Intergenerational Survival of Family Businesses: Succession Planning, Board Composition and Stakeholder Accountability in the Kenyan Context.

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Abstract

As the basic unit of society, the family has been a central pillar of organising societal affairs, including the conduct of business activities in Kenya. However, few family enterprises survive to the third and fourth generation. This article demonstrates that three main governance challenges cause failure of family enterprises. These include: lack of proper succession planning, poorly constituted boards and lack of stakeholder accountability. This article evaluates the case of Tusker Mattresses Limited being a family enterprise that has experienced liquidity challenges. It examines: the extent to which poor succession planning in family enterprises leads to poor governance; the extent to which lack of proper board composition leads to flawed strategic decision making; and the extent to which lack of stakeholder accountability leads to loss of stakeholder's confidence and thus inhibiting the growth of family enterprises. The paramount goal of this article is to demonstrate that Kenya's corporate governance law is inadequate to mitigate the

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governance challenges that family enterprises face. This article demonstrates that having the governance structures for family enterprises embodied under one corpus would contribute to improving their governance practices.

Introduction

A family enterprise refers to an entity controlled by a particular family that owns a significant amount of the entity's equity and greatly influences who manages the business's daily operations.[2] Family enterprises are considered one of the most common yet more complex forms of business worldwide. This is because the family's involvement in the enterprise, creates a complexity that requires to be adequately understood prior to advising any family-owned company on issues related to governance.[3] In Kenya, family-owned companies are a driving force towards economic growth and development.[4] There are more than four hundred and ninety family-owned companies that generate annual revenue of more than ten million dollars.[5] Their total contribution to the national Gross Domestic Product (GDP) amounts to over 70%.[6] They create a large tax base for the government to facilitate the redistribution of resources within the country.[7] They also create social opportunities in the form of employment

2. Qaiser Rafique Yasser, 'Challenges in Corporate Governance: A Family Controlled Business Perspective' (2011) 2 International Journal of Innovation Management and Technology 73.

3. The Family Firm Institute, Inc., *Family Enterprise: Understanding Families in Business and Families of Wealth* (John Wiley and Sons Inc 2014) 1.

4. PricewaterhouseCoopers Limited, 'Kenya Family Business Survey 2018' <https://www.pwc.com/ke/en/assets/pdf/kenya-family-business-survey-2018.pdf> accessed 20th December 2020.

5. Asoko Insight, 'Kenya's Leading Family-Owned Business' (31st May 2019) <https://www.asokoinsight.com/content/market-insights/kenya-s-leading-family-owned-businesses> accessed 1st January 2021.

6. Rachel Mugure Mburu, Robert Gichira and Teresiah Kyalo, 'Innovativeness and Firm Performance among Family-Owned Enterprises in Nairobi County' (2017) 9 European Journal of Business and Management 186.

7. Salahuddin A, 'Robert Nozick's Entitlement Theory of Justice, Libertarian Rights and the Minimal State: A Critical Examination (2018) 7 Journal of Civil and Legal Services 1.

and supply essential goods and services.[8] Therefore, family enterprises are instrumental in achieving the eighth Sustainable Development Goal (SDG) which is to advance economic growth and decent employment for everyone.[9]

A profound characteristic of family-owned companies is the family's commitment to pass on the enterprise to future generations.[10] However, despite this commitment, only twelve percent of family enterprises survive to the third generation and three percent to the fourth generation.[11] Due to kinship ties in family-owned companies, there is often a lack of formalism in their management and hence they have weak corporate governance structures.[12] Corporate governance is the system through which companies are directed and controlled.[13] It is aimed at assisting companies in building an environment of transparency and accountability with a view to promoting financial stability and business integrity.[14] Therefore, family-owned companies must implement good governance practices to enhance their progression to future generations. In Kenya, there are several statutes and codes providing for corporate governance best practices. To name a few: the Constitution of Kenya 2010; the Companies Act 2015; and the Code on Corporate Governance for Issuers of Securities to the Public. That notwithstanding, this fragmented legal framework has proved ineffective in addressing the governance challenges

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8. PricewaterhouseCoopers Limited, 'Kenya Family Business Survey 2016' 4 https://www.pwc.com/ke/en/assets/pdf/kenya-family-business-survey-2018.pdf accessed 20th December 2020.

9. United Nations, 'Transforming our World : The 2030 Agenda For Sustainable Development' 24 https://sustainabledevelopment.un.org/content/documents/21252030%20Agenda%20for%20Sustainable%20Development%20web.pdf accessed 24th November 2022.

10. Sir Adrian Cadbury, *Family Firms and their Governance Creating Tomorrow's Company from Today's* (Egon Zehnder International) 7.

11. Karen Mwai, Joseph Ntale and Thomas Ngui, 'Effect of Entrepreneurial Orientation on the performance of Family-Owned Businesses: A case study of Supermarkets in Nairobi County' (2018) 2 International Academic Journal of Innovation, Leadership and Entrepreneurship 73, 78.

12. Raghuveer Kaur and Hamitesh Singh, 'Corporate Governance in Family Business-A Review' (2018) 11 Pacific Business Review International 131,138.

13. Bow Group Economic Committee, *Report of the Committee on The Financial Aspects of Corporate Governance* (1992) 14.

14. OECD, *G20/OECD Principles of Corporate Governance* (OECD Publishing, Paris) <http://dx.doi.org/10.1787/9789264236882-en> accessed 2nd January 2021.

faced by family-owned companies as this economically beneficial class of companies struggles to survive to the third and fourth generations. This article, therefore, discusses how poor succession planning, lack of proper board composition and lack of stakeholder accountability has affected the performance of family enterprises. This has been done through an analysis of the case study of Tusker Mattresses Limited being a family-owned company that has experienced liquidity challenges. This article also determines whether loopholes in the corporate governance legal framework constrain it from addressing these challenges. Additionally, this article makes proposals on the legal and regulatory intervention that should be implemented to promote adequate succession planning, proper board composition and improved stakeholder accountability in family enterprises. This shall enhance the chances of survival of family-owned companies to future generations.

