-term approach to decision-making' (34 and 40 per cent);
  - 'take more risks' (32 and 38 per cent); and
  - 'are less open to new thinking and ideas' (36 and 36 per cent).[47]

3.42 The committee draws attention to the very small sample size of the PwC survey. It is very difficult from this sample to postulate about the views of 'Australian family businesses'. Indeed, if the survey is of any utility, it is really only as a guide to the type of issues that might interest policy makers should they decide there is a need for official data (see chapter 2).

Submitters' and witnesses' views on the availability and reliability of data

3.43 During the committee's public hearings, several witnesses commented on the lack of reliable data that is currently available on family businesses in Australia. Some witnesses made these comments principally to caution that the survey findings should not be endorsed. Others referred to existing data as at least a good estimate. They argued that the data, while not strictly reliable, provide enough evidence of the significance of the family business sector to warrant the collection of official statistics.

3.44 The lack of official data was clearly frustrating for several witnesses. MGI Australasia told the committee:

> …we have become more and more aware that there is very little reliable statistical data available that can act as a foundation for ensuring that this sector of our economy is properly serviced and gets what it needs.[48]

3.45 Mr Yasser El-Ansary of the Institute of Chartered Accountants, put a similar view:

> …there is no broad based research platform or statistics on which the government can rely at the moment. There is some very comprehensive private-sector research that has been undertaken…but from an Australian Bureau of Statistics point of view we certainly agree that there is not sufficient information collected about the size or composition of the sector in Australia at this point. That is something we think is worthy of further consideration and, if appropriate, we would certainly support designing a framework to improve the quality, breadth and depth of information that could be collected about family businesses and the contribution they make to the broader economy.[49]

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47 PricewaterhouseCoopers, *Private clients family business survey*, p. 16.

48 Mr Desmond Caulfield, MGI Australasia, *Committee Hansard*, 14 November 2012, p. 23.

49 Mr Yasser El-Ansary, Institute of Chartered Accountants, *Committee Hansard*, 14 November 2012, pp 16–17.

3.46 MGI Australasia also drew the committee's attention to the cost of the surveys it has conducted, their infrequency, how quickly the findings date and the small sample size that was used. Mr Des Caulfield explained:

> I guess the way that we look at it is that it is an expensive exercise for us to undertake. Whilst we are a medium-sized accounting group, we are certainly not up there with the big boys. We therefore conduct a survey in detail only once every three years. The world is growing at a fairly fast rate these days…and it becomes obvious that the data can get out of date fairly quickly. We do not believe that we are in a position to fund to any greater extent than what we do, and we are very grateful to RMIT for providing their people to undertake the stuff for us. But the situation is that we are only doing this once every three years, which I believe is not often enough. Our view would be that it would be good if there could be a mechanism in place where people could be encouraged to do regular, properly research study into family business in a more significant manner than what is done at the moment. In our last survey we asked 5,000 people to respond and we had responses from about 1,000, give or take.[50]

3.47 The committee asked PwC if it was confident with the accuracy of the figure that 70 per cent of Australian businesses are family businesses. Mr Paul Brassil, a partner with the firm, was frank in his response:

> No, certainly not. It is a bandied-around number at the moment, which seems to have a fair bit of traction. One of the questions goes to: what is the reliability of information about family business? There are all sorts of ways of slicing and dicing it, none of which are accepted as gospel truths, but there is a consistency about it, I suppose. That is what I am getting a sense of…Is it more than half? Yes, I would have thought so. Is it 60, 65 or 70 per cent? I do not know.[51]

3.48 The committee probed for the reasons why official data on family businesses is necessary. Mr Michael Claydon, the Managing Director of a Perth-based corporate training business, emphasised the importance of accurate and more complete information to assist government in its decision-making. He explained:

> The one thing I know is that we deal with government a fair bit in terms of funding and other things, but the government does not make decisions based on having no information. The more information you have, the better the decisions that you can make. I can confirm that most businesses who start out as individual operators would still consider themselves family businesses. You look at the impact on family: what happens when you go home? You talk about your family business constantly, because you are trying to grow it in the initial stages. Then as its gets bigger you actually just incorporate more members of the family, but you still talk about it a lot

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50 Mr Desmond Caulfield, MGI Australasia, *Committee Hansard*, 14 November 2012, p. 23.

51 Mr Paul Brassil, Partner, PricewaterhouseCoopers, *Committee Hansard*, 14 November 2012, p. 25.

> inside the business. But from a government perspective, you cannot make decisions based on having no information. At the moment, the definition is up in the air; the number of businesses is up at in the air. But I would surmise that there would be a complete surprise about how many people actually consider themselves to be part of a family business. It would be a very high percentage.[52]

3.49 Mr Stephen Sampson, Director of the Lionel Sampson Sadlier Group, put the case for better data collection on family businesses in terms of understanding a significant sector of the Australian economy. As he told the committee:

> Because of the sector employing half the population of Australia, there is a growing need to make sure that you get good information about something so significant. I actually spoke at a conference overseas in June. It was run by IFERA, which is the International Family Enterprise Research Academy. They are all about getting information and working with academics to find out what makes this part of the market sector tick. It is critical that you get good information. Without information, you just cannot make any judgements or any determinations. For something that covers such a broad sway of the Australian economy, it is amazing that we do not have good information.[53]

3.50 Mr David Smorgon of Generation Investments also put the case for collecting official data in terms of quantifying assumptions about the contribution of the family business sector:

> …we are reliably told that today, family businesses make a major contribution to our society, although we do not have the data to put a figure to that. We are also told today that 70 per cent of all Australian businesses are family businesses—not 83 per cent as it was in 1994—and they employ 50 per cent of Australia's workforce. That is outdated data. I think those reports were done in 2006 and 2009. But, if you think about it, it is staggering that family businesses would employ 50 per cent of all Australian workers. We still do not have the facts. As a former editor of the Manchester Guardian once said: 'Comments and views are free but facts are much more expensive to obtain.' I think it is about time that the money was spent on getting the data, because we have to know. We need clear and comprehensive data, and then strategies and policies can be established where the contribution by family businesses to our society can be further enhanced.[54]

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52 Mr Michael Claydon, Managing Director, National Corporate Training, *Committee Hansard*, 7 February 2013, p. 22.

53 Mr Stephen Sadlier, Director, Lionel Sampson Sadliers Group, *Committee Hansard*, 7 February 2013, p. 21.

54 Mr David Smorgon, *Committee Hansard*, 14 November 2012, p. 2.

3.51 The Chamber of Commerce and Industry Queensland expressed interest in identifying the competitive advantages enjoyed by small and medium sized family businesses over SMEs generally. Mr Nick Behrens put the Chamber's view as follows:

> …being a small or medium sized family owned business presents opportunities that are unique to family businesses. For example, being a family business often has a competitive advantage attributable to family values influencing business values and by being able to offer a boutique product or service that differentiates them from other market players. However, what is also clear is that there is insufficient research to inform the current discussion about the importance and significance of family businesses in Australia and their contribution to the economic and social fabric of Queensland and Australia. The current lack of qualitative and quantitative data needs to be progressively improved upon.[55]

3.52 Mrs Genevieve Power, Managing Director of the Canberra-based family business Iken Commercial Interiors, suggested particular areas that needed official data to test the anecdotal evidence about family business. As she told the committee:

> If the statistics could differentiate or arrange questions that would allow us all to determine small, medium and large and the sector into which they fit. Are they a public corporation? Are they a private corporation? Are they a family business? Or do they consider themselves a family business? That would then allow some long-term look at the anecdotal evidence that we all talk about—60 per cent of Australia is run by family businesses…I think that one of the ways the government could definitely help is by annual—or biannual [surveys]; whatever it is—statistical collection or by doing some core sampling of businesses.[56]

3.53 The committee notes that some government departments have seen merit in collecting better data. This is of particular importance given the recommendations in chapter 2 of this report. The Department of Regional Australia, Local Government, Arts and Sport told the committee:

> One of the constraints on the conversation about family business in regional Australia, as we look at it, is that there are no readily available ABS statistics on family business in regional Australia, which makes it difficult for us to speak authoritatively about the regional versus non-regional aspects of it; there is not that solid data set.[57]

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55 Mr Nick Behrens, Queensland Chamber of Commerce and Industry, *Committee Hansard*, 16 November 2012, p. 1.

56 Mrs Genevieve Power, Managing Director, Iken Commercial Interiors, *Committee Hansard,* 13 November 2012, p. 50.

57 Mr Simon Atkinson, First Assistant Secretary, Regional Policy and Coordination, Department of Regional Australia, Local Government, Arts and Sport, *Committee Hansard*, 13 November 2012, p. 33.

3.54 The lack of reliable data at present was apparent from several submitters' reliance on SME data to indicate the dimensions of Australian family businesses. In reference to its submission, the RBA told the committee:

> We would not profess to have any specialised knowledge on family businesses. In fact, to a large degree that is actually why we have focused on small and medium-sized enterprises: it is about availability of statistics.[58]

3.55 Deloitte Private's submission refers to a CPA survey of small business.[59] It also notes that the ABS and the Australian Taxation Office (ATO) have data on household income, household expenditure, employment and business counts which is 'somewhat aligned to family business'. Deloitte Private recognised there is little data available on the extent to which family businesses contribute to Australia's GDP, employment and other economic indicators.[60] Mr David Hill, Managing Director of Deloitte Private, told the committee that the need for data collection on family businesses in Australia reflects the diversity of these businesses. He argued that government has a role to make the voice of these businesses heard by collecting reliable data on the sector. In terms of what data should be collected, Mr Hill told the committee:

> Information on the definition, the number, the employees, issues such as growth—are they experiencing growth?—and the contribution to the broader GDP of the country is very important. We have highlighted a number of issues that I believe would be really interesting to know. For example, how many of them operate across state boundaries? How many of them have expanded internationally? For family businesses those two things are quite considerable constraints. I would love to know about things like their investment in R&D and their focus upon innovation. I think it is a very long list; it is a wish list. At the moment we are starting with a very minimal base. I think the other very good idea would be to go out and consult with people like David [Smorgon] and other leading family businesses to say, 'What would you like to be able to say?' and drive it from the market back.[61]

Farm sector data

3.56 While there is no official data on family businesses, there is data on family ownership in the farm sector. The Australian Bureau of Agricultural and Resource

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58 Mr Christopher Aylmer, Head, Domestic Markets Department, Reserve Bank of Australia, *Committee Hansard*, 15 November 2012, p. 1.

59 Deloitte Private, *Submission 16*, pp 26–28. The *CPA Australia Asia-Pacific Small Business Survey 2011*.

60 Deloitte Private, *Submission 16*, p. 4.

61 Mr David Hill, Managing Director, Deloitte Private, *Committee Hansard*, 14 November 2012, p. 3.

Economics and Sciences (ABARES) told the committee that its farm dataset is collected through face-to-face interviews with farmers, which enables the Bureau to construct 'a comprehensive picture of the economic performance of farm businesses'. It elaborated:

> ABARES's farm surveys collect some information on the ownership of farm assets and the distribution of farm profits of farm businesses. On the basis of this information, more than 95 per cent of Australian broadacre and dairy farms are estimated to be family operated, and at least partly family owned. Broadacre and dairy farms account for about 68 per cent of Australian farm businesses, and surveys conducted in recent years of vegetable industry farms and irrigated farms in the Murray-Darling Basin indicate a similar proportion of family farms in these sectors. Major challenges faced by family farms are similar to those faced by all farms in Australia, including the long-term decline in farmers' terms of trade; the important role of productivity growth to maintain cost competitiveness; the relatively high volatility in yields and prices on agricultural markets; and the economic impact of the resource boom.[62]

3.57 The committee asked ABARES how it distinguishes between family farms and non-family farms. ABARES responded that this distinction is not made given that more than 95 per cent of all farms are likely to be family farms. However, it added:

> There are issues around how we classify farms in the sense of what is family owned versus operated. I think our definition is probably closer to a family operated farm as opposed to family owned. You might very well have, for example, a farm which might be leased by a family. They are operating the business, but they are leasing the land. We might still regard that as a family farm, even though the land might be owned by someone else.[63]
>
> …If we were pressed we could do a segregation of family farm specific information, but, as I indicated, I do not think it would vary that much from the overall farm numbers in any case. For farming we already have a very good set of information and data on farm family businesses.[64]

3.58 ABARES told the committee that the quality of the information it collects on farm statistics—of which family farm data is the substantive component—is based on the quality of its collection processes. It explained that:

> For ABARES to have credibility in terms of the work we do—the analysis and research that we do—we need to have a relationship with the businesses that we are working with, and we do that in a number of ways. One is the direct relationship that we have through collecting information

62 Mr Paul Morris, Executive Director, ABARES, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 13 November 2012, p. 39.

63 Mr Paul Morris, Executive Director, ABARES, *Committee Hansard*, 13 November 2012, p. 39.

64 Mr Paul Morris, Executive Director, ABARES, *Committee Hansard*, 13 November 2012, p. 42.

> from individual farmers but we also do things like our regional outlook conferences, where we have a regional conference in each of the states and the Northern Territory each year. This is where we actually get out and talk directly to people who attend those conferences. Often we get a mix of local and rural businesses and farmers and so forth. We invite our survey participants along to those conferences for free. I think part of our social licence, our credibility, if you like, is about making sure that we have those connections with the people that we are doing analysis for and that we are providing analysis to the government on.
>
> …I would just add that the surveys are voluntary. We invite farmers to participate in our surveys, and so I guess we do need to demonstrate value back to them for being willing to allow us to visit their properties and spend several hours collecting that information. Part of that is being able to hand back something that might help them in their business planning.[65]

3.59 ABARES explained that its current survey covers 1,600 broadacre farms and 300 dairy farms. It noted that this is 'probably about the right number' to provide a statistically valid sample. ABARES told the committee that the larger the sample size, the more regional level information it can provide. The current sample of 1,600 farms allows for some state regional numbers as well as state-based information.[66]

3.60 The committee was informed that the ANZ Bank and the University of Adelaide Business School are currently conducting a joint three-year study into the issues impacting the future of Australia's family-run farms. This project is focussing on succession planning for family farms, the development of options to ensure their sustainability and farmers' access to credit and appropriate financial management practices (see chapter 9). The project's researcher, Mr Andrew Harrison has observed:

> Currently there are limited statistics on issues surrounding the sustainability of Australian family farms. ABARE [sic] does collect statistics on Australian farms through its annual survey but it focuses mainly on financial performance. There is a lack of data on other important issues such as succession planning. Given the fact that the farming industry is unprepared for succession and transition, more research needs to be conducted in this area.[67]

3.61 The committee notes that this work is in its early stages and it looks forward to the research findings.

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65 Mr Paul Morris, Executive Director, ABARES, *Committee Hansard*, 13 November 2012, p. 43.

66 Mr Paul Morris, Executive Director, ABARES, *Committee Hansard*, 13 November 2012, p. 43.

67 Mr Andrew Harrison, 'Survival of Family Farms: Capital raising and credit access', *Document supplied to the committee by Dr Chris Graves*, received 14 December 2012.

Data on trusts

3.62 Chapter 6 of this report details with the use of trust structures by family businesses. The 2010 MGI survey found that 12 per cent of respondents surveyed operated a family trust structure. This was down from previous MGI surveys (19 per cent in 2006 and 15 per cent in 2003).[68]

3.63 The committee asked the ATO if it had any data on the number of family trusts currently operating in Australia. It responded:

> We have some data. We do not actually have data in relation to family trusts. There is no such definition as such in terms of the data we use. But we have data in relation to discretionary trusts, and, by and large, because of the nature of discretionary trusts, they are quite likely to be owned by families, albeit they could be quite extensive families.[69]

3.64 The committee then asked the ATO if it could indicate the number of discretionary trusts as a proportion of all trusts. It gave the following response:

> …we have data in terms of discretionary trusts where the main source is from trading and therefore you might think of it as being a family business trust. We have about 225,000 operating, from figures in 2009–10. We have a total figure of trusts in the system of 700,000.[70]

Data on culturally and linguistically diverse communities

3.65 The committee also asked the ABS whether it had data on family businesses formed by new migrants and within culturally and linguistically diverse (CALD) communities. The ABS responded:

> Not directly. In the past collections focusing on immigrants per se have often been followed more by the Department of Immigration and Citizenship. That said, there is potential work on our future work program which may open opportunities. We have recently negotiated access to personal income tax information and are investigating opportunities to match that with the immigration data base so that would give potential opportunities to follow that up. That in turn could then be linked with business information where we find what businesses employ which individuals through the old equivalent of group certificates and the like. There are future analytical possibilities on the horizon but they would need to be investigated.
>
> …The ABS Census provides information on the year they arrive in Australia, their employment, their education and the like. These details are

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68 Kosmas Smyrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2010*, 2010, p. 8.

69 Mr Tony Poulakis, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 14.

70 Mr Tony Poulakis, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 14.

> collected in a detailed census to a small granular level. That can be supported with other information such as that which can be matched to immigration statistics and the like on immigration in each year.[71]

3.66 The committee believes that the establishment rates and contribution of family businesses from CALD communities could be an area of particular interest for government agencies. It recommended in chapter 2 that the proposed IDC consider the need to identify the number and type of family businesses established from CALD communities.

3.67 The committee also draws attention to the dearth of academic research into issues affecting family businesses in CALD communities in Australia. It believes that official data collection will spur academic interest on a range of issues relating to these businesses. This includes the owners' level of education and that of their children, the location and sector in which these businesses operate, and their capacity to access professional services such as financial advice and accounting services.

Committee view

3.68 This chapter has presented the findings of several surveys into various dimensions of family businesses in Australia. Although the nature of the research is important and the findings are interesting, the usefulness and reliability of the data is questionable. In terms of the consultancies' surveys, the sample sizes are small and the research lacks independence. Any comparison between the surveys—even those conducted by the same consultancy—is difficult given that different definitions of family business are used and their questions and methodology vary over time. While there is some ABS data, the most recent data is confidential while the BLS data is now at least 15 years old.

3.69 Nonetheless, this chapter has drawn attention to the type of issues that may be worth exploring should the IDC decide that official data on family businesses is needed. Most obviously, there is the number of Australian businesses that are family businesses. Of course, this will depend on the definition of family business: whether it is based solely on governance structures or whether it also includes an intention and/or a plan to pass the business on. The committee does emphasise that the IDC should consider the types of issues and concerns related to inter-generational transfer of wealth, and the benefit to policy makers of clear data on these issues.

71 Mr Bill Allen, Assistant Statistician, Australian Bureau of Statistics, *Committee Hansard*, 12 November 2012, p. 20.

Chapter 4

The characteristics and mindset of family businesses in Australia

> *We have a stronger engagement with our staff than typical companies. Our employees value that the owners are visibly known people that they can talk to. The success of many family businesses is something employees take great pride in. We measure our organisation culture to ensure family values and expectations are embraced by our people…Our decision making is not confined to reporting periods and bonus horizons but reflect a vision over decades. This contrasts starkly with much of the listed corporate sector…*[1]

> *I believe they are the fabric, heart and soul, of our local communities.*[2]

Introduction

4.1 The third article of the terms of reference directs the committee to the contribution of family business to the Australian economy, in terms of financial, social, employment, innovation and sustainability outcomes. The previous chapter noted the view of Deloitte Private, among others, that little data is available on the extent to which family businesses contribute to Australia's GDP, employment and other economic indicators. Government agencies also acknowledged the paucity of evidence in this area. As the Department of Resources, Energy and Tourism (DRET) noted in its submission:

> According to research undertaken by Tourism Research Australia, as at June 2011, there were approximately 283,000 tourism businesses in Australia, representing in excess of 13 per cent of 2.1 million businesses across the Australian economy.
>
> Approximately 91 per cent of tourism businesses were non-employing, micro, and small businesses (employing less than 19 persons). Whilst there is a lack of data relating to the number of family businesses in the tourism industry, the structure of the industry and anecdotal evidence suggest that a significant number of small tourism businesses are family operated.[3]

4.2 There is obvious interest in not only the economic contribution of family businesses, but their economic performance relative to non-family businesses. As a

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1 Kennards Self Storage, *Submission 15*, pp 1–2.

2 Mr Donald McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 9.

3 Department of Resources, Energy and Tourism, *Submission 31*, p. 1.

2010 paper by Linda Glassop, one of the co-authors of the 2005–2008 FBA–KPMG surveys, observed:

> If Australian family firms do outperform non-family firms, then their presence in the economy should be encouraged and the practices that render them successful identified so they can be emulated. In the absence of concrete data regarding family firm contribution to the economy, such assertions are meaningless.[4]

4.3 The committee believes that the need for data on the economic contribution of family businesses to the Australian economy should be a matter for the proposed IDC (see chapter 2). This will be an opportunity for departments such as DRET and the Department of Regional Australia, Local Government, Arts and Sport (DRALGAS)—both of which have an interest in disaggregating the small business data to identify family businesses—to argue the need for, and the form of, the data.

Recommendation 8

4.4 The committee recommends that in its deliberations on the specific public policy need to identify a family business, the IDC should consider the need for data on the economic contribution of family businesses. This should include the need for data on the contribution of family businesses to Gross Domestic Product, export earnings and employment, both in aggregate and by sector.

Key family business characteristics

4.5 In the absence of solid, reliable data, this chapter approaches the contribution of family businesses in terms of the characteristics that they exhibit. The evidence gathered by this committee—both from witnesses and the academic literature—has identified a set of characteristics that form a mindset that is qualitatively different to that of non-family businesses. Although the evidence is largely anecdotal, the observations have been made too consistently and too widely to ignore. They should be considered by the IDC.

4.6 This chapter considers evidence received by the committee that family businesses possess the following attributes:

- a risk averse mindset;
- a long-term mindset, looking beyond short-term returns (what some have termed 'patient capital');
- more flexibility in their decision-making than non-family businesses, enabling greater responsiveness to market needs;
- a commitment to retaining staff;

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4 Linda Glassop, 'Family owned businesses: Perspectives on Australian Policy', Deakin University, 2010, p. 5, http://dro.deakin.edu.au/eserv/DU:30031227/glassop-familyownedbusinesses-2010.pdf (accessed 24 February 2013).

- a significant contribution to the community in which they operate; and
- higher labour productivity than non-family firms.

A long-term mindset—causes and benefits

4.7 Several submitters and witnesses to this inquiry emphasised the long-term mindset of family businesses. In the academic literature, the expression sometimes used is 'patient capital'—a long-term approach to investment. In part, this approach was attributed to the absence a board demanding short-term performance on share price. The other key influence is the need for the owners to preserve the legacy and reputation of the family name.

4.8 Various submitters highlighted the benefits of family businesses' long-term mindset. These include the stability and resilience of the business, a commitment to retaining staff and an attachment and contribution to community.

4.9 Mr Chris Lowe of Bus Association Victoria drew direct parallels between the reputation of the family name and the long-term approach of the family business. He told the committee that:

> …family values are very much transmitted over to the family business, unlike with non-family firms. With family businesses, it is all about continuity and continuance. There is…the legacy factor. The family name is all over the business, so it is very important that the family values are transmitted into the business. If there is a complaint against the business, it is a complaint against the family. Further, family businesses have a long-term orientation second to none. They are not so much in the game for the term of a contract which might be seven or 10 years; this is the industry that the family has chosen to commit itself to over generations, and this is how the family has made its name.[5]

4.10 Mr Sam Kennard, Managing Director of Kennards Self Storage stated that family business owners have 'a long-term enduring view to preserve our brand and assets for many generations'.[6] Mr Michael Claydon, owner of the Perth-based firm National Corporate Training, noted that the owners of long-standing family businesses are particularly conscious that they are continuing the family legacy and have a responsibility to ensure that it is preserved.[7]

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5 Mr Chris Lowe, Chief Executive Officer, Bus Association Victoria, *Committee Hansard*, 14 November 2012, p. 9.

6 Mr Sam Kennard, Kennards Self Storage, *Submission 15*, p. 2.

7 Mr Michael Claydon, Managing Director, National Corporate Training Pty Ltd, *Committee Hansard*, 7 February 2013, pp 24 and 26.

4.11 Mr Andrew Mostyn from the agribusiness company Craig Mostyn Group also linked the longevity of family businesses with their focus on their reputation. He explained that:

> …there are some underlying things that are prevalent in all family businesses. For many of us, our name is part of the company name. I think when that happens then there is a responsibility that you have for the longevity of the business and for the integrity of the business. So I do think that because that is the situation there is very much some underlying and common themes amongst the culture of family businesses.[8]

4.12 KPMG linked the long-term mindset of family businesses to their unique values and their connection with the community in which they operate. As Mr Bill Noye, National Leader of Family Business Services, told the committee:

> Family businesses do take a much longer term view. They are not so much focused on the short-term financial outcome but rather the long-term return on capital. Theirs is a different mindset from non-family businesses. Family businesses have applications that involve more than merely serving a financial purpose. They are a means of sharing certain values and providing a service to the community in which they are integrated. They are different. They do feel different. Their values are different. Culturally, they are different and they offer a unique benefit to our communities.[9]

4.13 Deloitte Private continued the theme. Mr David Hill, National Managing Partner of the firm, put the following argument:

> Virtually every family business has a long-term horizon. The family values are attached to the family business. The family name is attached to the family business. The legacy is attached to the family business. So decisions that family businesses take are for the long-term. One of the regular criticisms of government, for example, is that decisions are taken on terms. Corporates often are challenged by taking decisions based on quarterly reporting cycles—very short-term decisions designed to either buoy up a stock price or report a profit. Family businesses do not think that way; they think for the longer term because of their legacy, their values and their reputation. That is a wonderful culture in business for the future of this country of which we're all very proud. So I think that any attempt to sponsor family business with that long-term view—that view to a sustainable business to hand on to future generations—in various forms has to be a great thing for this country.[10]

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8 Mr Andrew Mostyn, Executive Director, Craig Mostyn Group Pty Ltd., *Committee Hansard*, 7 February 2013, p. 24.

9 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 10.

10 Mr David Hill, National Managing Partner, Deloitte Private, *Committee Hansard*, 14 November 2012, p. 8.

4.14 Mr Peter Taylor, the owner-manager of the Queensland-based construction company T & T Corporation, also contrasted the long-term mindset of family businesses with the short-term imperatives faced by corporates:

> It is a resilient sector which usually handles the volatility and variability of our economy better than corporations. There have been numerous surveys that have confirmed the advantages of family businesses compared to corporations…They plan longer term, with many owners focused really as much on stewardship as on short-term profit. They are not driven by the need to increase share value or generate large performance bonuses which often lead to short-term and sometimes high-risk strategies in corporations.[11]

4.15 Mr Robert Powell of Grant Thornton Australia contrasted the short-term decisions of investor-led businesses with the stability of family businesses' decision-making processes. As he told the committee, family businesses:

> …make long-range decisions. They are more stable because of that and they are not prone to making snap decisions about firing people or shutting down a division. They are prepared to ride out situations a lot more than investor led businesses because the investors are only interested in what happens to their money in the next 12 months as they may choose to sell out in six months.[12]

4.16 Professor Ken Moores told the committee that the long-term mindset of family businesses provides resilience in times of economic downturn, greater retention of labour and an effort to preserve their communities around them. He added:

> The average CEO of a family business is there for about 20 years. The average CEO of a non-family firm is there for about 3.89 years and going down. If you think about that for a moment, this is a person who has been there, learnt their job and has got the time and capacity to pass it on to the next generation, because they have learned a bit of wisdom. So there are a lot of characteristics about these firms that really need to be understood.[13]

4.17 The committee took evidence from Mr Steve Sampson, the fifth generation owner of the Lionel Samson Sadliers Group—Australia's oldest family business. Mr Samson noted that the company's long-term mindset created resilience and a commitment to staff retention:

> To give you our story, during the very tough times during the 1970s and 80s, when things were very, very tough, we made sure that we never sacked any person who was an employee of our business, because that is what the family wanted to do. They were willing to forgo a dividend, a profit, to

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11 Mr Peter Taylor, Family Business Australia, *Committee Hansard*, 16 November 2012, p. 26.

12 Mr Robert Powell, Grant Thornton Australia, *Committee Hansard*, 15 November 2012, p. 15.

13 Professor Kenneth Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 18.

> make sure that we supported and protected those employees. That is where you build loyalty, that is where you build a foundation for a business that is different to a corporate. The corporate is about the next quarter. The corporate is about: how do we fly somebody in to solve this problem?—whereas family business is about: how do we actually, long term, get through this together? The government needs to know the size and scope of that. It is a solid foundation to our economy that should be supported, because that is the resilient part of our economy, and hence they should know all about it.[14]

4.18 Professor Mary Barrett of the School of Management at the University of Wollongong noted that the tenure of Chief Executive Officers (CEOs) in family businesses is significantly longer than in the corporate world. She explained that the CEOs of family businesses:

> …are not jumping ship after three or four years like a lot of CEOs are, for the quick rewards and the golden parachutes. I believe the figure that somebody was groping for earlier is something like an average of 17 years, compared with three or four years. It is an order of magnitude longer that CEOs tend to stay there.[15]

4.19 Mr Matthew Power explained that the long-term perspective of family businesses is apparent in their decision-making processes. In particular, he noted that family businesses are more prepared to have assets on their balance sheets to provide long-term security:

> Most family businesses take a very, very long term view about things. They are looking to grow wealth not only for the current generation but for future generations, and they do it in a very conservative way…
>
> As a family business you take decisions that are going to make sure that they are going to run for five, 10, 15 or 20 years, so you will purchase a building, a piece of property or a piece of equipment not because of its immediate return but rather because of its long-term return and security of asset for the business, going forward, and to give the family assurance, going forward. It is quite a different time perspective in terms of the decision-making process. We do not have to answer to a corporate board, where we are driven by final rate of return on investment, and you will notice that if you look at a lot of the Australian public companies, they are divesting themselves of assets, insofar as a big corporation like Bunnings does not own its buildings. They rent their buildings because they do not

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14 Mr Stephen Samson, Director, Lionel Samson Sadliers Group, *Committee Hansard*, 7 February 2013, p. 22.

15 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 36.

> want those assets on their balance sheets—that reduces their rate of return on their asset usage.[16]

4.20 The committee believes that these issues of the tenure of CEOs in family businesses and the value of assets on family businesses' balance sheets could be areas of public policy interest (see recommendation 10).

An aversion to risk

4.21 A corollary of the long-term mindset of family businesses is that in general, they are also more conservative and risk-averse than non-family businesses. A November 2012 article published in the *Harvard Business Review* identified seven key differences between family firms and non-family firms that could explain the greater resilience of family businesses. The first three of these traits were as follows:

- family businesses keep their expenses under control and are 'frugal in good times and bad';
- family businesses tend to invest only in very strong projects. While they miss opportunities in periods of expansion, in times of crisis they have limited exposure (see chapter 9); and
- the firms studied were much less leveraged than the comparison group. From 2001 to 2009, debt accounted for 37 per cent of the capital of family firms compared to 47 per cent of non-family firms' capital.[17]

4.22 These themes were also prominent in witnesses' and submitters' evidence to this inquiry. Mr Des Caulfield, Director of MGI Australasia, told the committee that while family businesses may not agree:

> …as an observer and as an accountant who deals with them nearly all the time, I can see that they are much more cautious than many and were therefore better placed financially to handle the downturns in turnover et cetera that occurred.[18]

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16 Mr Matthew Power, ACT Chairman, Australian Family Business, *Committee Hansard*, 13 November 2012, p. 47.

17 Nicholas Kachaner, George Stalk and Alain Bloch, 'What you can learn from family business?', *Harvard Business Review*, November 2012, p. 104.

The research draws on a compiled list of 149 publicly traded, family controlled businesses with revenues of more than $1 billion across the United States, Canada, France, Spain, Portugal, Italy and Mexico where a family owned a significant percentage (not necessarily a majority) of the stock and family members were actively involved on the board and in management. The researchers used a comparison group of non-family controlled businesses, similar in size and in the same countries and sectors.

18 Mr Desmond Caulfield, Director, MGI Australasia Ltd, *Committee Hansard*, 14 November 2012, p. 24.

4.23 Mr Chris Lowe directly linked the long-term mindset of family businesses with their cautious approach and aversion to risk. He explained this link well in his submission:

> Family owners and managers often tend to have lengthy tenures and anticipate long careers, not only for themselves but for their offspring. Therefore they can be parsimonious stewards – careful to ensure that today's actions do not jeopardise the longer term prospects, or that an obsession with futuristic ambitions does not rob the firm of resilience or sustainability. Family owners' needs often span different time horizons: current needs such as income, dividends, and secure employment of family members; intermediate term projects and investments in capabilities and resources to perpetuate success across the long tenures of most family CEOs; and long-term projects to ensure a robust company for future generations. This is preservation of traditions from the past increasing family security as it encourages productive talent that can sustain the firm during periods of crisis or renewal, and family community status that provides access to resources today and builds reputation for the future.[19]

4.24 Some witnesses sought to qualify the image of family businesses as simply risk-averse. Mrs Janice Taylor, the owner of a third generation Tasmanian shipping business, told the committee that while the business is 'fairly conservative', it is 'not frightened to take a little risk'.[20] Mr Robert Pennicott, the owner of Pennicott Wilderness Journeys, told the committee that while the business prides itself on innovation, it is also 'a bit conservative as well'.[21] Mrs Philippa Taylor, Chief Executive Officer of Family Business Australia (FBA), described family business as a paradox: both conservative and at the same time 'extremely opportunistic'.[22]

4.25 Submitters gave three reasons for the risk-averse nature of family businesses. First, it was argued that family businesses are not under pressure to increase share value or generate large performance bonuses, which often leads to short-term and sometimes high-risk strategies in corporations.[23] Second, family businesses are often constrained in the extent to which they can borrow from financial institutions (see chapter 9).[24] And third, family business owners are conservative in their decision-

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19 Mr Chris Lowe, Bus Association Victoria, *Submission 20*, p. 11.

20 Mrs Janice Taylor, Taylor Bros, *Committee Hansard*, 21 January 2013, p. 44.

21 Mr Robert Pennicott, Pennicott Wilderness Journeys, *Committee Hansard*, 21 January 2013, p. 28.

22 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 35.

23 Mr Peter Taylor, Queensland Committee Member, Family Business Australia, *Committee Hansard*, 16 November 2012, p. 27; Mr Matthew Power, ACT Chairman, Australian Family Business, *Committee Hansard*, 13 November 2012, p. 47.

24 Mr Hugh McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 17.

making because they stand to lose their personal possessions if they make poor business decisions.

Skin in the game

4.26 Mr Matthew Power, a Canberra-based family business owner and the ACT Chairman of Family Business Australia, contrasted the mindset of family businesses and non-family businesses prior to the Global Financial Crisis. He attributed the difference to the personal equity that family businesses have at stake:

> The reality is that if you have got a good project with good numbers, it will get up. It is no different. During the pre-financial global crisis period, there was a whole stack of projects that got up that simply should not have—they were bad projects. Everybody was running on this whole concept of this growth which was beyond normal and therefore it was going to continue and there was money to be made—but they were bad projects before they started.
>
> With us, we typically cannot operate like that—because it is our house. Therefore, you are trying to be very, very conservative. If I have to sign a piece of paper that says at some stage in the future if all goes belly up my house is on the line and I am going to lose it all, you take a very, very different perspective about whether you are going to go into the project or not.[25]

4.27 Mr Donald McKenzie, a former partner at KPMG and a long-time advocate of family business, argued along similar lines:

> In some instances I have seen some very aggressive family businesses who have taken lending to the level that you probably would not see in a lot of other businesses. But I guess inherently a family business operator…generally has the family home on the line, basically just about lock, stock and barrel, other than the things we can set up by protecting them in structures that we try to do to protect some of the assets from things. They will tend to sit there and say, 'Well, we do have a more conservative view, because if I get this wrong not only have I lost my business but I have probably lost my home as well.' So I guess that drives people to be a little bit more sensitive about how they take investment risks.[26]

Flexible decision-making

4.28 A third characteristic of family businesses relates to the flexibility with which they make decisions and employ staff. Family businesses are often unencumbered by a board structure and can convene meetings and make decisions at short notice. They

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25 Mr Matthew Power, ACT Chairman, Australian Family Business, *Committee Hansard*, 13 November 2012, p. 51.

26 Mr Donald McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 17.

have flat and informal organisational structures that allow more responsiveness to immediate and unexpected challenges than hierarchically structured corporations.[27] In addition to flexible decision-making, the flat structure of many family businesses engenders flexibility in employing and providing opportunities for staff.

4.29 Mr Taylor of T&T Corporation emphasised the importance of family businesses' quick and responsive decision-making:

> There have been numerous surveys that have confirmed the advantages of family businesses compared to corporations. They are more flexible and can adjust more quickly to change, mainly because there is a concentration of ownership and you do not have to wait for a decision; you can ring up mum, dad and the kids and almost make the decision in an afternoon.[28]

4.30 Mrs Philippa Taylor of FBA expressed similar sentiments:

> They [family businesses] are very capable of making quick decisions. They do not have quarterly reporting in the way that a lot of corporations do. They can bring the family together and say, 'There will be no new Mercedes Benzes or utes this year because we're going to invest in some research and development,' or 'We're going to pull the horns in.'[29]

4.31 The issue of the flexibility of family businesses' practices also arose in the context of career opportunities for women. Professor Moores told the committee that on the basis of his research, the flexibility of family businesses' working arrangements benefitted women. He claimed that family businesses tended to be more accommodating of women in their need for time off work to raise a family.[30]

4.32 As gender roles become more fluid in modern families, the flexibility of family businesses will increasingly enable men to take up part-time work and caring responsibilities. It is likely that many more family businesses—particularly those conducted online—will have at least periods in which wives assume full-time responsibility for the running of the business while husbands assist in a part-time role. This could be an interesting trend to monitor.

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27 Mr Chris Lowe, Bus Association Victoria, *Submission 20*, p. 11.

28 Mr Peter Taylor, Queensland Committee Member, Family Business Australia, *Committee Hansard*, 16 November 2012, p. 27.

29 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 35.

30 Professor Ken Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard,* 16 November 2012, p. 19.

See also Professor Mary Barrett and Professor Ken Moores, *Women in Family Business Leadership Roles: Daughters on the stage*, Cheltenham, United Kingdom: Edward Elgar Publishing Limited, 2009.

4.33 Family businesses can also provide more flexible working practices in relation to the payment of family members. Mr Alan Berechree, the owner and manager of a family newsagency in Burnie, told the committee:

> I do pay my children the same as the award wage, mainly for ease of operation and because it takes all of the problems out of it. But also there is a lot more flexibility there that you would not be able to ask of employees. That is probably the bottom line. They work the couple of extra hours or they come in for half-shifts, which legally you cannot do under the Fair Work system.[31]

4.34 The committee recognises that the issue of under-payment of family members in family businesses is a matter of some controversy (see chapter 8). While there is no data to gauge the extent to which this is happening, the committee received some anecdotal evidence that the problem of underpayment may not be as pronounced as it once was. Professor Moores noted:

> As to this question of sweat equity and the lower rates of pay, the family firms that I speak to nowadays—and they are probably the more enlightened, I suppose, if we could call it that—tend to be not of that ilk. These days—and given the last 20 years of conversations—you pay real wages for real work and you do not necessarily want to have children beholden to the business.[32]

4.35 Nonetheless, the committee flags the issue of non-payment and underpayment of family members as an area of continuing concern. While it may be true that there are fewer family businesses these days that underpay family members, there are undoubtedly still many family businesses that emphasise that proper payment for work is a secondary issue to the health of the business. The argument, presumably, is that these arrangements assist the business, which in turn assists the family to provide for all of its members. However, the committee notes that registered businesses must comply with the terms of *Fair Work Act 2009*, including the provisions on the underpayment of wages. This issue is revisited in Chapter 8 of this report.

