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9B21M048

BauZentrAL: Compensation and Governance in the Family Firm

Stephen Sapp wrote this case solely to provide material for class discussion. The author does not intend to illustrate either effective or ineffective handling of a managerial situation. The author may have disguised certain names and other identifying information to protect confidentiality.

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It was June 12, 2017, and Pieter Meister and Jens Schmidt, the chief executive officer (CEO) and chief financial officer (CFO), respectively, of BauZentral, were leaving the most recent meeting of the family shareholders. They were reviewing the meeting’s discussion, regarding where the firm wanted to be in five years and how to get there. They knew they had only one month before the next meeting to present their recommendations on how to update the firm’s organizational structure and employee compensation package to optimally manage the increasingly sprawling BauZentral business.

The challenges with managing the company were a result of the significant acquisition strategy that had started in the years before the retirement of the previous CEO, Josef Meister, Pieter’s father. Pieter, who had taken over in 2014 as the company was starting to deal with the growth associated with its successful international acquisition strategy, felt that for the company to survive, it needed to grow, which meant expanding beyond its base in Switzerland.

Because these acquisitions were relatively recent, Pieter, as the newly appointed CEO, was tasked with integrating these firms under the BauZentral umbrella. He needed to ensure BauZentral took advantage of everything its acquisitions had to offer. Pieter knew he would need to restructure the organization to achieve the firm’s goals of growing its footprint around the world and becoming a truly global supplier, while also respecting the family’s values.

The problem was that the company had been structured to be a tightly held and tightly controlled family business; however, this structure was ill-suited to the new reality. Rapid expansion across borders meant that BauZentral needed to expand its decision-making base to (1) allow for the various affiliates to feel more involved in the decision-making process; (2) benefit from the foreign affiliates’ unique knowledge of the local markets, which head office might not fully appreciate; and (3) allow those working at the affiliates to benefit financially from their role in making the expansions work in different countries. Pieter and Jens needed to take a step back and determine what types of changes to the organization would help to achieve these goals. How should the governance structure be changed? How should the compensation structure be changed?

Before working on the specifics, they felt it was important to better understand the environment in which they were operating.

Outlook for the Building Industry

The building industry had a marginally positive outlook globally for 2018 and beyond. Part of the reason for BauZentral looking to expand globally was that Europe had a marginally negative growth outlook as perceived by the rest of the world, especially by the Asia-Pacific (APAC) countries, which were seeing improvements with marginally positive growth. Forecasts for the industry recognized that the return of inflation, due to increasing energy costs, would likely limit any further progress in margins.

Many assumed that over 2018 and 2019, supportive macroeconomic fundamentals would be observed in North America and continental Europe (except the United Kingdom, which was experiencing increased uncertainty due to Brexit, the withdrawal of the United Kingdom from the European Union in 2020). APAC countries were forecasting a mild demand recovery and price stabilization. On the downside, risks were posed by the relaxed financial discipline in developed markets and overcapacity and political risk in emerging markets. Weakening political cohesion in continental Europe and the possibility of a hard Brexit (i.e., a sharp break in the economic relationship between the United Kingdom and the European Union) could impair business sentiment in those regions.

With relatively weak growth forecasted, many believed that companies would continue to use their cash flow to undertake growth opportunities. The forecast for continued market consolidation in developed markets would mainly involve small, regional manufacturers and distributors. BauZentral’s growth strategy followed this pattern.[[1]](#footnote-1)

BauZentral

The company started as a small electrical company in Zug, Switzerland, in 1952. Since that time, it had grown to become a multinational enterprise with its headquarters in Switzerland but with production facilities and sales offices in various countries. BauZentral’s three product lines were electrical systems, plumbing systems, and smart security and energy solutions. BauZentral products were used in Europe, North America, Africa, Asia, and Australia.

BauZentral had an established position and reputation in Europe. Despite the strong position in its domestic market, the company’s strategy was to increase turnover and market share as much as possible in each market in which it operated. The company’s global focus was highlighted by the BauZentral Group having sales offices and production facilities in various countries. Each production facility had its own specialty, which allowed BauZentral to expand its product offerings globally using products manufactured in the most efficient manner at its different facilities. From its headquarters in Switzerland, BauZentral managed the entire process, from product development to manufacturing to sales.