The Historical Development of Family Enterprises in Kenya

The establishment of the corporation, in its formal nature, was first recorded during the colonial era. The first thirty-five companies in Kenya were established between 1907 and 1922. They were dominated by a few of the most powerful and influential European settlers, including Lord Delamare and Captain E.S Grogan. It is noteworthy that several companies established during this period were family-owned. For instance, the Kilindini Harbour and Wharf Company, Maasai Trust Cooperation, and the Upper Nairobi Township and Estate Company, which the family of Captain E.S Grogan owned.[15] The Mackinnon brothers owned the Nairobi Prospecting & Acquiring Syndicate and Mackinnon Brothers Limited.[16]

15. RMA van Zwanenberg and Anne King, *An Economic History of Kenya and Uganda 1800-1970* (Macmillan Press Limited 1975) 49.

16. Ibid 50.

The thirty-five companies did not, however, thrive for long due to the nature of their speculative business, debt, and governance challenges, including lack of separation between ownership and management.[17]

After Kenya gained its independence in 1963, several political families utilized state power to control production factors and consequently established family enterprises to conduct their economic activities on a large scale.[18] These included the Kenyatta family which owns or has controlling interest in a number of key companies, such as Brookside Dairy Limited and Commercial Bank of Africa (now NCBA Bank Kenya PLC).[19] The Matiba family was also famous during the post-colonial period for not only intensive political involvement, but also for owning an expansive business empire. Apart from being a Permanent Secretary in the Kenyan Government, Kenneth Matiba established the Hillcrest Group of Schools, People's Daily Newspaper and several hotels.[20] However, his fortunes began to dwindle once he championed for multiparty democracy, a move that pitted the incumbent government headed by President Moi against him.[21] His heirs did not match his business acumen in running the family businesses when his health deteriorated.[22] As a result, most of his establishments were sold off to recover outstanding liabilities.[23]

Other noteworthy cases of corporate collapse included the Akamba Public Road Services Limited which was a reliable public transport company in Kenya and East Africa. The company is reported to have collapsed just

17. Ibid.

18. R.M.A. van Zwanenberg and Anne King (n 15) 122.

19. Victor Juma, 'Kenyatta business empire goes into expansion drive' Business Daily Africa (Kenya, 11th November 2013) https://www.businessdailyafrica.com/bd/corporate/companies/kenyatta-business-empire-goes-into-expansion-drive-2045420 accessed 25th November 2022.

20. Peter Theuri, 'How Kenneth Matiba sunk from a billionaire politician to poverty'(Kenya, 16th April 2018) https://www.standardmedia.co.ke/entertainment/news/article/2001277082/how-kenneth-matiba-sunk-from-a-billionaire-politician-to-poverty accessed 25th November 2022.

21. John Kamau, 'How Kenneth Matiba's entry into politics killed his business empire' Daily Nation (Kenya, 16th April 2018) https://nation.africa/kenya/news/how-kenneth-matiba-s-entry-into-politics-killed-his-business-empire--33576 accessed 25th November 2022.

22. Ibid.

23. Ibid.

twelve years after the death of its founder due to mismanagement.[24] Another example is the collapse of Nakumatt Holdings Limited which caught the public by surprise. Poor strategic decisions by the company's managing director drove the company to its demise. An ambitious expansion drive that was fueled by debt was one such poor decision. By the time the court placed the company under administration, it had accumulated a total debt of over thirty billion shillings.[25]

Tusker Mattresses Limited, which was established by Joram Kamau in 1983, is also worthy of mention. It opened its first outlet in Nakuru[26] and later opened a branch in Nairobi in 1990.[27] It sought to fill a significant gap in the retail industry by serving the country's lower and middle-income citizens.[28] After Joram Kamau's demise in 2002, his sons took over the company's management. The company appeared to be doing well as it had become the second-largest retailer in the country. However, the company is currently heavily indebted, a factor that is attributable to its poor corporate governance practices. Its board appeared to lack independence as it mainly comprised family members.

From the foregoing, it is evident that governance challenges have been rife in family enterprises since the advent of the corporation during the pre-colonial period. Several family-owned companies in Kenya have collapsed or experienced liquidity challenges due to governance challenges, such as poor succession planning, lack of proper board composition, and lack of stakeholder accountability. In the ensuing paragraphs, this article will

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24. Kuria Kimani, ' Akamba Bus Company: How sibling incompetence brought the best bus company in Kenya down'(26th December 2021) 'https://whownskenya.com/index.php/2021/12/26/akamba-bus-company-how-sibling-incompetence-brought-the-best-bus-company-in-kenya-down/ accessed 6th March 2022.

25. Duncan Miriri, 'Kenyan Retailer Nakumatt to close as creditors back liquidation' (7th January 2020) https://www.reuters.com/article/us-kenya-nakumatt-idUSKBN1Z610M accessed 29th May 2022.

26. Wainaina Wambu, 'How founder's magic faded from Tuskys store' *The Standard* (Kenya, 13th December 2022) https://www.standardmedia.co.ke/business/business/article/2001397119/how-founders-magic-faded-from-tuskys-stores accessed 2nd June 2022.

27. Ibid.

28. Ibid.

analyze each of these challenges as experienced in Tusker Mattresses Limited. This analysis is essential to demonstrate the extent to which each of the challenges negatively affects the operation and performance of family enterprises.

Succession Planning

According to William J. Rothwell[29], succession planning takes place when a deliberate and systematic effort is made to ensure the continuity of leadership in key positions and to retain and develop knowledge capital for the future.[30] The issue of succession in family enterprises is sensitive and crucial. The question always arises in relation to who is to take up the reins once the founder exits the entity either through retirement, death, or incapacitation.