Retaining staff

4.36 The 2012 *Harvard Business Review* article presented research that found family-run businesses retained labour better than non-family firms.[33] The annual turnover of staff in family firms was nine per cent compared to 11 per cent for non-family firms. The article also observed that family businesses generally do not rely on financial incentives to increase retention. Instead:

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31 Mr Alan Berechree, *Committee Hansard*, 21 January 2013, p. 20.

32 Professor Ken Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 19.

33 Nicholas Kachaner, George Stalk and Alain Bloch, 'What you can learn from family business?', *Harvard Business Review*, November 2012, p. 104.

> …they focus on creating a culture of commitment and purpose, avoiding layoffs during downturns, promoting from within, and investing in people. In our study we found that they spent far more on training: €885 a year per employee on average, versus an average of €336 at nonfamily firms.[34]

4.37 Similar arguments were put to the committee. Submitters and witnesses identified the retention of staff as a key characteristic of family businesses. They noted that this is consistent with the view of family businesses as long-term planners with a conservative mindset and a need for staff that retain knowledge and take on tasks outside their immediate duties. They also argue that staff remain because they want to: they are treated better in family businesses than in non-family businesses.

4.38 Mrs Janice Taylor, the director of the Hobart-based shipping company Taylor Bros, emphasised her firm's commitment to its staff. As she told the committee:

> Consideration of staff is of prime importance. Some of the longer serving members commenced straight from school, completed apprenticeships, married, and now have young family members about to enter the workforce. These people have worked alongside you and provided you with loyalty and support, and have become extended members of your own family. Many of the younger newer staff members look to these long serving people for guidance, and you need to ensure that they receive the encouragement they need to follow in those footsteps. You must extend to these people stability, knowledge, diversity of skills and projects, ethics, work opportunity, workplace satisfaction, and mateship. In a field as diverse as ours, the loss of long term skills and knowledge is damaging, and retention of long term staff is the only way to ensure the retention of this valuable asset.[35]

4.39 Burnie Newsagent Mr Berechree told the committee that he currently employs seven non-family staff members. Two of these staff members were employed by Mr Berechree's late father in 1967 and in 1984.[36] Other witnesses, such as Mr Mark Kagan (formerly of Kagan Logistics), Mr Peter Levi of Colorific and Mr Peter Taylor of T&T Corporation, emphasised that retaining staff is a key part of the culture of family business.[37] Mr Taylor argued that there is a 'familyness' about belonging to a family business which is of major benefit for the company.[38] Mr Levi explained:

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34 Nicolas Kachaner, George Stalk, and Alain Bloch, 'What you can learn from family business?', *Harvard Business Review*, November 2012, p. 104.

35 Mrs Janice Taylor, Taylor Bros, *Submission 38*, p. 3.

36 Mr Alan Berechree, *Committee Hansard*, 21 January 2013, p. 22.

37 Mr Peter Levi, Managing Director, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 48; Mr Mark Kagan, *Committee Hansard*, 14 November 2012, p. 48.

38 Mr Peter Taylor, Queensland Member, Family Business Australia, *Committee Hansard*, 16 November 2012, p. 26.

> For a business like ours, our people are everything to us and I think that does distinguish family business very much from a lot of other businesses. A lot of people in our team, a lot of our senior people, come to us having worked in big business. They can no longer work with the culture of politics that is prevalent naturally in big businesses and so our family values are very important. Everyone who joins us signs a statement of family values as part of the professionalism of our business.[39]

4.40 FBA argued that the perception that they do not treat their staff well is something that grates with family businesses. Mrs Taylor of FBA claimed that family businesses are incredibly good employers. She cited the example of Akubra Hats which:

> …through two world wars and several recessions, have never laid off a member of staff. The family themselves have taken pay cuts to keep their staff—because a loyalty gets built up and the family employees become part of the family.[40]

4.41 Indeed, other family business owners sought to qualitatively differentiate their treatment of staff to the way that non-businesses deal with staff. Mr Samson noted that this difference was 'not necessarily all about the wage', but rather:

> People like working for a family business because of the relationships and the way they are treated. So we see that as a way of securing good people and keeping them.[41]

4.42 Mr Mostyn agreed:

> I think that family businesses tend to treat staff differently to how they are employed in the larger corporates. And I think that does play a part in keeping hold of staff. So I do think there is a difference. We try and encourage a number of family-oriented things within the workforce that I do not think exist outside. Yes, occasionally we lose people to a larger corporate and quite often they come back to work for us, because they think the grass is greener but they find out that it is not.[42]

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39 Mr Peter Levi, Managing Director, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 39.

40 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 35.

41 Mr Stephen Samson, Director, Lionel Samson Sadliers Group, *Committee Hansard*, 7 February 2013, p. 23.

42 Mr Andrew Mostyn, Executive Director, Craig Mostyn Group Pty Ltd, *Committee Hansard*, 7 February 2013, p. 24.

Community-based and community-oriented

4.43 An oft-cited characteristic of family businesses is the extent to which they are engaged with, and contribute to, the community in which they operate. This community-orientation is regarded by many as a key point of difference between family businesses and non-family businesses.

4.44 FBA emphasised the role that family businesses play in contributing to their community not only in terms of the services they provide and their understanding of the community, but also their contribution to non-profit organisations. Mrs Taylor made reference to the Dyson Bus Company, which in its 65 years of business has employed 5000 people. She told the committee that the Dyson family:

> …are enormously embedded in that community. Without that business there would be so many attributes and advantages in that community that would disappear from footy clubs to others. I do believe they have an enormously important role to play in the community and in the social fabric.[43]

4.45 Mr Smorgon told the committee that family businesses are involved in community activities that are 'well outside' their business interests. He claimed that family businesses are at the top of the list of donors to charitable organisations and 'give back more to the community than most other sectors'.[44]

4.46 Mr Lowe argued that a key point of difference between a multinational and a family business is the family business's connection with, and service to, the community. He argued that this contribution is not made by multinationals who are only focused on delivering the terms of the contract.[45]

4.47 The committee received accounts from family businesspeople themselves about the contribution that their business has made to their local community. Mr Michael Sharpe, the Joint Managing Director of the Gosford-based Sharpe Bros Australia, gave the following summary of his firm's involvement with the local community:

> Our father, Ron Sharpe, joined the business and started earth-moving works. Dad spent his life quietly helping others and was acknowledged as Gosford council's 2005 citizen of the year. In 2006 he was awarded the Order of Australia medal in recognition of his service to the community of

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43 Mrs Philippa Taylor, Director, Family Business Australia, *Committee Hansard*, 14 November 2012, pp 35–36.

44 Mr David Smorgon, Director, Generation Investments, *Committee Hansard*, 14 November 2012, p. 2.

45 Mr Chris Lowe, Chief Executive Officer, Bus Association Victoria, *Committee Hansard*, 14 November 2012, p. 9.

> the Gosford region through a range of service and social welfare organisations.
>
> My brothers, Richard and Hayden, and I continue that proud tradition, helping the community whenever we can. As we grow and expand our production as the third generation of Sharpe companies. We continue the philosophy of providing support to community groups through donations, sponsorships and volunteering. We have placed $25,000 over five years to support Australian artists through the Gosford Regional Gallery. My brothers and I feel that this long-term commitment has enabled the gallery to plan and build the art prizes with the confidence of sponsorship dollars…
>
> For many years the Sharpe family have all been involved with community organisations, including chambers of commerce across the Central Coast, Rotary International and Apex—just to name a few. We have been active in our support to the Australian Olympic team, the Salvation Army Red Shield Appeal, the Royal Volunteer Coastal Patrol, the Judo Federation of Australia, HunterNet Co-operative and Family Business Australia, serving on board positions and just helping where we can.
>
> As a family we have been able to help raise funds and commit donations to a full range of activities including medical research, volunteer bush fire brigades, surf clubs, art galleries and sporting groups from tennis clubs to judo clubs.
>
> Our community works are interwoven with our business.[46]

4.48 The committee received some comment from government agencies on the contribution of family businesses to the community. DRALGAS told the committee that the Regional Development Australia (RDA) Committees have highlighted that family businesses:

> …are important and valued employers in regions and communities; that they often provide essential goods and services to their communities; that they often buy locally from other businesses when they can; and that they often support clubs and community activities as part of the social fabric of communities and regions.[47]

4.49 Some witnesses emphasised the contribution of family businesses to the community in terms of the loss that their demise has caused to local communities. By way of illustration, Mr Donald McKenzie, a former partner at KPMG, gave the following example:

> The problem is that the consumer is, in the main, insensitive or even ignorant to the needs of the family business operator. Take, for example,

46 Mr Michael Sharpe, Joint Managing Director, Sharpe Bros Australia, *Committee Hansard*, 15 November 2012, pp 45–46.

47 Mr Simon Atkinson, First Assistant Secretary, Regional Policy and Coordination, Department of Regional Australia, Local Government, Arts and Sport, *Committee Hansard*, 13 November 2012, p. 33.

> the local golf professional. He has members of the club come into his shop, borrow a demonstration club, receive some free advice, return the club after a practice round and then go and buy the same club on the internet because they can buy it for a lower price. The members have not understood that if everyone did this it would mean one less family business into the future and a further breakdown in the community social structure.[48]

4.50 Mr McKenzie argued that there would be benefit in educating consumers about the importance of family businesses to the community, and buying products from local businesses. He claimed that if consumers do not recognise the impact of their decisions to buy online, businesses within small municipalities will close which could lead to some towns ceasing to exist.[49]

4.51 The same argument was put by Mr Berechree:

> It is vital that businesses in a community are supported by their community. In Burnie there is a thing called rate differential, where the CBD properties pay a higher percentage in rates than the houses and businesses in the rest of the town. Ten years ago you used to justify that by the fact that you are living off the support of that community. They are coming down there and giving you a business and everything like that, so you are prepared to pay a little bit extra. But now, the minute you lose the support of your community—as they take the easy options of buying online or buying out of town and all that sort of stuff—it is very hard to justify why you are doing it when the softball club comes in and asks for a donation. It becomes harder and harder to justify it if you are not getting the support of your community.
>
> As we mentioned earlier, education is probably the important thing because if I go out of business then nobody is going to be supporting the softball club and the football club. That is what makes a region and makes a small town. It is important that we have a level playing field. If somebody who has an option to buy online is paying a GST component it is the same as they would be paying if they were buying off us. With a level playing field the customer gets the choice of who they are going to support. We have all bought products online because it is cheaper, but it does not help the long term of your community.[50]

Committee view

4.52 The committee recognises that many family businesses in Australia make a significant contribution to their local community. Committee members, and indeed all parliamentarians, frequently attend awards ceremonies and charity fundraising events

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48 Mr Donald McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 9.

49 Mr Donald McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 9.

50 Mr Alan Berechree, *Committee Hansard*, 21 January 2013, p. 25.

where the efforts and contributions of local businesses are recognised. Many of these businesses are family businesses.

4.53 However, the committee believes that more could be done to publicise the contribution that these businesses make to local communities. A new set of awards could be created whereby parliamentarians are able to nominate a family business in their own State (for Senators) or electorate (for Members).

4.54 The committee notes that FBA currently has an awards system in each state and territory, as well as nationally, with the winners selected through a broad-based nomination process. These awards are important. The committee's suggestion would be in addition to these awards, with the objective of raising parliamentarians' awareness of family businesses' contribution to the local community.

4.55 The committee suggests that the Department of Industry, Innovation, Science, Research and Tertiary Education (DIISRTE) form a secretariat to appoint a judging panel for the awards:

- one from Family Business Australia;
- a notable family business owner (perhaps a winner of a previous FBA award);
- a DIISTRE official or an official from Enterprise Connect;
- a representative of a consultancy or a major bank;
- an academic with expertise in family business matters.

National Family Business Day, developed by Family Business Australia (see chapter 1), would be an ideal forum to recognise formally the winners, and to further raise the profile of family businesses within the Australian Parliament. Sponsorship of the awards could be financed by the adjudicating financial institution and consultancy.

Labour productivity, governance and performance

4.56 The committee also received comment on the possible influence that family businesses' size and governance structures have on their productivity and performance. This is an area of particular interest for the committee. If family businesses' governance structures and decision-making patterns contribute to higher growth and productivity than non-family firms, this should be a matter of genuine public policy interest. It should lead government to consider carefully the need for official data collection that is focussed on identifying a correlation between firm performance and factors that are unique to family businesses.

4.57 In a 2011 paper, Mr Francesco Barbera and Professor Kenneth Moores found that the contribution of labour productivity to the output of family firms was much greater than the relative contribution of labour to comparable non-family firms. The contribution of labour to output in family firms was also significantly greater than that of capital to output in these firms. The authors summarised their findings as follows:

> This study has investigated the effect of family involvement on Australian SMEs from 1995 to 1998, so we cannot claim to have definitively established whether family firms are more or less productive than non-family firms; however, we can claim that the assumption of homogeneous labour and capital shares between family and non-family firms is inappropriate. Moreover, on the basis of the unique characteristics of family firms, heterogeneous production inputs do matter empirically. Therefore, if we account for the role for family involvement and allow for unequal factor elasticities, perhaps we could better understand the differences in production strategy, planning, and other important productivity drivers between family and non-family firms. These results hopefully shed further light on the unique attributes of family firms and bring us closer to understanding the specific economic impact family involvement may have on a firm level.[51]

4.58 In evidence to the committee, Mr Barbera explained that family firms tend to cluster in certain industries which are more labour intensive because they tend to get more output from their labour force than non-family firms would. He added:

> The explanations that I offered in my paper were that they are a more flexible labour force which is willing to work for less money if need be and which has tacit knowledge because they have spent a large portion of their life working in that firm and in multiple departments in the firm. So, overall, the human capital in family firms is arguably much higher and thus contributes more to output than it does in non-family firms.[52]

4.59 Mr Lowe, who is currently conducting doctoral research into the links between the governance and performance of family businesses, made the following observations in his submission:

> Some studies conclude the performance of family firms is worse than non-family counterparts, which suggests that the family's desire for capital preservation, stability, and risk aversion keep the firm from pursuing strategies that might otherwise improve performances, but would also threaten the family’s continued control. Conversely, research suggesting that family firm performance is superior to others suggests that families are better stewards of firm resources because of an overall aversion to managerial opportunism.[53]

4.60 In evidence to the committee, Mr Lowe expanded on his PhD proposal:

> I am trying to prove that the family business governance model has cultural characteristics, capability and competitive advantages over the

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51 Mr Francesco Barbera and Professor Kenneth Moores, 'Firm ownership and productivity: a study of family and non-family SMEs', *Small Business Economics*, vol. 29, October 2011, pp 1–24.

52 Mr Francesco Barbera, *Committee Hansard*, 16 November 2012, p. 39.

53 Mr Chris Lowe, Chief Executive Officer, Bus Association Victoria, *Submission 20*, p. 11.

> multinational enterprise governance model in order to deliver on public transport outcomes…
>
> So in my PhD I will be outlining what those family business and multinational enterprise governance capabilities are. Then I will be formally quantifying that by way of a formal survey next year. I will be starting off by holding some focus groups just before Christmas and after Christmas with both Victorian-based [public transport] family business operators and international-based [public transport] multinational enterprise operators. I will be going to New Zealand, South Africa, England, Norway, Sweden and Canada in order to do an international comparison of the governance models and to formally quantify this competitive advantage which I suspect the family businesses have. So far my research is anecdotal and it is qualified but it is not quantified. But, in order to have government policy implications, I need to quantify it.[54]

4.61 Other submitters also drew attention to the mixed research evidence on the performance of family businesses relative to non-family businesses. In their submission, Professor Barrett, Dr Graves and Dr Thomas noted several academic papers that focus on how family businesses' characteristics influence SME growth, profitability and the propensity to export.[55] They observed that the findings of this research, in terms of the performance of family businesses relative to non-family businesses, were mixed:

- A 2000 article by Mr Jon Hall and Mr Clem Tozer of the ABS, for example, found that while management structure had a significant influence in those SMEs that experienced rapid growth in turnover between 1994–95 and 1997–

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54 Mr Chris Lowe, Chief Executive Officer, Bus Association Victoria, *Submission 20*, p. 9.

55 *Submission 14*, p. 3; The academic papers include:

Richard McMahon, 'An exploratory study of under and over-investment amongst manufacturing SMEs from Australia's Business Longitudinal Survey', *International Small Business Journal*, vol. 21, no. 1, 2003, pp 29–53;

Richard McMahon, 'Equity agency costs amongst manufacturing SMEs', *Small Business Economics*, vol. 22, no. 2, 2004, pp 121–140;

Chris Graves and Jill Thomas, 'Internationalization of Australian family businesses: A managerial capabilities perspective', *Family Business Review*, vol. 19, no. 3, 2006, pp 207–224;

Max Smith, 'An empirical comparison of the managerial development of family and non-family SMEs from Australia's manufacturing sector', *Journal of Enterprising Culture*, vol. 14, no. 2, 2006, pp 125–141, http://www.flinders.edu.au/sabs/business/research/papers/05-6.pdf (accessed 24 February 2013);

Bernice Kotey and Cathleen Folker, 'Employee training in SMEs: Effect of size and firm type—Family and nonfamily', *Journal of Small Business Management*, vol. 45, no. 2, 2007, pp 214–238.

98, family businesses were less likely to have experienced rapid growth in turnover and employment over the period.[56]

- A 2005 article by Associate Professor Bernice Kotey of the University of New England Business School examined the impact of firm size on performance (as measured in terms of profits, growth, efficiency and liquidity). It found that family SMEs perform at least as well as non-family SMEs, but that larger family firms would benefit from improved management of employee performance.[57]
- Another 2005 article by Associate Professor Kotey found that small family firms were less likely to pursue growth compared with similar non-family firms. The growth of medium-sized family businesses was lower than similar sized non-family firms. Management practices were less formal in family firms and the gap between family and non-family firms in this area widened with growth. Small family firms achieved greater profits than their non-family counterparts, although this disparity disappeared at the medium-sized level.[58]

Committee view on links between governance and performance

4.62 The committee believes that research into those factors that contribute to the performance of family businesses is an important and largely untapped area of inquiry. The committee commends the completed research to the proposed Inter-Departmental Committee (IDC) for its consideration. It believes that in terms of identifying the public policy rationale for a definition of family business and the collection of data, this research could hold some important leads.

4.63 To reiterate the point made in chapter 2, the IDC must be focused on the policy need for this data. It may be that on the basis of these discussions—and aided by the academic research—the IDC decides that data should be collected on the profits, growth, labour productivity and capital productivity of family businesses of different sizes.

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56 Jon Hall and Clem Tozer, 'Gazelles in the 1990s: Why did they leap so high?: An analysis of high growth firms from the Australian Business Longitudinal Survey 1994–95 to 1997–98', *Small Enterprise Research*, vol. 8, no. 2, 2000, pp 71–84, http://sbaer.uca.edu/research/icsb/2000/05.pdf (accessed 24 February 2013).

57 Bernice Kotey, 'Are performance differences between family and nonfamily SMEs uniform across all firm sizes?', *International Journal of Entrepreneurial Behaviour & Research*, vol. 11, no. 6, 2005, pp 394–421.

58 Bernice Kotey, 'Goals, management practices, and performance of family SMEs', *International Journal of Entrepreneurial Behaviour & Research*, vol. 11, no. 1, 2005, pp 3–24. This study was based on 233 small non-family and 362 small family firms. Medium firms comprised 305 family and 341 non-family firms.

Recommendation 9

4.64 The committee recommends that the Inter-Departmental Committee consider the policy need for data on issues including the profits and growth of family businesses of different sizes, and the labour and capital productivity of these businesses.

Final comment

4.65 The committee believes that the various characteristics of family businesses discussed in this chapter warrant the attention of policy makers. As part of the proposed IDC process, government agencies should reflect on whether the benefits of gathering data to test the strength of these characteristics outweigh the opportunity costs (in terms of other questions that could be put). These characteristics should be considered in addition to the 'definitional' and 'information' issues identified in Table 2.3.

4.66 There would need to be careful thought given to how these characteristics might be gauged. Some of the consultancies' surveys simply ask respondents whether they believe that family businesses value their staff more, or contribute to the community more than other businesses. It is not surprising that if they identify as a family business, they will tick these boxes.

4.67 If the IDC does decide to incorporate some of these family business characteristics into a survey, the measures need to be concrete. They could include:

- the value of assets on balance sheets;
- debt to equity ratios;
- the tenure of Chief Executive Officers;
- the average number of years of employee service to the business; and
- the business' philanthropic contributions as reported to the ATO.

Recommendation 10

4.68 The committee recommends that the proposed Inter-Departmental Committee assess whether data should be gathered to measure the key characteristics and behaviours of family businesses. In particular, consideration should be given to:

- **the value of assets on balance sheets;**
- **debt to equity ratios;**
- **the tenure of Chief Executive Officers;**
- **the average number of years of employee service to the business; and**
- **philanthropic contributions, as reported to the Australian Taxation Office.**

4.69 The interest in these issues, of course, is how they compare with the same indicators in non-family businesses. The committee understands that the Business Characteristics Survey conducted by the ABS contains a section on Business Performance Assessment.[59] Respondents were provided with a list of business performance measures (financial, cost, operational quality, innovation, human resources and environmental) and asked to indicate the extent to which they focussed on these measures. Respondents were also provided with a list of performance indicators and activities (income, range of products, productivity, profitability, social contributions etc.) and were asked to self-assess whether any of these had decreased, stayed the same, or increased compared to the previous year. If the IDC does consider that data should be gathered on the issues identified in Recommendation 9, the questions in the BCS Business Performance Assessment would be useful.

59 Australian Bureau of Statistics, 8167.0—Selected Characteristics of Australian Businesses, http://www.abs.gov.au/ausstats/abs@.nsf/Products/8167.0~2010-11~Main+Features~Business+Performance?OpenDocument (accessed 28 February 2013).

Chapter 5

The challenge of succession

> *...one of the big things globally that everyone is struggling with is succession—how do you transfer wealth from one generation to the next generation; how do you do it properly without causing a lot of issues within the family and sometimes breaking up the family? Globally I think Australia is probably leading the way as far as that is concerned.*[1]

> *...people need to be educated as to benefits and the consequences of a great succession plan...[F]rom my experience and from what I have seen, people who have the foresight and thinking get to where they need to go, because they plan to get there.*[2]

Introduction

5.1 The fourth article of this inquiry's terms of reference relates to the structural, cultural, organisational, technological and governance challenges facing family businesses. Arguably the most significant challenge that family businesses must address is the challenge of succession: preparing for and passing the business on to the next generation.

5.2 Indeed, many argue that it is this challenge that defines the success of a family business and distinguishes the business from non-family businesses.[3] Representatives of the family business sector, academic commentators and families in the sector identified succession as 'a major issue'.[4] The 2010 *Australian Family and Private Business Survey* found that matters affecting succession were among the more critical issues confronting family businesses.[5] Succession was listed first among the challenges identified by KPMG:

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1 Mr Peter Pagonis, Partner, Deloitte Private, *Committee Hansard*, 14 November 2012, p. 4.

2 Mr Ian Joseph, Executive Chair, Agribusiness Council of Australia, *Committee Hansard*, 7 February 2013, p. 16.

3 See, for example, Moores Family Enterprise, *Submission 8*, p. 5; Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40; Family Business Australia, *Submission 1*, p. 2; MGI Australasia, *Submission 9*, p. 6.

4 See, for example, Dr Christopher Graves, Professor Mary Barrett, and Dr Jill Thomas, *Submission 14*, p. 4; Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 38; Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 34; Ms Rosaria Panteleo, Chief Executive Officer, La Porchetta, *Committee Hansard*, 14 November 2012, p. 39.

5 Lucio E. Dana and Professor Kosmas Smyrnios, *The MGI Australian Family and Private Business Survey 2010*, RMIT University, July 2010, p. 15.

> The key issues facing family businesses are: management and equity succession, fostering and support of the complexity within the business, recognition and support of the complexity facing families in business as the owners and managers, the conflict inherent in family business where you have an overlap of ownership, family and business in management.[6]

5.3 The challenge of succession is common to family businesses across a range of sectors including transportation,[7] agriculture and primary industry,[8] and manufacturing.[9] Succession appeared as an issue common to all businesses in the family business sector regardless of their size.[10] Family Business Australia (FBA) told the committee:

> It is an enormously difficult task to find something that all family businesses completely agree upon, but I would say that there are certain fundamentals in common. One of them, for example, would be the issue of succeeding to the next generation and how policy can affect that positively.[11]

5.4 There is also a perception of the family business sector as a global community, with succession challenges common to family businesses regardless of geographical location:

> [O]ne of the big things globally that everyone is struggling with is succession—how do you transfer wealth from one generation to the next generation; how do you do it properly without causing a lot of issues within the family and sometimes breaking up the family?[12]

5.5 The succession challenge was depicted as an issue of ongoing concern. Mr Christopher Lowe, Chief Executive Officer (CEO) of Bus Association Victoria noted that 'succession has been an issue in my industry since year dot.'[13] PricewaterhouseCoopers argued that succession required continual management as economic and legal frameworks change:

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6 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 10.

7 Mr Christopher Lowe, Chief Executive Officer, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 10.

8 National Farmers' Federation, *Submission 29*, pp 7–8.

9 Mr Albert Beard, Chairman and Managing Director, A H Beard Manufacturing, *Committee Hansard*, 15 November 2012, p. 52.

10 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 40.

11 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 34.

12 Mr Peter Pagonis, Partner, Deloitte, *Committee Hansard*, 14 November 2012, p. 4.

13 Mr Christopher Lowe, Chief Executive Officer, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 10.

> Succession planning is not new in any sense but it is something that needs to be looked at anew given the post-World War II complexity that came about in business regulation, not only with family law and succession law from a wills and estates perspective.[14]

Strategies to assist intergenerational business transfers

5.6 Evidence varied on the essential features of viable succession plans. Research by MGI Australasia recommends that succession plans contain the following features:

- documentation of buy-sell agreements providing clearly defined and fair ownership options;
- a designated mandatory retirement age for all senior executives and owner managers;
- the appointment of a family leader to perform the role of supporting the family emotionally; and
- a definite date for the transfer of leadership responsibility and control to the next generation.[15]

5.7 Family businesses appearing before the committee noted varying features including the use of family trusts, family constitutions and transition periods to allow for graduated transfers of control.[16] Mr Albert Beard, Chairman and Managing Director, A H Beard Manufacturing, spoke of the necessity for clear documentation:

> How you join the business and all those sorts of things will be documented, they will have a much better understanding how the transition will work.[17]

5.8 Deloitte Private defined succession planning as a process of establishing measurable objectives and clear parameters on the roles and responsibilities of family members. It was further submitted that the process could usefully involve external expertise:

> Families need to clarify the qualities, educational requirements, work experience and expectations they have of the next generation. They also need to consider what support they will provide, i.e. a number of our clients have found using an independent mentor to work with next-generation

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14 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 27.

15 Lucio E. Dana and Professor Kosmas Smyrnios, *The MGI Australian Family and Private Business Survey 2010*, July 2010 p. 18.

16 See, for example, Mr Peter Ciliberto, Group Managing Director, Ciliberto Nominees Pty Ltd, *Committee Hansard*, 14 November 2012, p. 43; Mr Andy Kennard, Owner, Kennards Hire, *Committee Hansard*, 15 November 2012, p. 49; Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, pp 38–39.

17 Mr Albert Beard, Chairman and Managing Director, A H Beard Manufacturing, *Committee Hansard*, 15 November 2012, p. 52.

> family members is very helpful as a mentor is able to provide objective feedback free of family bias and uncluttered by family issues. It is also important to clarify who the next generation will report to, how they will be compensated and the performance criteria they will be measured on. It is critical these expectations are articulated from the outset and measures are as objective as possible.[18]

5.9 Professor Mary Barrett emphasised that while approaches may differ, the key is that succession planning takes place:

> What the research seems to say is that it is not the actual succession planning or the involvement of the next generation in strategic planning that actually makes a difference; it is more the fact that it happens. It is more the fact that it is addressed. It is not so much that the solution might be really fantastic, but more the fact that somebody's paying attention and attending to the issue.[19]

Barriers to managing succession

5.10 The evidence before the committee is that many family businesses are under-prepared for the challenge of succession. KPMG's 2009 family business survey (see chapter 3) indicated that the majority of family businesses do not have in place succession management plans. Of the family businesses surveyed in 2009, only 15 per cent reported having formal secession plans. A further 31 per cent reported 'they were currently working on one'.[20] The Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) advised of a 2006 survey of Australian farms which indicates that less than 10 per cent have established documented succession plans:

> ABARES included questions on farmers' succession planning in the National Farmer Survey 2006 undertaken to review the Agriculture Advancing Australia (AAA) package. The survey targeted farms with an estimated value of agricultural operations (EVAO) of $22,500 or more and the industries surveyed were: crops, mixed crops–livestock, sheep, beef, mixed sheep–beef, vegetables, fruit, sugar, cotton and wine grapes.
>
> In this survey, 52 per cent of farms indicated that they expected to pass the farm to a family member. Around 25 per cent of farms had a written business plan and a succession plan was included in only 35 per cent of business plans.[21]

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18 Deloitte Private, *Submission 16*, p. 17.

19 Professor Mary Barrett, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 37.

20 KPMG and Family Business Australia, *KPMG and Family Business Australia Survey of Family Businesses 2009*, p. 26.

21 Australian Bureau of Agricultural and Resource Economics and Sciences, answer to question on notice, 14 November 2012 (received 13 December 2012).

5.11 Pitcher Partners Consulting Pty Ltd identified 'a hesitation about succession, a reluctance to engage in what is seen as an uncomfortable discussion, uncertainty about how to proceed, and the resulting delay in commencing or engaging in a meaningful way in the process of succession'.[22]

Recognising the need for a succession plan

5.12 The committee heard of several reasons why family businesses may be hesitant to engage with succession planning issues. Mr Peter Taylor, a member of the Queensland chapter of FBA, identified a fundamental reason:

> One of the biggest difficulties we have in family businesses is owners who are yet to work out that they are in a family business and they need to work on succession. I have no idea how you get that light turned on in people's heads. I was fortunate in that I went to a family business gathering on Hamilton Island with about 500 other people. While I was there I sort of realised that this is not my business; this is a family business. The moment people recognise that they have a family business all these other opportunities—such as getting succession happening in a logical way, which might take a couple of years—can start to be taken.[23]

5.13 Conversely, it was put to the committee that businesses that identify as family enterprises may not be actively considering the role of future generations:

> I am the second generation, and a third generation is in the business. Up until 10 years ago I was really not conscious of necessarily passing it on to the next generation. It might have been there in the very background but there was no clear intention or plan or anything. It was only when I joined FBA and started learning about succession that I became aware of it.[24]

Balancing future planning with immediate management needs

5.14 It was acknowledged that predominantly family businesses are 'time poor'.[25] KPMG noted that time pressures can compromise planning, particularly in the area of succession:

> [Research] suggests that the main reason why family businesses fail is a 'failure to effectively and thoughtfully communicate' and finding the time to develop strategic planning involving multiple generations of the family, when faced with the day to day demands of the business itself.

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22 Pitcher Partners Consulting Pty Ltd, *Submission 28*, p. 8.

23 Mr Peter Taylor, Queensland Committee Member, Family Business Australia, *Committee Hansard*, 16 November 2012, p. 29.

24 Mr Andy Kennard, Kennards Hire, *Committee Hansard*, 15 November 2012, p. 49.

25 See, for example, Mr Nick Behrens, General Manager, Advocacy, Chamber of Commerce and Industry Queensland, *Committee Hansard*, 16 November 2012, p. 8.

> The failure to communicate typically revolves around the question of the future management and control of the business e.g. the capacity of the current owners to step aside, the confidence of the current generation in the ability of the next generation, the dilemma of moving from a dictatorship to a democratic environment.[26]

5.15 Family business owners noted similar time pressures. As Mr Matthew Power, manager and owner of the Canberra-based family business, Iken Furniture, explained:

> You go into a family business, you start the business, you have come out of a job and you probably have a small amount of cash. You are really working hard, you have brothers, sisters, mums, children and whoever to help you get going and you are working weekends.
>
> You start to see some cash, which is great. But then there is compliance and you have to do the minimum because you are selling and doing whatever you need to do. Then the next thing comes along and you do a bit more compliance, and then you start to put in place some procedures. A lot of this takes time. It is not even about the cash you are generating, it is the time to get your head around it. You are so busy trying to keep the business rolling along and getting the next order, whatever that order is, that is what tends to be the situation.[27]

5.16 KPMG identified that immediate business pressures can limit an enterprise's capacity to plan for succession:

> [V]ery often, when people are in business they do not have their minds on what is going to happen 20, 30 or 40 years out. They are focusing on growing the business and making the business work.[28]

5.17 Indeed, research conducted by KPMG in 2011 indicated that:

> …the main reason why family businesses fail is a failure to effectively and thoughtfully communicate and finding the time to develop strategic planning involving multiple generations of the family, when faced with the day-to-day demands of the business itself.[29]

5.18 In this context, the committee notes the implications of family business failure for family members' superannuation arrangements. In particular, it is of concern if family businesses presume that their assets are the best form of retirement savings. Should the business fail, those assets may need to be sold to cover debts, leaving family members without adequate retirement savings.

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26 KPMG, *Submission 21*, p. 10.

27 Mr Matthew Power, ACT Chairman, Family Business Australia, General Manager, Power Family Group, *Committee Hansard*, 14 November 2012, p. 53.

28 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 47.

29 KPMG, *Submission 21*, p.8.

The willingness and capacity of the next generation to manage the family business

5.19 The perceived and actual capacity of the next generation to assume ownership or management positions can also be a challenge to effective succession planning. FBA has noted research indicating that the success or failure of intergenerational transfers can be affected by the level of trust in the abilities of potential successors and the level of interest of potential successors in the business.[30] This research is consistent with the views of submitters to this inquiry.

5.20 The evidence before the committee highlighted concerns among the current generation that the next generation is not qualified, or is unwilling, to continue the family business. PricewaterhouseCoopers noted concerns that the next generation may not possess the requisite expertise:

> The proverbial, 'The first generation starts a business, the second generation consolidates it and the third generation loses it altogether' is a maxim that we would not want to be part of perpetuating, but there is some truth in some of these things.[31]

5.21 The committee was referred to research indicating that approximately 50 per cent of family businesses will be 'unable' to transfer ownership to the next generation 'due to lack of qualifications'.[32] Similarly, Deloitte Private advised that the current generation may consider delaying succession due to concerns that family members are not qualified to operate the business:

> They advise us they don't feel ready to hand over their business because they don't believe their children are ready to manage and grow it.[33]

5.22 Commenting on the decline of the next generation's interest in assuming responsibility for the business, MGI Australasia noted anecdotal evidence indicates that succession management practices have had to change to accommodate changing societal attitudes:

> [T]here is a change of the attitudes in the community or perhaps in the younger generations. Once it was almost assumed that if mum and dad had a business, the children would take over. That has certainly changed due to a number of things including the fact that business has changed so much now. The traditional business, the local supermarket or whatever, was never much different. All of a sudden there are all these other things out there

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30 Family Business Australia, *Australian family business sector statistics*, http://fambiz.org.au/documents/AustralianFamilyBusinessSectorStatistics.pdf (accessed 9 November, 2012).

31 Mr Paul Brassil, Partners, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 14 November 2012, p. 26.

32 Dr Christopher Graves, Professor Mary Barrett, and Dr Jill Thomas, *Submission 14*, p. 4.

33 Deloitte Private, *Submission 16*, p. 16.

> now so people are finding that the next generation does not necessarily want to take on mum and dad's business.[34]

5.23 Within the family business sector, there is a view that ownership is an entitlement not a privilege. As a family business adviser Mr Mark Cleary stated:

> [T]here is an assumption that I am part of the family I am going to manage it. Well, here is some news: not necessarily. That is not genetically passed on. There is no right.[35]

5.24 Mr Cleary argued that succession planning must prioritise 'commercial imperatives' rather than family ties:

> [T]here are commercial imperatives that I think some family businesses are light on because they have not been exposed at that tough edge of the world. They are full of heart, they are full of family values, but until they get that commercial edge I think that is an inhibitor. That is what I was getting at, that they need to be forced out and told, 'There is no place here for you until you earn a place at this table.'[36]

5.25 Mr Beard also spoke of the priority given to skills. He linked qualifications to financial stability and the capacity to raise necessary funds:

> Because our business relies very much on cash flow lending, the quality of the people looking after the business is very high on the agenda, without involving bricks and mortar. So yes the qualifications are very important to what I know about the ANZ Bank. They are probably already ticking those boxes themselves.[37]

5.26 There is an expectation by some family businesses for prospective owners to acquire skills outside the family business.[38] As Mr Desmond Caulfield, Director, MGI Australasia, noted family business advisors may encourage family members to gain experience outside the business:

> When the younger generation start getting into the business we will suggest to them that they need to go and do some outside training, even to the

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34 Mr Desmond Caulfield, Director, MGI Australasia Ltd, *Committee Hansard*, 15 November 2012, p. 25.

35 Mr Mark Cleary, Business Adviser, Sharpe Bros, *Committee Hansard*, 15 November 2012, p. 52.

36 Mr Mark Cleary, Business Adviser, Sharpe Bros, *Committee Hansard*, 15 November 2012, p. 49.

37 Mr Albert Beard, Chairman and Managing Director, AH Beard Manufacturing, *Committee Hansard*, 15 November 2012, p. 52.

38 See, for example, Mr Mark Cleary, Business Adviser, Sharpe Bros, *Committee Hansard*, 15 November 2012, p. 49.

extent of saying, 'Perhaps it might be worth going to work for someone else for a while, just to see how somebody else does things.[39]

5.27 Similarly, Deloitte Private advised:

Some of our clients insist family members must gain outside experience before being allowed to have a role in the family business, which gives family members an opportunity to prove themselves free of actual or perceived nepotism. They can then join the business with more to offer, having gained confidence and self-esteem from working in and proving themselves in an independent organisation.[40]

5.28 However, outside training and skills development does not appear to be a well-established practice in the family business sector. MGI Australasia conducted research in 2010 which indicates that 58.4 per cent of family businesses do not require family members to gain external experience prior to employment with the family enterprise.[41]

5.29 Submitters also noted that the success of intergenerational transfers can be affected by the willingness of the next generation to take responsibility for the family business. Some submitters were quite positive about the willingness of the next generation to be part of the business:

[Y]ou have to get the next-genners engaged in the business; that is No.1… I have seen young next-genners—people in their 20s—willing to step up and take on those roles.[42]

5.30 Mr Justin Taylor, Director of T & T Corporation, argued that there are factors that can encourage and motivate the next generation to be involved in the business. He explained:

It starts quite early. It depends what sort of family business you are in. The entrepreneurial spirit is alive and well in some of those families. It has a lot to do with your upbringing and whether you work inside the family business for a little while or whether the family lets the kids go and make mistakes on someone else's money and time. It is about bringing those experiences back into the family and encouraging growth and the concepts you get from outside the family to help the family business grow internally.[43]

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39 Mr, Desmond Caulfield, Director, MGI Australasia Ltd, *Committee Hansard*, 15 November 2012, p. 27.