To succeed with this business model, BauZentral developed a highly engaged team who were all ambassadors of the BauZentral brand and worked to sell its products globally, not just in the home market where they were originally developed. Although the company originally focused on production, it was now more actively focused on improving its sales and marketing to take advantage of its newly acquired and growing production expertise. As the size of the organization increased, it became more difficult to integrate the processes and procedures. The challenge facing Pieter was to determine how to keep the different teams acting in the best interests of their local customers while maintaining the company’s global focus and thus considering how its decisions impacted both the local market and the global firm (i.e., BauZentral needed to think globally and act locally, but it was thinking locally and acting locally).

The BauZentral group identified several trends influencing its business: global economic growth, technological developments, financial systems, the quest for energy, worldwide conglomeration, and demand for safety.

Global Economic Growth

Due to world population growth, industrialization, and the technological revolution, the world economy would continue to grow. Although the CEO and CFO saw growth in BauZentral’s markets, the majority of this growth would take place outside of the European Union.

Technological Developments

Technology had enabled BauZentral to do things that its management previously could not have imagined. Technology changed products, services, and processes in an unbelievably fast way. New materials were being developed, production technology was becoming less expensive, and new supply chains and sales channels were emerging.

Financial Systems

The world’s financial systems were being challenged. A lack of trust resulted in increased rules and legislation. As a result, it could be more difficult for companies to finance their future growth.

The Quest for Energy

A worldwide quest for energy would change the energy supply industry. Renewable energy was becoming more important, and market-changing developments were taking place in the nuclear and fossil energy industries.

Worldwide Conglomeration

Urbanization was occurring all around the world. Urbanization was changing housing needs, infrastructure, and transport. In parallel, conglomeration was creating huge companies with higher demands.

Demand for Safety

Demand was increasing for more regulation and legislation to create a feeling of safety. As a result, there was an increased requirement for approved and certified products.

Reorganization

To start addressing the concerns related to the struggles of managing this growth, Pieter had started restructuring the most senior levels of the organization. Specifically, the global operations were divided into four regions based on geographic, cultural, and product similarities: Eastern Europe, Western Europe, North America, and the Rest of the World. Each region had a three-person regional management board that was responsible for making its region’s daily decisions and for overseeing strategic and operational decisions. These regional boards all reported to the main management board located at the head office in Zug.

Although this structure provided clear reporting relationships for senior managers and put local managers in charge of operations at the regional level, it left as an open question how to most efficiently run the individual operations within each region. As this new structure started to demonstrate its value, the focus moved to how to increase and improve individual employee engagement. A consulting firm interviewed BauZentral’s employees to better understand their views on this rapid growth. Although employees felt engaged, they were not entirely satisfied with their remuneration. This finding suggested that BauZentral might want to consider changing the compensation and incentive structure to both improve employee compensation and align the compensation with the firm’s long-term goals by nurturing in their employees a stronger connection with the firm and its success.

Pieter, as the CEO, and as a family member and shareholder, knew that any decision would need to address as many of the family values as possible while simultaneously addressing the business concerns. Jens, as the CFO, and as one of the few non-family shareholders, knew that he needed to ensure the firm was meeting its financial goals while also addressing the family’s values. This balance was challenging because the family goals were not always easily quantifiable and achieving these non-financial goals would have financial implications.