The Legal Framework on Succession Planning

The Code of Corporate Governance Practices for Issuers of Securities to the Public recommends that the tenure of board members should not expire simultaneously so as to ensure a smooth transition and maintenance of institutional memory.[31] Consequently, new board members can be partnered with existing directors to ensure that they are adequately inducted on the organization's vision and culture. The Mwongozo Code of Governance for State Corporations (Mwongozo Code) also buttresses the point that the board's tenure should be staggered.[32] It further provides that the board should assist the Chief Executive Officer (CEO) to ensure that a proper succession plan exists for the CEO and senior

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29. William J. Rothwell, *Effective Succession Planning: Ensuring Leadership Continuity and Building Talent From Within* (4th Edition, American Management of Association 2010).
30. Ibid 6.
31. The Code of Corporate Governance Practices For Issuers of Securities to the Public, Recommendation 2.1.7
32. The Mwongozo-The Code of Governance for State Corporations, Recommendation 1.14 1.

management staff.[33] According to the Corporate Governance Code for Issuers of Securities to the Public and the Mwongozo Code, the CEO and board play a major role in succession planning. Family enterprises would benefit from having succession plans. However, these codes apply to issuers of securities to the public and state corporations respectively and hence family enterprises fall outside their scope. Further, they do not address the presence of the family dynamic in family enterprises and do not prescribe how family enterprises can have succession plans that ensure that qualified leaders from within or outside the family are selected to succeed the founder.

The Principles of Corporate Governance prepared by the Private Sector Initiative for Corporate Governance (PSICG) reiterate that the board is tasked with ensuring that a proper succession plan is put in place for the C.E.O, the Board Chairman, and other senior management staff.[34] The Code of Corporate Governance for Private Organisations prepared by the Institute of Certified Secretaries (ICS) provides that the Board Chairman should ensure that there is a formal succession plan for the board.[35] Likewise, the CEO should ensure that there is a formal succession plan for the CEO and the executive management team.[36] These Codes emphasize that a succession plan for senior executive staff and for the board should be in place. The limitation of the Codes in addressing succession planning within family enterprises is that they are general and do not elaborate on the steps that should be taken in establishing and implementing succession plans in family enterprises. Despite the existence of various corporate governance codes, poor succession planning continues to plague family enterprises in Kenya.

33. Ibid, Recommendation 1.18 (f).

34. Private Sector Initiative for Corporate Governance, ‘Principles for Corporate Governance in Kenya and a Sample Code of Best Practices for Corporate Governance’ (1999) 12.

35. The Institute of Certified Secretaries, ‘Code of Governance for Private Organizations in Kenya’ (2014), Principle 1.13.

36. Ibid, Principle 1.17.4.

Poor Succession Planning in Tusker Mattresses Limited

Upon the death of Mr. Joram Kamau Kago, the founder of Tusker Mattresses Limited in 2002, all seven of his children obtained shares in the company. His five sons, namely Sammy Kamau, Yusuf Kamau, John Kamau, George Kamau, and Stephen Kamau, immediately took up directorship roles.[37] In this instance, the entity's founder did not have a clear succession plan, consequently his children felt entitled to take up leadership roles. While the company appeared to have been performing well, leadership wrangles were rife within the boardroom. The Board of Directors was reported to be egoistic and devoid of professionalism. As a result, they made decisions that were not in the company's best interest. As seen in the case of *Patrick K Maina v Tusker Mattresses Limited [2018] eKLR,* they would walk into stores and collect money for personal use. The plaintiff in this case was a store manager at Tusky's Midtown Supermarket in Nakuru. He had sued the company for unfair dismissal. Mr. Yusuf Mugweru, one of the directors, had stormed into the store and demanded to be granted a sum of three million shillings from petty cash which was approved by the regional manager and the rest of the directors. In fact, according to the plaintiff, such requests for withdrawals from petty cash were common at the company's branches. The court found that the respondent did not employ procedural justice and fairness in dismissing the employee.

In another case, *Republic v Chief Magistrate Milimani & another Ex-parte Tusker Mattresses Ltd & 3 others [2013] eKLR***,** Yusuf accused his brothers, Stephen and George, of embezzling funds to the tune of one billion, six hundred and forty-two million shillings and transferring the sums to other companies wherein they were directors.

37. This information is in accordance with a current Official Search (Form C12) from the Companies Registry.

The boardroom wrangles and mismanagement of funds by top directors are expected consequences of lack of succession planning. Implications of mismanagement have been witnessed since 2020 when the store began by shutting down three branches in Nairobi, Mombasa, and Kitale.[38] By August 2020, the company was indebted to its suppliers to the tune of six billion two hundred million shillings.[39] By 2021, the company had shut down fifty nine branches reducing its branch count from sixty four to five.[40]

Board Composition

Companies are artificial persons and, as such, they require human agents (directors) to conduct their operations and make profits for the benefit of shareholders and investors.[41] In this regard, directors are deemed to be the most important persons in an organization.[42] They determine the company's strategic direction. In *Lennard's Carrying Company Limited v Asiatic Petroleum Company Limited*,[43] it was established that directors are the directing minds of a company and, owing to this, heavily influence the corporation's activities. Indeed, an experienced and independent board contributes to a company's sustainability.[44] However,

38. Citizen Digital, '3 Tuskys supermarket branches closed in Nairobi, Kitale Mombasa' (21st April 2020) https://www.citizen.digital/business/3-tuskys-supermarket-branches-closed-in-nairobi-kitale-mombasa-330515/ accessed 29th June 2022.

39. Wainaina Wambu, 'It is all our fault, no says Tusky's sibling on retailer downward spiral' *The Standard* (Kenya, 18th June 2020 https://www.standardmedia.co.ke/business/financial-standard/article/2001382875/it-is-all-our-fault-now-says-tuskys-sibling-on-retailer-downward-spiral accessed 29th June 2022.

40. Kepha Muiruri, 'From 64 branches to just 5, Retailer Tuskys nears its last breath' (25th January 2021) (https://www.citizen.digital/business/from-64-branches-to-just-5-retailer-tuskys-nears-its-last-breath-4933965 accessed 29th June 2022.

41. Kiarie Mwaura, 'The Kenyan Regulation of Company Directors: An Analytical Study' (PhD Thesis, University of Wolverhampton 2003) 35.

42. Ibid 56.

43. (1915) AC 705.