40 Deloitte Private, *Submission 16*, p. 17.

41 MGI Australasia Ltd, *Submission 9*, p. 5.

42 Mr Justin Taylor, Director, T&T Corporation Pty Ltd, *Committee Hansard*, 16 November 2012, p. 32.

43 Mr Justin Taylor, Director, T&T Corporation Pty Ltd, *Committee Hansard*, 16 November 2012, p. 32.

5.31 In contrast, Mr Michael Stillwell of Stillwell Motor Group, argued that engaging the current generation is a key challenge for family businesses:

> The challenges for us in taking over the business were putting in place an effective governance regime and an effective reporting regime. Today we find that our challenge is one of engaging the third generation and making sure we can educate them and provide them with the professional development that they need to run the business going forward.[44]

5.32 The committee was advised of factors that could deter the next generation from assuming responsibility for the family business. In particular, it was noted that difficulties in communicating expectations relating to the role of running the business could hinder the succession process by creating uncertainty for the next generation. Pitcher Partners Consulting Pty Ltd advised that:

> Our research to date has identified…[a]n overwhelming view that children are not expected to follow in the family business and that they do have a choice, combined with the belief that they also do not have a natural entitlement to ownership and control. These views create uncertainty on both the part of the existing and new generation with neither being sure what the future holds.[45]

5.33 The problem of an apparent lack of interest among the current generation appeared to be particularly marked in rural areas. The National Farmers' Federation (NFF) reported that succession arrangements for Australian farmers have been affected by 'a decline in the rate of entry of young people into farming'.[46] ABARES also reported a decline in interest in family-owned agricultural enterprises:

> There is a lot of concern, too, with young people leaving the farm and a lot of people not wanting to come back to farming, so part of the succession planning is the fact that the next generation is not necessarily always wanting to go back to farming.[47]

The willingness and capacity of the current generation to relinquish control

5.34 The capacity of the next generation to take over, however, is only part of the necessary ingredients for a successful intergenerational transfer of the family business. It was argued that the willingness and capacity of the current generation to relinquish control is of equal importance. The 2010 *Australian Family and Private Business Survey* found that financial security of the current generation can influence succession

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44 Mr Michael Stillwell, Director, Stillwell Motor Group, *Committee Hansard*, 16 November 2012, p. 44.

45 Pitcher Partners Consulting Pty Ltd, *Submission 28*, p. 8.

46 National Farmers' Federation, *Submission 29*, p. 8.

47 Mr Paul Morris, Executive Director, Australian Bureau of Agricultural and Resource Economics and Sciences, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 13 November 2012, p. 44.

strategies. A 'substantial proportion' of the businesses surveyed reported that they are 'relying either on the sale of the business or continuing family business ownership for the cash to fund their retirement'.[48] Similarly, KPMG's 2011 survey records the view of family business owners that succession planning needs to provide for the current owners in their retirement. As one owner commented:

> No one is going to move aside for the next generation unless they know they're secure actuarially for the rest of their life. As John D. Rockefeller said, "I worked out how much it's going to cost me for the rest of my life to live and I am going to add a nought to it and make sure I get there".[49]

5.35 Evidence before the committee also captured the impact of succession on the current generation's ongoing financial security. Generally, it was noted that owners and operators of family businesses can be confronted with the challenge of funding retirement. Mr Michael Stillwell, Director, Stillwell Motor Group, reported being confronted with the challenge to 'fund our retirement out of the business'.[50] The Power Family Group also noted the challenges of funding retirement, submitting that succession places additional financial demands on the business without increasing the business' asset base:

> The next thing that challenges family businesses are equity, equity sharing and equity transfer. This is going to become particularly difficult over the next 15 years as the baby boomers, who have generated so much wealth and have been so successful, now want to transfer that wealth onto the next generations, and want to know how that is going to be achieved in a manner which both keeps the businesses as viable, going concerns and keeps people employed—which is the nature of where it is up to—so that it does not get continually divested, cut down and split as we go along.[51]

5.36 In addition to financial constraints, the committee's attention was drawn to concerns that the current generation may be unwilling to transfer ownership. Ms Pamela Low of Pamela Low and Associates reported that family businesses can be affected by an '[u]nwillingness of patriarchs and matriarchs to relinquish control and change habits'.[52] Similarly, Mr Justin Taylor, T & T Corporation Pty Ltd, argued that

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48 Lucio E. Dana and Professor Kosmas Smyrnios, *The MGI Australian Family and Private Business Survey 2010*, RMIT University, p. 23.

49 Focus group participant, as cited in, KPMG and Family Business Australia, *Stewards: Moving Forward, Moving Onward – KPMG and Family Business Australia's Family Business Survey 2011*, 2011, p. 24.

50 Mr Michael Stillwell, Director, Stillwell Motor Group, *Committee Hansard*, 16 November 2012, p. 44.

51 Mr Matthew Power, ACT Chairman, Family Business Australia, General Manager, Power Family Group, *Committee Hansard*, 14 November 2012, pp. 47-48.

52 Ms Pamela Low, *Submission 13*, p. 2.

successful succession planning should also focus on 'getting the incumbent willing to let go'. This aspect was identified as presenting challenges for family businesses.[53]

5.37 KPMG has noted a correlation between individual identity and business identity. As one participant to KPMG's 2011 family business survey commented 'I need to retire, that is a fact. But if I'm not that business, who am I?'[54] The NFF also suggested that the link between personal identity and involvement in the family business may deter the current generation from relinquishing the business:

> There are many obstacles to be overcome while developing a sound succession plan. For example, parents passing the farm business on to their children may be concerned that they will be marginalised.[55]

Management structures and family conflict

5.38 Two further and related issues were put forward as having the potential to derail successful succession planning. The Institute of Chartered Accountants Australia submitted that businesses with poor or informal management structures are less likely to successfully manage the succession process:

> Many family businesses, especially those in the SME sector, have little depth of management and the retention/attraction of key managers is critical for the successful transition of the business from the current owner/manager.[56]

5.39 Regional Development Australia Pilbara also noted the importance of appropriate management structures to the succession process:

> A key challenge for family businesses is the transference of ownership and management when leaders are seeking to retire or leave the business. Succession may be passed to family members, if there are any suitable and willing, yet there can be resistance to changes brought in by new family management. Ideally, family businesses need to balance the founding family values and culture that drive the business with an appreciation for new ideas and the changing business environment. These issues are also relevant when family businesses are sold or external professionals are introduced to run the business.[57]

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53 Mr Justin Taylor, T&T Corporation Pty Ltd, *Committee Hansard*, 16 November 2012, p. 32.

54 Focus group participant, as cited in, KPMG and Family Business Australia, *Stewards: Moving Forward, Moving Onward – KPMG and Family Business Australia's Family Business Survey 2011*, 2011, p. 26.

55 National Farmers' Federation, *Submission 29*, p.8.

56 Institute of Chartered Accountants Australia, *Submission 25*, p. 3.

57 Regional Development Australia Pilbara, *Submission 33*, p. 2.

5.40 Submitters also argued that family conflict can present a barrier to successful succession planning. Deloitte Private identified the following opportunities for conflict arising out of the succession process:

- Sibling competition, e.g. where all children want to be CEO of the business
- Parental expectations which can lead to feelings of unworthiness
- Inequality, both emotional and monetary, which can lead to conflict and unresolved issues among family members.[58]

5.41 Ms Pamela Low, Principal, Pamela Low and Associates, also referred to the potential for family conflict to derail the succession process. The committee was advised that succession is one area where private family dynamics can influence the business operation. As Ms Low stated, it is this challenge of addressing family dynamics within a business governance model that distinguishes family from non-family enterprises:

> The additional challenge for family businesses is this dynamic of the sense of entitlement of people that are members of the family outside the family [business] and the jostling for position in that organisation, status...That is the additional challenge for them.[59]

5.42 Ms Low went on to argue that communication between family members is a critical component of managing the intergenerational transfer of family business.[60]

Transferring the business to non-family members

5.43 There is a divergence of views on the merits of transferring ownership or management of the business outside the family. Pitcher Partners Consulting Pty Ltd argued that selling the business or otherwise incorporating non-family members are valid strategies to manage succession:

> Succession planning is often thought of only in the context of transferring a business within a family. However succession takes many forms and can comprise the outright sale of the business to third parties, merging the business with others and the sale of the composite business, the sale of the business to a management team and employees, the closure of the business and sale of assets, or in some cases doing nothing and facing the gradual decline of the business.[61]

5.44 In contrast, KPMG conceptualised a family business as an entity that is retained within a family:

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58 Deloitte Private, S*ubmission 16*, p. 17.

59 Ms Pamela Low, Principal, Pamela Low and Associates, *Committee Hansard*, 15 November 2012, p. 10.

60 Ms Low, Pamela Low and Associates, *Committee Hansard*, 15 November 2012, pp 10–11.

61 Pitcher Partners Consulting Pty Ltd, *Submission 28*, p. 7.

> To help support the long term stability and sustainability of family businesses, government should adopt policy measures that recognise the benefits of long-term multi-generational ownership by specifically recognising that on succession whilst individual ownership may change the family's ownership does not.[62]

5.45 PricewaterhouseCoopers indicated that KPMG's concept of a family business may be more in line with the views held by businesses within the family business sector. PricewaterhouseCoopers advised that there is a reluctance among Australian family businesses to involve non-family members. Its research indicates that almost 40 per cent of the businesses surveyed intend to transfer business management and ownership to the next generation. The remainder are twice as likely to sell or float rather than transfer ownership of the business to the next generation but assign management of the business to persons outside the family unit.[63] The data suggested that the concept of 'family' is intertwined with the concept of 'business'—the business cannot be viewed apart from the involvement of family members. As KPMG submitted:

> Central to all family businesses is the need for control to remain within the family and to have a mechanism in place that is sufficient to allow for the next generation to take over the family business.[64]

5.46 It was also argued that there may be limited opportunities to sell the business to non-family members. The committee heard comments that, in the absence of willing buyers, transferring ownership to third parties is 'not a viable alternative succession strategy'. Dr Chris Graves, University of Adelaide, Professor Mary Barrett, University of Wollongong, and Dr Jill Thomas, University of Adelaide, argued that the number of family businesses unable to transfer the business to the next generation exceeds the pool of third parties with the capacity to buy the businesses.[65] The problems associated with the absence of available buyers appear to be particularly marked in rural and regional areas. The Department of Regional Australia, Local Government, Arts and Sport identified particular challenges in selling businesses in rural areas given the absence of buyers.[66]

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62 KPMG, *Submission 21*, p. 2.

63 PricewaterhouseCoopers, *Submission 11*, p. 2.

64 KPMG, *Submission 21*, p. 15.

65 Dr Christopher Graves, Professor Mary Barrett, and Dr Jill Thomas, *Submission 14*, p. 4

66 Mr Simon Atkinson, First Assistant Secretary, Regional Apology and Coordination, Department of Regional Australia, Local Government, Arts and Sport, *Committee Hansard*, 14 November 2012, pp 34 and 37.

Growing expertise in succession management across the family business sector

5.47 Despite the challenges confronting family businesses, it was also evident there is growing expertise in the area of succession management. Mr Lowe from Bus Association Victoria advised that succession matters have received increasing attention over the past decade:

> When I look at my current membership of 470 bus operators, 95 per cent of them are third or more generation, so grandad or great-grandad started the business. So it is something that is not new to them. They have been working on succession planning in a very unsophisticated, non-academic manner for some years but in the last, say, 10 years we have seen a move by my membership, the 470 bus and coach operators, to adopt a more formal and documented process of succession planning.[67]

5.48 KPMG noted that preparing and training a successor is an issue of high to very high importance for 59.5 per cent of the family businesses surveyed by KPMG in 2011.[68] Data from the 2009 and 2011 KPMG surveys indicate that succession planning is increasingly on family businesses' radar. In 2009, 19.3 per cent of family businesses surveyed had established succession plans for the CEO.[69] In 2011, this figure had increased to 35 per cent.[70] The number of succession plans for other senior positions held by family members has also increased, from 18.4 per cent in 2009 to 28 per cent in 2011.[71]

5.49 The committee heard there is momentum within the sector to address the challenges of succession. As Deloitte Private advised, family businesses are seeking to increase skills relevant to managing the succession process:

> Deloitte Private believe educating the next generation of family members is the key to ensuring the successful transition of family businesses to future generations. In the majority of our Client Service Assessment interviews, the patriarchs/matriarchs of our family business clients ask us whether we have a program to educate their next generation.[72]

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67 Mr Christopher Lowe, Chief Executive Officer, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 10.

68 KPMG, *Submission 21*, p. 9.

69 KPMG and Family Business Australia, *KPMG and Family Business Australia Survey of Family Businesses 2009*, 2009, p. 10.

70 KPMG and Family Business Australia, *Stewards: Moving Forward, Moving Onward – KPMG and Family Business Australia's Family Business Survey 2011*, 2011, p. 12.

71 KPMG and Family Business Australia, *KPMG and Family Business Australia Survey of Family Businesses 2009*, 2009, p. 10; KPMG and Family Business Australia, *Stewards: Moving Forward, Moving Onward – KPMG and Family Business Australia's Family Business Survey 2011*, 2011, p. 12.

72 Deloitte Private, *Submission 16*, p. 16.

5.50 Similarly, Family Business Australia noted interest in professional development, advising that the organisation has instituted 'the first comprehensive Succession Planning Course designed to address both transactional challenges and the important emotional challenges of "handing over", whether it's a family (inter-generational transfer), non-family (external CEO) or sale'.[73]

5.51 Family business owners told the committee that the sector is developing sophisticated approaches to succession management that respond to the businesses' needs and the economic and legal environment. Mr Peter Levi of Colorific told the committee of his strategies to transfer the management and ownership of the company.[74] Mr Sam Kennard of Kennards Self-Storage spoke of the benefits of planning for both the transfer ownership and the transfer of management.[75] Mr Andy Kennard of Kennards Hire advised that his business is 'quite structured now in our succession planning', adopting measures that include a family constitution.[76]

5.52 Mr Graham Henderson, the managing director of a long-standing family business, and Director of Family Business Australia, also highlighted the significance of succession planning for businesses' success:

> With increased education maybe this would reduce the level of business failures in Australia. Business failures cost the economy lots of money, so education is very important and certainly I would encourage greater education in the area of family businesses and things like succession planning and governance. Those things I believe are very important.[77]

5.53 Education is seen as the key to fostering a culture of proactive succession management within the family business sector. Family business sector representatives, family business advisors and family businesses were united in the view that education is critical to the longevity of family enterprises.[78] Deloitte Private argued:

> We believe any efforts from the government to support education and assist family businesses and intergenerational wealth transfer would be very important. Training is key.[79]

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73 Family Business Australia, *Submission 1*, p. 7.

74 Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, pp 38–39.

75 Mr Sam Kennard, Kennards Self-Storage, *Committee Hansard*, 15 November 2012, p. 50.

76 Mr Andy Kennard, Kennards Hire, *Committee Hansard*, 15 November 2012, p. 49.

77 Mr Graham Henderson, Director, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 43.

78 See, for example, Mr Michael Sharpe, Joint Managing Director, Sharpe Bros Australia, *Committee Hansard*, 15 November 2012, p. 51; Mr Peter Taylor, Queensland Committee Member, Family Business Australia, *Committee Hansard*, 16 November 2012, p. 27.

79 Mr David Hill, National Managing Partner, Deloitte Private, Deloitte Touche Tohmatsu, *Committee Hansard*, 14 November 2012, p. 43.

Advantages of family trusts for succession planning

5.54 In addition to education and training, the committee heard of a number of options to assist the intergenerational transfer of family businesses. These include removing existing shareholder limitations in order to attract suitable business managers,[80] and the creation of a family trust.

5.55 The committee heard that family trusts play a legitimate role in the management of the intergenerational transfer of family businesses.[81] Notably, it was argued that family trusts are integral to successful succession planning:

> The reality is that a family business is not just the individuals currently running it; it is a family business, which means it is for the children and the grandchildren. There needs to be a mechanism whereby this family business can be transferred for the future generations to grow up and work in it. That is what the family trust really achieves. It enables that successful succession planning. It enables assets to be held for future generations.[82]

5.56 It was argued that family trusts possess features that facilitate business transfers. These included the apparent capacity of family trusts to provide structure and order to the succession process:

> [I]t can enable transition of control as well as transition of profits and entitlements from the company to be done in a structured and meaningful way over a period of time.[83]

5.57 Additionally, family trusts reportedly 'keep the business intact' by retaining family control. Mr Simon Le Maistre of KPMG argued that family trusts in effect encourage businesses to remain family enterprises as, in contrast to a company structure, a family trust structure does not provide family members the opportunity to divest their interests to third parties:

> If you had this in a vehicle like a company, the challenge is that it is likely the interests will be sold off, and very often those interests will be sold outside the family group. That will then change [the business] fundamentally. It will go from being a family operated and owned business to being something that is shared and owned amongst a variety of partners – and that changes very much the structure and the whole ethos behind what the family business is. If you keep in a trust it forces those involved, the family members, to work together…the ownership and control, ultimately, are not split amongst many.[84]

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80 See, for example, MGI Australasia, *Submission 9*, p. 5.

81 Institute of Chartered Accountants, *Submission 25*, p. 5.

82 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

83 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

84 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

5.58 Similarly, Mr Robert Powell, a Partner at Grant Thornton Australia, told the committee:

> I have also found that having family business assets in a trust is a way that people try to keep the family involved in the business. It is quite difficult to cash in your share of the trust. In fact, it is difficult if not impossible a lot of the time.[85]

5.59 This view was shared by several of the family businesses that contributed to the inquiry. Mr William Winter, BW Business Development, provided a personal account of the effect of not operating under a family trust structure:

> I will tell a story about me. When my father died, he did not leave a will. There are five children, as well as in-laws. We picked up on a phrase that you might have heard before: 'Where there's a will, there's a relative.' It was so true in our case. If he had had some kind of trust structure set up, my brother and I would probably still be running that family business.[86]

5.60 It was also argued that family trusts can remedy the barriers to successful succession planning posed by capital gains tax (CGT). Family business owners and advisers have claimed that CGT can undermine the prospects of a successful succession process, as CGT rules are 'restrictive and impact on their [family businesses'] ability to structure to continue to operate into the future.'[87] Family trusts were presented as a legitimate means to avoid the financial implications of CGT and, thereby, reduce the financial impact of a succession event:

> When you operate outside a trust you face many challenges – capital gains tax, stamp duty – with trying to transfer your business. Within the environment of family trust, this can be done when it is commercially right with minimal tax costs.[88]

5.61 However, it was further noted that due to changes to the *Income Tax Assessment Act 1997* effective as of 1 November 2008 family trusts could no longer operate to protect businesses from incurring capital gains tax when transferring business ownership to the next generation.[89] This issue is explored in chapter 6.

5.62 In contrast to views that family trusts provide, or could previously provide, an optimal means of ensuring intergenerational business transfers, the committee heard

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85 Mr Robert Powell, Partner, Grant Thornton Australia, *Committee Hansard*, 15 November 2012, p. 13.

86 Mr William Winter, BW Business Development, *Committee Hansard*, 14 November 2012, p. 41.

87 Mr Yasser El-Ansary, General Manager, Leadership and Quality, Institute of Chartered Accountants in Australia, *Committee Hansard*, 14 November 2012, p. 17.

88 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

89 See, for example, Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

evidence that family trusts present challenges to the succession process. The challenge of funding the retirement of the current generation remains for family businesses trading as family trusts.[90] It was also suggested that family trusts may impede a family business from evolving. Mr Stillwell commented that the family trust structures may reflect previous business needs rather than current business practice:

> The importance of trust structures has been touched upon today. My father did set up a trust when he went to work in the USA for 10 years back in the early 1980s. That structure has now passed on to us. The structure is out of date and we need to change that to modernise it and reflect custodianship from generation to the next generation going forward.[91]

Is succession necessary?

5.63 As chapter 4 observed, representatives and members of the family business sector have argued that family businesses are the bedrock of the Australian economy. By extension, the argument was put that continuing family businesses is necessary to maintain a productive and growing economy. As Dr Graves, Professor Barrett, and Dr Thomas argued:

> …a successful transition of family firms (e.g. to the next generation, via management buyout or sale) is critical to national economies because a successful transfer is estimated to conserve, on average, five jobs, whereas start-up generates on average two jobs.[92]

5.64 Mr Levi reiterated this view, arguing that family business closures that result from a failure to successfully transfer the business jeopardise the health of Australia's economy:

> If we can encourage the next generation to come through, take control and truly feel ownership of the business, that is going to benefit the employee, so there is a multiplier effect, because the business will not only continue but also flourish and continue to grow. If we do not do that, we are really at risk. I think it is a massive issue for this economy.[93]

5.65 Mr Levi argued the need for government policy and legislative support is required to assist the succession process. As he told the committee:

> I think it is vital, not only to the business – in this case, our business – but the economy as a whole that legislation supports the future of family business. Without a fair and effective transition mechanism, it is not going

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90 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 46.

91 Mr Michael Stillwell, Director, Stillwell Motor Group, *Committee Hansard*, 14 November 2012, p. 45.

92 Dr Christopher Graves, Professor Mary Barrett, and Dr Jill Thomas, *Submission 14*, p. 4.

93 Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 47.

> to be possible. There have been so many points raised today where it has been highlighted how family business adds value to the economy.[94]

5.66 The Institute of Chartered Accountants Australia also called for government policy to actively support the continuance of family businesses:

> We need to make sure that we do everything possible, as stated earlier, to put in place policies that help support and promote the viability of the family business sector in the future.[95]

5.67 The statistics indicate that a significant portion of family business owners are intending to retire in the coming decade. The Institute of Chartered Accountants Australia submitted that responding to the retirement of the baby boomer generation, and the resulting consequences for the family business sector, is one of the most significant challenges confronting Australia's economy:

> In this country we do have, as the committee would be well aware, a number of economic challenges, one of the most significant challenges related to demographic profiles our economy and the workers in our economy. There is cause for concern for us in this particular area if we are staring down the barrel of the situation where a very significant number of small businesses of family businesses are looking to exit the economy, in effect – to stop trading, to stop conducting business, to stop employing people and to stop making profits upon which they pay tax.[96]

5.68 Mr Levi argued that with the impending retirement of the baby boomer generation, support for the succession process is a pressing priority:

> [I]f, as I understand it, 70 per cent of Australian businesses are family businesses and 80 per cent of those are going to transition [in] the next 10 years, then it is a major issue for the Australian economy.[97]

5.69 The Institute of Chartered Accountants claimed that it is a priority issue that requires deliberate government intervention:

> There is certainly an argument that market forces will do whatever job they need to do in order to pick up gaps or fill voids. But I do not think that it is appropriate to leave all of the hard work to markets. There is an equally important role for policy to help guide and shape the way in which the market responds to various issues. If we get the policy settings right and put

94 Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 47.

95 Mr Yasser El-Ansary, General Manager, Leadership and Quality, Institute of Chartered Accountants in Australia, *Committee Hansard*, 14 November 2012, p. 21.

96 Mr Yasser El-Ansary, General Manager, Leadership and Quality, Institute of Chartered Accountants in Australia, *Committee Hansard*, 14 November 2012, p. 21.

97 Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 38.

> in place the right frameworks to help support rather than impede the growth of the family business sector then that can help.[98]

5.70 Pitcher Partners Consulting Pty Ltd concurred:

> As you are aware family businesses are among the most important contributors to wealth and employment creation in virtually every country in the world. They are a critical part of the Australian economy. It is forecast that family businesses valued at some $3.5 trillion+ will change hands over the next decade as the baby boomer generation pass their businesses on. The smoothness of this transfer will impact the prosperity of the Australian economy but no government policy exists to support the effectiveness of this transfer.[99]

5.71 Statistics were provided to support the view that the retirement of the baby boomer generation will significantly affect the family business sector and, by extension, the Australian economy.[100] The 2006 MGI Australasia *Australian Family and Private Sector Survey* estimated that 80 per cent of family businesses owners will retire in the coming decade. In citing this statistic, Pitcher Partners provided the following data:

> Commonly cited statistics from The MGI Family and Private Business Survey 2006 are:
>
> - 97% of businesses are privately owned
> - Average age of owners is 55 years of age (and therefore in 2012, the average age will be closer to 60 years)
> - Percentage intending to retire in the next 10 years is 81% (but most likely delayed by GFC)
> - Owners with no exit strategy is 75%
>
> And when considering the demographics of the Baby Boomer Generation:
>
> - Comprises persons born between 1946–1964
> - In 2012 their ages range from 48–66 years of age
> - In 2020 they will be between 56–74 years of age with the weighting heavily towards the higher end.[101]

5.72 The 2006 MGI Australasia *Australian Family and Private Sector Survey* reports that '84 per cent of CEOs plan to retire within the next 10 years'.[102] The survey

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98 Mr Yasser El-Ansary, General Manager, Leadership and Quality, Institute of Chartered Accountants in Australia, *Committee Hansard*, 14 November 2012, p. 21.

99 Pitcher Partners Consulting Pty Ltd, *Submission 28*, p.7.

100 See, for example, Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 47; Pitcher Partners Consulting Pty Ltd, *Submission 28*, p.7.

101 Pitcher Partners Consulting Pty Ltd, *Submission 28*, p. 7.

draws on information received from approximately 1000 Australian businesses, both family businesses and non-family enterprises. The definition of family business, or the methodologies used to distinguish a family enterprise from a non-family business, is unclear. While the survey report outlines various definitions of family businesses, the report does not indicate which definition was used for the purpose of the survey. However, the report does assert that the responses 'can be seen as representative of Australian privately owned enterprises'.[103] More recently, the 2010 MGI Australasia *Australian Family and Private Sector Survey* did not speculate on the number of family business owners intending to retire in the coming decade. However, the survey report noted that 45.2 per cent of family business owner-managers are intending to work beyond 65 years of age.[104]

5.73 Chapter 3 of this report discussed submitters' views on the KPMG estimate that 61 per cent of family business owners plan to retire by 2016.[105] The KPMG survey states that '26 per cent intend to retire within five years and 35 per cent between 5 and 10 years'.[106] With six years having passed since the survey was released, this suggests that less than half, indeed approximately a third, of Australia's family businesses will be affected by the retirement of the baby boomer generation.

5.74 Hunter Business Chamber and Regional Development Australia Hunter queried whether it was applicable to family businesses in the Hunter region, stating that 'we do not have on hand enough detail of the Deakin Uni's [sic] 2006 findings to know for sure if the data apply to The Hunter.'[107] Accordingly, further data collection was recommended:

> Given the potential impact of the statistics, and our roles as representatives and information providers to policymakers, it would be preferable to have current and local data regarding the intentions and future plans of the family business sector in the Hunter over the short, medium and long-term.[108]

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102 Professor Kosmas Smyrnios and Lucio E. Dana, *The MGI Australian Family and Private Business Survey 2006*, Melbourne, p. 24.

103 Professor Kosmas Smyrnios and Lucio E. Dana, *The MGI Australian Family and Private business Survey 2006*, Melbourne, p. 9.

104 Lucio E. Dana and Professor Kosmas Smyrnios, *The MGI Australian Family and Private Business Survey 2010*, RMIT University, July 2010, p. 23.

105 See, for example, Dr Christopher Graves, Professor Mary Barrett, and Dr Jill Thomas, *Submission 14*, p. 4; Family Business Australia, *Submission* 1, p. 7; Hunter Business Chamber and Regional Development Australia Hunter, *Submission 27*, p. 4.

106 Lynda Glassop, Pauline Hagel and Diane Waddel, *KPMG and Family Business Australia Family Business Needs Survey 2006*, 2006, p. 8.

107 Hunter Business Chamber and Regional Development Australia Hunter, *Submission 27*, p. 4.

108 Hunter Business Chamber and Regional Development Australia Hunter, *Submission 27*, pp 4–5.

5.75 The significance of the impending retirement of the baby boomer generation was also challenged by views that succession is not necessary to ensure a viable, growing economy. It was suggested that there is a natural evolution in the life cycle of family business. The committee received representations from Mr David Smorgon, Director, General Investments Pty Ltd, that their family businesses can take various forms and, consequently, their success may not require sustaining the business within the family:

> When you talk about family business, clearly dealing with succession goes hand in hand with that. But there is life after a family business. One of the things it is important that the committee understands is, particularly with the larger groups which may go through to the second, third and even the fourth generation, if the family business then sells out, for whatever reason, there is still life after the family business for the next generations, albeit in a different form.[109]

5.76 Deloitte Private concurred, arguing that the family business sector is broader than a conglomerate of individual family businesses. Mr Peter Pagonis argued that a family business can evolve into a 'family office':

> [i]t goes from a business to a family office, which is the Smorgon story. But it gets even better than that…All these family offices do help the next generation of new family businesses. That is the key point.[110]

5.77 Mr Smorgon noted that family businesses can divide and in doing so strengthen the economy through supporting further business initiatives:

> To highlight the point I made earlier, since then there are now probably up to 30 different Smorgon family offices—I will not call them business—set up for the seven branches of the family. This is because, once the funds were distributed to the seven families, each of those seven families then split up into brothers and cousins. So today I would estimate that there are up to 30 of them, all out in the marketplace, all doing their own thing, but making a contribution to the community as well.[111]

Committee view

5.78 The committee acknowledges that succession is a key challenge that separates family businesses from non-family businesses. The challenge relates not only to the governance of the firm, but also the underlying dynamics and culture of the business including its perception as a family business that can be passed on. Family businesses are unique in that they not only face the economic and financial hurdles common to all

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109 Mr David Smorgon, Director, General Investments Pty Ltd, *Committee Hansard*, 14 November 2012, p. 47.

110 Mr Peter Pagonis, Deloitte Private, *Committee Hansard*, 14 November 2012, p. 5.

111 Mr David Smorgon, Director, General Investments Pty Ltd, *Committee Hansard*, 14 November 2012, p. 5.

businesses, but in addition they must plan and time a succession that leaves the business with the requisite skills, knowledge and leadership.

5.79 The extent to which business ownership and management within the family business sector will change in the coming decade as a result of the retirement of the baby boomer generation is unclear. Without sufficient longitudinal data, the economic consequences of this generation's retirement are largely unknown. The committee reiterates recommendation 2 of this report, which draws the attention of the proposed IDC to the issue of succession and whether a public policy response is needed. To this end, the IDC must also consider whether it is necessary to quantify the extent to which ownership of family businesses will be transferred in the coming decade as a result of the retirement baby boomer generation.

Recommendation 11

5.80 The committee recommends that the proposed IDC consider the need to quantify the extent to which family businesses will be transferred or closed in the coming decade as a result of the retirement of the baby boomer generation, and the policy implications for the economy.

Chapter 6

The role of family trusts

6.1 Family trusts are considered important for the operation of many family businesses. Used properly, trusts enable family businesses to use available resources strategically and optimally. However, the committee heard that the existing legislative frameworks across the Commonwealth, States and territories pose challenges for family businesses trading through a trust structure.

6.2 This chapter considers the following three challenges to the effective use of a family trust structure.

- First, some have argued that the rule against perpetuities in State and Territory legislation undermines business longevity.
- Second, concerns were raised with the effect of taxation requirements under Division 7A of the *Income Tax Assessment Act 1936* (the 1936 Act), Division 6 of the 1936 Act, and the capital gains tax provisions.
- Third, some submitters criticised the inclusion of family trusts in the pool of assets available for distribution as part of a family law property settlement.

Trading trusts — overview

6.3 To understand these challenges, it is important firstly to understand the role that family trusts play in the family business sector. The following section provides:

- an overview of the trust structure, and its capacity to be used to facilitate business transactions (paragraphs 6.4–6.11);
- a summary of the use of trusts by family businesses (paragraphs 6.12–6.32); and
- various aspects of current Australian trust law (6.33–6.122).

6.4 The Australian Taxation Office (ATO) defines a trust as 'an obligation imposed on a person or other entity to hold property for the benefit of beneficiaries'.[1] Trusts are typically established by trust deed.[2]

6.5 Trusts are administered by trustees, which may be individuals or corporations.[3] Trustees hold legal title in the trust property and associated income.

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1 Australian Taxation Office, *Guide to the taxation of trusts*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&doc=/content/00245963.htm&page=3#P44_3570 (accessed 7 December 2012).

2 Harold AJ. Ford, Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law*, 12th edition, LexisNexis Butterworths, Chatswood, 2005, p. 24.

However, trustees are subject to two strict fiduciary duties. First, trustees must avoid a situation where their own interest may conflict with their duties as trustee. Second, trustees must not take an unauthorised profit from the trust.[4] The trustee may also be a beneficiary, provided they are not the sole beneficiary.[5] Unless otherwise specified in the trust deed, trustees are personally liable to third parties including creditors.[6] Trustees are appointed by, and may be removed by, an 'appointer', which is 'normally the person who has the greatest immediate interest in the affairs of the trust'.[7]

6.6 For beneficiaries, a trust creates an equitable interest in the trust property and associated income.[8] Their interest may be discretionary or clearly defined. Discretionary trusts do not provide beneficiaries definite rights to the income or capital generated by the trust. Their entitlements depend on the trustee electing to distribute income or capital.[9] This contrasts with 'fixed trusts' in which beneficiaries' entitlements to property and/or income is established, in writing, as part of the trust deed. Accordingly, fixed trusts do not provide the trustee discretion to determine the beneficiaries' entitlements.[10] While nominally entitled to the income generated by the trust property, beneficiaries may also be 'personally liable to the trustee to the extent of their interest in the trust'. Accordingly, it has been argued that where trust assets are

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3 Australian Taxation Office, *Guide to the taxation of trusts*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&doc=/content/00245963.htm&page=3#P44_3570 (accessed 7 December 2012).

4 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 4th edition, Lawbook Co, Pyrmont, 2007, p. 570.

5 Harold AJ. Ford, Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law*, 12th edition, LexisNexis Butterworths, Chatswood, 2005, p. 24.

6 The Hon Justice Paul Brereton, *A trustee's lot is not happy one: Address to the National Family Law Conference*, 19 October 2010, p. 1, http://www.lawlink.nsw.gov.au/lawlink/Supreme_Court/ll_sc.nsf/vwFiles/brereton191010.pdf/$file/brereton191010.pdf (accessed 7 December 2012).

7 The Hon Justice Peter Nygh and Andrew Cotter-Moroz, 'The Law of trusts in the Family Court', *Australian Journal of Family Law*, 1992, vol.6, pp 4 and 5, as cited in The Hon Justice Paul Brereton, *A trustee's lot is not happy one: Address to the National family law conference*, 19 October 2010, p. 2, http://www.lawlink.nsw.gov.au/lawlink/Supreme_Court/ll_sc.nsf/vwFiles/brereton191010.pdf/$file/brereton191010.pdf (accessed 7 December 2012).

8 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 2007, p. 49.

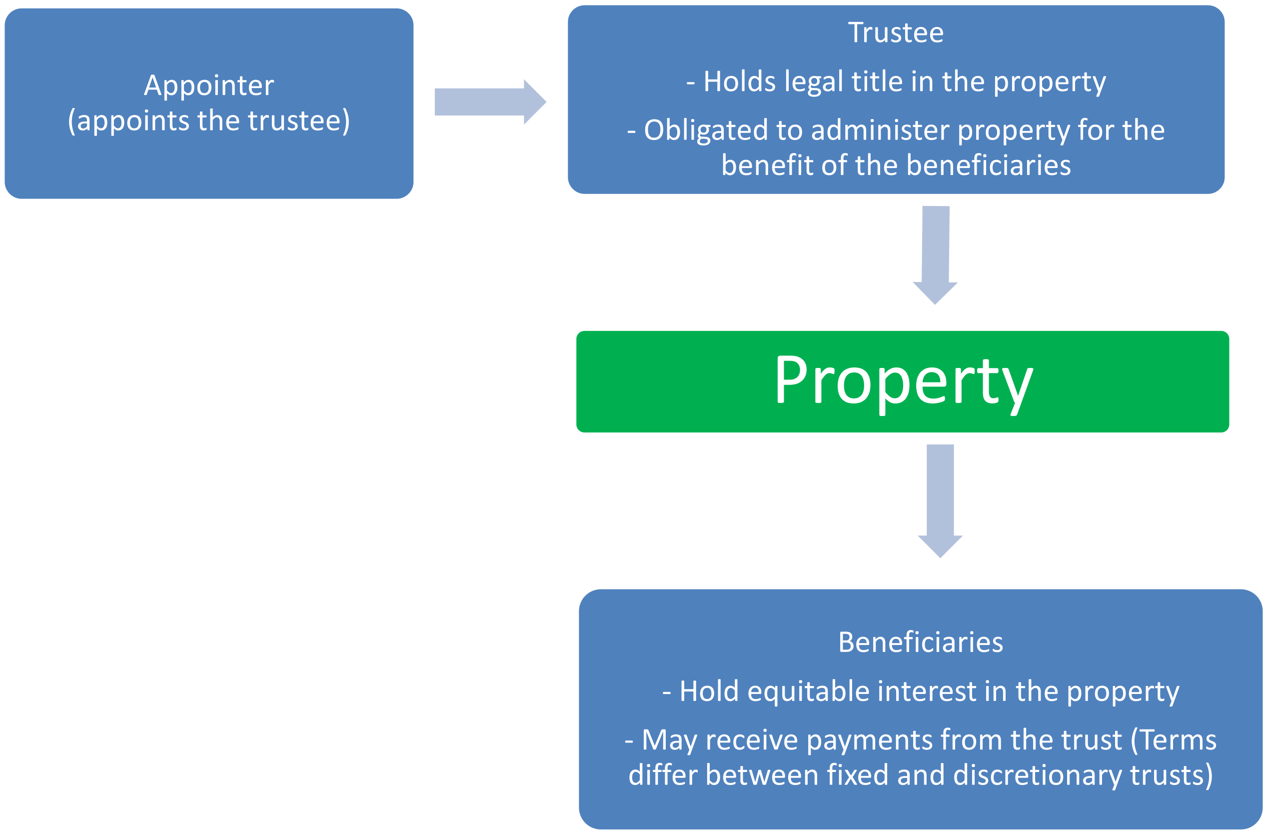
9 Australian Taxation Office, *Guide to the taxation of trusts*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&doc=/content/00245963.htm&page=3#P44_3570 (accessed 6 December 2012).

10 Australian Taxation Office, *Guide to the taxation of trusts*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&doc=/content/00245963.htm&page=3#P44_3570 (accessed 6 December 2012).

insufficient to repay creditors, beneficiaries may be personally liable to address any shortfall.[11]

6.7 Figure 6.1 shows the basic relationship between a trustee and beneficiaries.

Figure 6.1: The trust structure



The use of trusts to facilitate commercial transactions

6.8 Historically, trusts were used for private arrangements. Their origins lie in medieval English property and succession law. Trusts, or 'uses', were primarily used for estate planning purposes to transfer property to heirs and descendants.[12] However, Trusts were also used to 'circumvent the payment of [feudal] dues'.[13] There was a decline in the use of trusts following the introduction of legislation in 1535 which sought to disrupt the effect of the trust by recognising beneficiaries as the property

11 Philip Lipton and Abe Herzberg, *Understanding Company Law*, 12th edition, Lawbook Co, Pyrmont, 2004, p. 43.

12 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 2007, pp 432–433.

13 Treasury, *Consultation paper: Modernising the taxation of trust income—options for reform*, November 2011, p. 4.

owners for the purposes of levying duties. This legislation prompted the further development of the trust structure.[14]

6.9 The 20th century witnessed a marked expansion in the use of trusts. Trusts 'expanded from being principally a landholding device to instruments of commercial activity'.[15] Accordingly, as academic commentators have noted:

> companies, partnerships and unincorporated non-profit associations do not represent all the structures available for collective action towards a common goal. A commercial enterprise requiring contributions of capital from a number of contributors can be organised as a trust.[16]

6.10 Trusts have retained their traditional role in estate and succession planning, while expanding into other commercial settings. They are, for example, used as investment vehicles (typically known as 'unit trusts'), for charitable purposes, and to prioritise payments to certain creditors.[17] Trusts established for trading purposes, also known as 'trading trusts', hold property for the purpose of conducting business. Trading trusts typically consist of a limited liability corporate trustee holding the business on a discretionary trust for beneficiaries or in a fixed trust for unit holders.[18] Ultimately, businesses that operate through a trust structure will be subject to trust law requirements.