44. Mukul Gulati, 'Board of Directors: The Importance of good corporate governance in family-run businesses' *The Economic Times* (India, 8th July 2022 https://economictimes.indiatimes.com/small-biz/hr-leadership/leadership/board-of-directors-the-importance-of-good-corporate-governance-in-family-run-businesses/articleshow/77297720.cms accessed 8th July 2022.

many family enterprises lack a well-constituted board. In reference to the agency theory, board composition refers to the ratio of executive to non-executive directors on the board.[45]

A properly constituted board should have more independent non-executive directors than executive directors to enhance its independence and minimize conflicting interests in decision-making. Executive directors have executive roles within the organization, while non-executive directors lack such roles. They are mainly recruited to bring in their skills and experience and enhance the quality of decision-making on the board. However, board composition is a multifaceted concept as various measures of board composition exist including diversity in skills and experience and CEO duality.[46] Board composition is a major factor influencing the success of a corporate entity.

The Legal Framework on Board Composition

The Companies Act 2015 provides that directors should act within their powers as prescribed by the company's constitution.[47] Directors are legally obliged to foster the organization's success,[48] exercise independent judgment in decision making,[49] exercise reasonable care, skill, and diligence while performing their roles[50] and avoid conflicting interests.[51] The board should be structured to ensure that the directors' duties are fulfilled for the benefit of the company and its stakeholders. However,

45. Muchemwa, Munyradadzi Raymond, Padia, Nirupa and Chris William, 'Board Composition, Board Size and Financial Performance of Johannesburg Stock Exchange Companies,' (2016) South African Journal of Economic and Management Sciences,497.

46. Amira Akhmetava and Yulia Betamunekueva, 'Board Composition and Financial Distress: An Empirical Evidence from Sweden and Denmark' (2014) http://www.diva-portal.org/smash/get/diva2:732206/FULLTEXT01.pdf accessed on July 12th, 2022.

47. The Companies Act 2015, s 142.

48. Ibid s 143.

49. Ibid s 144.

50. Ibid s 145.

51. Ibid s 146.

the Act does not advise family enterprises on how their boards should be constituted in terms of size, experience, expertise, and the ratio of executive to non-executive directors.

The Code of Corporate Governance for Issuers of Securities to the Public provides that the board should be of a size that ensures that the company's strategic goals are met.[52] It further provides that the board should not be too large so as to inhibit constructive dialogue and pose challenges in decision-making.[53] Conversely, the board should also not be too small so as to compromise diversity in skills.[54] The Code recommends that independent non-executive directors should constitute at least one-third of the board.[55] These provisions are relevant to family enterprises, as they could ensure diversity of skills and board independence. However, the Code is only enforceable against issuers of securities to the public. Further, the Code does not define independence in the context of family enterprises. Independent members in a family enterprise would mean board members that are not part of the founding family and contribute to mitigating conflicting interests in decision making. The Code recommends that the board establishes relevant committees to perform specific functions such as audit, risk management, and governance.[56] This provision is fundamental and useful to larger companies. However, it may be expensive and impractical for smaller family enterprises with few directors to appoint various board committees.

The Mwongozo Code similarly provides that at least one-third of the board should consist of independent members.[57] Independent members in State Corporations (SCs) are described as those who do not serve the

52. The Code of Corporate Governance Practices for Issuers of Securities to the Public, Recommendation 2.1.4.
53. Ibid.
54. Ibid.
55. The Code on Corporate Governance for Issuers of Securities to the Public, Recommendation 2.1.3.
56. Ibid, Recommendation 2.2.2.
57. Ibid, Recommendation 1.1 (8).

National or County Government and do not have a relationship with the state corporation in question.[58] The Code prescribes that the board's role should be separated from that of management[59] and therefore prohibits CEO duality. This provision is useful to family enterprises as it could minimize chances of unfettered discretion in decision making. However, this Code is only enforceable against state corporations and not family enterprises. Further, it only defines independence in the context of SCs and not family enterprises and therefore does not guide such organisations on how they can have independent boards.

The Principles for Corporate Governance by PSICG recommend that the board should include a balance of executive and non-executive independent directors so that no individual or group's interests dominate in decision-making.[60] The justification given under the principles for the separation of the CEO and Chairman's roles is to prevent a situation where one party has unfettered discretion in decision-making.[61] The Code of Governance for Private Organisations by ICS additionally proposes a higher threshold for non-executive directors. It provides that at least two-thirds of the board should consist of non-executive directors. Further, the Code prescribes that the board should have at least five members. The provisions prohibiting CEO duality and prescribing for independent boards are relevant to family enterprises as they could inhibit poor strategic decision making and enhance sustainability. Nonetheless, the Principles by PSIG and the Code of Governance by ICS, do not take into account the overlap between the familial relationships and business in family enterprises. Therefore, they do not define board independence in a family enterprise setting. There was a lack of consideration of the

58. Ibid.
59. Ibid, Recommendation 1.22 (2).
60. Private Sector Initiative for Corporate Governance (n 35) 12.
61. Ibid.

unlisted family enterprises, a factor that renders the current corporate governance law ineffective in addressing the governance challenges of family enterprises.

Lack of Proper Board Composition in Tusker Mattresses Limited

As previously highlighted, after the founder's death, the board of directors consisted of his five sons. Stephen Mukuha Kamau, the third-born son, became the Managing Director and CEO of the company, while John Kamau, the first-born son, was appointed Chairman of the board. The only external board member at this time was Frank Kamau, the finance director.[62] However, he lacked independence as he was heavily influenced by the other board members. The board consisted of family members who were the company's sole shareholders. Therefore, it lacked independent and professional members which affected the nature of its strategic decisions.

Following the scandal in 2012 when Yusuf Mugweru filed a suit against his brothers as directors of Tuskys for alleged misappropriation of funds, the company appointed Mr. Dan Githua as CEO and Managing Director. Mr. Githua was the first Managing Director who was not a family member. He had been the company's head of internal audit for three years up to 2012 and had been a consultant to the board.[63] The company appointed him as CEO as it was desirous of bringing professionalism to the board in order to enhance its reputation in anticipation of having its shares listed in the Nairobi Securities Exchange.[64] Unfortunately, his

62. Brian Wasuna 'Kenya: How Tuskys' Directors Lived Large as the Retailer Struggled' *The Daily Nation* (Kenya, 25th February 2021) https://allafrica.com/stories/202102250444.html accessed 26th July 2022.

63. Kennedy Kangethe, 'Tuskys hires CEO ahead of Public Offer (5th May 2015). https://www.capitalfm.co.ke/business/2015/05/tuskys-hires-ceo-ahead-of-public-offer/ accessed 26th July 2022.

64. Ibid.

appointment as CEO barely lasted a year as some of the shareholders' family members ousted him from his office.[65] His ejection from office was because some family members were not agreeable to some of the changes he made to the company's management structure. Further, they claimed he had been disrespectful to the company's stakeholders.[66] This is illustrative of the discomfort that family members may have with regard to external directors, a factor that might inhibit the implementation of innovative ideas.

It is evident that the board lacked independent directors who could act as gatekeepers to ensure proper governance and decision-making. As a result, it made poor decisions that negatively impacted the organisation's financial performance. Such decisions included: shareholders were awarded dividends amounting to two hundred and six million shillings in 2009 and 2010;[67] directors cumulatively earned salaries amounting to thirty-seven million shillings, meaning each director was paid a monthly salary of five hundred and thirteen thousand, eight hundred and eighty-nine shillings per month in 2009;[68] and in 2010, directors cumulatively earned a salary of forty six million shillings, meaning that each director earned a monthly salary of six hundred and thirty eight thousand, eight hundred and eighty nine shillings.[69]

The company could not afford to pay out such high amounts of dividends and salaries as evidenced by the financial distress it incurred in the longrun. Numerous related party transactions could be identified from the company's financial statements.[70] Notably, many of these transactions

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65. Yvonne Kawira Mutisya 'Kenya: How Tuskys boss ejected from office' *The Standard (*Kenya, 24th February 2016) https://www.standardmedia.co.ke/entertainment/the-standard/2000192954/tuskys-boss-ejected-from-office accessed 29th July 2022.
66. Ibid.
67. Brian Wasuna (n 65).
68. Ibid.
69. Ibid.
70. Ibid.

were not conducted at arm's length.[71] These decisions negatively affected the company's financial performance. An independent and qualified board would have mitigated the risk of implementing such egoistic decisions that in the long run adversely impacted the financial performance of the company.

Stakeholder Accountability

A company's stakeholders are critical contributors to its survival. It is, therefore, fundamental for the directors to consider stakeholders' interests during decision-making. This would ensure that a good relationship and understanding between the corporation and its stakeholders is maintained which is crucial for survival of the company. However, many family enterprises do not recognize their responsibility towards stakeholders and do not hold themselves accountable to them. The lack of stakeholder accountability in family enterprises leads to consequences that inhibit their operations and threaten their survival to future generations. One consequence is family wrangles due to lack of appropriate disclosures of information. Another consequence is the failure to deliver on contracts with suppliers, creditors, and employees, which turns these relationships sour to the extent that the stakeholders refrain from granting essential services to the operations of the family business.

Corporate accountability refers to an organization's preparedness to explain its acts, omissions, and strategic decisions.[72] Stakeholder Accountability is based on the stakeholder theory which recognizes that a corporate body is obliged to realize its stakeholders' interests. These stakeholders include its shareholders, consumers, creditors, and suppliers.

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71. The East African, 'Trouble in the Empire: An inside look at Tuskys Supermarkets family drama'(28th April 2012) https://www.theeastafrican.co.ke/news/Trouble-in-the-empire--An-inside-look-at-Tusky-family-drama/-/2558/1395600/-/v4bb53/-/index.html accessed July 26th, 2022.

72. Andreas Rosche and Daniel E. Esser, 'From Stakeholder Management to Stakeholder Accountability,' (2006) 65 Journal of Business Ethics, 251-252.

Stakeholder accountability involves expanding the frontiers of corporate governance by extending corporate accountability to stakeholders. It would therefore include making adequate disclosures to stakeholders on the conduct and performance of the company while also considering their interests in decision-making and ensuring that contractual obligations to the various stakeholders are fulfilled.[73] Stakeholder accountability addresses the information needs of all the organization's stakeholders.[74]

The Legal Framework on Stakeholder Accountability.

The Constitution of Kenya 2010 is our grund norm and binding on all natural and corporate persons.[75] It provides that accountability is a core governance principle.[76] Pursuant to this provision, family enterprises as corporate persons are obliged to be accountable to their stakeholders. However, the Constitution does not prescribe the methods through which family enterprises can be accountable to stakeholders. The Companies Act recognizes that directors are obliged to consider stakeholders' interests in decision-making. According to section 143 of the Companies Act, directors are required to perform acts which promote the corporation's success and, in the process, consider its employees' interests and the need to maintain a good relationship with its suppliers, consumers and creditors. Directors are also obliged to consider the implication of the organization's activities on the community and environment. Therefore, this section acknowledges that decision-making should not just be shareholder-centric, but should consider the needs of all stakeholders. Nonetheless, just like the Constitution, the Act does not prescribe methods of accountability.

73. Ibid.
74. Ibid.
75. The Constitution of Kenya 2010, Article 2 (1).
76. Ibid Article 10 (c).

Pursuant to the Code of Corporate Governance Practices for Issuers of Securities to the Public, accountability is a pillar of good governance. Therefore, directors should be able to give justifications to stakeholders for decisions made.[77] Some of the mechanisms proposed by the code for promoting corporate accountability include ensuring the integrity of the corporation's financial statements by having an internal audit function, an audit committee, and an independent external auditor. The company's internal audit function would ensure that the internal controls and operating systems are functioning efficiently while the audit committee oversees the internal audit function. The audit committee also defines the scope of the audit to be conducted by the external auditor. The external auditor evaluates the company's financial statements and renders an unqualified report on whether they accurately reflect the company's financial position. Integrated reporting is recommended to give stakeholders a holistic view of the company and promote adequate disclosure. Integrated reports contain data regarding the organisation's governance structure, financial performance and strategy. These provisions provide relevant mechanisms through which family enterprises can be accountable to stakeholders. However, this code is only binding upon issuers of securities to the public.