6.11 The legal implications for businesses operating through a trust structure differ to those that operate as a corporation. Unlike a company, a trust is not a legal entity — this means that the trust cannot sue or be sued.[19] Trustees therefore may be personally liable for debts incurred in administering the trust. Beneficiaries, unlike members of a company, have no power to direct the trustee on the administration of the trust unless this power is specified in the trust deed. Trustees of a trust, unlike directors of a corporation, cannot personally guarantee a trust liability.[20]

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14 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 2007, p. 434.

15 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 2007, p. 434.

16 Harold AJ. Ford, Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law*, 12th edition, LexisNexis Butterworths, Chatswood, 2005, p. 20.

17 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 2007, pp 434–435.

18 Gino E. Dal Pont and Donald RC. Chalmers, *Equity and Trusts in Australia*, 2007, p. 435.

19 Australian Taxation Office, *Guide to* the *taxation of trusts*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&doc=/content/00245963.htm&page=3#P44_3570 (accessed 7 December 2012).

20 Harold AJ. Ford, Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law*, 12th edition, LexisNexis Butterworths, Chatswood, 2005, pp 23–24.

Family trusts in Australia

6.12 Estimates vary as to the number of family businesses that operate through a trust structure. MGI Australasia found in its 2010 Australian Family and Private Sector Survey that only 12.2 per cent of family businesses operate as family trusts. The vast majority, 80 per cent, are structured as private companies; 5.1 per cent trade as partnerships; and the remaining 1.2 per cent operate as public companies.[21]

6.13 Treasury officials estimated that of the 700,000 discretionary trusts operating in Australia in 2009–10, approximately 225,000 were family trusts. However, Treasury also noted the limitations of the data:

> How accurate that is is difficult to say because it is a self-assessing label. It is just something you tick on your tax return. Some people might misunderstand…[22]

6.14 Anecdotally, family trusts appear to be a common feature of family businesses. Deloitte characterised their use as 'typical':

> A typical family business comprises a corporate operating entity owned by a discretionary trust with both family members and a corporate entity as beneficiaries. For family groups the equity in the corporate operating entity is often the primary investment asset. A trust structure is regularly selected to hold significant long-term investments of family groups for asset protection and succession planning purposes.[23]
>
> MGI Australasia also identified trusts as a prominent feature of the family business sector. Its 2010 survey found that 80.0% of family businesses are structured as private companies and just 12.2% as private trusts, most of which we could presume are family discretionary trusts. At first glance this might give rise to the impression that trusts have a relatively minor role in family business structures.
>
> It is our contention, as experienced family business advisers, that trusts play a much more significant role in the structuring of family enterprises. Whilst there is no definitive data to validate this observation, we can point to substantial anecdotal evidence that supports:
>
> - that a substantial proportion of shareholdings in family businesses are held by family discretionary trusts and
> - that regularly "passive" assets associated with the family business, such as land and buildings, are held in family trusts.[24]

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21 MGI Australasia, *Submission* 9, p. 4.

22 Mr Tony Poulakis, Assistant Commissioner, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 14.

23 Deloitte Private, *Submission 16*, p. 22.

24 MGI Australasia, *Submission* 9, p. 6.

6.15 Family trusts are typically discretionary trusts.[25] Family trusts differ from other forms of discretionary trusts in that the pool of beneficiaries is limited to family members. Under the *Income Tax Assessment Act 1936*, a 'family' is defined for the purposes of discretionary trusts with reference to the 'test individual'. A person may be a beneficiary of the family trust if he or she is the spouse, parent, grandparent, brother, sister, niece or nephew, or the lineal descendant, of the test individual.[26]

6.16 Alternatively, as Deloitte Private explained, dividends may be distributed to a corporate beneficiary connected with the family—rather than to individual family members—to fund business activities. This mechanism reportedly reduces tax liabilities and reduces the funds available to the business, as the dividends are not subject to higher individual tax rates.[27]

6.17 KPMG suggested that company structures are often complemented by a family trust. Therefore, the data on the number of companies within the family business sector may also include companies that operate in conjunction with a subsidiary family trust:

> The main operating entity employed by family business is a private company. For reasons associated with asset protection and maintaining the family's long-term ownership and control of that capital, many families may own their equity in a business (the shares in the company) through a discretionary trust structure.[28]

6.18 The Australian Taxation Office (ATO) submitted a similar theory:

> On the face of it you might ask why aren't all family businesses or the lion's share using that family trust as the operating entity. The data indicated that it is the lion's share of the company that runs the business. It is fair to say that in some industries, or even in just trying to raise finance, it is easier to do so with a company as long as that is supported by a discretionary trust underneath owning the shares, and that makes a lot of sense to get the advantages of both structures or both entities in your family business structure.[29]

6.19 The chartered accounting firm, Grant Thornton, noted that family trusts are commonly established with a company acting as trustee:

> Companies are often used in conjunction with the family trust, most commonly to act as a trustee of the trust, due to the limitation of liability afforded by a company structure; thereby providing a degree of protection

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25 Grant Thornton, *Submission 18*, p. 1.

26 *Income Tax Assessment Act 1936,* Schedule 2F, ss. 272–95(1).

27 Deloitte Private, *Submission 16*, p. 22.

28 KPMG, *Submission 21*, p. 10.

29 Mr Tony Poulakis, Assistant Commissioner, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 15.

> for the business assets which are being held in trust, as well as the personal assets of the family members, which would potentially be exposed should those individuals act in the capacity of trustee. In this situation, one or more family members would normally be shareholders and directors of the trustee company.[30]

6.20 It added:

> [T]he two legal structures most favoured by family businesses in Australia are companies and trust estates, however the most prevalent structure used is the family trust. This is particularly the case for businesses commenced prior to the late 1970's, possibly due to the (then) existence of death duties.
>
> […]
>
> In recent years this writer has seen more family assets being owned in a company structure, which for new businesses is now as prevalent if not more prevalent than family trusts. Despite relative advantages of family trusts…I expect the trend away from family trusts to continue.[31]

The tax minimisation benefits of operating a family trust

6.21 One of the benefits of operating a trust structure is income streaming, whereby certain types of income, specifically franked dividends and capital gains, is diverted to beneficiaries. Income streaming is available to trust beneficiaries but not to members of a company.[32] In evidence to the committee, Treasury identified income streaming and the associated income tax advantages as a principal motive for operating a trust structure:

> I guess the key advantages from a family business perspective of operating a trust relate to the ability to stream income to beneficiaries and to retain the character of that income in the hands of beneficiaries. Neither of those advantages is available in a company structure.[33]

6.22 Academic commentators have also argued that the decision whether to operate as a company or through a trust will be guided by the taxation implications of both structures.[34] Professor Harold Ford, University of Melbourne, Dr Robert Austin, University of Sydney, and Professor Ian Ramsay, University of Melbourne, have

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30 Grant Thornton, *Submission 18*, p. 1.

31 Grant Thornton, *Submission 18*, pp. 1, 3.

32 Mr Hector Thompson, General Manager, Small Business Tax Division, Treasury, *Committee Hansard*, 13 November 2012, p. 14.

33 Mr Hector Thompson, General Manager, Small Business Tax Division, Treasury, *Committee Hansard*, 13 November 2012, p. 14.

34 Harold AJ. Ford, Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law*, 12th edition, LexisNexis Butterworths, Chatswood, 2005, p. 7.

concluded that '[w]hether a company or a trust will be employed will depend on the impact of current taxation legislation in respect of companies and trusts.'[35]

6.23 In its submission to this inquiry, the accounting and advisory firm, Pitcher Partners, emphasised the lure of capital tax concessions in opting to establish a trust structure:

> [T]rusts are often favoured to companies from a tax perspective, as they are able to access capital gains tax concessions that are not available to companies. This can be an important consideration when establishing a family business, as the disposal of the business at a later date will often result in a capital gain.[36]

Other benefits of operating a family trust

6.24 However, several submitters challenged the view that family trusts are established primarily to minimise taxation obligations. They cited broader advantages of operating a trust structure; namely to:

- assist the business to manage succession and related estate planning issues;[37]
- provide a mechanism to retain control of the business within a family;[38] and
- provide asset protection.

6.25 Family Business Australia put to the committee that a family trust structure allows control to be retained within the family and encourages an equitable business governance model:

> The use of trusts, particularly discretionary trusts, plays an integral part in any family or privately held group structure. In essence, any family unit is best described as a "socialist" system where all members are encouraged to be inclusive and treat one another fairly.[39]

6.26 Family Business Australia (FBA) also distinguished between tax avoidance and tax minimisation and emphasised the importance of trusts for protecting family assets:

> The other thing that annoys them [family businesses] is the perception that family businesses use trusts because they want to minimise or avoid tax. They will always want to minimise tax, but they will certainly not avoid

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35 Harold AJ. Ford, Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law*, 12th edition, LexisNexis Butterworths, Chatswood, 2005, p. 7.

36 Pitcher Partners Consulting Pty Ltd, *Submission 28*, p. 10.

37 See, for example, Family Business Australia, *Submission 1*, p. 7. This issue is explored in chapter 7 of this report.

38 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

39 Family Business Australia, *Submission 1*, p. 7.

> tax. In fact, the trust structures are there to protect the family assets from business mistakes. I think that there is a lot of misapprehension about things like trusts, and why family businesses embrace them.[40]

6.27 Mr Simon Le Maistre of KPMG also downplayed tax arrangements as a motivator for using a trust structure:

> I often see the tax advantages of family trusts and so forth, but when I deal with my clients, the amount you are talking about with the tax advantages around the income streaming and so forth is really lost in the enormity about what the real issue is here—that is, the more commercial drivers.[41]

6.28 He added:

> [I]n the family trusts we see I still recommend to many of my clients that a vital part of being able to achieve proper estate planning and proper asset protection is the need to keep the business intact for future generations.[42]

6.29 Mr Robert Powell of Grant Thornton, told the committee:

> [T]here has been a huge focus on the tax benefits of trusts and I think that is an overfocus…That is a very minor consideration for families that decide to use trusts in a family business situation. The other issues, in my experience, have more relevance and more prevalence as to why those trusts are set up. Tax is a by-product; it is not the main reason for doing it.[43]

6.30 MGI Australasia argued: 'it is timely to dispel the regularly dispensed myths that family trusts are no more than a tax avoidance measure'.[44] Mr Bill Winter of BW Business Development, similarly, suggested that the perception of family trusts as a tax avoidance mechanism is outdated:

> I had a family trust. When I set up my business with my brother, we were advised to set up a trust for tax reasons back in the 1970s. Obviously, that has changed.[45]

6.31 Deloitte Private conceptualised family business as a broad structure, referred to as a 'family group', of which family trusts are an integral part. Figure 7.2 illustrates Deloitte Private's concept of multiple business ventures conducted by the same family

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40 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 35.

41 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

42 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

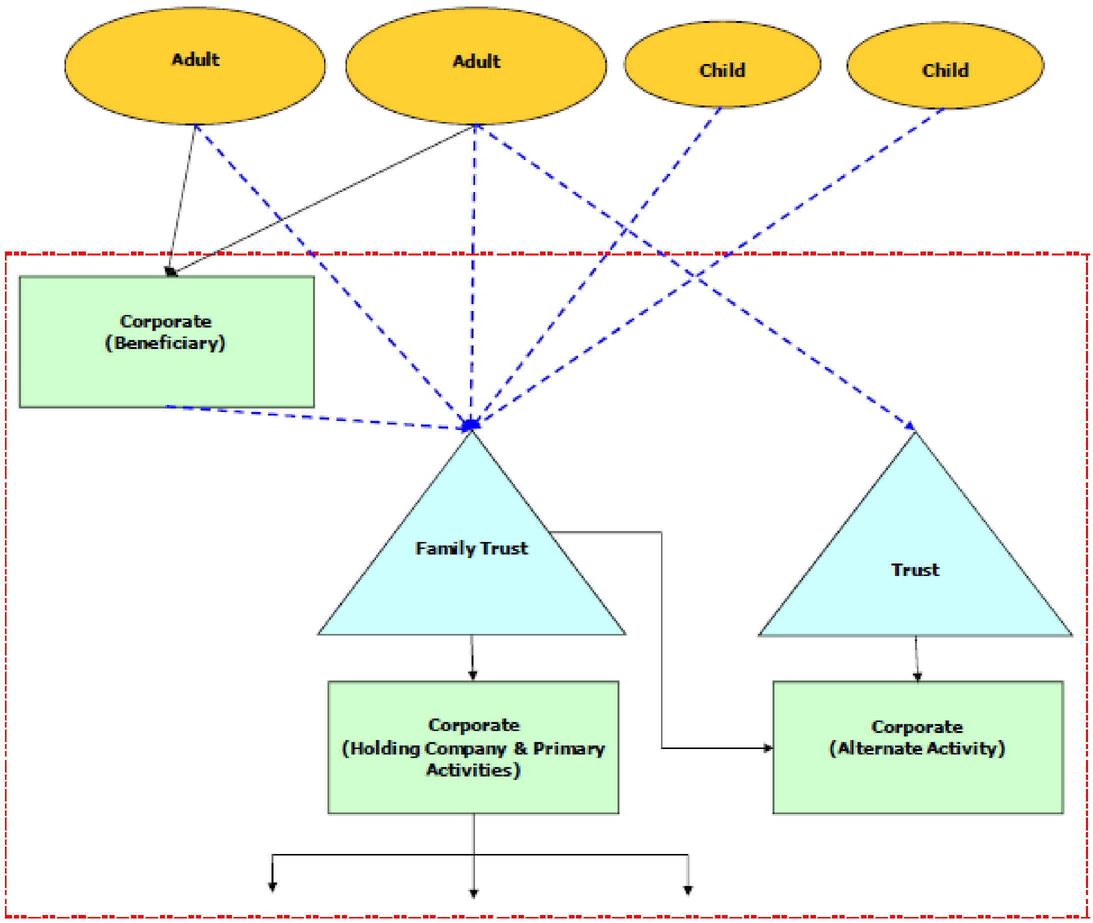
43 Mr Robert Powell, Partner, Grant Thornton, *Committee Hansard*, 14 November 2012, p. 13.

44 MGI Australasia, *Submission 9*, p. 7.

45 Mr William Winter, BW Business Development, *Committee Hansard*, 14 November 2012, p. 42.

being treated tax for purposes in the same way as transactions between subsidiary and parent companies:

Figure 6.2: Family trusts and the family group[46]



6.32 Significantly, the ATO told the committee that the advantages to succession planning, estate planning, asset protection and taxation arrangements are 'consistent generally with what the ATO observes'. The ATO further noted that 'the reasons are not just about tax effectiveness'.[47]

Legislative issues

6.33 The following section discusses a range of legislative matters relating to the operation of family trusts that have been raised with the committee. Specifically, the focus is on the following five aspects of Australian law:

- Division 7A of the *Income Tax Assessment Act 1936*;

46 Deloitte Private, *Submission* 16, p. 24.

47 Mr Tony Poulakis, Assistant Commissioner, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 15.

- Division 6 of the *Income Tax Assessment Act 1936*;
- the capital gains tax rules;
- the property settlement rules under the *Family Law Act 1975*; and
- the rule against perpetuities.

Issues relating to Division 7A of the Income Tax Assessment Act 1936

Policy purpose of Division 7A

6.34 The direct purpose of Division 7A is to ensure that private companies cannot make tax free distributions of profits to shareholders and their associates in the form of payments or loans. The provision ensures that disguised or informal distributions of company profits are included in the assessable income of the shareholder or associate in the form of unfranked deemed dividends (trustees can be shareholders or associates of shareholders of the private company).

6.35 However, underlying this is a broader purpose to protect the progressive income tax base. This is necessary because the current corporate income tax rate of 30 per cent is lower than the marginal tax rate for individuals on incomes above $80 000 (on current thresholds) and lower than the general trustee tax rate. Without such rules, individuals and trusts would have an incentive to divert their income into companies to access the lower tax rate whilst still being able to enjoy the benefit of the income.

ATO administrative practice

6.36 Taxation Ruling 2010/3 takes the view that an unpaid present entitlement is capable of amounting to the provision of financial accommodation (a loan) by the private company beneficiary in favour of the trust. The Commissioner's view is that where the funds representing the unpaid present entitlement are not used for the sole benefit of the private company (eg: other beneficiaries of the trust can benefit from the use of those funds by the trustee), the private company has provided the trust with a loan for the purposes of Division 7A. The alternative interpretation would mean that the provisions of Division 7A could easily be avoided through the use of an unpaid present entitlement being used by shareholders to fund private purposes. Accordingly, the view contained in Taxation Ruling 2010/3 is consistent with the policy intent of Division 7A.

6.37 Prior to issuing the ruling, there had been some public statements by the ATO (but no formal advice or rulings) to the effect that unpaid present entitlements would not constitute a financial accommodation by the private company beneficiary.

6.38 Taxation Ruling 2010/3 was finalised following the publication of a draft ruling and a consultation process to gain feedback from stakeholders and raise awareness of the departure from the ATO's previously held view. The ruling took effect prospectively (from 16 December 2009), to ensure that people who had relied upon the administrative practice were not disadvantaged.

6.39 When Division 7A of the *Income Tax Assessment Act 1936* was introduced in 1998 the ATO took the view that where a trust resolved to distribute income to a company in the same family group and the distribution was not physically paid (that is, it was intermingled funds), the ensuing outstanding unpaid present entitlement was not treated as a loan by the company to the trust and therefore Division 7A did not apply.

6.40 Taxation Ruling 2010/3 stated that Division 7A could apply to unpaid present entitlements involving family companies and other small business. The effect of this ruling and the ATO's change in view is that Division 7A is likely to apply to any trust that distributes income to a company where the distribution is not physically paid. If Division 7A does apply to an unpaid present entitlement, then the trust will be deemed to have received an unfranked dividend equal to the amount of unpaid present entitlement. Tax lawyer Ms Kay Papadopoulos has noted that the unpaid present entitlement will be taxed at the corporate rate in the hands of the company.[48]

6.41 Some have argued that Division 7A of Part III of the Income Tax Assessment Act 1936 inappropriately diminishes the resources available to family businesses that operate through a joint company and family trust structure.[49] The ATO explains the policy intent of Division 7A as follows:

> Division 7A of Part III of the *Income Tax Assessment Act 1936* is an integrity measure aimed at preventing private companies from making tax-free distributions of profits to shareholders (or their associates). In particular, advances, loans or other payments and credits to shareholders (or their associates) are, unless they come within specified exclusions, treated as assessable dividends to the extent that the private company has a distributable surplus.[50]

6.42 Division 7A is intended to disrupt attempts to minimise the tax paid on profits earned by a trust, such as a family business trading through a family trust structure. The ATO explains:

> Subdivision EA [is] designed to ensure that a trustee cannot shelter trust income at the prevailing company tax rate by creating a present entitlement to an amount of net income in favour of a private company without paying

48 Kay Papadopoulos, ‘Distributions to company beneficiaries from family trusts and Division 7A’, *Keeping Good Companies*, vol. 62, no. 9, October 2010, pp 562–564.

49 See, for example, Family Business Australia, *Submission 1*, p. 8; KPMG, *Submission 21*, p 10.

50 Australian Taxation Office, *Division 7A—Overview*, http://www.ato.gov.au/businesses/content.aspx?doc=/content/40223.htm&pc=001/003/075/001/001&mnu=44743&mfp=001&st=&cy= (accessed 21 December 2012).

> it, and then distributing the underlying cash to a shareholder (or their associate) of the company.
>
> The trust is treated as a notional company and the general Division 7A provisions are modified to determine the amount to be included in the assessable income of the shareholder (or their associate) as if it were a dividend.[51]

6.43 In evidence to the committee, the ATO advised that Division 7A responds to, and is intended to prevent, the following kinds of business practice:

> The ATO identified instances where family trusts were making what we call unpaid present entitlements to bucket companies...What is generally done with the company is that, if the money were retained in the trust, it will be taxed at the highest notional tax rate. If it were made an entitlement to a beneficiary, including a bucket company beneficiary, it will be taxed at the company rate and therefore it is taxed at 30 per cent. It appeared as though this bucket company strategy was being utilised to avoid tax at the higher rate…The ATO, after making this observation, came to the view that the unpaid present entitlements may actually be treated as loans for Division 7A purposes.[52]

6.44 However, KPMG has claimed that Division 7A goes beyond this intent and unfairly captures unpaid present entitlements to a company from a trust:

> The original intent of Division 7A was to be an integrity provision that was aimed at ensuring loans that were in substance distributions of profits from companies to individuals, were caught within these provisions. Hence, Division 7A required that these loans be repaid or a loan agreement with minimum repayments be executed. However, unpaid present entitlements to a company from a trust are not an arrangement to disguise the distribution of profits to family members…There are very few instances where the trust uses the unpaid present entitlement for nonbusiness purposes (such as payment of personal debt).[53]

6.45 PricewaterhouseCoopers submitted that Division 7A 'operates to penalise families'.[54] The FBA contended that the restriction adds unnecessary complications and costs:

> Recent changes, particularly the measures around Unpaid Present Entitlements owing by Trusts to Private Companies after 16 December

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51 Australian Taxation Office, *Division 7A—Overview*, http://www.ato.gov.au/businesses/content.aspx?doc=/content/40223.htm&pc=001/003/075/001/001&mnu=44743&mfp=001&st=&cy= (accessed 21 December 2012).

52 Mr Tony Poulakis, Assistant Commissioner, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 16.

53 KPMG, *Submission 21*, p. 12.

54 PricewaterhouseCoopers, *Submission 11*, p. 3.

> 2009 are now unnecessarily complicating family and privately owned business models causing additional compliance and transaction costs at a time when the entire economy is facing challenges.[55]

6.46 In KPMG's assessment, Division 7A can nullify the benefits of operating a family trust.[56] It argued that Division 7A:

- inappropriately lessens the resources available to family businesses. By requiring a loan agreement to be entered into between the trust and the company, there are additional administrative costs.[57] The Division also requires loans to be offered at a higher interest rate than what may be available on the open market.[58]
- limits the capital available to family businesses, as it restricts a family business from financing related family ventures[59]
- triggers a taxing point within a family group structure. Where a trust borrows funds from a company to buy a property and a loan is put in place, the company will be forced to pay a dividend to the family which will be taxed at the differential between the franking credit and the marginal tax rate. As KPMG put it: '…you force a taxing point to repay an artificial loan and that actually pulls capital outside the business'.[60]
- unfairly disadvantages family groups that operate through a trust structure. KPMG advised that the ATO's definition of an unpaid present entitlement has led to a situation where financial distributions between entities in the same family group, for example the transfer of funds from a corporate beneficiary of a family trust to the business' operating entity, are treated as Division 7A loans.[61] Family groups in particular are at a disadvantage because they are forced to pay a taxing point which other groups are not.[62]

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55 Family Business Australia, *Submission 1*, p. 8.

56 KPMG, *Submission 21*, p. 11.

57 KPMG, *Submission 21*, p. 11.

58 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 12.

59 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

60 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 12.

61 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 13.

62 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 12.

6.47 Deloitte Private also commented that 'the application of these rules within family groups can lead to additional costs, uncertainty and perception of inequity'.[63]

6.48 Several options were recommended to address the reported problems with the operation of Division 7A. PricewaterhouseCoopers recommended that Division 7A be reconfigured to not financially disadvantage intra-family transactions:

> We recommend Division 7A be amended so that the rules don't penalise private business borrowing arrangements where either:
>
> - the borrowing entities are entitled to claim an income tax deduction for servicing such debt – an 'otherwise deductible rule'; or
> - the terms relating to such loans are arms' length in nature.
>
> We would also recommend removing the strict requirements that documentation be prepared with certain timeframes.[64]

6.49 Deloitte Private argued that the taxation system should acknowledge and account for the operation of family groups, through 'essentially ignoring' intra-group transactions:

> A cohesive structure for the taxation of family groups would ideally allow for profits contributed back into a business to be excluded from individual tax rate treatment and provide a simple process for calculating group tax payable. Alternatively the introduction of a family tax unit concept would provide the ability to pool income (with or without the use of trusts).[65]

6.50 In support of this proposal, Deloitte Private submitted that such an approach would place family groups on equal footing with corporations. It stated that recognising intra-family transactions would provide the benefits of family groups benefits that are 'enjoyed by corporate groups who have entered the consolidation regime'.[66] Deloitte Private argued that this would be consistent with overseas practice.[67]

6.51 The ATO acknowledged that the inclusion of 'bucket company' loans, that is unpaid present entitlements, within Division 7A 'has been somewhat controversial'.[68] On 18 May 2012, the government announced that the Board of Taxation would be

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63 Deloitte Private, *Submission 16*, p. 23.

64 PricewaterhouseCoopers, *Submission 11*, p. 4.

65 Deloitte Private, *Submission 16*, p. 23.

66 Deloitte Private, *Submission 16*, p. 23.

67 Deloitte Private, *Submission 16*, p. 24.

68 Mr Tony Poulakis, Assistant Commissioner, Australian Taxation Office, *Committee Hansard*, 13 November 2012, p. 16.

reviewing Division 7A, which includes the treatment of unpaid present entitlements.[69] In announcing the review, the government noted that Division 7A has been identified as a 'particularly thorny issue for small business – especially for users of trusts that need working capital to reinvest in their business'.[70] The Board is scheduled to report to Government by 30 June 2013.[71]

Committee view

6.52 The committee acknowledges submitters' concerns with the operation of Division 7A. It recognises the concerns of family business representatives that Division 7A has imposed significant compliance costs for some family businesses. However, the committee also acknowledges that Division 7A was established for the legitimate purpose of ensuring the integrity of Australia's progressive taxation system. Division 7A should not be altered in a way that would expose Australia's taxation system to misuse.

6.53 ATO regulations should achieve an appropriate balance between supporting businesses while maintaining the integrity of Australia's taxation system. There is some evidence that at present Division 7A may not be achieving this balance. The committee therefore recommends the Board of Taxation take account of the evidence presented by the family business sector on the effect of Division 7A on business performance.

Recommendation 12

6.54 The committee recommends that as part of its current inquiry into Division 7A of the *Income Tax Assessment Act 1936*, the Board of Taxation closely review the evidence gathered through this inquiry about the effect of Division 7A on Australia's family business sector. In considering the evidence, the Board of Taxation should consider what measures can be taken to support Australian family businesses, and by extension the Australian economy, while giving due regard to appropriate taxation obligations.

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69 Mr Hector Thompson, General Manager, Small Business Tax Division, Treasury, *Committee Hansard*, 13 November 2012, p. 16.

70 The Hon David Bradbury MP, Assistant Treasurer, 'Board of Taxation to conduct a post-implementation review of Division 7A', Media release 033, 18 May 2012.

71 The Hon David Bradbury MP, Assistant Treasurer, 'Board of Taxation to conduct a post-implementation review of Division 7A', Media release 033, 18 May 2012.

Recommendation 13

6.55 The committee recommends that the government publicly release the Board of Taxation's report into the operation of Division 7A of the *Income Tax Assessment Act 1936*.

Issues arising out of Division 6 of the Income Tax Assessment Act 1936

6.56 The committee heard that the rules in Division 6, Part III of the *Income Tax Assessment Act 1936* (the 1936 Act) that govern the taxation of income of family trading trusts are complex and cumbersome.[72] Division 6, Part III of the 1936 Act establishes the rules to determine the taxation of trust income. This can include the income of family trusts used as a means of operating a family business.[73]

6.57 The final report of the 2009 review *Australia's future tax system* provided the following synopsis of the taxation requirements applying to trading trusts:

> Trusts can be used as an alternative structure for conducting business activities. Trusts are largely taxed on a flow-through basis, with the income of a trust allocated to its beneficiaries based on their 'present entitlements'. However, losses do not flow through to beneficiaries. Where there is income of the trust to which no beneficiary is presently entitled, it is taxed in the hands of the trustee at the top personal income tax rate plus the Medicare levy.
>
> […]
>
> The general rules governing the taxation of trusts rely on a mix of trust law concepts (which mostly derive from case law) and tax law concepts (which derive from case law and statute).[74]

6.58 Reflecting on the development of Division 6 and trading trusts in Australia, academic commentators have noted that trading trusts do not fit easily within the Division 6 framework:

> The assumption on which Div 6 and its antecedents were drafted was that there would be no significant differences between net or distributable trust income and what would be calculated as the notional taxable income of the trustee…Once a business is embarked upon, however, a whole range of discrepancies emerge.[75]

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72 National Farmers' Federation, *Submission 29*, p. 9; PricewaterhouseCoopers, *Submission 11*, p. 3.

73 Treasury, *Consultation paper: Modernising the taxation of trust income – options for reform*, November 2011, pp. 5, 9.

74 Dr Ken Henry et al, *Australia's Future Tax System: Final Report*, 'Chapter B: Investment and entity taxation', December 2009, p. 190, http://www.taxreview.treasury.gov.au/content/FinalReport.aspx?doc=html/publications/Papers/Final_Report_Part_2/chapter_b2-2.htm (accessed 21 January 2013).

75 Antony H. Slater QC, 'Taxing trust income after Bamford's case', 2011, 40 AT Rev 60 at 80.

6.59 The 2009 review *Australia's future tax system* also noted the difficulties of applying Division 6 to trading trusts. The review found that there is a lack of certainty about the concepts underpinning Division 6:

> Differing views on key concepts, such as 'present entitlement', 'income of the trust estate' and 'share', create uncertain tax outcomes for taxpayers, increasing compliance and administration costs.[76]

6.60 Accordingly, the review panel recommended that '[t]he current trust rules should be updated and rewritten to reduce complexity and uncertainty around their application'.[77]

6.61 As the ATO has stated, 'income of the trust estate' and 'share' of income are key concepts necessary to determine income tax liabilities of trusts. However, their meaning is not defined in the 1936 Act. These key taxation concepts were the subject of the 2010 High Court case *Commissioner of Taxation v Bamford & Ors* [2010] HCA 10 (the Bamford case). PricewaterhouseCoopers and the National Farmers' Federation submitted that rather than providing clarity and certainty for businesses, the Bamford case has added further complexity to trust taxation laws.[78] It is evident that the government shares these concerns:

> The recent High Court decision in *Commissioner of Taxation v Bamford* highlighted ongoing discrepancies between the treatment of trust income by trust laws, on the one hand, and by the tax system on the other. Tax outcomes for beneficiaries of trusts often do not match the amounts they are entitled to under trust law and the trust deed. This can result in unfair outcomes as well as opportunities for taxpayers to manipulate their tax liabilities.[79]

6.62 Following the release of the final report of the *Australia's future tax system* review and the High Court's judgement in the Bamford case, the Australian government announced it would 'undertake a process of public consultation as a first step towards updating the trust income tax provisions in Division 6 of Part III of the

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76 Dr Ken Henry et al, *Australia's Future Tax System: Final Report*, 'Chapter B: Investment and entity taxation', December 2009, p. 190, http://www.taxreview.treasury.gov.au/content/FinalReport.aspx?doc=html/publications/Papers/Final_Report_Part_2/chapter_b2-2.htm (accessed 21 January 2013).

77 Dr Ken Henry et al, *Australia's Future Tax System: Final Report*, 'Chapter B: Investment and entity taxation', Recommendation 36, December 2009, p. 191, http://www.taxreview.treasury.gov.au/content/FinalReport.aspx?doc=html/publications/Papers/Final_Report_Part_2/chapter_b2-2.htm (accessed 21 January 2013).

78 National Farmers' Federation, *Submission 29*, p. 9; PricewaterhouseCoopers, *Submission 11*, p. 3.

79 The Hon Bill Shorten MP, Minister for Financial Services and Superannuation, 'Farmers benefit with changes to trust laws', Media release 025, 16 December 2010.

Income Tax Assessment Act 1936 and rewriting them into the *Income Tax Assessment Act 1997'*.[80]

6.63 Where noted, family business representatives shared the view that there is a need to reform Division 6.[81] However, submitters were cautious about the outcome of the review. The National Farmers' Federation argued that, to enable farmers to clearly understand and work within taxation requirements, further reforms following the Division 6 review should be limited. PricewaterhouseCoopers noted with concern the potential for the reform process to introduce additional obligations on trustees.[82]

Committee view

6.64 The committee is concerned that the current operation of the rules in Division 6 is unclear, uncertain and may create unnecessary complexity for Australian businesses. The committee particularly notes the findings of the 2009 review *Australia's future tax system* which claims that Division 6 increases compliance and administrative costs for Australian businesses. The committee agrees that there is a need to review Division 6 to ensure it imposes clear and equitable taxation requirements. The committee looks forward to discussion as to how the operation of Division 6 could be improved, and encourages the government to release a timetable for the introduction of legislation.

6.65 It is apparent that Division 6 is of particular concern for the family business sector. While the exact proportion of the family business sector that operates under a trust structure is currently difficult to quantify, it is clear that family trusts are an established feature of the Australian business landscape. Accordingly, the committee recommends that in developing the draft legislation Treasury meet with representatives of the family business sector. The reform options should achieve an appropriate balance between promoting business interests and the proper operation of Australia's taxation system.

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80 The Hon Bill Shorten MP, Minister for Financial Services and Superannuation, 'Farmers benefit with changes to trust laws', Media release 025, 16 December 2010.

81 National Farmers' Federation, *Submission 29*, p. 9; PricewaterhouseCoopers, *Submission 11*, p. 3.

82 National Farmers' Federation, *Submission 29*, p. 9; PricewaterhouseCoopers, *Submission 11*, p. 3.

Recommendation 14

6.66 The committee recommends that as part of the current analysis of options to reform the Division 6, Part III of the *Income Tax Assessment Act 1936* the Department of the Treasury review the evidence gathered through the committee's inquiry into family businesses in Australia and consult with representatives of the family business sector.

Family trusts and capital gains tax

6.67 On 1 November 2008, Division 104 of the *Income Tax Assessment Act 1997* was amended to repeal the exception to capital gains tax events E1 and E2. The exception, commonly referred to as the 'trust cloning' exception, was a key focus of submitters to the inquiry.

6.68 Prior to their repeal, subsections 104–55(1) and 104–60(1) of Division 104 of the Income Tax Assessment Act removed the requirement to pay capital gains tax (CGT) in certain circumstances. CGT is incurred where a trust is created over a CGT asset by declaration or settlement (referred to by submitters to this inquiry as CGT event E1).[83] The trust cloning exception in subsection 104–55(1) removed the requirement to pay CGT in circumstances where the trust was created by transferring the asset from another trust with the same beneficiaries and operating terms. Similarly, CGT is incurred by transferring a CGT asset to an existing trust (referred to by submitters to this inquiry as CGT event E2).[84] The trust cloning exception in subsection 104–60(1) provided that capital gains tax was not incurred if the asset was transferred from another trust with identical terms and beneficiaries.

6.69 Family business advisors submitted that trust cloning was a legitimate, and necessary, business management practice. MGI Australasia argued that trust cloning was a 'valuable mechanism' that provided appropriate business management flexibility and reduced the potential for family conflict to derail the succession process.[85] The Institute of Chartered Accountants Australia submitted:

> One of the means open to family businesses to transfer business assets without triggering a CGT event was the practice of trust cloning…Trust cloning facilitated succession planning, allowing effective control of assets to pass between trusts, within a family group, without triggering a CGT liability.[86]

6.70 On 31 October 2008, the government announced its intention to repeal the tax cloning exceptions. It was further announced that the repeal would take effect on

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83 See, for example, Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

84 See, for example, MGI Australasia, *Submission 9*, p. 8.

85 MGI Australasia, *Submission 9*, p. 7.

86 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

1 November 2008. The trust cloning exceptions were repealed by the *Tax Laws Amendment (2009 Measures No. 6) Act 2010*.

6.71 The Tax Laws Amendment (2009 Measures No. 6) Act also introduced measures to allow limited CGT rollover relief for the transfer of assets between fixed trusts.[87] For family businesses, it is notable that the rollover relief was not designed to be available for the transfer of assets between discretionary trusts. The Explanatory Memorandum (EM) to the Tax Laws Amendment (2009 Measures No. 6) Bill 2009 makes clear that this distinction between discretionary and fixed trusts was intentional and based on the policy perspective that, unlike fixed trusts, it is difficult to establish the ownership of assets held in discretionary trusts:

> [S]o-called discretionary trusts cannot access the rollover. This is because it is difficult to establish, with any degree of certainty, the real underlying ownership of the assets of a discretionary trust. Therefore, it is equally difficult to test whether that ownership has been maintained.
>
> […]
>
> In effect, beneficiaries' interest should be 'fixed'. This requirement is consistent with the objective of ensuring that subsequent changes in effective ownership are subject to appropriate tax consequences.[88]

6.72 In announcing the intention to repeal the trust cloning exception, the Government emphasised that the proposed changes to the CGT rules were necessary to 'help ensure equity and the integrity of the tax system'.[89] As stated in the EM, the trust cloning exceptions were considered to undermine market integrity:

> The trust cloning exception allows the creation of a trust over a CGT asset or the transfer of a CGT asset to an existing trust without triggering a CGT taxing point, provided the beneficiaries and terms of both trusts are the same.
>
> However, this can be used to change ownership of an asset without a CGT taxing point. It potentially allows taxpayers to eliminate tax liabilities on accrued capital gains, undermining equity and the integrity of the tax system.[90]

6.73 The repeal of the trust cloning exception was intended to promote a fair marketplace, by ensuring that changes in asset ownership generally trigger a CGT taxation point:

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87 Schedule 1, Item 9, section 126–220, Tax Laws Amendment (2009 Measures No. 6) Bill 2009.

88 Explanatory Memorandum, Tax Laws Amendment (2009 Measures No. 6) Bill 2009, paragraphs 1.29; 1.32–1.33.

89 The Hon Chris Bowen MP, Assistant Treasurer, 'Government abolishes trust cloning tax concession', Media release 092, 31 October 2008.

90 Explanatory Memorandum, Tax Laws Amendment (2009 Measures No. 6) Bill 2009, paragraphs 1.4–1.5.

> The repeal of the trust cloning exception is consistent with the policy principle of taxing capital gains that arise where there is a change in ownership of an asset.[91]

6.74 Submitters to this inquiry acknowledged the market integrity principles that prompted the repeal of the trust cloning exception.[92] However, submitters disputed that the use of the trust cloning exception to facilitate family business transfers, and other 'legitimate' business purposes, presented a market integrity risk.[93] The submission of the Institute of Chartered Accountants Australia encapsulated the views put forward in defence of the trust cloning exception:

> The Institute acknowledges that the trust cloning exception was too wide and needed to be narrowed to protect the CGT base. However, we believe that the exception should not have been abolished entirely and should instead have been replaced with narrower provisions, with appropriate integrity measures, to preserve the use of trust cloning for legitimate business purposes (including asset and business protection, business restructuring and succession planning).[94]

6.75 The view that trust cloning is a legitimate means of operating a business was submitted as part of the consultation process on the proposed repeal of the trust cloning exception. For example, at the time of the consultation process the Institute of Chartered Accountants in Australia[95] argued:

> Discretionary trusts are a common conduit structure used by SMEs. Where SMEs operate through discretionary trust structures, outside of either section 104-55(5)(b) or section 104-60(5)(b), there is currently little or no CGT relief for restructuring arrangements.
>
> As demonstrated below, trust cloning is used by SMEs for legitimate family and commercial reasons. It is often used to facilitate asset or business protection and restructuring in cases where there is no change in the economic ownership of the underlying assets.
>
> We are concerned that the proposed removal of the exceptions to CGT event E1 and E2 will not be replaced by any provision allowing CGT relief involving the transfer of an asset from one trust to another. From an SME

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91 The Hon Dr Craig Emerson MP, Minister Assisting the Finance Minister on Deregulation, *House of Representatives Hansard*, 25 November 2009, p. 12776; The Hon Chris Bowen MP, Assistant Treasurer, 'Government abolishes trust cloning tax concession', Media release 092, 31 October 2008; Explanatory Memorandum, Tax Laws Amendment (2009 Measures No. 6) Bill 2009, paragraph 1.6.

92 See, for example, Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

93 See, for example, Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 32.

94 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

95 Currently known as the Institute of Chartered Accountants Australia.

> perspective…we submit that a narrower targeted exception should be considered by Government and the Treasury.[96]

6.76 However, as Treasury's response to the consultation process indicates, the Government did not support the view that the transfer of assets that occurs when a trust is cloned is a legitimate business practice that, accordingly, should not incur CGT:

> Most of the submissions on the policy design of the measure to abolish the CGT trust cloning exception opposed abolishing the exception. The submissions argued that there are non-tax reasons for using trust cloning, and uncertainty and integrity concerns should be addressed directly, by legislating a roll-over.
>
> This request is contrary to the policy intent of…the original decision to abolish the CGT trust cloning exception. Although there may be non-tax reasons for the transfer, this does not mean it should not give rise to a CGT taxing point. It is the change in underlying ownership, not the reasons for the transaction, that is the policy reason for a CGT taxing point.[97]

6.77 The EM to the Tax Laws Amendment (2009 Measures No. 6) Bill 2009 indicates that it was anticipated that the repeal of the trust cloning exception would have minimal financial impact. The EM also indicates that it was expected that Australian businesses would not incur significant costs to comply with the new taxation arrangements.[98] Evidence presented to this committee about the financial impact of the repeal of the trust cloning exception was largely anecdotal.

6.78 A number of family business owners spoke of the challenges presented by CGT, and advised that these challenges are preventing the transfer of business ownership to the next generation. Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, argued that CGT limits succession options. Mr Levi advised that while it was possible to transfer the management of the business, CGT effectively prevented the transfer of business ownership:

> Certainly in our own business—we are a 22-year-old business employing around 35 people and I have both sons in the business—to transition control is one thing; to transition ownership is another thing altogether. Without going into details, we have a trust structure, but to transfer part of the business we are subject to CGT issues. We want to retain control of the business, obviously, and ownership within the family. Our two boys are

96 Institute of Chartered Accountants in Australia, *Submission concerning the proposed abolition of the capital gains tax trust cloning exception*, 8 December 2008, p. 3, http://archive.treasury.gov.au/documents/1448/PDF/ICAA.pdf (accessed 15 January 2013).

97 Treasury, 'Abolishing the capital gains tax (CGT) trust cloning exception and providing rollover for fixed trusts—Summary of consultation process', 2009, p.1, http://archive.treasury.gov.au/documents/1435/PDF/Consultation_Summary.pdf (accessed 15 January 2013).

98 Explanatory Memorandum, Tax Laws Amendment (2009 Measures No. 6) Bill 2009, p.7.

> coming up and are effectively managing the business now. One is my second-in-charge—doing a fantastic job—– and they really deserve to have ownership, but we cannot afford to be in a CGT situation.[99]

6.79 Similarly, Mr Graham Henderson, co-owner of a family business and Director, Family Business Australia, commented:

> We have mentioned quite clearly the capital gains tax implications and complexities with regard to transfer of a business to the next generation. Our business is 63 years old, so we will be looking to transition to the next generation and certainly it is part of our succession planning policy, so the capital gains tax is a very important plan for us.[100]

6.80 Family business advisors also provided anecdotal comment on the effect of the repeal of the trust cloning exception. KPMG and the Institute of Chartered Accountants Australia both submitted that the repeal of the trust cloning exception, and the resulting CGT obligations, have undermined the sector's capacity to continue the business into the next generation. KPMG advised that:

> the legislative environment…does not encourage the implementation of planned succession due to the tax impost that could arise as a result of changes of ownership of equity or business assets, during the owner's lifetime.[101]

6.81 KPMG further stated:

> [f]amily businesses are united when it comes to their desire for a simpler and more supportive tax regime, particularly with respect to CGT and inheritance tax. All too often the value created by each generation is almost wiped out by the substantial tax that is imposed when transferring the business to the next generation.[102]

6.82 The Institute of Chartered Accountants Australia advised that with the removal of the trust cloning exception the intergenerational transfer of business ownership triggers a CGT event, which businesses fund within existing business assets. Accordingly, intergenerational transfers can reduce a business' asset pool and therefore it's potential productivity and trading capacity:

> To maintain the viability of the family business sector consideration needs to be given to ways to enable the legitimate intergenerational transfer of

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99 Mr Peter Levi, Managing Director, Co-owner, Colorific Australia, *Committee Hansard*, 14 November 2012, p. 38.

100 Mr Graham Henderson, Director, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 43.

101 KPMG, *Submission 11*, p. 7.

102 KPMG, *Submission 11*, p. 15.

> businesses without tax impost constituting a significant drain on the sector's resources and potential growth.[103]

6.83 KPMG also advised that CGT resulting from succession inappropriately erodes a business' asset base:

> We note that the CGT consequences create an unnecessary cash flow burden to family groups when looking to transition their business. So much so, that the tax consequences may outweigh the benefits and the parents may instead choose to dispose of their interest to third parties, or alternatively do nothing.[104]

6.84 KPMG further advised that the removal of the trust cloning exception exposes family businesses to poor business practices, such as including the business among the assets to be distributed as part of a deceased estate. KPMG noted that such transfers do not attract CGT while, with the repeal of the trust cloning exception, transfers during the life of the current generation are liable to CGT. Accordingly, it was argued that 'it is important for policymakers to look at offering the same concessions in life as we do in death.'[105] Treasury confirmed that CGT is not payable for assets transferred as part of a deceased estate.[106]

6.85 The committee was also advised that the removal of the trust cloning exception has increased the risk of family conflict and the difficulty of managing the succession process.[107] MGI Australasia submitted:

> [I]n our experience the results of this has not been to raise additional CGT revenue, but rather has meant that family members, particularly siblings, have chosen to share control of family discretionary trusts with all the potential for conflict that entails and the resultant damage that this brings to both business and family.[108]

6.86 The committee did not receive statistical data to support the view implicit in this anecdotal evidence that the repeal of the trust cloning exception is resulting in the closure or downsizing of family businesses.

6.87 Family business advisors advocated for amendments to the current CGT requirements. MGI Australasia called for the trust cloning exception to be

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103 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

104 KPMG, *Submission 11*, p. 16.

105 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 14.

106 Mr Paul McMahon, Manager, Small Business Tax General Unit, Treasury, *Committee Hansard*, 13 November 2012, p. 12.

107 See, for example, Mr Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 40.

108 MGI Australasia, *Submission 9*, p. 8.

reinstated.[109] Similarly, but not identically, the Institute of Chartered Accountants Australia recommended the committee 'give consideration to the merits of reinstating a narrow version of the previous tax cloning exception'.[110] KPMG effectively recommended the reintroduction of the trust cloning exception. However, the recommendation was nuanced as it was founded on the argument that family businesses should not incur additional costs for adopting smarter business practices and the concept that a family business is one part of a broader family group:

> [I]n order to encourage the longest term sustainability of family businesses, it is recommended that the CGT treatment the intergenerational transfers of interests in a business to their family members should mirror the CGT treatment of an asset passing to a beneficiary through a deceased estate.
>
> Alternatively, the transfer of the family's ownership interest in a family business to another member of the family should not be regarded as the change in ownership tantamount to a disposal.[111]

6.88 PricewaterhouseCoopers submitted that discretionary trust should be afforded the same opportunities as fixed trusts, recommending the introduction of a rollover mechanism to allow family discretionary trusts to disregard any capital gains resulting from the transfer of individual's assets to the trust. It was argued that this would not undermine the integrity of Australia's taxation system as a 'Family Trust election is an integrity measure that penalises those trusts that provide benefits to non family members'.[112]

Committee view

6.89 The committee appreciates the views of the family business advisors and family businesses who spoke of the effect of the repeal of the trust cloning exception. It is evident that among the family businesses that operate under a trust structure the repeal of the trust cloning exception is an ongoing concern, and has required changes to business practice. Given the evidence that CGT implications may be impeding the innovation and planning of family businesses' succession arrangements, this matter should be considered in the next five years as more data becomes available. The committee further notes that similar concerns were raised at the time the legislation to repeal the trust cloning exception was drafted. The Government's response to these concerns is compelling. The Government's current view is that there are sound policy reasons for all transfers of business assets to equally be subject to CGT laws.

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109 MGI Australasia, *Submission 9*, p. 8.

110 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

111 KPMG, *Submission 11*, p. 16.

112 PricewaterhouseCoopers, *Submission 11*, p. 2.

CGT and the sale of farms

6.90 The committee received some evidence that selling the family farm to the next generation would not trigger a CGT event, whereas CGT would be payable in selling a non-rural business to family members. Mr Donald McKenzie, formerly of KPMG, told the committee:

> Whilst these have been mitigated with some stamp duty concessions—for example, family farm roll-over and small business capital gains concessions—they still need to be reviewed as there is still stamp duty payable on property used in family businesses other than farms transferring from one generation to the next, other than by death.[113]

6.91 This issue was put to the ATO for its response. The ATO explained that:

> …the tax laws currently do not have any great distinction between whether you are in business as a farmer or in any other business in the sense of transferring assets and that sort of thing…
>
> …if you want to sell business assets in certain ways and you want to, say, then use those proceeds to, say, put into super or to acquire other assets then there are rollovers that prevent CGT events occurring. I am not familiar with the concession you are alluding to…

Family law property settlements

6.92 Concerns were raised with the inclusion of family trust assets and income in the pool of property available for distribution as part of a family law property settlement. Mr Robert Powell, Partner, Grant Thornton Australia, shared the view that trusts may be established to protect business assets. Mr Powell advised that historically trusts were created to isolate business assets from the assets that may be subject to property orders under the *Family Law Act 1975*. The committee was informed that sustaining the business through a family breakdown is an issue of some significance to family businesses:

> My experience with the businesses I have worked with is that a lot of those families, particularly the patriarch and the matriarch, are terrified that the children will marry badly and their relationships will break down and that the family's business assets will be under attack from ex-partners, ex-spouses. That is something that keeps them awake at night. That is a driving reason why a lot of businesses protect the assets within a trust structure.[114]

6.93 However, the committee was advised that following recent developments in family law case law, trust assets, and by extension a family business, may no longer be immune from the financial consequences of family breakdown:

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113 Mr Donald McKenzie, *Committee Hansard*, 21 January 2013, p. 10.

114 Mr Robert Powell, Partner, Grant Thornton, *Committee Hansard*, 14 November 2012, p. 13.

> If a trust is in control of those assets, technically speaking no one in the family directly owns anything. I will say though that there have been more and more family law challenges to that concept. I do not think that proposition holds as much water as it used to. I think there is a greater tendency for the courts to see through a trust and I would say that a lot of trusts are formed with the intention of protecting their assets but they are not necessarily operated in a way that actually provides that protection.[115]

6.94 Accordingly, Grant Thornton predicted 'a trend away from family trusts' as a form of asset protection.[116]

6.95 Implicit in this advice is the view that the family law system is eroding, or has the capacity to undermine, the stability and profitability of the family business sector. However, there are also policy reasons why it may be appropriate for business assets to be taken into account in family law proceedings. Mr Peter Strong, Executive Director, Council of Small Business Australia, noted that all parties who have contributed to a business, whether in a formal or informal capacity, should have their contributions acknowledged in the event of a family breakdown:

> I also agree with you on that issue about getting a share of the results of the business. If someone has been putting in time and effort in doing the books and a whole range of other things and that is not recognised in a formal sense, we need to step back and recognise it for reasons of superannuation. If they do split up, they should get a proper and fair share of what they put in. It is an issue that we need to look at.[117]

Committee view

6.96 Family law matters are outside the mandate given to the committee under the *Australian Securities and Investments Commission Act 2001*.[118] The committee did not receive any evidence from family law experts such as the Commonwealth Attorney General's Department or the Family Court of Australia and the Federal Magistrates Court. Nor did the committee receive evidence from advocates for family members experiencing family breakdown such as the Women's Legal Service or the Lone Fathers' Association. Evidence was provided purely from a business perspective.

6.97 The committee understands that it is an established principle of Australia's family law system that the family courts may have regard to assets or income held on trust. The High Court of Australia has confirmed that trust assets and income may be treated as the property of the parties to property proceedings under the Family Law

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115 Mr Robert Powell, Partner, Grant Thornton, *Committee Hansard*, 14 November 2012, p. 13.

116 Grant Thornton, *Submission 18*, p. 3; Mr Robert Powell, Partner, Grant Thornton, *Committee Hansard*, 14 November 2012, p. 15.

117 Mr Peter Strong, Executive Director, Council of Small Business Australia, *Committee Hansard*, 13 November 2012, p. 28.

118 *Australian Securities and Investments Commission Act 2001*, s. 243.

Act.[119] Accordingly, beneficiaries' entitlements may be included in property settlements. Discretionary trusts, such as family trusts operated for business reasons, may be subject to family law property settlements regardless of the purpose for which the trust was established or the time at which the trust was created.[120]

6.98 The committee is aware of academic debate about whether business assets held in a discretionary trust may be inappropriately subject to family law property proceedings.[121] However, as the High Court has noted, 'the question whether the property of the trust is, in reality, the property of the parties...is a matter dependent upon the facts and circumstances of each particular case including the terms of the relevant trust deed.'[122] The committee notes that the High Court has held that:

> [w]here property is held under such a trust by a party to a marriage and the property has been acquired by or through the efforts of that party or his or her spouse, whether before or during the marriage, it does not…necessarily lose its character as property of parties to the marriage because the party has declared a trust.[123]

6.99 In the absence of compelling evidence to the contrary, it would appear there are sound reasons for including trust assets in family law property settlements. It is also evident that the family courts have broad access to trust assets; and therefore property settlements may affect other forms of trusts. The ambit of the Family Law Act is broader than discretionary trusts used as a vehicle for operating a family business. If changes were to occur to the family law system to appropriately isolate business interests, any unintended consequences that would prevent a fair and equitable distribution of property should be avoided. Accordingly, any amendments would need to be carefully considered.

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119 *Kennon v Spry* [2008] HCA 56. A useful summary of the case is provided in High Court of Australia, Public Information Officer, '*Kennon v Spry*', Media release, 3 December 2008; the Hon Justice Paul Brereton AM RFD, *A trustee's lot is not a happy one – Address to the National Family Law Conference October 2010*, 19 October 2010, http://www.lawlink.nsw.gov.au/lawlink/Supreme_Court/ll_sc.nsf/vwFiles/brereton191010.pdf/$file/brereton191010.pdf (accessed 18 January 2013).

120 *Marriage of Johnson* (2000) 155 FLR 44 at 50–52 per Warnick J, as cited in Dal Pont and Chalmers, *Equity and Trusts in Australia*, 2007, p. 525.

121 See, for example, the Hon Justice Paul Brereton AM RFD, *A trustee's lot is not a happy one – Address to the National Family Law Conference October 2010*, 19 October 2010, http://www.lawlink.nsw.gov.au/lawlink/Supreme_Court/ll_sc.nsf/vwFiles/brereton191010.pdf/$file/brereton191010.pdf (accessed 18 January 2013); McCullough Robertson, *Assets of the family trust not necessarily a risk on a family breakdown*, http://www.mccullough.com.au/icms_docs/126467_Structuring_-_14_June_2012.pdf (accessed 18 January 2013); Norton and Smailes, *Discretionary trusts, their treatment by the Family Court, and possible tax issues*, http://www.nortonsmailes.com.au/newsletters/discretionary-trusts-and-their-treatment-by-the-fa/ (accessed 18 January 2013).

122 *Kennon v Spry* [2008] HCA 56, at 57 per French CJ.

123 *Kennon v Spry* [2008] HCA 56, at 65 per French CJ.

6.100 The committee is charged with monitoring the operation of Australia's corporations legislation.[124] It is a principle of this legislation that Commonwealth law and policy should promote market integrity and stability.[125] The anecdotal evidence provided to this committee indicates that individual businesses can be affected by family law property settlements. However, the evidence has not demonstrated that this is a market stability issue. The committee acknowledges the concerns of family businesses about the family courts' access to trust assets. However, the case for legislative amendment has not been made.

The rule against perpetuities

6.101 In addition to concerns with the operation of the Commonwealth law, family businesses and family business advisors also expressed strong concerns with the rule against perpetuities, which is operative in States and Territories. The rule against perpetuities prevents property being indefinitely held in trust. The committee was informed that the rule is of long-standing.[126] However, submitters were uncertain of both its origins and the reasons for which it was established.[127]

6.102 The committee understands that the rule has its origins in the 1682 decision of Lord Nottingham in the *Duke of Norfolk's Case*.[128] The case established the principle that '[n]o interest is good unless it must vest if at all not later than twenty–one years after some life in being at the creation of the interest'.[129] Effectively, this requires trusts to cease operating no later than 21 years after the death of a specified person. This requirement reflects the traditional use of trusts for estate planning purposes. As outlined in the 1993 Northern Territory Law Reform Committee's report into the operation of the rule against perpetuities:

> [t]he rule of law known as the rule against perpetuities is one of the rules developed by English courts to restrict dispositions of property which might tie up land or wealth indefinitely or for too long a time. The rule developed in the late 17th century, when family settlements were often made with the intention of keeping property within the landed families from generation to generation and to protect family fortunes against profligate heirs and their

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124 *Australian Securities and Investments Commission Act 2001*, s. 243.

125 *Australian Securities and Investments Commission Act 2001*, s. 1.

126 See, for example, Mr Donald Hugh McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 17.

127 See, for example, Mr McKenzie, Private capacity, *Committee Hansard*, 21 January 2013, p. 17; Mr Robert Powell, Partner, Grant Thornton Australia, *Committee Hansard*, 15 November 2012, p. 15.

128 Queensland Law Reform Commission, *The law relating to perpetuities accumulations*, Report No.7, 24 May 1971, p. 2.

129 Law Reform Committee of South Australia, *Relating to the reform of the law to perpetuities*, Report No. 73, 8 November 1983, p. 2, citing *Grey on Perpetuities* and *Cadell v Palmer* (1833) 1 Cl. & Fin 372; E.R. 956.

> creditors. These settlements effectively prevented the sale or mortgage of land over substantial periods of time. The courts thought it necessary to place some restraint on schemes that tied up land 'in perpetuity'.[130]

6.103 Australian courts have also supported the rule against perpetuities, recognising that it 'performs a useful social function in limiting the power of members of generations passed from tying up property in such a form as to prevent its being freely disposed of in the present or the future'.[131]

6.104 The application of the rule against perpetuities differs across the states and territories. One jurisdiction, South Australia, has repealed the rule.[132] The rule was abolished in 1996[133] following a 1983 review by the Law Reform Committee of South Australia, which held that the rule had led to 'stupidities' and 'unbelievable results' and was ill-suited to the modern business and taxation environment.[134] Accordingly, South Australia adopted a legislative scheme that permits beneficiaries of trusts operative for 80 or more years to apply for court orders that the trusts be disbanded.[135] It follows that a trust may continue operating should the beneficiaries agree to its continuance.

6.105 A similar approach has been adopted by other common-law jurisdictions. In December 2010, the Law Reform Commission of Nova Scotia released its report *The rule against perpetuities*. The report notes that in addition to South Australia, legislation to abolish the rule has been adopted in Saskatchewan, Ireland and several US states and Caribbean nations.[136] However, the report also notes that '[a]bolition has not proven universally popular.'[137]

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130 Northern Territory Law Reform Committee, *Report on the rules against perpetuities and accumulations*, Report No. 15, October 1993, p. 3.

131 *Nemesis Australia Pty Ltd v Commissioner of Taxation* (2005) 225 ALR 576 at [24] per Tamberlin J, as cited in Dal Pont and Chalmers, *Equity and Trusts in Australia*, 2007, p. 512.

132 *Law of Property Act 1936*, s. 1.

133 Law of Property (Perpetuities and Accumulations) Amendment Act 1996 (SA).

134 Law Reform Committee of South Australia, *Relating to the reform of the law to perpetuities*, Report 73, 8 November 1983, pp 4 and 12.

135 *Law of Property Act 1936*, s. 62.

136 Law Reform Commission of Nova Scotia, *The rules against perpetuities—Final report*, December 2010, pp 22–23.

137 Law Reform Commission of Nova Scotia, *The rules against perpetuities—Final report*, December 2010, p. 29.

6.106 The rule continues to operate in all Australian states and territories other than South Australia.[138] In general, the States and Territories have modified the operation of the rule with effect that a trust can be in existence for no more than 80 years. In the Northern Territory, a trust instrument may specify either 80 years from the date on which the trust was established or the traditional period of a 'life in being plus 21 years'.[139]

6.107 Reviews conducted by the Northern Territory Law Reform Committee and the Queensland Law Reform Commission provide insight into the reasons for the rule's continued existence. Reporting in May 1971, the Queensland Law Reform Commission held that the rule 'remains a necessary aspect of a soundly based system of property law'.[140] Similarly, reporting in 1993, the Northern Territory Law Reform Committee concluded that it is fair and equitable for the law to 'limit the remoteness of vesting'.[141]

6.108 There is consensus among Australian jurisdictions that it is inappropriate to apply the rule to superannuation trust funds and charitable funds. In jurisdictions where the rule applies, legislation expressly excludes superannuation trust funds and trusts established for charitable purposes.[142] The exclusion is also supported by Commonwealth legislation, which expressly provides that the rule against perpetuities does not apply to trusts operated by superannuation entities.[143] Similarly, in South Australia, a court may not order the disposition of property held in superannuation trust funds or charitable trusts.[144]

6.109 Some international reviews have noted with concern the perpetuity rule's implications for commercial transactions. Recommending that the rule be abolished, in 1982 the Manitoba Law Reform Commission stated: '[t]hat commercial interests should be subject to any perpetuity rule is misconceived'.[145] Similarly, reporting in

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138 *Law of Property Act* (NT), Part 11; *Perpetuities Act 1984* (NSW); *Perpetuities and Relations Act 1985* (ACT); *Perpetuities and Accumulations Act 1968* (VIC); *Perpetuities and Accumulations Act 1992* (Tas); *Property Law Act* 1969, Part XI (WA); Property *Law Act 1974*, Part 14 (QLD).

139 *Law of Property Act* (NT), s. 187.

140 Queensland Law Reform Commission, *The law relating to perpetuities accumulations*, Report No.7, 24 May 1971, p. 3.

141 Northern Territory Law Reform Committee, *Report on the rules against perpetuities and accumulations*, Report No. 15, October 1993, p. 3.

142 The 1971 Queensland Law Reform Commission report—*The law relating to perpetuities and accumulations*—provides an overview of the policy reasons for excluding superannuation funds.

143 *Superannuation Industry (Supervision) Act 1993*, s. 343.

144 *Law of Property Act 1936*, s. 62.

145 The Manitoba Law Reform Commission, *Report on the rules against accumulations and perpetuities*, Report 49, 12 February 1982, pp 41 and 60.

2000, the Law Reform Commission of Ireland concluded that the rule should be abolished.[146] In reaching this conclusion, the Commission was concerned with the effect of rule on commercial transactions.[147]

6.110 Concern is also shared by jurisdictions that have elected to retain the rule against perpetuities. Reporting in 1998, the Law Commission (England) recommended precise legislative drafting to enable commercial transactions to be excluded from the operation of the rule against perpetuities. The Commission's recommendation was based on the view that 'as a matter of general principle transactions of a commercial character should be excluded'.[148]

6.111 Australian jurisdictions share the concern that the rule against perpetuities may adversely affect commercial transactions. Commenting in 1976, the New South Wales Law Reform Commission held that the rule should not affect commercial arrangements:

> It could be argued…that the rule has its origin in family settlements and to derive from it a general concept applicable to commercial transactions is wrong…We agree. In our view, the rule against perpetuities serves little purpose when applied to arrangements which are essentially of a commercial nature.[149]

6.112 Nearly two decades on, the same reasoning is evident in the 1993 report of the Northern Territory Law Reform Committee. Citing the 1976 New South Wales Law Reform Commission's report, the Northern Territory Law Reform Committee likewise concluded that 'the rule against perpetuities serves little purpose when applied to arrangements which are essentially of a commercial nature'.[150]

6.113 However, despite the view that the rule against perpetuities is unnecessary, and indeed problematic, in a commercial context, neither the Australian nor the international reviews expressly considered trading trusts. The New South Wales Law Reform Commission and the Northern Territory Law Reform Committee recommended express legislative exclusions for options to acquire an interest in

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146 The Law Reform Commission, *Report on the rule against perpetuities and cognate rules*, 2000, p. 98.

147 The Law Reform Commission, *Report on the rule against perpetuities and cognate rules*, 2000, p. 47.

148 The Law Commission, *The rules against perpetuities and excessive accumulations,* 1998, p. 91.

149 New South Wales Law Reform Commission, *Report of the Law Reform Commission on perpetuities and accumulations*, Report No. 6, 26 August 1976, p. 61.

150 Northern Territory Law Reform Committee, *Report on the rules against perpetuities and accumulations*, Report No. 15, October 1993, p. 18.

property, such as an option to renew a lease.[151] The reports do not analyse the effect of the rule on trading trusts. Internationally, the Law Reform Commission of Ireland focused on 'future easements, options to purchase land with third parties involved, options to purchase shares, [and] nominations and powers of advancement under pension schemes.'[152] The Commission did not consider the rule's effect on businesses that operate through a trust structure. The Law Commission (England) did refer to family trusts and arrangements between family members. However, the analysis is focused on contracts between members of the same family and does not expressly consider family trusts used as a means of conducting a business.[153]

6.114 Reflecting the concerns of the 1983 South Australian inquiry into the rule against perpetuities, submitters argued that the requirement that trading trusts should cease to operate after a specified period is unsuitable in the modern business context. Submitters noted that the 80 year limit may not reflect the longevity of family businesses. Mr William Noye, National Leader, Family Business Services, KPMG, noted that 'there are certainly examples in Europe where families have gone on for 200 or 300 years owning particular businesses'.[154] Mr Donald McKenzie, a former partner of KPMG, also highlighted that the termination of the trust may not coincide with the planned termination of the business:

> It seems a bit illogical…The issue is that, should that disadvantage somebody who is just going to continue on the business on the day after it vests–the same way they were running the business the day before it vested.[155]

6.115 Further, it was submitted that, rather than facilitating a robust private sector, the forced vesting of trading trusts will arbitrarily limit business growth.[156] In support of this argument, three significant business costs were identified. First, PricewaterhouseCoopers submitted that the rule against perpetuities restricts prudent business and asset management:

> The 80 year limit on trusts can also impact business decisions and structures before the trust is terminated. If a family is to acquire a major asset and their trust is already 50 years old, it would be unwise of them to place that

151 New South Wales Law Reform Commission, *Report of the Law Reform Commission on perpetuities and accumulations*, Report No. 6, 26 August 1976, p. 61; Northern Territory Law Reform Committee, *Report on the rules against perpetuities and accumulations*, Report No. 15, October 1993, Appendix F, p. 18.

152 The Law Reform Commission, *Report on the rule against perpetuities and cognate rules*, 2000, p. 47.

153 The Law Commission, *The rules against perpetuities and excessive accumulations*, 1998, p. 92.

154 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 14.

155 Mr Donald McKenzie, Private Capacity, *Committee Hansard*, 21 January 2013, p. 17.

156 See, for example, PricewaterhouseCoopers, *Submission 11*, p 3.

> asset in the existing trust–a vehicle with just 30 years remaining. This will prompt the creation of a new structure to hold the asset, further complicating the family's financial structure and increasing the cost of managing their assets.[157]

6.116 As Mr Paul Brassil, a partner at PricewaterhouseCoopers, informed the committee: '[o]ne would not even today sensibly put newly acquired assets into a family trust that has only 30 or fewer years left in it'.[158]

6.117 Second, the committee was advised that the rule against perpetuities will place a significant taxation burden on family businesses. Capital gains tax implications were commonly cited; the present generation will be required to finance the accumulated CGT of multiple generations. Mr Noye submitted that 'it is almost like a ticking time bomb from a family business perspective…there will be, if you like, a triggered CGT event'.[159] PricewaterhouseCoopers provided the following explanation of the CGT implications:

> The termination of a trust can have a serious impact on families and family businesses. When a trust is dissolved, assets must be transferred to a different owner. If the value of the asset is greater than the cost, it precipitates a Capital Gains Tax (CGT) event for the beneficiaries, who may be forced to find up to 46.5 per cent of the assets' value without a liquidity event. This forced tax point can threaten the viability of the family business.[160]

6.118 Mr Brassil alerted the committee to additional tax implications:

> [T]he states are treating the transfer of those assets out of the trust as being a matter that involves ad valorem stamp duty. So 5½ per cent, or more, of the market value of the asset potentially gets hit for stamp duty.[161]

6.119 Third, it was also evident that family businesses will incur additional costs to restructure the business. When asked to comment on the significance of the family trading trust for the Australian economy, Treasury officials commented that any change in business structure entails significant cost:

> If you have a business that has worked in a particular model or framework for a period of time there are costs potentially with respect to any sort of change to structures. There are potential costs to taxpayers and businesses

157 PricewaterhouseCoopers, *Submission 11*, p 3.

158 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 31.

159 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 13.

160 PricewaterhouseCoopers, *Submission 11*, p 3.

161 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 31.

> from those changes. The observation of why would particular structures be important to the broader economy are [that they are] the structures that businesses are currently operating under.[162]

6.120 As alluded to in Treasury's comments, it was argued that the rule against perpetuities will adversely affect the broader Australian economy. As PricewaterhouseCoopers submitted, '[t]rusts have become such a part of the Australian business fabric that even government I think is quite happy that they are here to stay.'[163] Family business advisors and representatives argued that the effect of the rule against perpetuities on family trading trusts is an 'issue we are increasingly starting to face'.[164] Estimates varied about when the 80 year timeframe for family trusts will expire. As Mr Noye acknowledged, the vesting date will differ for each family trust.[165] However, in general it was estimated that the effect of the rule against perpetuities will become acute in the next 10 to 20 or 20 to 30 years.[166] For example, Mr Donald McKenzie predicted that by 2030, 50 per cent of family trusts will vest.[167]

6.121 Accordingly, family business representatives and advisers strongly advocated for the government to address the concerns raised with the rule against perpetuities.[168] Mr McKenzie called for governments to be proactive in addressing the effect of the rule for trading trusts:

> 2030 might be a little bit of a stretch – it might be 2040 – but it is coming and all I am sitting here and saying is 'Let's get ahead of the game; let's have a good look at this now; let's sort it out so that we do not sit there'.[169]

6.122 It was further argued that the rule against perpetuities should be repealed. Mr Brassil told the committee that 'it is high time to challenge the 80 year rule'.[170] Mr Le Maistre concurred:

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162 Mr Hector Thompson, General Manager, Small Business Tax Division, Treasury, *Committee Hansard*, 15 November 2012, p. 15.

163 Mr Paul Brassil, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 31.

164 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 47.

165 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 13.

166 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 31; Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 14.

167 Mr Donald McKenzie, Private Capacity, *Committee Hansard*, 21 January 2013, p. 17.

168 See, for example, Mr Donald McKenzie, Private Capacity, *Committee Hansard*, 21 January 2013, p. 18.

169 Mr Donald McKenzie, Private Capacity, *Committee Hansard*, 21 January 2013, p. 17.

170 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 32.

> I cannot see any practical reason why that needs to continue to be in place. From a policy perspective, if you are looking to continue to grow and expand these businesses and have the generational transfer going forward is, I think that is something else which we really should be actively contemplating repealing.[171]

6.123 The effect of the rule against perpetuities was also noted by academic advisers, who held that, as a general principle, rules that are not relevant in the modern context should not be retained. As Professor Mary Barrett, Professor of Management at the University of Wollongong, argued:

> I am inclined to think, if nobody can remember why it was there and if it is holding people back, it is probably a 'cat at the temple door' kind of situation—it was part of the ritual once but nobody can remember why. Maybe it happened by accident and it does not seem to help any longer.[172]

6.124 Similarly, Dr Chris Graves of the University of Adelaide Business School, told the committee:

> [I]f there is a consensus that there are still some advantages of structuring a family in business through using trust structures as opposed to company structures, then it would appear that this arbitrary limitation of 80 years—if you have an artificial time period which is imposing costs which otherwise could be avoided—is obviously something that is serious to look at.[173]

6.125 In support of abolishing the rule against perpetuities, it was submitted that permitting family trading trusts to continue in perpetuity is in line with the opportunities available to family companies.[174] PricewaterhouseCoopers argued:

> When companies exist in perpetuity – and we are all comfortable with that – why would a trust need to end? Whatever historical reasons there were for them to have a life, I challenge them in the current climate and I see downsides.[175]

Committee view

6.126 Australia's legal system should support a robust economy and commercial certainty. While largely anecdotal, there is evidence that the rule against perpetuities has the counter effect. The committee notes with interest comments by the Manitoba

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171 Mr Simon Le Maistre, Partner, KPMG, *Committee Hansard*, 14 November 2012, p. 47.

172 Professor Mary Barrett, Professor of Management, University of Wollongong, *Committee Hansard*, 15 November 2012, p. 40.

173 Dr Chris Graves, Business School, University of Adelaide, *Committee Hansard*, 15 November 2012, p. 40.

174 See, for example, Grant Thornton, *Submission 18*, p. 3.

175 Mr Paul Brassil, Partner, Private Clients, PricewaterhouseCoopers, *Committee Hansard*, 15 November 2012, p. 32.

Law Reform Commission that the rule against perpetuities is 'yesterday's device for solving yesterday's problems...its day, certainly in this province, is done'.[176] The committee has received evidence supporting this view. The marketplace has evolved while the rule against perpetuities has substantially remained since it was first articulated. The rule against perpetuities is an example of Australia's legal system not keeping pace with developments in the business sector.

6.127 The effect and broad scope of the rule against perpetuities warrants further investigation. Given that the rule is likely to require family trading trusts to vest in the coming decades, it is necessary that prompt attention is given to the concerns raised by submitters to this inquiry. It is essential that State and Territory governments consider whether the rule continues to be appropriate for Australia's modern economy. Accordingly, the committee recommends that the Council of Australian Governments, or its relevant Ministerial Council, inquire into whether the rule can be abolished in each jurisdiction, or whether its scope can be limited to appropriately exclude all commercial arrangements.

Recommendation 15

6.128 The committee recommends that the Council of Australian Governments, or its relevant Ministerial Council, inquire into whether the rule against perpetuities can be abolished in each jurisdiction, or whether its scope can be limited to appropriately exclude commercial arrangements. In undertaking this review, the Council should consider how many trading trusts are likely to be affected in the next two decades. It should also consider the effect that abolishing the rule against perpetuities in South Australia has had on trading trusts operating in the State.

6.129 If the Council determines that it is not appropriate to abolish or amend the rule, the committee recommends that it should actively engage with the business sector to alert trading trusts to the financial implications of the vesting requirements.

176 The Manitoba Law Reform Commission, *Report on the rules against accumulations and perpetuities*, Report No. 49, 12 February 1982, pp 41–42.

Chapter 7

Legislative and common law frameworks – further challenges affecting Australian family companies

7.1 The *Corporations Act 2001* and the *Income Tax Assessment Act 1997* impose certain rules on the allocation of shares within a company. Family businesses trading under a company structure raised concerns about various rules affecting share allocation.

7.2 This chapter considers three challenges raised by family businesses. First, submitters argued that the restriction in section 113 of the *Corporations Act 2001* on the number of shareholders in a proprietary company undermines the effective administration of a family business. Second, submitters also questioned the rules regarding employee share schemes in Division 83A of the *Income Tax Assessment Act 1997*. Third, it was noted that family values may not easily align with more traditional concepts of corporate values. Accordingly, it was submitted that this can affect family companies' approach to engaging with corporate management structures such as boards of directors.

Section 113 of the *Corporations Act 2001*

7.3 As part of its 2008 report for its inquiry into 'the engagement and participation of shareholders in the corporate governance of companies in which they are part owners' (the 2008 shareholder inquiry),[1] the committee recommended that 'the government should amend section 113 of the Corporations Act to raise the limit for shareholders in a proprietary company to 100'.[2] The committee's recommendation responded to concerns that the corporate governance requirements under the Corporations Act may impede small, closely held, entities from incorporating. As the committee noted in its report:

> [t]he thrust of this disquiet is that the one size fits all approach best suited to regulating large financial entities is not necessarily suitable for small businesses without a diverse group of equity investors to protect.[3]

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1 Parliamentary Joint Committee on Corporations and Financial Services, *Better shareholders – Better company: Shareholder engagement and participation in Australia*, June 2008, p. 1.

2 Parliamentary Joint Committee on Corporations and Financial Services, *Better shareholders – Better company: Shareholder engagement and participation in Australia*, Recommendation 10, 2008, p. 35.

3 Parliamentary Joint Committee on Corporations and Financial Services, *Better shareholders – Better company: Shareholder engagement and participation in Australia*, 2008, p. 35.

7.4 Section 113 of the Corporations Act limits the number of non-employee shareholders in proprietary companies. A company with in excess of 50 non-employee shareholders is by virtue of section 113 required to incorporate. As the committee noted in its 2008 report, evidence before the committee included representations of Family Business Australia that family companies in existence for successive generations could inadvertently exceed this limit and, accordingly, be required to incorporate.[4] Family Business Australia advised that to avoid the automatic reconstitution of the business from a proprietary company to a public company, family businesses adopt inefficient governance practices. These practices can include minimum shareholding limits, joint share ownership and beneficial ownership, and 'no dividend' or 'low dividend' policies. Family Business Australia further advised that such arrangements can lead to family conflict and reduce the company's access to finance. For the 2005 shareholder inquiry, Family Business Australia concluded that section 113 leads to 'shareholder oppression: oppression by exclusion'.[5]

7.5 Similar concerns were raised by family business representatives during the committee's current inquiry. Family Business Australia reiterated its concerns with the effect of section 113, outlining two objections with the non-employee shareholder limit. First, Family Business Australia challenged the policy basis for the 50 non-employee shareholder cap:

> It is understood that the '50 shareholder rule'...is intended to protect the interests of those 'passive' shareholders. It not only unnecessarily duplicates other forms of legislative protection provided to such stakeholders, but represents a simplistic approach to that objective which adds considerable cost with, in most cases, little or no benefit to those it is designed to protect.[6]

7.6 MGI Australasia concurred with this view, also challenging the policy basis for the non-employee shareholder cap:

> We also agree with the observation of Family Business Australia that this legislation is unnecessary in that there are adequate remedies already available elsewhere in corporate laws to protect minority shareholders. It is our observation that the current law is able to be easily circumvented by those firms that do not wish to be burdened by the cost of a public company and therefore the provision has little practical use.[7]

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4 Parliamentary Joint Committee on Corporations and Financial Services, *Better shareholders – Better company: Shareholder engagement and participation in Australia*, 2008, pp 34–35; citing Mr Christopher Johnston, Family Business Australia, *Committee Hansard*, 15 April 2008, pp 36–37.

5 Family Business Australia, *Submission 3 - Submission to the 2008* '*Better shareholders – Better company' inquiry*, p. 7.