The Mwongozo Code prescribes similar methods of promoting accountability as those provided by the Code of Corporate Governance Practices for Issuers of Securities to the Public concerning audits and financial reporting. The Code recognizes the importance of State Corporations effectively managing their relationship with stakeholders to realize their objectives. It provides measures through which the maintenance of good relationships with stakeholders can be achieved. One of the mechanisms proposed by the Code is that a corporation should have a written stakeholder management policy which should be

77. The Code on Corporate Governance for Issuers of Securities to the Public, Recommendation 5.1.1(b).

reviewed regularly.[78] Further, the code provides that state corporations should identify the stakeholders' rights and interests and consider them in decision-making.[79] The code recognizes that disputes may arise between the corporation and its stakeholders and therefore encourages that such conflicts are resolved amicably through alternative dispute resolution mechanisms instead of litigation.[80] Family enterprises could also benefit from implementing mechanisms to maintain good relationships with stakeholders as those proposed by the Mwongozo Code. However, family enterprises are not state-owned and therefore fall outside the Mwongozo Code's scope.

The Principles of Corporate Governance by the PSICG provide that an organisation's board is obliged to identify the corporation's stakeholders and establish policies on how to relate to them. Under the principles, the company should also provide redress to stakeholders whose legal rights are violated.[81] The Code of Governance for Private Organisations by the ICS provides that disclosure of relevant information to stakeholders enhances stakeholder confidence.[82] Some pertinent information that the company should disclose to stakeholders includes the company's governance structure, policies on conflicts of interest, whistleblowing, procurement, and ICT. The code has similar provisions for maintaining good stakeholder relationships as those prescribed by the Mwongozo Code. These include consideration of stakeholders' interests in decision-making and amicable resolution of disputes that may arise with the stakeholders. The PSICG principles read with the ICS Corporate Governance Code provide useful recommendations on corporate accountability that are relevant to family enterprises. However, these codes are not binding on family enterprises. Therefore, there is laxity in

78. The Mwongozo-The Code of Governance for State Corporations, Recommendation 6.1 (b) and (c).

79. Ibid, Recommendation 6.2 (b).

80. Ibid, Recommendation 6.3 (b).

81. Private Sector Initiative for Corporate Governance (n 35)20.

82. Ibid.

their application especially in family enterprises. There is need for more sensitization on why stakeholder accountability is essential for family enterprises.

Lack of Stakeholder Accountability in Tusker Mattresses Limited

Tuskys failed to fulfill its contractual obligations to its various suppliers and service providers. This was revealed when several complaints were made to the Competition Authority of Kenya (hereinafter referred to as the Authority) that the retailer failed to pay for goods extended on credit in good time. Some suppliers that complained against Tuskys included Westside Construction Company which maintained and serviced the company's store lifts and elevators. The service provider claimed that the company owed it over four million, seven hundred thousand shillings.[83] Phontains Control (K) Limited complained of late payment for services rendered to the company and the unilateral termination of the supply contract.[84] Further, Exxon Trading Company Limited, and Kartech Engineering Limited complained of non-payment of fees for services rendered.[85]

After thoroughly investigating the retailer's debt portfolios, the Authority discovered that Tuskys was heavily indebted to its suppliers. The company had abused its buyer power according to section 24 A (5) (1) of the Competition Act of Kenya. The Competition Authority, therefore, directed that the company avails its financial statements and debt portfolio.[86] The Authority further directed that the company develops a debt settlement plan to settle any outstanding financial obligations with

83. Competition Authority of Kenya, *Competition Authority of Kenya Annual Report* 2020-2021, 278-280.
84. Ibid.
85. Ibid.
86. Press Release by the Competition Authority of Kenya dated 20th July 2022.

suppliers.[87] In addition to the numerous complaints made by suppliers to the Competition Authority, other suppliers opted to file a petition for liquidation against the company to recover their debts. These included Hotpoint Appliances Limited and Syndicate Agencies Limited.[88] However, the court allowed the adjournment of the liquidation petition hearing to allow the company to present its restructuring plan.

Equity Bank Kenya Limited extended banking facilities to Tuskys in 2014.[89] Tuskys created a charge over one of its properties, Land Reference Number 209/11392 (IR. No. 54287), where its Tom Mboya Street outlet was located, to secure the loan advance. The company defaulted on its obligation to repay the loan. The bank sought to sell the property under section 90 of the Land Act. The retailer had successfully applied for an injunction to stop the bank from auctioning the property. However, Justice Majanja allowed Equity bank to proceed with selling the property through a public auction to recover the outstanding liabilities owed by Tuskys. He allowed the statutory sale to avoid a situation whereby the bank was prevented from exercising its legal right due to insolvency proceedings to which the bank was not privy to.[90] The company also owed Diamond Trust bank, two million, five hundred thousand shillings in relation to several banking facilities extended to the company, including term loan and overdraft facilities.[91]

87. Ibid.

88. Tusker Mattresses Limited v Hotpoint Appliances Limited (Insolvency Cause E018 of 2020) [2021] KEHC 276 (KLR) (Commercial and Tax) (26 November 2021) (Ruling).

89. Boniface Otieino,'Equity kicks off auction of Tuskys Limited over Kes.650 million debt' *Business Daily Africa (*Kenya, 15th February 2022) https://www.businessdailyafrica.com/bd/corporate/companies/equity-kicks-off-auction-of-tuskys-over-sh650m-debt-3716954 accessed 9th August 2022.

90. Tusker Mattresses Limited v Equity Bank Kenya Limited and another (Insolvency Petition E018 of 2020) [2022] KEHC 258 (KLR) (Commercial and Tax) (29 March 2022) (Ruling).