6 Family Business Australia, *Submission 2*, p. 5.

7 MGI Australasia, *Submission 9*, p. 4.

7.7 Second, the committee was again advised that the 50 non-employee shareholder limit compromises the governance practices of an 'increasing number' of family businesses:

> FBA reiterates its objection to this provision, in respect of which anecdotal evidence indicates that increasing numbers of family businesses which are aware of the consequences of ownership by more than 50 shareholders adopt a range of shareholding arrangements to keep the share register below 50 non–employed owners. Examples of such strategies include: minimum shareholding limits and otherwise independent shareholdings being held jointly under various ownership, or beneficial ownership structures.[8]

7.8 As the statement indicates, the committee was informed that the 50 non–employee shareholder limit adversely affects a significant proportion of the family business sector. Family Business Australia put forward that it 'is an issue that most larger family businesses would concur with'.[9] MGI Australasia noted that approximately 11 per cent of family businesses reach the third or subsequent generations, a figure which it was submitted is significant.[10] While not estimating the proportion of family businesses affected, Mr William Noye, National Leader, Family Business Services, KPMG, provided the example of Coopers Brewery which has approximately '183 shareholders in [the] family group.'[11] In support of expanding the 50 non-employee shareholder limit, Mr Noye submitted that '[i]t is important to be able to cater for broader family groups.'[12]

7.9 The theme of supporting successful multigenerational family businesses was commonly put forward as a key reason for amending section 113. MGI Australasia noted that '[a]s family businesses progress through the generations the number of shareholders not employed in the business grows.'[13] MGI Australasia implied that section 113 operates to penalise highly successful family businesses:

> Such businesses, by virtue of their longevity, are often the larger family enterprises. It is such businesses that are often caught by the so-called 50 shareholder rule…section 113 of the Corporations Act 2001…requires corporations with more than 50 non-employed members to become unlisted public companies. This places unnecessary administrative costs on such enterprises.[14]

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8 Family Business Australia, *Submission 2*, p. 5.

9 Mrs Philippa Taylor, Chief Executive Officer, *Committee Hansard*, 14 November 2012, p. 35.

10 MGI Australasia, *Submission 9*, p. 4.

11 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 11.

12 Mr William Noye, National Leader, Family Business Services, KPMG, *Committee Hansard*, 16 November 2012, p. 11.

13 MGI Australasia, *Submission 9*, p. 4.

14 MGI Australasia, *Submission 9*, p. 4.

7.10 Similarly, the Institute of Chartered Accountants Australia submitted:

> [l]arger and older family businesses may have more than 50 non–employed members and the requirement for these businesses to restructure as unlisted public companies imposes administrative costs for questionable benefit.[15]

7.11 The 50 shareholder restriction in section 113 of the Corporations Act was not broadly raised by family business owners. However, where raised, the submissions of family business representatives reflected family business owners' concerns. Mr Stephen Sampson, Director, Lionel Sampson Sadleirs Group, supported an increase to the 50 non–employee shareholder cap. Mr Sampson advised that enacting the committee's 2008 recommendation 'would be incredibly helpful' as it would assist family businesses to respond to governance challenges.[16] Mr Graham Henderson, Director, Family Business Australia, and managing director of a 63-year-old third-generation family business, supported the increase of the 50 non-employee shareholder limit, stating that 'small or medium businesses–SMEs–certainly need more than 50 shareholders.'[17]

The government's response to the committee's 2008 report

7.12 The government has not provided a formal response to the committee's 2008 report. Rather, on 6 July 2011, the government advised the Speaker of the House of Representatives that '[t]he government does not intend to respond to the report because of the time elapsed since the report was tabled'.[18]

7.13 During the 2008 shareholder inquiry, Treasury advised that companies with more than 50 shareholders have a sufficiently diverse ownership base to justify the greater governance requirements that apply where companies incorporate. It was further noted that large proprietary companies have similar reporting obligations to listed public companies. As Treasury submitted:

> [t]he regulatory regime established for proprietary companies is based on the principle that these companies have a relatively non-disperse shareholder base. For this reason, the Corporations Act requires proprietary companies to have less than 50 non-employee shareholders. Companies with a wider shareholder base, for example listed or other public companies, face greater issues in providing effective oversight and control of company management. In order to address these issues, the

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15 Institute of Chartered Accountants Australia, *Submission 25*, p. 3.

16 Mr Stephen Sampson, Director, Lionel Sampson Sadleirs Group, *Committee Hansard*, 7 February 2013, p. 18.

17 Mr Graham Henderson, Director, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 38.

18 Government responses to parliamentary committee reports, *Response to the schedule tabled by the Speaker of the House of Representatives on 25 November 2010*, circulated by the Leader of the House, the Hon. Anthony Albanese MP, 6 July 2011, p. 3.

Corporations Act places greater governance requirements on companies with more disperse ownership.[19]

7.14 Accordingly, Treasury did not accept that there was a compelling rationale for amending section 113.[20] It was further noted that few stakeholders have raised concerns with its operation and effect:

> The requirement for proprietary companies to have no more than 50 non-employee shareholders existed when Australia first adopted a national regime for corporate regulation in 1982. Since this time, Treasury has received very few comments from stakeholders in relation to this requirement. The requirement was reviewed as part of the Corporations Law Simplification Program in 1994. This included stakeholder consultation on whether there should be a restriction of the number of non-employee shareholders in proprietary companies, and if so, what should be set as the maximum number. Following this review, a decision was made not to amend the existing requirement.[21]

7.15 Five years on, in evidence submitted for the committee's family business inquiry, Treasury affirmed the advice previously given during the committee's 2008 shareholder inquiry. The committee was advised that 'the views that were expressed at the time…are consistent with the views which we would hold today on the issue'.[22]

7.16 Treasury confirmed that the increased reporting obligations on companies with a diverse stakeholder base are intended to protect the integrity of Australia's financial system:

> The principle behind the limit goes to the heart of how the Corporations Act seeks to address the agency issue which can arise when control of the company is exercised on a day-to-day basis as distinct from by specialist management and as distinct from the owners of the company. The Corporations Act has developed a framework to address that…mainly through imposing levels of disclosure upon the company. Those levels of disclosure vary between proprietary companies and public companies–listed and unlisted. Section 113 limits at 50 non–employee shareholders, and the principle behind that is that the more diffuse and the greater the

19 Treasury, *Submission 40 – Submission to the 2008 'Better shareholders – Better company' inquiry*, p. 1.

20 Treasury, *Submission 40 – Submission to the 2008 'Better shareholders – Better company' inquiry*, p. 1; as cited in Parliamentary Joint Committee on Corporations and Financial Services, *Better shareholders – Better company: Shareholder engagement and participation in Australia*, 2008, p. 35.

21 Treasury, *Submission 40 - Submission to the 2008 'Better shareholders – Better company' inquiry*, p. 1.

22 Mr David Woods, General Manager, Corporations and Capital Markets Division, Treasury, *Committee Hansard*, 13 November 2012, p. 13.

> number of shareholders on the registry, the greater is the potential for the agency problems to arise.[23]

7.17 Further, Treasury officials reiterated that the reporting obligations applying to larger proprietary companies are similar to incorporated companies. Although it acknowledged that the 50 shareholder limit is 'an arbitrary line in the sand', Treasury maintained its previous advice that the Department had 'received very few representations from small businesses and family businesses' about the effect of section 113. Accordingly, it was submitted that 'it is not clear how great the benefits would be of raising the cap'.[24] Importantly, however, Treasury advised the committee that '[i]f there was a problem, and people came to talk to us, we would be happy to revisit the issue'.[25]

Committee view

7.18 In electing to inquire into the operation of the family business sector in Australia, the committee determined to establish whether Australia's marketplace appropriately accommodates family businesses. Evidence before the committee demonstrates that section 113 of the Corporations Act is an example of a general corporations law policy that does not correlate with the specific needs and operational realities of family businesses. The effect of section 113 for larger, multigenerational family business further demonstrates the need for government, and policymakers more broadly, to proactively engage with the family business sector.

7.19 The committee acknowledges Treasury's advice that the limit on non-employee shareholders imposed by section 113 is an integrity measure. However, in the context of family businesses, the committee questions the relevance of Treasury's advice that the more diffuse and the greater the number of shareholders on the registry, the greater is the potential for the agency problems to arise. Where the non-employee shareholders are members of the same family, supporting the same business objectives, it is not clear that these agency problems will be present.

7.20 The committee appreciates Treasury's advice that the Department has received few representations about the effect of section 113 on family businesses, or, indeed, small businesses. However, the evidence currently before the committee mirrors that which the committee obtained about section 113 during its 2008 shareholder inquiry. The time has come for government to consider whether the policy rationale behind section 113 is applicable in the family business context.

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23 Mr David Woods, General Manager, Corporations and Capital Markets Division, Treasury, *Committee Hansard*, 13 November 2012, p. 13.

24 Mr David Woods, General Manager, Corporations and Capital Markets Division, Treasury, *Committee Hansard*, 13 November 2012, p. 13.

25 Mr David Woods, General Manager, Corporations and Capital Markets Division, Treasury, *Committee Hansard*, 13 November 2012, p. 14.

7.21 A theme that has emerged throughout this inquiry is the need for the family business sector to assume a more active presence in policy and legislative development. The committee encourages family business representatives to collectively approach government to provide necessary advice about the sector, its operational successes and its needs going forward.

7.22 To this end, the committee recommends that Treasury officials meet with representatives of the family business sector to explore the effect of section 113, and whether the policy rationale for the 50 shareholder limit is applicable for family businesses. The government's response to this report should detail the consultation process, the issues raised, and the measures that the government proposes to actively support larger, multigenerational family businesses to respond to the non-employee shareholder limit. It is incumbent on family businesses to advise Treasury of the number of family businesses that have exceeded, or are actively taking steps to avoid exceeding, the 50 shareholder limit.

Recommendation 16

7.23 The committee recommends that the Department of the Treasury consult with representatives of the family business sector about the effect of section 113 of the *Corporations Act 2001* on large, multigenerational family businesses.

7.24 The committee considers that it would be appropriate for the Australian Bureau of Statistics to collect data on the effect of section 113 on Australian businesses, including family businesses.

Recommendation 17

7.25 The committee recommends that the Australian Bureau of Statistics collect data on the effect of section 113 of the *Corporations Act 2001* on Australian businesses.

Division 83A of the *Income Tax Assessment Act 1997*

7.26 Family business advisors MGI Australasia and the Institute of Chartered Accountants Australia argued that the rules in Division 83A of the *Income Tax Assessment Act 1997* (the 1997 Act) that regulate employee share schemes disadvantage small and medium sized family businesses trading under a company structure.[26]

26 Institute of Chartered Accountants Australia, *Submission 25*, pp 3–5; MGI Australasia, *Submission 9*, pp 5–6.

7.27 Employee share schemes provide employees shares, or the opportunity to acquire shares, in the company for which they work.[27] The Australian Taxation Office (the ATO) defines employee share schemes as:

> a scheme under which shares, stapled securities and rights (including options) to acquire shares or securities in the company are provided to its employees (including current, past or prospective employees and their associates) in relation to their employment.[28]

7.28 Employees' entitlements under employee share schemes are taken into account by the ATO for tax purposes. Division 83A of the 1997 Act establishes the rules that determine the taxation arrangements for employees' entitlements under employee share schemes. Division 83A was inserted in 2009 by the *Tax Laws Amendment (2009 Budget Measures No. 2) Act 2009*, which received Royal Assent on 14 December 2009. Division 83A replaced Division 13A of the *Income Tax Assessment Act 1936* (the 1936 Act), which was introduced in 1974. The rules in Division 83A were intended to address concerns that Division 13A of the 1936 Act was open to misuse and did not effectively prevent tax avoidance.[29] As Treasury informed the committee, the 2009 changes to the regulation of employee share schemes:

> were designed to better target eligibility for the concessions to employees to improve fairness and the integrity of the tax system. The changes improve horizontal equity in the tax system by treating different forms of remuneration more equally.[30]

7.29 As noted in the Explanatory Memorandum (EM) to the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, the taxation arrangements established in Division 83A are intended to strike an appropriate balance between ensuring that all remuneration received, regardless of its form, is subject to taxation, and encouraging business productivity and the retention of appropriately qualified staff:

> [T]he employee share scheme tax rules…specifically aim to improve the alignment of employee and employer interests. In recognition of the economic benefits derived from employee share scheme arrangements, the rules provide tax concessions for employees participating in employee share schemes. Tax support is provided on the grounds that aligning the

27 Australian Securities and Investments Commission and MoneySmart, *Employee share schemes*, https://www.moneysmart.gov.au/investing/shares/employee-share-schemes (accessed 1 February 2013).

28 Australian Taxation Office, *Employee share schemes – guide for employees*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&menuid=0&doc=/content/00224640.htm&page=4&H4 (accessed 1 February 2013).

29 The Hon Wayne Swan MP, Treasurer, 'Better targeting the employee share scheme tax concessions', Media release, 12 May 2009.

30 Treasury, *Submission 26*, p. 1.

interests of employees and employers, encourages positive working relationships, boosts productivity through greater employee involvement in the business, reduces staff turnover and encourages good corporate governance.[31]

7.30 This intention is given legislative force by section 83A.5 of the 1997 Act, which provides that the objects of Division 83A are:

- to ensure that benefits provided to employees under employee share schemes are subject to income tax at the employees' marginal rates under income tax law (instead of being subject to fringe benefits tax law); and
- to increase the extent to which the interests of employees are aligned with those of their employers, by providing a tax concession to encourage lower and middle income earners to acquire shares under such schemes.[32]

7.31 Accordingly, Division 83A establishes four categories of employee share schemes, namely:

- taxed-upfront scheme – not eligible for reduction (default tax position);
- taxed-upfront scheme – eligible for reduction;
- tax-deferred scheme – salary sacrifice; and
- tax-deferred scheme – real risk of forfeiture.[33]

7.32 The Institute of Chartered Accountants Australia provided the following explanation of the tax concessions available under Division 83A:

Division 83A of ITAA97 operates to tax employees upfront on the value of any discount they are allowed on the provision of shares. This tax may only be deferred if the arrangement is structured so that:

- there is a real risk that the shares will be forfeited, or
- the shares are acquired under a salary sacrifice arrangement and the employee receives no more than $5,000 worth of shares per annum.[34]

7.33 The Institute further explained that Division 83A defers but does not waive tax liabilities:

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31 Explanatory Memorandum, Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, paragraphs 1.84–1.86.

32 *Income Tax Assessment Act 1997*, s. 83A.5.

33 Australian Taxation Office, *Employee share schemes – guide for employees*, http://www.ato.gov.au/businesses/PrintFriendly.aspx?ms=businesses&menuid=0&doc=/content/00224640.htm&page=4&H4 (accessed 1 February 2013).

34 Institute of Chartered Accountants Australia, *Submission 25*, p. 4.

The tax will be deferred until the earliest of:

- the time when there is no real risk that the employee will forfeit the shares and there are no genuine restrictions preventing disposal;
- when the employee ceases the employment; or
- seven years after the employee acquired the shares.[35]

7.34 To access the concessions in Division 83A, employee share schemes must satisfy a number of preconditions. These include that the employee share scheme is non-discriminatory. A scheme satisfies this requirement if shares are offered to at least 75 per cent of the company's employees.[36] This requirement was carried over from the rules under the former Division 13A of the 1936 Act.[37] As Treasury explained, the 75 per cent rule does not apply to employee share schemes that only offer rights, that is, options, in the company.[38] Additionally, an employee may not hold more than five per cent of the company's shares, or be in a position to cast, or to control the casting of, more than five per cent of the maximum number of votes that might be cast at the company's general meetings.[39] As the Board of Taxation has commented, the requirements:

> aim to ensure, among other things, that participation in the scheme is widely available to employees, and that the concessions cannot be accessed by shareholders who are effectively able to exert control over the company's operations.[40]

Employee share schemes and executive remuneration

7.35 The Institute of Chartered Accountants Australia argued that for private family companies employee share schemes are primarily used to promote company loyalty, rather than to increase remuneration provided to executive employees:

> Providing shares to an employee in an SME is usually seen more as a means of aligning the long-term goals of the business with those of the employee rather than being a component of a remuneration package.[41]

7.36 However, employee share schemes are considered an essential recruitment tool for family businesses seeking to attract senior management personnel.[42] The

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35 Institute of Chartered Accountants Australia, *Submission 25*, p. 4.

36 *Income Tax Assessment Act 1997*, ss. 83A.35(6).

37 *Income Tax Assessment Act 1936*, s. 139CD.

38 Treasury, answer to question on notice, 4 February 2013 (received 8 February 2013).

39 *Income Tax Assessment Act 1997*, ss. 83A.35(9).

40 Board of Taxation, *Review into elements of the taxation of employee share scheme arrangements*, February 2010, p. 5.

41 Institute of Chartered Accountants Australia, *Submission 25*, p. 3.

Institute of Chartered Accountants Australia submitted that the judicious use of employee share schemes 'is about giving employees and employers in the family business the best opportunity they have…to ensure that the business can survive into the future.'[43]

7.37 However, the committee was advised that it is difficult for family companies and their employees to access the tax concessions under Division 83A. It was submitted that the requirements to access the tax concessions do not reflect the structure and financial arrangements of family companies. In particular, concerns were raised with the rules in Division 83A that require employee share schemes to be available to a broad range of employees. The Institute of Chartered Accountants Australia submitted that the requirement for employee share schemes to be non-discriminatory is at odds with the strategic use of employee shares to attract senior management personnel:

> Importantly deferral is only available where at least 75% of all of the permanent employees of the employer who have completed at least 3 years service are entitled to acquire shares.
>
> This requirement that the shares are broadly available effectively means that deferral is not available where shares are offered only to key employees, which will generally be the position where shares are provided to one or a few managers for succession planning purposes.[44]

7.38 MGI Australasia concurred with this view, arguing that Division 83A limits the opportunities available to family businesses to attract external expertise:

> According to the 2010 MGI survey around one third of family business owners believe that the current CEO is likely to be succeeded by a non-family member. The attraction and retention of suitably skilled outside managers is therefore key to the success of that transition.
>
> Attracting and retaining skilled and experienced successors is a critical component in the transitioning of family businesses from the current baby boomer owner-operators. Providing attractively-priced equity in order to achieve this is currently discouraged by Division 83A.[45]

7.39 To this end, the Institute of Chartered Accountants Australia recommended that Division 83A be amended to 'exempt SMEs from the broad availability requirements'. It was submitted that SMEs should be defined as 'businesses which characteristically have insufficient depth of management to ensure long-term viability

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42 Institute of Chartered Accountants Australia, *Submission 25*, p. 4; MGI Australasia, *Submission 9*, p. 6.

43 Mr Yasser El-Ansary, General Manager, Leadership and Quality, Institute of Chartered Accountants Australia, *Committee Hansard*, 14 November 2012, p. 19.

44 Institute of Chartered Accountants Australia, *Submission 25*, p. 4.

45 MGI Australasia, *Submission 9*, p. 6.

of the business' and 'with an aggregated group turnover of no more than $35 million per annum.'[46]

7.40 Treasury disputed the view that employee share schemes should be targeted towards executive management positions. Treasury argued that employee share schemes are not an appropriate means of fostering company loyalty:

> The interests of senior executives and directors of companies, including those working for family businesses, should already be strongly aligned with the interests of shareholders and therefore there is no productivity benefit that would arise by extending additional tax concessions to shares issued at a discount to such persons.[47]

7.41 Additionally, it was noted that providing employee share schemes to only a select proportion of employees would create disparity within the company. As Treasury submitted,'[a]llowing executives to defer the taxation point would provide a concession to a select group that was not extended to the majority of employees.'[48] Further, Treasury questioned the integrity of offering employee share schemes to only employees in senior management positions. Treasury advised that 'the 75 per cent requirement ensures the ESS [employee share scheme] tax concessions are not inappropriately accessed by those in control of the company.'[49]

7.42 In response to proposals to exempt a particular class of business from the 75 per cent requirement, Treasury informed the committee that 'it would be difficult to define "family business" to provide an exemption from the 75 per cent requirement, in a way that would robustly ring-fence particular types of companies.' It was further contended that the isolation of a particular category of Australian business in the manner recommended by family business representatives 'could also compromise the integrity of the ESS [employee share scheme] tax regime as a whole, potentially creating situations of inequity and increasing risk of tax avoidance'.[50]

Previous inquiries

7.43 The issue of whether employee share schemes can appropriately be used as a form of executive remuneration was the subject of previous inquiry. In 2009, the Productivity Commission examined 'the current Australian regulatory framework around remuneration of directors and executives, as it applies to companies which are disclosing entities regulated under the *Corporations Act 2001*.'[51] As the

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46 Institute of Chartered Accountants Australia, *Submission 25*, p. 4.

47 Treasury, *Submission 26*, p. 1.

48 Treasury, *Submission 26*, p. 1.

49 Treasury, answer to question on notice, 4 February 2013 (received 8 February 2013).

50 Treasury, answer to question on notice, 4 February 2013 (received 8 February 2013).

51 Productivity Commission, *Executive remuneration in Australia: Productivity Commission inquiry report*, Report No. 49, Terms of Reference, 19 December 2009, p. iv.

Productivity Commission noted, the 2009 amendments to the regulatory framework for employee share schemes restricted executive employees' access to the tax concessions.[52] Prior to 2009, the tax concessions applying to employee share schemes could be accessed by all employees regardless of their salary. In contrast, Division 83A limits the tax concession to taxpayers with an adjusted taxable income of less than $180 000.[53]

7.44 The EM to the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009 indicates the policy reasons for the introduction of a ceiling on the salary levels of eligible employees. As stated in the EM, the tax concessions under Division 83A are intended to be available only to lower and middle income earners.[54] Executives appear to be outside the contemplated scope of the tax concessions under Division 83A. As the Productivity Commission noted:

> [t]he taxation provisions for employee share schemes are not specifically designed for executives and must apply to all Australian employees. Furthermore, the concessions that enable deferral of tax for equity-based payments are targeted towards schemes to encourage broad employee share ownership.[55]

7.45 The Productivity Commission did not recommend that the $180 000 salary limit be increased. However, the Productivity Commission did recommend that the 2009 changes to the regulation of employee share schemes be reviewed as part of a broader review into corporate governance arrangements. The Productivity Commission further recommended that the review be undertaken no later than five years from the introduction of any new measures arising out of the Productivity Commission's report.[56]

Suitability of Division 83A for family companies – liquidity requirements

7.46 Family business advisors further submitted that Division 83A effectively discriminates between public companies and private family companies. MGI Australasia advised that '[f]amily businesses are at a great disadvantage competing with large enterprises, which offer discounted equity that can be market traded and/or structured to gain tax deferral.'[57]

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52 Productivity Commission, *Executive remuneration in Australia: Productivity Commission inquiry report*, Report No. 49, 2009, p. 328.

53 *Income Tax Assessment Act 1997*, s. 83A.35.

54 Explanatory Memorandum, Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, paragraph 1.117.

55 Productivity Commission, *Executive remuneration in Australia: Productivity Commission inquiry report*, Report No. 49, 2009, p. 341.

56 Productivity Commission, *Executive remuneration in Australia: Productivity Commission inquiry report*, Report No. 49, 2009, Recommendation 17, p. xli.

57 MGI Australasia, *Submission 9*, p. 6.

7.47 It was noted that, compared with public companies, shares in a private company are not liquid.[58] Accordingly, tax is levied on benefits that cannot easily be realised. The Institute of Chartered Accountants Australia argued:

> [t]his acts as a deterrent to family businesses providing discounted equity to successors, because it results in tax on a 'benefit' that may take decades to convert into cash. Unlike shares in a public company, shares and family business are highly illiquid.[59]

7.48 It was submitted that it is necessary for employees of private family companies to access the tax concessions under Division 83A. As the Institute of Chartered Accountants stated:

> Because of this lack of liquidity, paying full value for equity in an SME is not attractive to employees who have no certainty as to when, or if, they will be able to realise that value or indeed any value. It is therefore often both desired and necessary for SME owners to gift or discount equity to key managers. However the taxation impediments to this often mean that equity is not provided or is provided through complex, cumbersome arrangements in order not to fall foul of the current taxation provisions.[60]

7.49 Treasury disputed the view that legislative amendment is necessary to support family businesses to access tax concessions under Division 83A. In response to liquidity concerns raised by submitters, Treasury advised that liquidity 'is an issue that is not unique to family businesses and is faced by many other companies (for example smaller listed companies).'[61] Treasury also reiterated the accepted taxation principle that '[t]he economic value embodied in employee share schemes and rights is equivalent to any other form of employee compensation and should generally be taxed in the same manner.'[62]

Previous inquiries

7.50 The argument that access to tax concessions under Division 83A is necessary to support 'cash-strapped' companies was considered in 2009 by the Board of

58 Institute of Chartered Accountants Australia, *Submission 25*, p. 3.

59 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

60 Institute of Chartered Accountants Australia, *Submission 25*, p. 3.

61 Treasury, *Submission 26*, p. 1.

62 Treasury, answer to question on notice, 4 February 2013 (received 8 February 2013).

Taxation.[63] The Board acknowledged that there is some merit to the argument. However, the Board ultimately concluded that relaxing the current restrictions was unviable:

> The Board agrees that there is some merit to the argument that the existing restrictions that operate to limit access to the existing employee share scheme tax concessions tend to operate particularly onerously on these types of companies.
>
> However, the Board considers that due to the largely disparate nature of these types of companies there is a fundamental difficulty in attempting to define which entities should be eligible to access any relaxed restrictions. The Board considers that in light of the significant integrity concerns to the operation of the employee share scheme provisions created by the inability to adequately ring-fence eligibility, any relaxation of the current restrictions is not a viable alternative.[64]

Additional matters: The five per cent cap on the percentage of company shares held and the maximum seven year deferral period

7.51 Concern was also raised with the restriction on the percentage of company shares that an employee may hold in order to be eligible to access tax concessions under Division 83A. The Institute of Chartered Accountants Australia submitted that the five per cent limit is 'too low to provide a worthwhile succession planning mechanism'.[65] It was argued that a 'minority holding' test would be more appropriate for family companies:

> [A] more meaningful requirement would be for the shareholding to be a minority holding. Once majority holding is obtained, the succession has essentially taken place and the employee is then in a better position to be able to realise the value of the shares.

7.52 However, it is evident that there is a disconnect between the policy intent underlying Division 83A and the use of employee share schemes by companies within the family business sector. As noted in the EM to the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, the five per cent requirement reflects the policy of aligning employee interests with company interests. As the EM notes, it was not

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63 Senator the Hon Nick Sherry, Assistant Treasurer, 'Details of further industry consultation on employee share schemes tax reforms', Media release No. 017, 24 July 2009. In considering the terms of reference to inquire into 'whether shares and rights under an employee share scheme at a start-up, R&D or speculative focused company should have separate tax deferral arrangements', the Board of Taxation noted the attraction of employee share schemes for 'cash-strapped' companies - Board of Taxation, *Review into elements of the taxation of employee share scheme arrangements*, February 2010, p. ix.

64 Board of Taxation, *Review into elements of the taxation of employee share scheme arrangements*, February 2010, p. ix.

65 Institute of Chartered Accountants Australia, *Submission 25*, p. 4.

considered necessary to provide tax incentives to align the company's interests with the interests of employees who hold more than five per cent of the company's shares:

> This provision encourages the benefits of the employee share scheme to be spread widely among employees. The concession is intended to encourage employees with small or no ownership in their employer to take up an interest in the company. It is considered that if one employee owns more than 5 per cent of the voting rights, interests between the company and that shareholder are already aligned, and no tax concession is appropriate or warranted.[66]

7.53 The EM casts further doubt on the appropriateness of using employee shares as a mechanism to facilitate change of company ownership:

> Further, this acts as an integrity rule that prevents taxpayers from misapplying the concession in order to buy a business or indirectly access company profits through the employee share scheme rules. The concession is intended to apply in respect of the employee/employer relationship and not in relation to the company/shareholder relationship.[67]

7.54 It was further submitted that 'the maximum deferral period of seven years contained in Division 83A should be extended for SMEs, as generally the opportunity to realise shares in an SME is extremely limited'. The Institute of Chartered Accountants put forward that the deferral period for SMEs, including relevant family companies, should be 'extended to the earlier of a realisation event, termination of employment…and obtaining a majority shareholding.'[68]

7.55 Prior to 2009, Division 13A of the 1936 Act authorised tax liabilities incurred under employee share schemes to be deferred for a maximum of 10 years. With the introduction of the 2009 amendments, this timeframe was reduced to seven years.[69] Concerns with the introduction of a seven year maximum deferral period were raised at the time of consultation on the exposure draft legislation.[70] In response, the EM to the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009 states:

> The deferral period is limited by the ESS deferred taxing points to ensure fairness, [to] continue to align the interests of the employer and employee,

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66 Explanatory Memorandum, Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, paragraph 1.134.

67 Explanatory Memorandum, Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, paragraph 1.135.

68 Institute of Chartered Accountants Australia, *Submission 25*, p. 4.

69 Senator the Hon Nick Sherry, 'Taxation of employee share schemes', Media release No. 011, 1 July 2009.

70 See, for example, CPA Australia, *Submission re reform of the taxation of employee share schemes*, http://archive.treasury.gov.au/documents/1573/PDF/CPA_Australia.PDF (accessed 8 February 2013).

> and [to] preserve the integrity of the tax system by preventing unlimited deferral of tax on employment remuneration.[71]

7.56 While some submitters to the Exposure Draft consultation process raised concerns with the reduction of the maximum deferral period, others accepted the reduction as a revenue raisings measure.[72] The seven year deferral period is not included in Treasury's summary of the key matters raised during the consultation process.[73]

Committee view

7.57 On the basis of evidence before the committee, it is clear that there is tension between the preferred use of employee share schemes by family companies and the policy rationale underpinning Division 83A. In authorising the enactment of the Division 83A framework, Parliament intended to foster the productivity benefits that can be gained where employees have a personal stake in the success and profitability of their employer. Division 83A was not intended to facilitate management handovers or ownership transfers. Indeed, utilising Division 83A for these purposes attempts to re-engineer the operation and purpose of employee share schemes and the Division 83A tax concessions.

7.58 The committee notes the Productivity Commission's recommendation that the operation of Division 83A be reviewed. The committee also notes that the Board of Taxation's inquiry into the effect of Division 83A on 'cash-strapped' companies did not expressly include family businesses. Therefore, the committee considers that as part of a broader process of actively engaging with the family business sector, Treasury should review the challenges encountered by family businesses in recruiting executives and advise the government about whether the employee share scheme framework should be adjusted to support family businesses in their recruitment endeavours.

Recommendation 18

7.59 The committee recommends that the Department of the Treasury review the evidence gathered through the committee's inquiry into the family business sector in Australia and consider consulting the stakeholders identified through this inquiry about the sector's concerns about the effect of Division 83A of the

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71 Explanatory Memorandum, Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009, paragraph 1.191.

72 See, for example, PricewaterhouseCoopers, *Submission: Reform of the taxation of employee share schemes*, http://archive.treasury.gov.au/documents/1573/PDF/PriceWaterhouseCoopers.pdf (accessed 8 February 2013).

73 Treasury, *Employee share schemes: Summary of consultation process*, http://archive.treasury.gov.au/documents/1559/PDF/ESS_consultation_summary.pdf (accessed 8 February 2013).

***Income Tax Assessment Act 1997* on their capacity to engage suitably qualified executives. Treasury should advise government about whether appropriate support can be provided, whether through amendments to Division 83A or other mechanisms, to address the challenges faced.**

Family businesses, directors and directors' duties

7.60 The committee was informed that family values can affect a family business' management structure and financial operations. As David Hill, National Managing Director of Deloitte Private, noted, family values may not reflect corporate values:

> Corporates often are challenged by taking decisions based on quarterly reporting cycles—very short-term decisions designed to…report a profit. Family businesses do not think that way; they think of the longer term because of their legacy, their values and their reputation.[74]

7.61 For family businesses trading under a corporate structure, family values can impact corporate practice. Notably, the committee's attention was drawn to the composition and use of boards of directors.

7.62 As MGI Australasia has advised, formal boards assist companies to increase accountability, improve decisions making and planning without compromising privacy.[75] However, family businesses have shown a reluctance to engage more than the statutory minimum number of directors. MGI explained that the lack of formal boards is a result of family businesses' reluctance to engage more than the minimum amount of directors in order to maintain a certain level of asset protection and to minimise the liability of the family business.[76]

7.63 As a solution, MGI Australasia Ltd recommended in their submission that a separate class of directors should be created to encourage the adoption of separate formal boards. This sub class of director would not be subject to the liabilities that a standard director would be exposed to:

> [A]dditional persons should be able to act as actual or defacto directors without being subject to all the personal risks applied under the Corporations Law…as long as at least one member of the family business remains fully liable.[77]

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74 Mr David Hill, National Managing Director of Deloitte Private, *Committee Hansard*, 14 November 2012, p. 8.

75 MGI Australasia Ltd, *From the dining room to the board room – Family business in focus: The MGI Australian Family and Private Business Survey 2010,* July 2010, p. 7.

76 MGI Australasia Ltd, *Submission 9,* p. 5.

77 MGI Australasia Ltd, *Submission 9,* p. 5.

7.64 The submission suggested that this new category of a director could be named an 'associate director'.[78]

7.65 Reports into this issue have offered other reasons for family businesses only engaging the minimum amount of directors, separate to asset protection and the reduction in risk of liabilities. The MGI Australian Family and Private Business Survey 2010 stated that 'the main reasons provided for the lack of non-family, non-executive directors on the Board were: desire to retain privacy 52.5%...and skills required at Board level exist in-house 29.0%'[79].

7.66 Deloitte Private recommended a different approach to solve this issue—the creation of an advisory board. An advisory board would consist of a panel of external advisors who would aid directors. The advisors would not be considered directors, as they would not be entitled to vote on directors' resolutions, they would not receive directors' fees and they would hold only an advisory function. This would absolve the board of advisors of any liability.[80]

7.67 The duties of directors set out in the Corporations Act reflect the necessity of protecting investors.[81] It is expected that directors will uphold the highest of standards in the interests of investors and act with the degree of care and diligence that a reasonable person would exercise in their position.[82] The same standards apply for a director of a family business. In addition, a director owes fiduciary duties to their company. The director cannot have a conflict of interest and must act in the interest of the company.[83] After the Centro civil penalty case, the Australian Securities and Investments Commission (ASIC) explained that 'the role of a director is significant as their actions may have a profound effect on the community'.[84] Accordingly, ASIC has

78 MGI Australasia Ltd, *Submission 9*, p. 5.

79 MGI Australasia Ltd, *From the dining room to the board room—Family business in focus: The MGI Australian Family and Private Business Survey 2010*, July 2010, p. 14.

80 Deloitte Private, *Submission 16*, p. 19.

81 *Corporations Act 2001*, Part 2D.1.

82 *Corporations Act 2001*, s180.

83 *Corporations Act 2001*, s182.

84 Australian Securities and Investments Commission, 'Decision in Centro civil penalty case', Media release 11-125MR, 27 June 2011, http://www.asic.gov.au/asic/ASIC.NSF/byHeadline/11-125MR%20Decision%20in%20Centro%20civil%20penalty%20case?opendocument (accessed 19 February 2013)

also previously warned against directors heeding the advice of others without question.[85]

Committee view

7.68 As ASIC has recognised, directors are seen as the 'gatekeepers' of the Australian markets. [86] A director's duty is to act in the interest of the company, regardless of whether it is a public or family business. The committee notes that directors can be useful to family businesses in non-traditional ways, such as resolving family business conflicts.[87] Though family businesses will only tend to engage the minimum number of directors, those directors are responsible for ensuring the company functions in compliance with the Corporations Act.[88]

7.69 The committee believes there is no policy justification for the recommended change to add associate directors to the Corporations Act. A change such as the inclusion of associate directors could have unintended consequences in the broader Corporations Act, radically changing its framework while potentially affecting the general quality of directors' duties.

7.70 The suggestion for an advisory board for family business raises concerns for the committee. There is an inherent danger in directors relying uncritically on advisors, as the actions directors take can have a significant impact on shareholders, employees and the wider community. This danger was made evident by the Federal Court of Australia's decision in the Centro civil penalty case.[89]

7.71 The committee notes the hesitance of family businesses to engage more than the minimum number of directors. However, this uncertainty seems to be born of a discord between corporate and family values and a perceived need to keep the majority of the family business' decisions within the family, rather than a desire to

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85 Australian Securities and Investments Commission, 'Decision in Centro civil penalty case', Media release 11-125MR, 27 June 2011, http://www.asic.gov.au/asic/ASIC.NSF/byHeadline/11-125MR%20Decision%20in%20Centro%20civil%20penalty%20case?opendocument (accessed 19 February 2013)

86 Australian Securities and Investments Commission, 'Decision in Centro Civil Penalty Case', Media release 11 – 125MR, 27 June 2011.

87 KPMG, *Stewards: Moving forward, moving onward – KPMG and Family Business Australia's Family Business Survey 2011*, 2011, p. 11.

88 Australian Securities and Investments Commission, *Your company and the law*, Information Sheet No. 79, http://www.asic.gov.au/asic/asic.nsf/byheadline/Your+company+and+the+law (accessed 19 February 2013).

89 Australian Securities and Investments Commission, 'Decision in Centro civil penalty case', Media release 11-125MR, 27 June 2011, http://www.asic.gov.au/asic/ASIC.NSF/byHeadline/11-125MR%20Decision%20in%20Centro%20civil%20penalty%20case?opendocument (accessed 19 February 2013).

maintain a certain level of asset protection and to minimise the liability of the family business.

Recommendation 19

7.72 The committee recommends that the Australian Securities and Investments Commission consult with family businesses to gauge their understanding of the *Corporations Act 2001*, in particular directors' duties and liabilities, and work with Family Business Australia and other interested organisations that represent family businesses to disseminate information through education and training. Information could also be usefully provided in plain terms on the MoneySmart website.

Chapter 8

The family business sector's access to finance and its response to the global financial crisis

8.1 The sixth and seventh articles of the terms of reference direct the committee's attention to the capacity of family businesses to access to finance and insurance, and their resilience in response to the global financial crisis (the GFC). This chapter addresses these issues.

A family business or a small and medium enterprise?

8.2 Chapters 2, 3 and 4 of this report noted the lack of reliable official data on most aspects of family businesses in Australia. This is also the case in terms of family enterprises' access to finance and insurance, and the sector's resilience in the wake of the GFC.

8.3 The committee's evidence about the family business sector's access to finance and resilience following the GFC was predominantly focused on small and medium family enterprises.[1] Data on large family businesses was limited.

8.4 Evidence received from Authorised Deposit-taking Institutions (ADIs) and financial regulators particularly illustrated the overlap between SME data and family business statistics. The Reserve Bank of Australia (the RBA) advised that it 'would not profess to have any specialist knowledge about family businesses'. Rather, the RBA 'focuses on small and medium enterprises' reflecting its 'area of particular interest, which is monetary policy and how decisions on monetary policy are flowing through to small, medium and large businesses'.[2]

8.5 In response to a question on the importance of distinguishing between family and non-family enterprises, the RBA advised that such data 'is not irrelevant'. However, at this time the RBA does not perceive any clear benefits to isolating family business data:

> It is not irrelevant. It is about the marginal benefit of going down that route versus the cost. For us, we may not decide that the benefits would be enough, because we think we get enough information on small businesses. But if you are trying to develop policy and family businesses you will have a different view on that. In an ideal world, the statistical form that people fill in would be bigger and there would be a field to do with family

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1 See, for example, Commonwealth Bank of Australia, *Submission 24*, pp 1–4; Deloitte Private, *Submission 16*, pp 26–27; Reserve Bank of Australia, *Submission 17*, p. 1.

2 Mr Christopher Aylmer, Head, Domestic Markets Department, Reserve Bank of Australia, *Committee Hansard*, 15 November 2012, p. 3.

> businesses. That would let you slice or dice the information in the way that you wanted to instead of adopting a single standard everyone.[3]

8.6 Similarly, the Commonwealth Bank of Australia (the CBA) advised that it 'does not categorise information from our customers on the basis of "family" as opposed to "small" business'.[4] The CBA also questioned the practicality of isolating family business data from non-family businesses, advising that 'it is difficult to distinguish a "family business" from a "small business" from a policy perspective'.[5]

8.7 The RBA acknowledged the limitations in the statistics presented. As Mr Christopher Alymer of the Domestic Markets Department advised:

> I would like to...draw the committee's attention to the fact that a lot of the observations we have made in the supporting documentation have actually been focused on small and medium-sized enterprises as opposed to family businesses. To a large degree that reflects the availability of statistics, if the truth be known.[6]

8.8 The lack of a clear demarcation between SME data and data focused on family business was also evident in representations of family business advisers and others concerned with the family business sector. For example, BusinessSA, Bond University, and the Institute of Certified Bookkeepers, oscillated between references to the family business sector and references to SMEs.[7] Accordingly, data was extrapolated from SME statistics and conclusions were based on inference. The submission from Deloitte Private is illustrative of this approach:

> Commercial banks have significantly reduced their lending since the GFC, particularly to small and medium businesses in which family businesses predominate…many family businesses have difficulty accessing bank funding. According to the results of the above-mentioned CPA survey on small businesses, 32 per cent of small businesses seeking additional financing in 2011 found it difficult or very difficult. [8]

8.9 Similarly, the Chamber of Commerce and Industry Queensland (CCIQ) linked the family business sector to the SME sector. It advised that 'many small businesses reported adverse impacts as ongoing following the GFC, and family businesses as a subgroup of SMEs was not immune'.[9]

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3 Mr Aylmer, Reserve Bank of Australia, *Committee Hansard*, 15 November 2012, p. 1.

4 Commonwealth Bank of Australia, *Submission 24*, p. 2.

5 Commonwealth Bank of Australia, *Submission 24*, p. 1.

6 Mr Aylmer, Reserve Bank of Australia, *Committee Hansard*, 15 November 2012, p. 1.

7 BusinessSA, *Submission* 23, p. 2; Bond University, *Submission 3*, p. 9; Institute of Certified Bookkeepers, *Submission 36*, p. 4.

8 Deloitte Private, *Submission 16*, pp 26–27.

9 CCIQ, *Submission 19*, p. 2.

Submitters' acknowledgement of data limitations

8.10 The lack of targeted data was also the subject of comment by family business advisers and academic researchers. It was strongly submitted that there would be economic benefits to obtaining data specific to family businesses. For example, in their joint submission, Dr Chris Graves, Professor Mary Barrett and Dr Jill Thomas identified three potential benefits of longitudinal data about the financing preferences of family businesses. First, the data would increase understanding of the impact of business culture on the sector's economic performance. Second, the information would lead to more targeted professional advice and ultimately 'allow external advisers to help family firms professionalise their management and governance structures'. Third, the data would broaden the scope of finance available to the family business sector, as a more professional sector would more easily attract private equity providers.[10]

Access for small and medium business to finance

8.11 The committee's analysis of the family business sector follows its earlier inquiry into access to finance for SMEs. Reporting in April 2011, the committee considered the types of finance that are available to SMEs, the degree of competition in SME lending, and the impact of prudential regulation and the GFC on the availability of finance.[11]

8.12 The committee's inquiry found that while Australia weathered the GFC, the crisis reduced the number of providers and increased the cost of finance. SMEs continued to have access to finance, albeit on less favourable terms.[12] Notably, SMEs appeared to fare better than large businesses. Lending to large businesses declined dramatically while lending to SMEs declined more modestly and recovered more swiftly.

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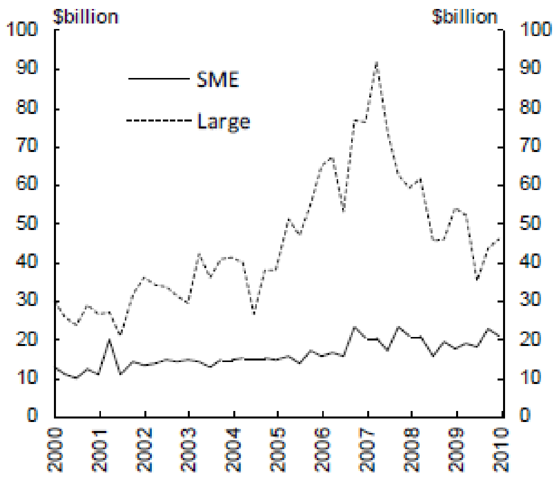
10 Dr Chris Graves, Family Business and Education and Research Group, University of Adelaide, Professor Mary Barrett, School of Management and Marketing, University of Wollongong, Dr Jill Thomas, Family Business Education and Research group, University of Adelaide, *Submission 14*, p. 5.

11 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, 'Terms of Reference', April 2011, p. vii.

12 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, April 2011, pp 15–16.

Figure 8.1: Bank lending to business[13]



Source: RBA D7 – Bank lending to business

8.13 In evidence provided to this inquiry, the RBA confirmed that growth in lending to small business has accelerated since the height of the GFC.[14]

Committee view: a word of caution

8.14 The utility of evidence from ADIs and the RBA is limited. This evidence was largely extrapolated from SME data and is based on inference and supposition. The committee further notes that it is not a broad sample of the banking and finance sector. The committee invited 18 ADIs, and other lending and insurance institutions, to contribute to the inquiry. Despite this, only two lending institutions—the CBA and the Commercial Asset Finance Brokers Association of Australia—participated in the inquiry process. Notably, no representations were made by members of the mutual banking sector. No representatives of the insurance sector participated in the inquiry.

8.15 Noting these limitations, the committee draws general conclusions about the sector's access to finance and insurance, and resilience in response to the GFC. Where possible, it compares family and non-family enterprises. In doing so, the committee seeks to identify any overlap in circumstances faced by family businesses and the SME or large business sector.

Access to finance

8.16 A theme that emerged from the committee's 2011 inquiry into access to finance for SMEs was the significant link between business lending and business

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13 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, April 2011, p. 14; Treasury, *Submission 16—Access for small and medium business to finance*, 2011, p. 5.

14 Reserve Bank of Australia, *Submission 17*, p. 1.

growth and profitability. As the committee was advised at the time of that inquiry, SMEs 'need financial support to grow and thrive'.[15] Evidence submitted as part of the committee's current inquiry indicated that the family business sector places the same emphasis on the importance of access to financial resources.

8.17 PricewaterhouseCoopers told the committee that in the international context, securing access to finance is a critical issue common to family businesses regardless of geographical location. The PricewaterhouseCoopers' 2012 survey of approximately 2000 family businesses from Africa, the Asia-Pacific, the Middle East, Europe and Canada found that 'family businesses often face difficulties accessing significant levels of new capital to fund expansion'.[16] For Australian family enterprises, accessing finance is reportedly one of the critical issues demanding the businesses' attention.[17] The link between access to finance and the health of the family business sector was family business owner, Mr Robert Pennicott: 'without bank assistance we would not have been able to expand in the way we have, for sure'.[18]

8.18 The New South Wales Business Chamber told the committee that the health of the family business sector is linked to the health of the economy and the community. It argued that any difficulties accessing finance have ramifications that extend beyond individual family businesses:

> [A]t the end of the day what we are missing out on is opportunities. This is the 30 per cent who had to forgo growth and expansion opportunities. There is a cost to jobs and there is the cost to local communities and the broader economy as a result.[19]

The experience of family enterprises compared with non-family enterprises

8.19 Views differed on whether the difficulties encountered by family business are greater than those experienced by non-family enterprises. On the one hand, the committee was advised that the difficulties encountered by family businesses do not measurably differ from non-family enterprises. Conversely, the committee was told that family businesses encounter challenges unique to the family business sector.

8.20 In support of the proposition that there is little to distinguish the financial experience of non-family enterprises from family businesses, family business owner,

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15 NAB, *Submission 19—Access for small and medium business to finance*, 2011, p. 1.

16 PricewaterhouseCoopers, *Family firm: A resilient model for the 21st century*, October 2012, p 11.

17 Professor Kosmas Smyrnios, *The MGI Australian Family and Private Business Survey*, July 2010, p. 15.

18 Mr Robert Pennicott, Managing Director, Pennicott Wilderness Journeys, *Committee Hansard*, 21 January 2013, p. 28.

19 Mr Paul Orton, Director, Policy and Advocacy, New South Wales Business Chamber, *Committee Hansard*, 15 November 2012, p. 20.

Mr Andy Kennard, reported that there is '[n]othing different due to being a family business'.[20] The Commercial Asset Finance Brokers Association of Australia reported that its members experienced similar challenges regardless of whether the entity is a family or a non-family business.[21] The Agribusiness Council of Australia observed that access to finance, and the cost of finance, 'is not significantly affected by the status of the business being a family business'. Further, the Agribusiness Council of Australia maintained that businesses status as a family enterprise 'is of little or no consequence to finance providers'.[22]

8.21 Similarly, while acknowledging slight variances, the New South Wales Business Chamber reported that barriers to finance do not significantly differ between family and nonfamily enterprises. Commenting on the results of its most recent quarterly survey of business conditions among its membership, the Chamber advised that family businesses were more likely to have had a formal loan application formally rejected. It found that in terms of loan approvals, family businesses were:

> …somewhat more likely to have been rejected: 26 per cent versus 19 per cent of businesses of their type that actually applied. Overall, though, the indication is that family businesses had about the same level of problems accessing finance as other businesses.[23]

8.22 In contrast, several submitters characterised the family business sector as unique, particularly in the area of business finance. The Australian family businesses that participated in PricewaterhouseCoopers' 2012 survey submitted that the barriers to accessing funding are greater for family businesses than for their non-family counterparts. The apparent, but unspecified, additional challenges are reportedly among the 'downsides' of operating a family enterprise.[24] Bond University also commented on the challenges that may be unique to the family business sector, noting that the desire to retain control within the family can limit available financing options and, accordingly, exacerbate the 'SME finance gap' for family businesses.[25]

8.23 Submitters also commented on the effect of governance structures on the sector's capacity to access finance. Several family business owners advised that the more sophisticated and experienced a family business is, the easier it is to acquire finance. Councillor Steven Kons, Mayor of the Burnie City Council, speculated that the more informal, community-based management style of family businesses can hinder businesses from accessing finance:

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20 Mr Andy Kennard, *Submission 5*, p. 2.

21 Commercial Asset Finance Brokers Association of Australia, *Supplementary Submission*, p. 1.

22 Agribusiness Council of Australia, *Submission 37*, p. 8.

23 Mr Tim Hicks, Policy Adviser, Business, Regulation and Economics, New South Wales Business Chamber, *Committee Hansard*, 15 November 2012, p. 17.

24 PricewaterhouseCoopers, *Submission 11*, Attachment A, p. 17.

25 Bond University, *Submission 3*, pp 8–9.

> It is probably easier for non-family businesses. The level of sophistication and capacity to prepare documentation is much easier for non-family businesses, because when you are on top of it, and you are having a look at your daily cash flows and those sorts of things, you tend to gloss over the detail that other entities—whether it is banks or financiers, you know it inside out; if you are a small company that reports to someone else you have those at hand and you are distanced from it. I know exactly how much money I have in the bank, how much is coming in and all those sorts of things. So in relation to the expectations of banks and other agencies that may be interested in my business: I know them, so I gloss over them when it is necessary to provide them. That is probably an impediment because of the hands-on way we run our businesses.[26]

8.24 It was implied that family dynamics and future planning are relevant to the sector's capacity to access finance. Mr Albert Beard, Chairman and Managing Director, A. H. Beard Manufacturing, argued that the education and experience of family members is a criteria considered when seeking finance:

> Because our business relies very much on cash flow lending, the quality of people at the business is very high on the agenda, without involving bricks and mortar. So yes the qualifications are very important to what I know about the ANZ bank. They are probably already ticking those boxes themselves.[27]

8.25 Similarly, Mr Mark Cleary, a business adviser to the Gosford-based family firm, Sharpe Bros, spoke of the relevance of governance structures and succession plans to family businesses' capacity to access finance.[28]

Funding sources

8.26 It was further submitted that the funding preferences of family businesses distinguish the sector from non-family enterprises. SMEs can access a combination of debt and equity finance, which can include internal funding, owner equity, venture capital, secured and unsecured intermediated credit, and bank bills. Overall, however, SMEs primarily rely on debt funding from ADIs followed by internal resources.[29]

8.27 In contrast, anecdotal evidence before the committee indicated that the funding priorities of family businesses differ from that of the SME sector more

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26 Councillor Steven Kons, Mayor, Burnie City Council, *Committee Hansard*, 21 January 2013, p. 3.

27 Mr Albert Beard, Chairman and Managing Director, A. H. Beard Manufacturing, *Committee Hansard*, 15 November 2012, p. 52.

28 Mr Mark Cleary, Business Adviser, Sharpe Bros, *Committee Hansard*, 15 November 2012, pp 52–53.

29 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, April 2011, pp 6–7.

broadly. It was apparent that family businesses access a mixture of debt finance, equity and reinvestment of business profits.[30] From the available anecdotal evidence, a funding hierarchy emerges with own-source funding by way of family loans or reinvestment of profits being the preferred source of finance.[31] As KPMG advised, bank debt is incurred only after own-source funding options have been exhausted.[32] As explored below, private equity was reportedly the least favoured finance option.[33]

8.28 This hierarchy, it was suggested, reflects the conservative mindset of family businesses.[34] Chapter 4 identified the conservative, 'patient capital' approach to business finance as a key point of difference between family businesses from non-family enterprises. As Institute of Chartered Accountants Australia (ICA) reported:

> [r]esearch and anecdotal information indicates that family businesses tend to be more risk averse and desire to retain greater control over their business affairs than non–family businesses. This is reflected in their appetites for credit, with greater use of bank finance and lower use of external sources of equity finance.[35]

8.29 Bond University agreed with this view, advising that the reliance on own source funding is particularly pronounced for smaller family businesses:

> [S]mall family businesses in particular tend to rely heavily on family loans, rather than loans to outsiders as a source of finance. Consistent with their noneconomic objectives, these preferences protect the family's influence over the firm's operations…family firms will utilise more internal rather than external sources of finance.[36]

8.30 On the basis of available research, Bond University concluded that while SMEs can rely on own-source finance, there is a greater reliance on internal equity among family businesses.[37]

Concerns with access to ADI debt finance

8.31 Family businesses and their representatives reported four concerns with debt financing from ADIs. The first of these is the lack of competition between lenders.

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30 See, for example, KPMG, *Submission 21*, p. 19; Kosmas Smyrnios, and Lucio Dana, *MGI New Zealand Family and Private Business Survey 2007*, 2007, p. 16.

31 Professor Kenneth Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 24.

32 KPMG, *Submission 21*, p. 19.

33 See, for example, Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

34 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

35 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

36 Bond University, *Submission 3*, p. 10.

37 Bond University, *Submission 3*, p. 11.

The committee was advised that the majority of family businesses borrow from 'the Big 4' as opposed to smaller lenders or the mutual sector.[38] Pitcher Partners argued that there is a lack of banking competition within the Australian market, which presents challenges for family businesses:

> With access to debt funding, there is a current lack of competition in the banking sector that acts as an impediment to family businesses. The loss of St George into Westpac and Bank West into CBA during the immediate aftermath of the GFC removed two emerging and competitive financial institutions from the market place. This void is slowly being filled again but it will take many years for rising institutions to reach sufficient critical mass to be truly competitive and have the breadth of finance options available.[39]

8.32 Pitcher Partners further submitted that the absence of competition undermines family businesses' capacity to negotiate favourable finance terms:

> Examples have also been noted of what could be described as a brinkmanship approach by financiers to re–negotiation of facilities at a time when alternative options are few. The lack of competition therefore has a real cost to family business and influences its competitiveness.[40]

8.33 MGI Australasia also argued that there is currently a lack of choice and product diversity in the Australian ADI market:

> The Australian banking market is dominated by the Big 4…Whilst the existence of four players should in theory lead to substantial competition the reality is that it does not and the offerings of these 4 banks are constantly very similar and rarely substantially different…The other smaller banks have been regularly acquired by the Big 4 over the last decade so that the remaining smaller banks are ill placed to provide meaningful competition across the full range of products.[41]

8.34 MGI Australasia also submitted that the absence of meaningful competition increases operating costs for family businesses:

> By world standards Australian banks are extremely profitable. Large public listed corporations and multi–national companies are the only enterprises in the Australian economy that can extract competitive deals in our banking market. The result of this lack of real competition is that family businesses are incurring substantially higher funding costs than their competitors in other world markets.[42]

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38 MGI Australasia, *Submission 9*, p. 8.

39 Pitcher Partners, *Submission 28*, p. 12.

40 Pitcher Partners, *Submission 28*, p. 13.

41 MGI Australasia, *Submission 9*, p. 8.

42 MGI Australasia, *Submission 9*, p. 8.

8.35 Second, it was submitted that the terms and conditions of ADI finance are inappropriate for family businesses. Several submitters noted that family businesses may be required to blur the boundaries between personal and business assets in order to secure business finance. Commenting on her experience as a family business owner, Mrs Janice Taylor of Taylor Bros. Holdings Pty Ltd, informed the committee that:

> [t]o enable finance to be put in place it is usually an expectation of the financial provider that the business shareholders/directors/family members will provide asset backing whether it be business premises, private property, private share holdings, or any other privately held assets.[43]

8.36 Mr Michael Claydon, the Managing Director of the Perth-based firm National Corporate Training Pty Ltd, recounted a similar experience:

> We are in the growing phase and we find it extremely difficult to get finance from banks. You basically need to have it to get it—that is the thinking behind banks. I do not know whether there is any particular issue with family business versus a standard business, but certainly the basic rule is that if you do not have it you cannot get it. The only way to get finance is to put your home up as part of the collateral.[44]

8.37 Family business advisers also commented on this practice. Pitcher Partners noted that accessing even a 'modest amount' of capital will 'frequently…involve pledging private assets such as a family home as security'.[45] A 2009 KPMG survey of family businesses observed that finance options can merge a family's private life with the family's business ventures. It found that 41 per cent of directors in a family business had given personal guarantees to obtain debt funding. In contrast, only approximately 25 per cent of non-family businesses surveyed reported giving personal undertakings in order to secure business finance.[46]

8.38 Family business advisers told the committee that the security requirements indicate that the ADI sector that does not appropriately support family businesses. The ICA submitted that it is the value of security, rather than the success or the viability of the business, that determines a family business' capacity to access capital.[47] Deloitte Private argued that the requirement to provide security limits the growth of the family business and hinders family businesses from reaching their economic potential:

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43 Taylor Bros, *Submission 38*, p. 3.

44 Mr Michael Claydon, Managing Director, National Corporate Training Pty Ltd, *Committee Hansard*, 2 February 2012, p. 21.

45 Pitcher Partners, *Submission 28*, p. 12.

46 KPMG and Family Business Australia, *KPMG and Family Business Australia Survey of Family Businesses 2009*, p. 17, http://peak.fambiz.org.au/education/resources/australian-family-business-surveys-statistics (accessed 23 October 2012).

47 Institute of Chartered Accountants Australia, *Submission 25*, p. 5.

> As shown in the CPA survey, the commonly cited difficulty in accessing bank funding related to the willingness of the financiers to provide the funding. Other factors include the reluctance of financiers to provide cashflow based loans to small and medium sized enterprises, which includes many family businesses. Consequently, a family business' ability to fund its growth potential is often constrained by the security available to be offered. Many family businesses are reluctant to provide security and therefore face a funding squeeze when seeking to financing their growth potential.[48]

8.39 Ultimately, it was questioned whether ADIs are willing to engage with the family business sector. As the Institute of Certified Bookkeepers stated:

> It also appears in the current banking environment family business is not supported by the lenders. Without family providing security (the house, or other property, personal guarantee), a family business cannot generate the finance. It would appear that the lenders do not in fact a wish to lend to a family business but will lend to the family if there is sufficient security and other income to service the debt.[49]

8.40 The accountancy firm, FINH, argued that the reticence of the ADI sector to engage with family businesses requires family businesses to merge private and business assets, thereby increasing their reliance on family funds and internal revenue.[50]

8.41 Third, it was argued that the risk ratings attached to family business finance applications are inappropriate. Deloitte Private noted that in response to the GFC, the level of funding had decreased while the cost of funding has increased.[51] While acknowledging the higher costs of long-term wholesale funding, Deloitte stated that the business lending rate has remained relatively unchanged from July 2006 to September 2012.[52] The New South Wales Business Chamber reported that it is a widely held view among family and non-family businesses that in response to the GFC, lending conditions have become 'too strict'.[53]

8.42 The ICA also disputed the SME loan rates, noting that the RBA interest rate cuts have not been passed on in full.[54] It noted that debt finance has been difficult to access for many businesses, with banks in the current economic environment

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48 Deloitte Private, *Submission 16*, p. 28.

49 Institute of Certified Bookkeepers, *Submission 36*, p. 4.

50 FINH, *Submission 34*, p. 1.

51 Deloitte Private, *Submission 16*, p. 26.

52 Deloitte Private, *Submission 16*, p. 26.

53 Mr Paul Orton, Director, Policy and Advocacy, New South Wales Business Chamber, *Committee Hansard*, 15 November 2012, p. 17.

54 Institute of Chartered Accountants Australia, *Submission 25*, p. 6.

tightening eligibility requirements.[55] Pitcher Partners also questioned whether ADI finance appropriately takes account of family businesses' financial acumen or potential:

> [D]uring the aftermath of the GFC, many family businesses were, and are still, striking maximum lending limits that capped a bank's exposure to any one customer. These limits were often arbitrary and did not reflect the size of the business or its prospects.[56]

8.43 The committee did not receive an indication from ADIs that the finance applications of family businesses are considered separately to the finance applications of non-family enterprises. As the Agribusiness Council of Australia told the committee:

> There is a high level of indebtedness. I do not want to go into banking 101, but banks fundamentally risk rate all industries. They risk rate them based on their perceived loss. That perceived loss is not necessarily an actual loss, but they rate them and charge interest rates based on whatever the risk rating is for those particular clients. So there is the perception and there is the reality. The reality is that agriculture is not as high a risk as the banks have perceived it to be. I think the GFC has had a part to play in this in terms of banks being, not reluctant to lend, but looking more closely at their lending policies with regard to which industries they lend to and how they lend. If you had family businesses as a separate class…the banks would develop their own risk strategy around the family business category and therefore they would risk rate it accordingly.[57]

8.44 Packer Leather provided a personal account of the risk categories applied by ADIs, reporting that ADIs are very risk-averse:

> Our Australian Banks are extremely adverse to any form of risk! The risk analysis of our business – an exporter and manufacturer certainly does not give them a lot of confidence in our industry…The finance models that they use for risk assessment seemingly make no or little allowance for the personal factor – who they are supporting.[58]

8.45 However, these concerns were not shared by all family businesses that contributed to the inquiry. Mr Robert Pennicott, Managing Director, Pennicott Wilderness Journeys, described the family business sector as being in partnership with ADI sector:

> I have a bit of a philosophy with banks that we need each other…We do borrow a lot of money from one bank. We are very fortunate that we have

55 Institute of Chartered Accountants Australia, *Submission 25*, p. 6.

56 Pitcher Partners, *Submission 28*, p. 13.

57 Mr Ian Joseph, Executive Chair, Agribusiness Council of Australia Ltd, *Committee Hansard*, 7 February 2013, p. 15.

58 Packer Leather, *Submission 4*, p. 5.

> had a very good relationship with our bank and they bend over backwards to help us…personally, I think our bank has been very fair and reasonable. Obviously we can complain about fees, interest rates and everything that goes with it, but without bank assistance we would not have been able to expand in the way we have, for sure.[59]

8.46 It was further contended that the introduction of the Basel III prudential regulations would increase the cost of business finance. Developed in response to the GFC, Basel III aims to improve the banking sector's ability to absorb market shocks arising from financial and economic stress, whatever the source, improve risk management in governance and strengthen banks' transparency and disclosures.[60] As the Australian Prudential Regulation Authority (APRA) has stated, the global liquidity reforms are intended to remedy weaknesses in the international financial framework that existed at the time of the GFC:

> The Basel III capital framework was introduced by the Basel Committee on Banking Supervision in December 2010 to raise the quality and consistency of the capital base and harmonise other elements of capital. In addition, Basel III improves the risk coverage of the Basel II Framework by strengthening the capital requirements for counterparty credit risk exposures arising from banks' derivatives, repurchase and securities financing activities.[61]

8.47 However, Deloitte Private noted that measures that are intended to promote economic stability may adversely affect the financial stability of family enterprises. Citing the opinion of the NAB Chief Financial Officer, Mr Mark Joiner, Deloitte Private, advised that the impact of the Basel III capital requirements will reduce the available finance for SMEs and, accordingly, increase finance costs.[62]

8.48 The concerns raised are not unique to the family business sector. Similar concerns were raised by SME representatives during the committee's 2011 inquiry into access for small and medium business to finance. SME representatives also disputed whether the interest rates attached to SME loans actually reflect the cost of, and risks associated with, providing SME finance.[63]

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59 Mr Robert Pennicott, Managing Director, Pennicott Wilderness Journeys, *Committee Hansard*, 21 January 2013, p. 28.

60 Bank for International Settlements, 'International regulatory framework for banks (Basel III)', http://www.bis.org/bcbs/basel3.htm (accessed 21 February 2013).

61 Australian Prudential Regulation Authority, 'APRA releases final package to implement Basel III capital reforms', Media release, 13 November 2012.

62 Deloitte Private, *Submission 16*, p. 26.

63 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, April 2011, pp 24–33.

Family finance and private equity finance

8.49 The committee was informed that private equity is an underutilised financial resource for the family business sector. It was reported that family businesses are reluctant to engage with the private equity sector. According to the Council of Financial Regulators, 'private equity' encompasses two forms of investment. Firstly, private equity refers to 'venture capital'—the investment of equity funding in small and relatively high risk companies with strong growth potential. Secondly, private equity can include 'the acquisition of a public company by a group of investors who take the company ‘private’, delisting it from the stock exchange'.[64]

8.50 According to PricewaterhouseCoopers, private equity 'is a term for pools of capital, managed by professional fund management teams, specifically to invest in unlisted companies'.[65] As outlined by PricewaterhouseCoopers, in exchange for providing capital private equity firms:

- obtain a share in the company;
- typically establish closely monitored performance targets; and
- generally retain their share for three to five years. At the end of the investment period, the private equity fund will sell its share of the company to 'a suitable acquirer'.[66]

8.51 MGI's 2006 Australian Family and Private Sector Survey found that external equity is the 'least favoured' finance option for family businesses.[67] This reluctance was linked to the conservative, family-orientated nature of family businesses.[68] The committee was advised that family businesses' desire to retain control of the business acts as a significant deterrent to obtaining private equity finance. Bond University reported that numerous research projects 'have found that the financial development of family firms with regard to equity is governed by a "keep it in the family" tradition'. Bond University further advised that 'these characteristics suggest that family SMEs tend to have a more limited external equity financing base, but a wider base of internally generated equity'.[69]

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64 Reserve Bank of Australia, 'Private equity in Australia', *Financial Stability Review 2007*, March 2007, p. 59.

65 PricewaterhouseCoopers, *Private clients private business barometer—Private equity supplement – Winter 2012*, 2012, p. 4.

66 PricewaterhouseCoopers, *Private clients private business barometer—Private equity supplement – Winter 2012*, 2012, p. 16.

67 MGI Australasia, *Submission 9*, p. 8.

68 MGI Australasia, *Submission 9*, p. 8.

69 Bond University, *Submission 3*, p. 12.

8.52 Professor Ken Moores characterised the short-term focus of private equity investments as 'an anathema to the value system of a family firm'.[70] Similarly, Deloitte Private commented that the objectives of family firms are not easily reconcilable with the investment strategies underlying private equity finance. The committee was advised that the short-term, high risk outlook of private equity investment is inconsistent with the 'patient capital' approach preferred by family businesses:

> An additional hurdle to raising private equity funds for family businesses is the mechanism by which private equity investors realise their return on their investment. Private equity firms generally strive to achieve cash on cash returns of three times their investment in three to five years. Such an investment horizon and growth imperative (often coupled with a more aggressive debt appetite) is often not aligned with the goals and objectives of the family members.[71]

8.53 It was also noted that private equity investors may be reluctant to engage with family businesses. Separate to this inquiry, PricewaterhouseCoopers has noted that the 'majority of deals [by private equity firms] involve small and medium-size enterprises'. However, it defined SMEs as firms valued between $10 million and $100 million.[72] Deloitte Private told the committee that family enterprises seeking capital to fund expansion may not meet the investment criteria applied by private equity firms:

> Australian private equity firms, which could be valuable sources of equity capital for family businesses, are generally focused on larger and more mature businesses to maximise their return on investment in the current economic environment. The majority of private equity firms look for opportunities to write equity cheques starting at $10m - $20m which, combined with the leverage associated with such transactions makes the overall capital investment too large for many family businesses.[73]

8.54 It was unclear whether the family business sector's engagement with private equity differs from that of non-family businesses and SMEs more broadly. The committee was advised that 2012 research by PricewaterhouseCoopers found that there is a widespread misconception about what private equity is and the role it can play for owners considering investments and/or succession'.[74]

8.55 Nevertheless, some submitters advocated greater use of private equity by family firms. Associate Professor Pi-Shen Seet advised that private equity is

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70 Professor Ken Moores, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 24.

71 Deloitte Private, *Submission 16*, p. 29.

72 PricewaterhouseCoopers, *Private clients private business barometer – Private equity supplement – Winter 2012*, 2012, p. 16.

73 Deloitte Private, *Submission 16*, p. 28,

74 Associate Professor Pi-Shen Seet, *Submission 35*, p. 1.

increasingly a feature of ownership transfers of family firms in Europe and North America.[75] It was recommended that the government promote the use of private equity firms through providing information to educate family businesses on private equity options.[76]

8.56 FINH argued that the risks associated with private equity investment would be mitigated if the investor were 'another business-owning family'.[77] Professor Ken Moores put a similar proposal, referring to the benefits of a 'family office' or investment by family firms in other family enterprises:

> In the United States, for example, there is the firm of Francois de Visscher who is a Belgian by origin from a fifth generation business but operates out of Boston. He has partnered up with a Pitcairn trust and they have bought together 400 family offices and have this pool of family money. They are looking to invest in other family businesses specifically. So it is the mobilisation of that patient capital from a supply side that is looking for the demand side.[78]

8.57 To promote greater access to the private equity market, FINH recommended that:

> Government specifically look at the present incentivisation of the private equity markets and identify performance-enhancing policy measures that incorporate a greater level of knowledge of the capital needs of successful multigenerational business owning families.[79]

Access to finance: Committee view

8.58 The committee acknowledges the concerns raised with the cost of finance and the security requirements attached to business loans. On the basis of the evidence presented, family and non-family businesses can encounter similar barriers to accessing finance. The two sectors share similar concerns with the activities of ADIs and the application of prudential regulations.

8.59 However, despite the similarities, there are two points of difference. First, there appears to be greater significance attached to own-source funding. This reliance appears to be indicative of a sector that emphasises the 'family'-based nature of its economic activities. The committee notes submitters' suggestions for government to promote the private equity market. However, the committee recognises the challenges that the private equity market presents for family businesses wanting to retain control

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75 Associate Professor Pi-Shen Seet, *Submission 35,* pp 1–2.

76 Associate Professor Pi-Shen Seet, *Submission 35,* p. 5.

77 FINH*, Submission 34*, p. 2.

78 Professor Ken Moores, Moores Family Enterprise, *Committee Hansard*, 16 November 2012, p. 24.

79 FINH, *Submission 34*, p. 2.

of the business within the family, and for smaller non-family businesses. Additional information about the operation of private equity sector may assist family businesses, and the sector more broadly, to determine whether it is appropriate to seek private equity finance. This matter could be usefully considered by the Australian Securities and Investments Commission.

Recommendation 20

8.60 The committee recommends that the Australian Securities and Investments Commission review information available on the MoneySmart website about private equity investments, and design information that would assist family and non-family businesses to determine whether it is appropriate for their business to seek private equity finance.

8.61 Second, it is evident that ADIs do not consider family businesses separately from non-family enterprises when determining the risk attached to a family business' finance application. The committee considers that the integrity of the risk assessment models used by ADIs is compromised where ADIs do not accurately understand the business structures of applicants. It is of particular concern that submitters believe that ADIs do not understand the circumstances, business strategies and outlook of family businesses.

8.62 The committee extends its thanks to the CBA, CAFBA and the RBA for their contribution to the inquiry. However, the overall lack of engagement with this inquiry by the ADI sector is surprising and raises legitimate questions about the sector's understanding of family owned and operated enterprises. To ensure the efficacy of risk assessments, the committee encourages ADIs to analyse the characteristics of family businesses, as distinct from broader categories of micro, small, medium, or large businesses.

8.63 Given the apparent prevalence of family businesses in Australia's business sector, and, by extension, Australia's economy, the RBA's apparent lack of direct engagement with the family business sector must be addressed. The committee recommends that the RBA include on its annual small business panel in each state and territory representatives of the family business sector.

Recommendation 21

8.64 The committee recommends that the Reserve Bank of Australia include representatives of the family business sector on its annual small business panels as an interim measure.

8.65 The committee reiterates its 2011 recommendation that the RBA track the impact of the introduction of Basel III on the cost of small and medium business finance and residential mortgages.[80] Any improper increase in costs should be immediately addressed.

8.66 As discussed in chapter 4, should the proposed Inter-Departmental Committee (IDC) decide to gather data about the key characteristics and behaviours of family businesses, these characteristics should include the debt-to-equity ratios and the value of assets on the balance sheets of family businesses compared with non-family enterprises. As part of the IDC process, consideration should be given to gathering data on family businesses and data on non-family enterprises in the Business Finance component of the ABS Australian Business Characteristics Survey (see paragraph 4.69).

Access to insurance

8.67 The issue of family businesses' access to insurance received little attention from family businesses and family business representatives during this inquiry. Broadly, family businesses can access a range of insurance products including public liability[81] and workers compensation insurance.[82] Two points were raised regarding the sector's access to insurance.

8.68 First, Pitcher Partners and the Council of Small Business of Australia questioned whether family businesses have all the necessary and appropriate insurance cover.[83] Second, there were concerns raised with the cost of insurance. Mr David Shave of David Shave Investments Pty Ltd, reported that the cost of insurance could prohibit business expansion, advising that his business had not pursued an opportunity due to the costs associated with obtaining the required insurance.[84] Mr Robert Pennicott of Pennicott Wilderness Journeys stated that insurance and associated compliance costs are an important but costly component of running a business.[85] Pitcher Partners submitted that insurance costs may be fuelled by a lack of competition among insurance providers.[86] Family Business Australia also commented

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80 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, Recommendation 2, April 2011, p. 38.

81 Institute of Certified Bookkeepers, *Submission 36*, Attachment A, p. 13.

82 Pitcher Partners, *Submission 28*, p. 13.

83 Pitcher Partners, *Submission 28*, p. 13;
Mr Peter Strong, Executive Director, Council of Small Business Australia, *Committee Hansard*, 13 November 2012, p. 26.

84 Mr David Shave, Principal, David Shave Investments Pty Ltd, *Committee Hansard*, 14 November 2012, p. 41.

85 Mr Pennicott, Pennicott Wilderness Journeys, *Committee Hansard*, 21 January 2013, p. 29.

86 Pitcher Partners, *Submission 28*, p. 13.

on the cost of insurance, but held that insurance costs could be reduced through businesses adopting more professional governance practices.[87]

8.69 However, it was widely held that family businesses can encounter the same challenges accessing insurance as non-family businesses. The Agribusiness Council of Australia argued that a business' status as a family enterprise is of little consequence to an insurance company in assessing or costing an insurance application.[88] Two family businesses also commented on whether the challenges they face differ from their non-family counterparts. There was consensus that their business' status as a family business does not affect their ability to access insurance.[89] This advice is consistent with research into the small business sector, with information provided by CCIQ indicating that the cost of insurance is a concern for both family and non-family small businesses.[90]

The family business sector's response to the global financial crisis

8.70 Neither the anecdotal nor the empirical evidence before the committee conclusively demonstrates that the family business sector outperformed non-family enterprises in response to the GFC. Nor was it established that the family business sector proved unusually resilient in response to the economic crisis. The evidence did, however, point to attributes of family enterprises that could assist businesses to respond to economic challenges.

Anecdotal views

8.71 Two markedly different pictures of the family business sector emerge from the anecdotal evidence.

A resilient family business sector

8.72 The first is a sector capable of meeting the challenges of the financial crisis. Family Business Australia reported that family businesses fared better on average than their non-family counterparts. Indeed, it argued that the characteristics that distinguish family businesses from nonfamily enterprises 'meant family businesses were bound to survive the GFC better'.[91] In particular, Family Business Australia highlighted the sector's conservative business mindset and capacity to quickly determine business

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87 Family Business Australia, *Submission 1*, p. 8.

88 Agribusiness Council of Australia, *Submission 37*, p. 8.

89 Mr Pennicott, Pennicott Wilderness Journeys, *Committee Hansard*, 21 January 2013, p. 29; Kennards Hire, *Submission 5,* p. 2.

90 CCIQ, *Submission 19*, Attachment A, p. 8.

91 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 35.

strategies in response to changing circumstances.[92] This view was shared by Mr Christopher Lowe, Chief Executive Officer of Bus Association Victoria, who reported that the experience of non-family businesses differed from that of family enterprises:

> I have had many a conversation with CFOs and, indeed, CEOs of global public transport operations who are feeling the pinch, who have not had a happy time through the GFC, which is in direct contrast to the feedback that I am getting back from my family business members, who are all about continuance and sustainability.[93]

8.73 Consistent with the advice of Family Business Australia, the Bus Association Victoria attributed the apparent resilience of the sector to its unique mindset:

> They have got…a resilience factor there where they are able to weather storms like GFCs. I think it comes down to their propensity to innovate and the fact that the success of the business is very much dependent upon the name of the family. All the family and those who share those family values get involved to ensure that that business is self-sustaining and self-perpetuating.[94]

8.74 Mr Des Caulfield of MGI Australasia concurred. He reported that approximately 40–45 per cent of family businesses felt supported by ADIs during the financial crisis. The committee was advised that this statistic is testament to the sector's performance:

> The fact 45 per cent of them could say that their bank has supported them is a very good indication to me that their banks actually felt they were pretty safe. I do not think the general business community would have answered in that manner.[95]

8.75 Mr Caulfield attributed the sector's resilience to its conservative business strategies and streamlined governance arrangements, which provided the flexibility to quickly respond to changing financial conditions:

> [T]hey are much more cautious than many and were therefore better placed financially to handle the downturns in turnover et cetera that occurred. Also, by their nature, they are not over-governed they make decisions relatively quickly. A lot of them—mum and dad having lunch together or

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92 Mrs Philippa Taylor, Chief Executive Officer, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 35.

93 Mr Christopher Lowe, Chief Executive Officer, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 12.

94 Mr Lowe, Bus Association of Victoria, *Committee Hansard*, 14 November 2012, p. 12.

95 Mr Des Caulfield, Director, MGI Australasia, *Committee Hansard*, 14 November 2012, p. 25.

> the kids having lunch with them—say, 'We've got to fix this,' and they can make decisions much more quickly.[96]

8.76 Family business owners also spoke of the sector's resilience. Mrs Diane Tompson, Managing Director of Powercom Group Pty Ltd, agreed that the family business sector can readily adapt to change:

> Our accountant sums it up when he says that you have to hold your nerve in times of stress and trouble. I think that family businesses are very responsive. We are quick to respond. In fact, one of our market advantages is that we are able to build things for customers, if they want one plug or two. We can change our designs quite easily instead of only being able to produce the one product. It is no different in a so-called global financial crisis. We have not lost anybody at all. We have just had to work a bit harder. Our sales people are pretty much on board with that. They are constantly on the road trying to sell a product.[97]

8.77 Personal stories collected by Family Business Australia also linked the values and culture of family businesses to the sector's apparent capacity to withstand the GFC. Family businesses reported that 'familiness' was central to the business' success.[98] Firms reported high incidences of customer loyalty,[99] with one firm commenting that:

> times are still tough. "But we're well positioned so that when times are better, as someone who continued to support the industry through the tough times, we will be rewarded accordingly".[100]

8.78 Interestingly, not all family businesses shared the view that family involvement safeguarded the business against the GFC. Mr Alan Berechree, the owner of a Burnie Newsagency, reported that the business 'really had not had much of a downturn' in response to the GFC. However, the continued profitability of the business was attributed to the nature of the industry rather than any family-based characteristics.[101]

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96 Mr Caulfield, MGI Australasia, *Committee Hansard*, 14 November 2012, p. 24.