91. Kepha Muiruri, 'Tuskys discloses Kes 2.8 billion Equity, DTB debt' (26th October 2020) https://www.citizen.digital/business/tuskys-discloses-ksh-2-8-billion-equity-dtb-debt-349021 accessed 9th August 2022.

Private companies are not mandated by law to avail their financial statements or information related to governance to their stakeholders. This creates a loophole for impropriety on the part of miscreant directors. In the case of Tuskys, the company did not have external auditors to verify the integrity of their financial statements. Tuskys had reported in 2020 that it had a debt to the tune of eight hundred and eighty-four million, three hundred thousand shillings. However, a financial review by the Competition Authority, revealed that the company had understated its debt by four hundred million, nine hundred thousand shillings.[92] The company was not honest with its stakeholders about its financial position, demonstrating a lack of accountability to its stakeholders. Accountability to stakeholders would have mitigated financial impropriety in the company.

Employees are instrumental stakeholders of any company as they carry out its daily operations to ensure that its specific objectives are achieved. Therefore, corporations are not functional without their employees. In 2020, when the cashflow problems of Tuskys began to become more evident to the public, they failed to pay their employees for three months. This prompted the employees to strike against the company for non-payment of their dues. Several employment contracts were arbitrarily terminated.[93] The strikes and demonstrations outside the supermarket's outlets further disrupted the company's operations and gave it bad publicity deteriorating its financial health further as it caused a major decline in sales.

From the case study of Tuskys, it is observed that stakeholders are instrumental to the survival of any corporation. It is, therefore, important for family-owned companies to be accountable to their stakeholders.

92. Mwakaneno Gakweli, 'Tuskys Suppliers' Debt is due on July 16-CAK' https://kenyanwallstreet.com/tuskys-suppliers-debt-is-due-on-july-16-cak/ accessed 7th March 2023.

93. Judah Ben-Hur, 'Tuskys Employees' strike enters second day' *The Standard (*Kenya, 1st October 2020) https://www.standardmedia.co.ke/business/business/article/2001388408/tuskys-employees-strike-enters-second-day accessed 20th August 2022.

Firstly, by prioritizing and fulfilling their obligations to their stakeholders. Secondly, by making adequate disclosures to them to avoid making selfish decisions and to demotivate miscreant directors. Lack of stakeholder accountability makes stakeholders lose their confidence in the corporation, and once this happens, they begin to withdraw their support from the corporation.

Specific Recommendations

Succession Planning

Lack of proper succession planning threatens the sustainability of family enterprises.[94] Succession can be a great strategic opportunity for the growth of family businesses when heirs of the company's founding directors are trained to become successors.[95] Family governance refers to the structures and processes employed by families that own enterprises to organize themselves and guide their relationship with the enterprise.[96] The focus of family governance is to provide the family members, involved in the business, with a shared sense of identity and mission and enhances the enterprise's sustainability. [97]

In order to mitigate the challenge of poor succession planning, family-owned companies should consider implementing the following family governance mechanisms:

i) **Establishing family constitutions that encompass written succession plans**

94. Leonardo Roth, Maria Clara Heinz Tissot and Roberto Birch Conclave, 'Family-Owned Business and Governance: A multiple case study in Brazil' (2017) 19 Journal of Public Administration 96, 97.

95. Ibid 100.

96. Deloitte, 'What is 'family governance''https://www2.deloitte.com/uk/en/pages/private-markets/articles/family-governance.html accessed 22nd August 2022.

97. The Institute of Family Business Research Foundation, '*Family Business Challenges No.6 Building Family Governance'* (2021) 1.

Developing a succession plan begins with the founder identifying his or her goals for the company.[98] If the Founder would like to pass on the enterprise to future generations, then he or she must identify successors that can realize that goal. For a succession plan to be effective, it should be in writing so that members of the organization know how the succession process will take place. A written succession plan would create clarity and certainty in the succession process. It would minimize opposition and lack of respect for the chosen leaders from the rest of the family members. It would also ensure that skilled leaders who are dedicated and well-prepared for the job are chosen according to a concise criterion. A family constitution is a written document that contains the goals, vision, mission, and values that the founder and the shareholder share concerning the company.[99] Therefore, the written succession plan could be contained within the family constitution.

ii) Establishment of a family council

The family council is a crucial family governance institution. It is the representative body of the shareholders in the family enterprise.[100] The council discusses family matters that have a bearing on the business. It is noteworthy that the family council does not replace the board's role in setting the enterprise's strategic direction. However, it defines the family's vision and mission for the company. It also ensures that family matters are discussed at the family level and do not spill over to the business. This study recommends that the family council takes up the drafting of succession plans in consultation with professionals, such as the family lawyer, to ensure clarity on the succession process. The family council could also be important in ensuring that chosen successors

98. Stephen Clifford, *An Owner's Guide to Business Succession Planning* (2nd Edition, Kent Popular Press 2010) 11.

99. Corporate Governance Guidance and Principles for Unlisted Companies in the UK, Phase 1, Principle 9.

100. The Brazilian Code of Best Practices of Corporate Governance, Principle 1.10.

undergo the requisite training and education needed to take up the role of CEO, this is relevant especially where the successor is identified among the family members following suitable criteria.[101] Where no eligible successor is identified, the family council could also engage the services of professional headhunters to identify a suitable candidate for the role.[102]

Board Composition

For a company to be in the right strategic direction, it needs to have an effective board. For the board to be effective, it must be structured appropriately. However, there is no one size fit all approach to board composition.[103] It is relative to the company, its size, scale of operations, and its long-term goals. In order to ensure a properly constituted board, family-owned companies should consider implementing the following governance mechanisms:

i) **Involvement of the family council in preparing family employment policies and appointing eligible family members to the board.**

As a family governance institution, the family council plays a vital role in drafting family policies. One of the policies that should be drafted is a family employment policy.[104] The family employment policy would ensure that members of the founding family understand that it is not their birthright to hold executive positions within the company.[105] They would have to work hard and meet specific qualifications to participate

101. The Brazilian Code of Best Practices of Corporate Governance Principle 1.10 1 (b) (vii).

102. International Financial Corporation, 'IFC Family Business Governance Handbook' 25 https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+cg/resources/guidelines_reviews+and+case+studies/ifc+family+business+governance+handbook accessed 10th September 202251.