97 Mrs Diane Tompson, Managing Director, Powercom Group Pty Ltd, and Family Business Australia, *Committee Hansard*, 21 January 2013, p. 38.

98 Technigro, as cited in Family Business Australia, *Soul stories*, Free Run Press Pty Ltd, Kent Town, 2012, p. 188.

99 Vellex, as cited in Family Business Australia, *Soul stories,* p. 206; Tobin Brothers, as cited in Family Business Australia, *Soul stories*, p. 194.

100 WSL – Wine Storage and Logistics, as cited in Family Business Australia, *Soul stories*, p. 216.

101 Mr Alan Berechree, Owner, Burnie Newsagency, *Committee Hansard*, 21 January 2013, p. 20.

A contrary view: the family business sector's shared experience

8.79 In contrast to the view of the sector as resilient, there is also evidence that the sector was adversely affected by the GFC. The CCIQ acknowledged that the family business sector was 'not immune' from the effects of the global financial crisis.[102] The Institute of Chartered Accountants wrote in its submission that 'the post GFC environment has presented challenges for family businesses as it has for many other forms of business in the economy'.[103] Somewhat pessimistically, Pitcher Partners reported:

> [l]ike all business cycles that have preceded it, the GFC and post-GFC has, and will continue to, claim victims among family businesses in Australia. Family businesses accept the risks of failure at this time but that knowledge does not ease the pain, suffering and personal anguish that is experienced when it actually happens. Business failure will often cause a breakdown of the family unit leading to divorce, extreme financial hardship, and division of families.[104]

8.80 Family businesses also commented that the GFC adversely affected business profitability. The multi-generational Queensland firm, Packer Leather, noted that the global economic downturn had a measurable impact on family businesses operating in international markets.[105] Mr Raymond Hind, Chief Executive Officer of the Western Australian firm Hind's Transport Services, told the committee:

> [t]he difficulty now, after the GFC, is obtaining finance. So we are finding that we are putting a lot of our own money back into the business for it to survive because of the inability to raise finance.[106]

8.81 However, the demarcation between the experience of family and non-family businesses is again not clear. The anecdotal evidence focused on the family business sector as a subset of the SME sector. For example, the Institute of Certified Bookkeepers reported that 'SMEs are doing it tough'.[107] BusinessSA also grouped family businesses with SMEs, advising that the 'GFC hurt consumer and business confidence, affecting many businesses including family businesses'.[108]

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102 CCIQ, *Submission 19*, p. 2.

103 Institute of Chartered Accountants Australia, *Submission 25*, p. 6.

104 Pitcher Partners, *Submission 28*, p. 15.

105 Packer Leather, *Submission 4*, p. 6.

106 Mr Raymond Hind, Chief Executive Officer, Hind's Transport Services, *Committee Hansard*, 7 February 2013, p. 23.

107 Institute of Certified Bookkeepers, *Submission 36*, p. 4.

108 BusinessSA, *Submission 23*, p. 2.

Empirical evidence - conflicting data

8.82 The challenge of identifying the family business sector's response to the GFC is complicated not only by the heavy reliance on often conflicting anecdotal evidence, but also by inconsistent empirical data.

Statistics that support the view that the family business sector was uniquely placed to respond well to the global financial crisis

8.83 Several witnesses drew attention to the 2009 KPMG survey as evidence that the family business sector successfully weathered the GFC.[109] The 2009 KPMG survey of approximately 457 entities self-identifying as family businesses found that while over half expected negative or low growth in the coming 12 months, over 90 per cent reported being well-prepared or moderately well prepared to face changes over the coming year. Accordingly, KPMG concluded that '[m]any family businesses appear to have shrugged off credit and finance constraints' resulting from the GFC.[110] Reporting in 2011, KPMG subsequently noted that '56 per cent of survey respondents agreed that being a family businesses helped them deal with the post-GFC economic downturn while only 10 per cent actually disagreed with this proposition (the remainder were unsure)'.[111]

8.84 Moores Family Enterprise cited the KPMG survey's results as evidence that 'many family businesses appear to have shrugged off credit and finance constraints'.[112] The findings also attracted media attention, with the *Herald Sun* reporting in 2009 that '[m]ost family businesses felt little or no effect from the tougher credit conditions during the economic slowdown, KPMG research has found'.[113]

Contrary data

8.85 However, as Dr Chris Graves, Professor Mary Barrett and Dr Jill Thomas noted, findings about the resilience of the family business sector are 'difficult to

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109 Moores Family Enterprise, *Submission 8*, p. 6. Dr Chris Graves, Family Business and Education and Research Group, University of Adelaide, Professor Mary Barrett, School of Management and Marketing, University of Wollongong, Dr Jill Thomas, Family Business Education and Research group, University of Adelaide, *Submission 14*, p. 5.

110 KPMG and Family Business Australia, *KPMG and Family Business Australia Survey of Family Businesses 2009*, 2009, p. 5.

111 KPMG and Family Business Australia, *Stewards: Moving Forward, Moving Onward – KPMG and Family Business Australia's Family Business Survey 2011*, 2011, p. 8.

112 Moores Family Enterprise, *Submission 8*, p. 6.

113 Rachel Hewitt, 'Family businesses weather the financial crisis', *Herald Sun*, 12 October 2009, http://www.news.com.au/business/worklife/family-businesses-weather-the-financial-crisis/story-fn3p68a7-1225785663194 (accessed 26 February 2013).

empirically verify'.[114] Deloitte Private observed 'there is very little data to make an informed response to this term of reference'.[115] Both submitters called for additional research to determine the sector's response to the GFC and whether there are broader lessons for Australia's business sector.[116]

8.86 Additionally, findings vary across data sources. The optimistic findings of KPMG can be compared with the results of MGI Australasia's 2010 Australian Family and Private Business Survey. The survey found that the GFC adversely affected 35.7 per cent of family businesses, leading to unspecified 'cost cutting' activities by slightly over 50 per cent, delays in hiring staff by 34.5 per cent, and postponing expansion plans by 26.9 per cent of the businesses surveyed.[117] Securing adequate capital for growth and retirement was among the top four concerns reported.[118] On the basis of this data, it was concluded that the concerns of family business owners about the future of their businesses has generally risen since 2006, with the family business sector's confidence declining as a result of the GFC.[119] According to MGI Australasia, the GFC weakened the sector's performance and confidence:

> Today, as Australia disentangles itself from the grip of the Global Financial Crisis (GFC), the current survey shows that family businesses have changed from pre-GFC days. Despite Australia having weathered the GFC better than most countries, the concerns of family business owners about the future of their businesses has generally risen since 2006, the date of the previous survey. More business owners are significantly more concerned about competition, funding for growth and for the future of their particular industry than they were in 2006 and 2003.
>
> The survey reveals a less confident family business sector post-GFC than pre-GFC – with family business owners more reliant on the continuity of

114 Dr Chris Graves, Family Business and Education and Research Group, University of Adelaide, Professor Mary Barrett, School of Management and Marketing, University of Wollongong, Dr Jill Thomas, Family Business Education and Research group, University of Adelaide, *Submission 14*, p. 5.

115 Deloitte Private, *Submission 16*, p. 30.

116 Deloitte Private, *Submission 16*, p 30; Dr Chris Graves, Family Business and Education and Research Group, University of Adelaide, Professor Mary Barrett, School of Management and Marketing, University of Wollongong, Dr Jill Thomas, Family Business Education and Research group, University of Adelaide, *Submission 14*, p. 5.

117 Kosmas Smyrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2010*, July 2010, p. 15.

118 Kosmas Smyrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2010*, July 2010, p. 15.

119 Kosmas Smyrnios and Lucio Dana, *The MGI Family and Private Business Survey: 2010*, July 2010, p. 4.

> their business to fund their retirement and more concerned over the future of their business.[120]

8.87 The committee did not receive evidence on this point from ADIs or the RBA. However, some empirical information is available from international sources. As the committee reported in April 2011,[121] the Organisation for Economic Co-Operation and Development (OECD) concluded that Australia's financial system 'proved very resilient during the global crisis'. As the OECD reported:

> [t]he performance of the Australian economy has remained solid. It weathered the world financial and economic crisis better than most of the OECD countries and, indeed, and avoided a recession...In contrast to most other OECD countries, the short-term outlook is favourable.[122]

8.88 In part, this was attributed to 'solid domestic banking supervision'. As the OECD noted, Australia's '[b]anks have remained profitable with stable capital ratios, and the largest Australian banks are now among the soundest in the world'.[123] Other factors the OECD cited were 'the dynamism of Asian markets [and] well-functioning financial and labour markets and the timely and strong policy response to the crisis'.[124]

The mindset of family businesses – lessons for the broader economy?

8.89 While neither the anecdotal nor the empirical evidence clearly demonstrated that family businesses outperformed non-family enterprises, the data did reveal key features of family businesses that may enhance financial stability. The European Commission's review of the family business sector in Europe found that in general family businesses are risk-averse and focus on 'long-term sustainability rather than the realisation of short-term profits'.[125] Statistical research in the Australian context has highlighted similar investment trends among Australian-based family businesses. On the basis of its 2009 survey, KPMG concluded that '[f]amily businesses generally take a more conservative financing approach and long-term are more likely to have a 'patient capital' financial outlook'. This approach was considered to have assisted the

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120 MGI Australasia, *Family business owners concerned about their future post the global financial crisis*, http://www.mgiaust-survey.com/articles/family-business-owners-concerned-about-their-future-post-global-financial-crisis (accessed 26 February 2013).

121 Parliamentary Joint Committee on Corporations and Financial Services, *Access for small and medium business to finance*, April 2011, pp 29–30.

122 Organisation for Economic Co-Operation and Development, *OECD Economic Surveys, Australia: Volume 2010/21, Supplement 3 – Overview*, p. 3.

123 Organisation for Economic Co-Operation and Development, *OECD Economic Surveys, Australia: Volume 2010/21, Supplement 3*, p. 12.

124 Organisation for Economic Co-Operation and Development, *OECD Economic Surveys, Australia: Volume 2010/21, Supplement 3 – Overview*, p. 3.

125 European Commission and the Austrian Institute for SME Research, *Overview of family business relevant issues – Final report*, 2008, p. 56.

family business sector to withstand the GFC.[126] Anecdotal evidence collected by Family Business Australia also highlighted that family firms attributed resilience to 'long-term investments rather than a short-term view'.[127]

8.90 Mr Francesco Barbera of Bond University commented on his research findings suggesting that family businesses adopt a 'patient capital' approach to business planning:

> [F]amily firms tend to have a longer term time horizon and strategic planning happens over multiple generations rather than simply in the short run. In fact, a couple of weeks ago I interviewed a company which during the financial crisis spent most of their time buying assets rather than selling. That was because they recognise the good price currently and realise they are in business for the next 20, 40 or 60 years so now would be a good time to buy. But a non-family firm might not necessarily have such a long time horizon. It might have investors who are demanding dividends and liquidation of assets rather than the purchasing of assets, for example.[128]

8.91 As chapter 4 of this report has noted, family businesses tend to minimise debt and maximise their asset base.[129] KPMG argued that this approach to business management gives family businesses a competitive advantage over non-family entities, and provided family businesses with a sound economic basis on which to operate throughout the GFC:

> As they tend to take the longer term view; interested in growing the family wealth and having a different set of strategic goals compared to non-family and private companies, their long-term economic contribution is significant, and will be increasingly so. For many family businesses the ability to plan long-term can give them a huge competitive edge, allowing them to be more innovative than the corporate sector…A strong focus towards cash reserves are also qualities that will continue to give traditional family businesses a genuine competitive edge in the marketplace as the global economy recovers.[130]

8.92 Mrs Genevieve Power of the Canberra-based firm Iken Commercial Interiors, advised that a reliance on 'patient capital' and asset accumulation provided family businesses with financial stability despite the challenges presented by the GFC:

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126 KPMG and Family Business Australia, *KPMG and Family Business Australia Survey of Family Businesses 2009*, 2009, p. 5.

127 Hawkins Family Group, as cited in Family Business Australia, *Soul stories*, p. 104.

128 Mr Frank Barbera, *Committee Hansard*, 16 November 2012, p. 39.

129 See, for example, Dr Chris Graves, Family Business and Education and Research Group, University of Adelaide, Professor Mary Barrett, School of Management and Marketing, University of Wollongong, Dr Jill Thomas, Family Business Education and Research group, University of Adelaide, *Submission 14*, p. 5.

130 KPMG, *Submission 21*, p. 22.

> Good family businesses have strong assets. Whether they are liquid assets, in terms of stocks and shares, property assets or whatever assets, family businesses are asset based businesses. Therefore, in a crisis you rely on those assets to support your borrowings from the bank or you go to the bank and put up more assets to borrow more or you sell off those assets to enable you to continue to operate the business.[131]

8.93 Several submitters also commented on the personal commitment to the business displayed by family business owners. Mrs Power commented that this personal commitment enabled family businesses to better respond to the GFC:

> Combined with passion and commitment, and a bit of 'We won't let the buggers beat us; we'll keep going,' you reduce every cost you can, you ask your staff to recycle every piece of paper and you do absolutely everything you can to reduce every cost.[132]

8.94 Chapter 4 identified that family businesses' personal and long-term commitment to the business promotes a long-term view of financial gain. It was argued that this commitment is common among family businesses and is atypical of managers and directors of non-family companies. As Deloitte Private stated, 'owners will accept more modest growth in the longer term returns to ensure the sustainability of the business rather than relentlessly strive for short-term results'.[133]

8.95 These views are consistent with international research which indicates that the long-term focus of family businesses leads to risk averse investment strategies and 'significantly lower leverage than non-family firms'.[134] Nicolas Kacher, George Stalk and Alain Bloch wrote in a November 2012 *Harvard Business Review* (HBR) article that based on their research:

> …during good economic times, family-run companies don't earn as much money as companies with a more dispersed ownership structure. But when the economy slumps, family firms far outshine their peers. And when we looked across business cycles from 1997 to 2009, we found that the average long-term financial performance was higher for family businesses than for nonfamily businesses in every country we examined.[135]

8.96 Kacher, Stalk and Bloch found that the factors that contribute to this performance include:

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131 Mrs Genevieve Power, Managing Director, Iken Commercial Interiors, *Committee Hansard,* 13 November 2012, p. 51.

132 Mrs Power, Iken Commercial Interiors, *Committee Hansard*, 13 November 2012, p. 51.

133 Deloitte Private, *Submission 16,* p. 13.

134 Mr Francesco Barbera and Professor Ken Moores, 'Firm ownership and productivity: a study of family and not family SMEs', *Small Business Economics*, Vol. 29, October 2011.

135 Nicolas Kacher, George Stalk and Alain Bloch, 'What you can learn from family business', *Harvard Business Review*, November 2012, pp 103–106.

- a focus on resilience rather than short-term performance;
- low levels of debt and judicious capital expenditure;
- avoidance of risky ventures, desiring to 'forego the excess returns available during good times in order to increase the odds of survival during bad times'; and
- the personal investment by chief executive officers, who often adopted a 10–20 year investment horizon (see chapter 4).[136]

8.97 These characteristics can be contrasted with the business strategies that the OECD concluded contributed to the GFC. In 2009, the OECD Steering Group on Corporate Governance released its report *The Corporate Governance Lessons from the Financial Crisis*,[137] which outlined concerns that corporate governance structures did not safeguard against excessive risk-taking in a number of financial companies. The report points to concerns with the asset holdings of companies and remuneration systems that encouraged and rewarded high levels of risk-taking behaviour.[138]

8.98 The authors of 2012 HBR article concluded that 'well-run family businesses can serve as role models' for non-family enterprises.[139] The researchers concluded that a 'patient capital' approach is a sound model through which to respond to economic crisis:

> [T]he resilience–focused strategy of family-owned companies may become more attractive to all companies. In a global economy that seems to shift from crisis to crisis with alarming frequency, accepting a lower return in good times to ensure survival in bad times may be a trade-off that managers are thrilled to make.[140]

Employment and the global financial crisis

8.99 The committee heard that stable employment within the family business sector may have assisted family enterprises to respond to the GFC. Mr Barbera told the committee:

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136 Nicolas Kacher, George Stalk and Alain Bloch, 'What you can learn from family business', *Harvard Business Review*, November 2012, p. 104.

137 OECD Steering Group on Corporate Governance, 'The Corporate Governance Lessons from the Financial Crisis', 11 February 2009, ISSN 1995–2864, *Financial Market Trends*, Vol. 1, 2009.

138 OECD Steering Group on Corporate Governance, 'The Corporate Governance Lessons from the Financial Crisis', 11 February 2009, ISSN 1995–2864, *Financial Market Trends*, Vol. 1, 2009, pgs 3 and 5.

139 Nicolas Kacher, George Stalk and Alain Bloch, 'What you can learn from family business', *Harvard Business Review*, November 2012, p. 104.

140 Nicolas Kacher, George Stalk and Alain Bloch, 'What you can learn from family business', *Harvard Business Review*, November 2012, p. 106.

> As far as their capacity to withstand economic crisis is concerned, I am looking into that at the moment. One of the arguments is that employment—and you said it yourself—is much more stable in those family firms because they are more reluctant to lay off staff during tough times.[141]

8.100 This position was supported by Mr Graham Henderson, a managing director of a third-generation family business. He advised that family businesses have the capacity to remain stable despite volatile financial circumstances:

> Family businesses can respond to the challenges of the global financial crisis and of resilience. We are not inclined to put off people or to get rid of employees. You only have to look in the media most days to see ANZ getting rid of 600 people or Qantas getting rid of 500 people. That is not our make-up. Our make-up is we value our employees and we try to protect our employees and keep them on in very difficult circumstances. We have this positive attitude that things are going to get better, and we would rather keep these people on and support them so that when things get better we can fly off a lot earlier than the bigger people who are saying, 'I think we should rehire'.[142]

8.101 CCIQ commented:

> Time and again we see a spectrum of behaviour in terms of business. They will cut discretionary expenditure, they will cut advertising and they will cut training, but one of the very last things they do before they have to physically close is let go of their employees. It is really the second-last trigger point for most businesses.[143]

8.102 However, the Chamber also observed that family businesses are prepared to cut staff if necessary:

> [T]here is definitely a willingness—nobody wants to see their family business go under; they feel responsible. I think that in turn results in a greater tenacity. When it is a choice between sink or swim, if it means having to let some staff go then family businesses—and small businesses—generally are prepared to make the necessary decisions. Nobody likes to fire people. Nobody likes to risk being uncompetitive. But it is a reality of running a business, and I think family businesses understand that better than

141 Mr Francesco Barbera, PhD Scholar and Adjunct Lecturer, Faculty of Business, Bond University, *Committee Hansard*, 16 November 2012, p. 3.

142 Mr Graham Henderson, Director, Family Business Australia, *Committee Hansard*, 14 November 2012, p. 43.

143 Ms Sophie Andrew, Senior Policy Analyst, Chamber of Commerce and Industry Queensland, *Committee Hansard*, 16 November 2012, p. 3.

> anybody. That has certainly become apparent to us in conducting our case studies.[144]

8.103 The anecdotal evidence suggests that in addition to a preference to retain staff, family businesses owners are prepared to reduce their salaries, while staff in these businesses forego higher earning opportunities elsewhere. Mrs Power told the committee that in response to crisis, family businesses restrict expenditure: 'You do not pay yourself or you take half salary or only what you need to live on'.[145] The personal stories collected by Family Business Australia included reports that family members remain with the business in times of financial difficulty, accepting lower wages than they could receive elsewhere.[146] Mr Barbera described the family business sector as 'a more flexible labour force which is willing to work for less money if need be'.

8.104 The New South Wales Business Chamber speculated that access to unpaid labour assisted family businesses to meet the financial challenges of the GFC. Mr Paul Orton told the committee:

> I think the ownership plus operational responsibility means that the business has a life beyond simply the set of books. It is a big part of individuals' and families' reasons for being, in a sense, and I am sure that they have done things that may not necessarily have stacked up, in strict financial terms, to ensure the businesses were in a position to survive and prosper beyond the GFC.[147]

8.105 The Chamber also explained that the 'measures that may not necessarily have stacked up in strict financial terms' may have included access to free family-based labour:

> Part of it is simply that businesses that have a lot of family members involved can probably rely on those family members to support the business, even when there is not a great deal of access to cash flow or much by way of sales coming in. It is much more difficult, I suppose, if a business has to rely on employees that it pays, to wind things back or ramp them up. It is a lot less flexible for businesses that have those formal employee-employer relationships more to the fore.[148]

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144 Ms Sophie Andrew, Senior Policy Analyst, Chamber of Commerce and Industry Queensland, *Committee Hansard*, 16 November 2012, p. 3.

145 Mrs Power, Iken Commercial Interiors, *Committee Hansard*, 13 November 2012, p. 51.

146 Decorative Imaging Pty Ltd, as cited in Family Business Australia, *Soul stories*, p. 62.

147 Mr Paul Orton, Director, Policy and Advocacy, New South Wales Business Chamber, *Committee Hansard*, 15 November 2012, p. 22.

148 Mr Tim Hicks, Policy Adviser, Business, Regulation and Economics, New South Wales Business Chamber, *Committee Hansard*, 15 November 2012, p. 22.

8.106 CCIQ also hinted at this practice, providing an example of a family business that, in response to the GFC, 'fired only non-family members'.[149] It added:

> [i]t also poses an interesting question about whether or not those family members who work in a family business see themselves as operating outside of the Fair Work Act and, accordingly, are prepared to take what would not be considered to be a wage and would forgo income with a view to supporting that business through difficult times.[150]

8.107 The committee was also advised that family businesses may perceive the business operates outside the parameters of the *Fair Work Act 2009*:

> [M]any members who work in a family home business are effectively shareholders in that business and, accordingly, are prepared to forgo an income to ensure that that business prevails through a difficult operating environment. I would hazard a guess—it would need to be confirmed—that award rates of pay would not be considered of relevance to many family members. So clearly they do operate outside of the Fair Work Act.[151]

The global financial crisis and the family business sector: Committee view

8.108 On the basis of the available evidence, it cannot be concluded that the family business sector in Australia outperformed non-family businesses in response to the GFC. There is strong anecdotal evidence that a number of family businesses performed well, and the committee recognises the conviction underlying statements by family business representatives that the sector proved particularly resilient in response to the GFC. However, there is little empirical data to support a conclusion that the sector's performance eclipsed that of non-family enterprises.

8.109 There are aspects of the mindset of family businesses that could allow them to respond to periods of financial instability. The committee notes arguments that a patient capital approach safeguards businesses from economic downturn and the OECD's conclusions highlighting the drawbacks of risky, highly leveraged investments.

8.110 The committee believes that the patient capital approach is a remedy against business closures in the event of economic instability. An analysis of the family business sector's response to the GFC indicates that this approach has distinguished many family businesses from non-family enterprises. The sector's contribution to the Australian economy includes the promotion of the benefits of a risk-averse, long-term approach to investment and business profitability (see also chapter 4). While its

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149 Ms Sophie Andrew, Senior Policy Analyst, Chamber of Commerce and Industry Queensland, *Committee Hansard*, 16 November 2012, p. 3.

150 Mr Nick Behrens, General Manager, Advocacy, Chamber of Commerce and Industry Queensland, *Committee Hansard*, 16 November 2012, p. 3.

151 Ms Sophie Andrew, Senior Policy Analyst, Chamber of Commerce and Industry Queensland, *Committee Hansard*, 16 November 2012, p. 3.

effects have not been measured, the committee considers that it is an approach that the broader economy could consider.

8.111 The committee considers that family businesses' patient capital approach warrants further analysis. It reiterates that the proposed IDC should give consideration to whether data should be collected on family businesses' debt to equity ratios and the value of assets on balance sheets (see recommendation 10).[152] This information would be useful in identifying the conservative, long-term investment focus of the sector.

8.112 The anecdotal evidence that family businesses may perceive that they operate outside the parameters of the Fair Work Act is of concern. That said, the evidence on the employment practices of family businesses is inconclusive. It is insufficient to draw conclusions about the extent to which non-compliance with employment requirements may be occurring.

152 See Recommendation 7, chapter four.

Chapter 9

Conclusion

9.1 This is the first federal parliamentary inquiry to focus specifically on family business issues. It is long overdue. Too often, the understanding of family business has been conflated with micro and small business issues. The media may point to highly successful large and medium-sized businesses that are owned and managed by a family. But for policy makers, the key issue has been the size of the business (in employee numbers and turnover) and the type of legal organisation. The issue of business ownership has not, generally, been of concern.

9.2 Family businesses come in all sizes—micro, small, medium and large—and in all legal forms—companies, trusts, partnerships and (if a definition allows) sole traders. In a financial sense, their issues and interests certainly overlap with those of non-family businesses. However, as this report has discussed, family businesses face unique challenges including internal governance and dealing with sibling rivalry, developing and retaining the family's skill set while employing outside talent, and planning and executing succession (chapter 5). They also appear to have unique characteristics: a long-term risk-averse mindset, greater flexibility in their decision-making than non-family businesses; a commitment to retaining staff; and a significant contribution to the community in which they operate (chapter 4). As one witness described family businesses: '[T]hey are different; they are significant and they are overlooked'.[1]

9.3 The principal reason why family businesses have been either ignored, or subsumed within the debate on small business in Australia, is that very little reliable data is available. Indeed, there is no definition of 'family business' upon which official data could be gathered (chapter 2). Without a definition, and without accurate and reliable data, the debate on family business in Australia has been stunted: it has not captured the attention of Australia's policy makers in any systematic way.

9.4 For the past 20 years, consultancies and academics have conducted their own surveys on family businesses (chapter 3). The surveys have various shortcomings. Among surveys conducted by the same researchers, the methodology and even the definition of 'family business' has changed over time; the questions have changed one survey to the next; and the sample sizes have often been low. Nonetheless, these surveys have begun a discussion about family businesses. The findings draw attention to the diversity, economic contribution and resilience of these businesses. There has also been growing academic interest in family businesses, particularly in the links between their governance and performance and whether they employ labour more

1 Professor Ken Moores, Executive Chairman, Moores Family Enterprise, *Committee Hansard*, Brisbane, 16 November 2012, p. 18.

productively than businesses that are not family owned and managed (chapter 4). This research is important and to be encouraged.

9.5 The main purpose of this report is to further the conversation within government about family business issues that this inquiry has started. Given the early stages of this discussion, at this time the committee believes it may be counterproductive for it to present a conclusive definition of family business to be used by policymakers in Australia. Rather, to encourage the best outcome and to ensure that the costs associated with the collection of any official data on family business are justified, it appears that various government departments and agencies require a process through which they can: (a) further consider the issues that are particularly or uniquely relevant to family business and how these issues interconnect with distinct policy areas; and (b) deliberate on how a definition can capture these issues.

9.6 Accordingly, the committee's central recommendation is that government agencies should meet as part of an Inter-Departmental Committee (IDC) to discuss a number of issues related to this inquiry's terms of reference. Most crucially, the committee recommends that the IDC should focus agencies' attention on the public policy need to identify family businesses. In particular, it must identify what has been, and what could be, the need for these agencies to use data relating to family businesses in the development of public policy. This task would lead the IDC to consider whether a survey is needed and if so, how questions could be framed.

9.7 Chapter 2 of this report suggests that the IDC would have to consider two broad types of questions: a first set that relate specifically to determining whether a respondent is a family business; and a second providing policy-makers with the necessary information about these businesses (such as location and sector, financing, productivity, tenure of employment, philanthropic contributions and planning for succession). From this discussion, a definition of family business would be formed. It must address key threshold issues such as whether to include sole traders, how to define a family member, whether to require the intent to pass the business on, and whether to set a limit on size (by number of employees or annual turnover).

9.8 The proposed IDC is an opportunity for policy makers to consider carefully the issue of succession. Chapter 5 of this report has identified succession planning as a key and unique challenge for family businesses. It has also suggested that succession planning should be of concern for government, given some survey evidence of the large number of family business owners intending to retire over the next decade. The committee has recommended that the proposed IDC should consider whether to quantify the number of family businesses in different sectors whose owners plan to retire over the next ten years.

9.9 The committee is not prescriptive about how government should handle the matter of family businesses' succession planning. However, it does consider that the IDC should discuss certain succession issues. For instance, should it be of public policy concern that a large block of family business owners in various sectors of the

Australian economy are soon to retire? Should it be of concern to government if these businesses do not have a succession plan in place? More specifically, should it be an objective of public policy to assist in the preservation of family ownership of a business passing from one generation to the next? Is there a productivity or employment gain possible that a public policy response could enable? There may be a constructive role for government in certain industries to conduct an education campaign to inform family business owners of issues relating to succession planning. Without data, it is difficult to discern a public policy response to these and other questions that have emerged in the course of the inquiry.

Representing and educating the sector

9.10 This inquiry has provided the committee with insight into the representation of the family business sector. Family Business Australia (FBA) is the national peak body devoted to the promotion of family business issues. It is not-for-profit and membership based. The committee commends the FBA for its work in developing and conducting national education programs, as well as state based programs run by the local FBA chapters. It also encourages the FBA's efforts to involve academic institutions in these programs.

9.11 As this report has noted, there is a small but growing body of important research into the family business sector in Australia. The proposed IDC will benefit from these insights. The committee is impressed with the work of the Australian Centre for Family Business at Bond University, Professor Smyrnios and his colleagues at RMIT, Dr Graves and Dr Thomas at the University of Adelaide Business School and Professor Barrett at the University of Wollongong. The committee recognises that the work of these academics will be greatly enhanced if official data is collected.

9.12 The FBA emphasised in evidence to this inquiry that family business is more than simply small business. The point is well taken. Indeed, the committee's observation is that many FBA members are medium and large-sized businesses. They are generally highly successful and attuned to the complex structural and governance issues that face them as the owner-managers of a family business. The contribution that many of these members made to this inquiry was substantial.

9.13 On the other hand, the committee believes that many micro and small family businesses are not aware and not engaged in issues that affect them as family businesses. The committee received only one submission from a family business owner that was not a member of the FBA.[2] The Council of Small Business of Australia (COSBOA) told the committee that many of its members equate family business with small business. COSBOA leaves the representation of large family

2 Laserforce International, *Submission 32*.

businesses to the FBA.[3] The concern, therefore, is that many micro and small family businesses may not be adequately informed about issues that relate specifically to their family business structure, including the remuneration of family members, superannuation, taxation matters and succession planning.

9.14 There does not currently appear to be a body that is genuinely representative of all family businesses in Australia. Recommendations 3, 14, 15, 16, 18, 19 and 21 of this report refer to the need for consultation with the family business sector. The question arises, however, as to which body represents the sector's interests. To paraphrase a former United States Secretary of State, 'who do I call if I want to call the family business sector?'

9.15 The committee believes that at present, the groups best able to participate in these consultations are the FBA and COSBOA. The FBA should consult primarily on matters relating to section 113 of the Corporations Act (recommendations 16 and 17), Division 83A (recommendation 18) and director's duties and liabilities in the Corporations Act (recommendation 19). Recommendation 21 calls on the Reserve Bank of Australia to include representatives of the family business sector on its annual small business panel in each state and territory (chapter 8). COSBOA should have principal responsibility for identifying these representatives.

9.16 The committee anticipates that, depending on the deliberations of the proposed IDC, the representation of family businesses in Australia will broaden and mature. It understands COSBOA's current position on family businesses given the lack of a definition and official data on the family business sector. It is likely that should this information become available, the sector will quickly find representatives that reflect how policy makers identify the sector. In the interim, however, the committee encourages COSBOA to give consideration to how the findings of this report might enrich their current understanding of the small and medium-sized business sector with a richer awareness of the family elements of Australian businesses.

9.17 The committee also foresees that if official data is collected based on a definition of family business, the needs of family businesses will be articulated and more likely to be served. It may be, for instance, that the government's Enterprise Connect program could be tailored to reflect the needs of small and medium-sized family businesses identified in the official data. There may be a need for Enterprise Connect to run the type of programs that are currently being offered by the FBA.

9.18 A final note on the proposed IDC: while the committee believes it is important that the IDC is established, it does not wish to pre-empt or pressure its findings. As this report has emphasised, the key concern of the IDC should be the

3 Mr Peter Strong, Executive Director, Council of Small Business of Australia, *Committee Hansard*, 14 November 2012, p. 26.

agencies' policy need. Only after this discussion should a judgment be made whether to collect data and if so, on what definition and in what form.

Ms Deborah O'Neill MP
Chair

Appendix 1

Submissions

1 Family Business Australia

2 Australian Bureau of Statistics

3 Bond University

4 Packer Leather Pty. Ltd.

5 Kennards Hire Pty Ltd

6 Commercial Asset Finance Brokers Association

Supplementary Submission

7 Mr Bill Winter

8 Moores Family Enterprise

9 MGI Australasia Ltd

10 Name Withheld

11 PricewaterhouseCoopers

12 Confidential

13 Pamela Low and Associates

14 Professor Barrett, Dr Graves and Dr Thomas

15 Kennards Self Storage

16 Deloitte Private

17 Reserve Bank of Australia

18 Mr Robert Powell, Grant Thornton Australia

19 Chamber of Commerce and Industry Queensland

20 Bus Association Victoria Inc

21 KPMG

22 Council of Small Business of Australia

23 Business SA

24 Commonwealth Bank of Australia

25 Institute of Chartered Accountants Australia

26 The Treasury

27 Regional Development Australia Hunter and Hunter Business Chamber

28 Pitcher Partners Consulting Pty Ltd

29 National Farmers' Federation

30 Empower Business Solutions

31 Department of Resources, Energy and Tourism

32 Laserforce International

33 Regional Development Australia Pilbara

34 FINH

35 Associate Professor Pi-Shen Seet

36 Institute of Certified Bookkeepers

37 Agribusiness Council of Australia

38 Taylor Bros

Answers to questions on notice

1 Australian Bureau of Agricultural and Resource Economics and Sciences, received 13 December 2012

2 Department of Regional Australia, Local Government, Arts and Sport, received 14 December 2012

3 Department of Industry, Innovation, Science, Research and Tertiary Education, received 21 December 2012

4 Australian Bureau of Statistics, received 10 December 2012

5 Treasury, received 8 February 2013

6 Agribusiness Council of Australia, received 28 February 2013

Appendix 2

Public hearings and witnesses

Canberra, 13 November 2012

Department of Industry, Innovation, Science, Research and Tertiary Education
Mr Peter Chesworth, SB Division
Ms Chris Butler, AusIndustry
Ms Michelle Henderson, Enterprise Connect
Mr Raphael Cicchini, SB Division

Treasury
Mr Hector Thompson: General Manager, Small Business Tax Division
Mr Paul McMahon, Manager, Manager, Small Business Tax General Unit
Ms Kate Preston, Manager, Revenue Group
Mr Michael Wilson, Analyst, Small Business Tax Entities Unit
Mr David Woods, General Manager, Markets Group

Australian Bureau of Statistics
Mr Bill Allen, Assistant Statistician
Ms Jacky Hodges, Regional Director

Council of Small Business Organisations of Australia
Peter Strong, Chief Executive Officer

Regional Development Australia
Mr Simon Atkinson, First Assistant Secretary for Regional Strategy and Coordination
Mr Shane Bennett, Assistant Secretary Regional Economic and Infrastructure Policy
Mr Michael Heard, Director, RDA Strategy

Department of Agriculture, Fisheries and Forestry
Australian Bureau of Agricultural Resource Economics and Sciences (ABARES)
Dr Lisa Elliston, Assistant Secretary
Mr Peter Martin, Policy Officer

Melbourne, 14 November 2012

Deloitte Touche Tomatsu
Mr David Hill, National Managing Partner, Deloitte Private
Mr David Pring, Partner
Mr Peter Pagonis, Partner
Mr David Smorgon, Generation Pty Ltd

Bus Association of Victoria Inc
Mr Chris Lowe, Chief Executive Officer

Institute of Chartered Accountants
Mr Yasser El-Ansary CA, General Manager of Leadership & Quality
Ms Sue Prestney, Small business spokesperson

MGI Australasia
Mr Desmond Caulfield, Director

Family Business Australia
Mrs Philippa Taylor, Chief Executive Officer

Family business roundtable
Mr Peter Ciliberto, C-Direct Pty Ltd
Mr Graham Henderson, Mitchell Laminates
Mr Mark Kagan, ex Kagan Transport Pty Ltd
Mr David Shave, David Shave Investments Pty Ltd
Mr Bill Winter
Mr Simon Le Maistre, KPMG
Ms Sara Pantaleo, La Porchetta

Sydney, 15 November 2012

Reserve Bank of Australia
Mr Chris Aylmer, Head of Domestic Markets Department, Financial Markets Group

Pamela Low & Associates
Ms Pamela Low, Principal

Grant Thornton Advisers
Mr Robert Powell, Partner

NSW Chamber of Business and Commerce
Mr Paul Orton, Director Policy and Advocacy
Mr Tim Hicks, Policy Advisor, Business, Regulation and Economics

PricewaterhouseCoopers
Mr Paul Brassil, Partner, Private Clients

Professor Mary Barrett
Professor of Management, University of Wollongong

Dr Chris Graves,
Business School, University of Adelaide

Roundtable
Mr Andy Kennard, Kennards Hire
Mr Sam Kennard, Kennards Self Storage
Mr Richard Sharpe, Joint Managing Director, Sharpe Bros.

Mr Hayden Sharpe, Mr Michael Sharpe
Mr Mark Cleary
Mr Garry Beard, AH Beard Pty Ltd
Mr Keith Drewery

Brisbane, 16 November 2012

Chamber of Commerce and Industry Queensland
Ms Sophie Andrew
Mr Nick Behrens

KPMG
Mr William Noye, National Leader Family Business Services

Moores Family Enterprise
Ms Anthea Moores, Managing Director
Professor Kenneth Moores, Executive Chairman

Bond University
Professor Mark Hirst
Mr Frank Barbera

Family business roundtable
Mr Peter Taylor, Townsend Building Services Pty Ltd
Mr Nick Bloor, Technigro Pty Ltd

Devonport, 21 January 2013

Burnie City Council
Councillor Steven Kons

Mr Hugh McKenzie
Former KPMG partner and from Launceston City Council

Burnie Newsagency
Mr Alan Berechree

Pennicott Wilderness Journeys
Mr Robert Pennicott

Novaris
Mrs Diane Tomson, Director

Taylor Bros.
Mrs Jan Taylor

Canberra, 7 February 2013

Australian Taxation Office
Mr Tony Poulakis, Assistant Commissioner, S&ME – Policy and Corporate Risks

Treasury
Mr Paul McMahon, Acting General Manager, Small Business Tax Division

Agribusiness Council of Australia
Mr Roy Duncanson, Chief Executive Officer
Mr Ian Joseph, Chair

Lionel Samson Sadleirs Group
Mr Stephen Samson, Director

Craig Mostyn & Co Pty Ltd
Mr Andrew Mostyn, Executive Director

National Corporate Training
Mr Michael Claydon, Managing Director

Hind's Transport Services
Mr Raymond Hind, Chief Executive Officer