103. Deloitte, 'Board Composition: Greater than the Sum of its Parts' (2016) https://www2.deloitte.com/us/en/pages/center-for-board-effectiveness/articles/on-the-boards-agenda-us.html accessed 13th September 2022.

104. International Financial Corporation (n 105) 25.

105. Ibid.

in the organisation's business. The employment policy should include minimum requirements such as obtaining a bachelor's degree in a particular field related to the company's business.[106] A higher threshold should be established for membership into the board, such as a master's degree in a relevant field and external working experience for a certain number of years. The council could employ the services of a professional, for instance a lawyer, in drafting the policy. The policy should also prescribe how many family members should be appointed, given that the board should have more independent members.

ii) Appointment of an advisory board for family enterprises small in size and scale of operations.

As an interim measure, the family council may appoint an advisory board of independent professional members.[107] The advisory board's role would be to guide the family board on specialized matters such as risk and financial management.

iii) Appointment of independent members of the board

Independent members of the board in family enterprises would mean board members with no familial relationship with the company's shareholders. The case study of Tusker Mattresses established that family-owned companies prefer to retain control over the company. Therefore, they refrain from appointing many independent board members. However, family boards are in dire need of these independent members to ensure there is constructive debate and healthy dissent. Having independent board members would also ensure that the management is adequately challenged in its operations for the company's benefit. Further, the

106. Ibid.

107. Corporate Governance Guidance and Principles for Unlisted Companies in the UK, Phase 1, Principle 2.

number of independent members should exceed the number of directors appointed by the family council. The board's independent members should supplement the company's skill requirement.

Stakeholder Accountability

Maintaining a cordial relationship with stakeholders is essential for a company to continue obtaining resources necessary for its operations.[108] Therefore, jeopardizing the relationship with stakeholders places the financial and reputational health of the company at risk. A company's good relationship with its stakeholders is maintained through accountability. Accountability is enhanced by responsibility and adequate disclosures. To promote stakeholder accountability in family enterprises, family enterprises should ensure:

i) Disclosure of Annual Reports to Stakeholders

Family-owned companies in Kenya are not mandated by statute or regulation to disclose their financial or governance information to stakeholders. Accountability is enhanced through adequate disclosures and by being responsible. It would therefore be prudent as a matter of best practice for family-owned companies to disclose to their stakeholders how the company is performing and utilizing the resources obtained from its stakeholders. This ensures that the board does not act beyond the limits of its powers and misuse resources for its benefit. Through honest disclosures, stakeholders can also advise the company on strategies that may be put in place to improve the company's operations and put it back in a position of profitability in the case of financial distress.

108. Migle Matuleviciene and Jurgta Stravinskiene, 'The Importance of Stakeholders for Corporate Reputation' (2015) 26 Engineering Economics' 75, 77.

ii) Establishment of Whistleblowing and Complaint Handling Systems

Family enterprises should establish systems whereby stakeholders are able to report any malpractices or complaints that they have concerning the company. [109]These complaints could be about governance, management, or lack of performance of contracts. The complaints should be investigated, and remedial action taken. This will enhance the stakeholders' confidence in the company and enable them to continue providing the company with the resources it needs to continue operations. It is far better for family-owned companies to settle complaints by stakeholders at the corporate level before the same escalates to the public, as this would ruin the company's reputation.

General Recommendations

Codification

Codification is considered one of the most reliable methods of keeping up with the necessary evolution of laws.[110] Having the governance structures of family enterprises embodied under one corpus ensures that they have a reference point for suitable governance structures applicable to them. It would clarify what family-owned companies need to do to improve their governance. Therefore, it is recommended that proposals on how to ensure succession planning, board composition, and stakeholder accountability in family-owned companies be codified. This would enhance the implementation of good governance practices in family enterprises and facilitate their survival to future generations. Although properly designed laws, regulations, or codes would not be helpful

109. The Brazilian Code of Best Practices of Corporate Governance, Principle 5.2.

110. Daniele Bourcier and Pierre Mazzega, 'Codification, Law, Articles and Graphs' (2007) 165 Frontiers in Artificial Intelligence and Applications 29.

without mechanisms to ensure their enforcement,[111] clarifications of rules would raise the standards of corporate governance and ensure that its enforcement is more achievable.[112]

Sensitization

In addition to codification, it would be necessary for Kenyan family enterprises to be sensitized on the need to set up governance structures and not just take shortcuts. Although founders have sentimental attachment to their establishments, exiting the company through circumstances such as death is inevitable. Therefore, founders need to be sensitized on the need to employ proper family and corporate governance structures to ensure that what they worked so hard to establish is passed on to future generations. It is well-known that family-owned companies, especially at the outset, do not comply with proper governance practices. This is attributable to them not knowing how to properly manage the businesses and ensure that family matters do not seep into the business. Creating awareness of family and corporate governance structures would assist family-owned companies in compliance. This could be done through awareness campaigns and seminars with invitations to owners of family-owned businesses. Another reasonable approach could be the publication of booklets or pamphlets on family governance and corporate governance for family businesses by organizations keen on ensuring compliance with good governance practices. These include the Institute of Certified Secretaries of Kenya, which is dedicated to promoting excellence in governance in Kenya, the Capital Markets Authority that licenses companies as market intermediaries, and the African Family Business Association, which is a regional association whose purpose is to help African family business succeed.[113]

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111. Kiarie Mwaura (n 41) 249.
112. Ibid 250.
113. African Family Business Association website https://www.africanfamilyfirms.org/african-family-firms-what-we-do accessed on 13th September 2022.

In all, family-owned companies need to evolve in their governance practices to enable them to survive to future generations. This article has highlighted the importance of codification to ensure that family-owned companies have a reference point for appropriate family and governance structures to mitigate some of their common governance challenges and enhance sustainability.