Ownership Structure of BauZentral

To understand how decisions were made at BauZentral, it was important to first understand the structure of the family ownership and thus how the family owners made decisions. The family had established a trust to hold all of the shares on behalf of the family members. Although the shares had the economic rights to dividend payments from the firm, the dividends were spread across 18 family shareholders according to their percentage ownership. The decision-making, however, was controlled by the trust’s four trustees, or board members, all of whom were shareholders who had been elected by the 18 family shareholders. The four trustees each had one vote. The 18 shareholders did not have the same number of shares and voting rights when voting for the trustees. Specifically, two sisters (who were also board members) each owned 25 per cent of the voting rights, and the remaining 50 per cent of voting rights were split among the remaining 16 shareholders in stakes ranging from 1 per cent to 14 per cent. As the owner of the shares, the trust was required to approve all major decisions. The board of the trust had significant confidence in its family CEO, so his recommendations held substantial sway with the board of the trust and the shareholders. Consequently, the CEO wanted to ensure that he presented the best recommendation possible to the board.

Although Pieter realized that the board of the trust would ultimately guide the decision-making process, he also knew that each family member did not interpret the family values similarly. For example, for some within the family, the financial trade-offs were most important, whereas others put more weight on the less tangible outcomes, such as highly educated and engaged employees and a culture in which the employees worked on projects that supported society and family harmony. Any decisions stemming from family values required trade-offs, which meant Pieter and Jens had their work cut out for them.

To prepare their recommendations, they needed to first ensure they had a solid understanding of all of the challenges ahead. To do this, they started by looking at where the company was and where it was going.

Current Situation

BauZentral’s growth strategy created challenges in terms of integration. The company was healthy financially (see Exhibits 1 and 2 for the firm’s balance sheet and income statement), but experienced some challenges with respect to quality and service, due to inefficiencies in the system. Growth was to be financed internally to limit BauZentral’s exposure to market conditions. Although approximately 80 per cent of turnover originated from two product groups, electrical and plumbing, high growth was expected in the security and integrated smart systems.

To increase sales across segments and geographic regions, it was necessary to determine how to align organizational culture, structure, and human resources (HR) processes. BauZentral spent significant funds on training, development, and monitoring, in an attempt to ensure it retained the best people. BauZentral’s current operations were in Switzerland, Czech Republic, Poland, Russia, the Netherlands, Italy, Germany, United Kingdom, Belgium, China, Turkey, France, United States of America, and Spain.

The firm’s stated goals included (1) achieving a turnover of CHF125 million[[2]](#footnote-2) in 2020; (2) becoming among the top three players in the markets in which the company was active; (3) earning a 20 per cent return on invested capital (ROIC); (4) attaining 30 per cent of total turnover from products less than five years old; (5) attaining 35 per cent of total turnover in 2020 realized from outside the European Union; and (6) receiving no customer complaints.

To attain these goals, BauZentral acquired a large number of firms outside of Switzerland, which resulted in substantial changes in how the business operated. In their roles as CEO and CFO, respectively, Pieter and Jens had spent the past two years redefining the strategy for the company and working with their employees to determine how to restructure the firm, both to be more efficient and to better execute its strategy. The integration of the recent acquisitions required more time than Pieter and Jens had foreseen. Pieter and Jens realized that to better use their time, they needed to delegate more authority to their employees in the different markets.

Both Pieter and Jens felt there had to be a better way to run their rapidly growing operations. Although they had recently updated their senior management structure by introducing the regional management boards, Pieter and Jens felt it would be beneficial for the employees to play an increasing role in decision-making. They wanted their employees to be entrepreneurial and to act as if BauZentral were their own company. They wanted the employees to take initiatives consistent with the overall company vision while also recognizing the unique needs of their local markets.

By setting up processes to unite all employees to consider the company’s vision in unison with their own goals, Pieter and Jens hoped to reduce the overall complexity of the organization and to make the employees feel closer to the firm. Specifically, they felt that giving their employees the opportunity to build some ownership in the firm would help create engagement. Although the firm had a global focus, it was also important to recognize that it was also competing locally.

An obvious solution was to change the compensation structure. A challenge in this regard was that, in the past, BauZentral had experimented with a flexible rewards system but it had not worked. It had failed to drive the desired alignment between employees and owners. The employees could not see the direct link between their efforts and changes in their compensation.

Starting from scratch, Pieter and Jens knew the importance of clearly defining goals before deciding on any incentive structure. The goals of the business and the shareholders were to share wealth with the people who had helped to create it, to engage with the employees, and to align the employees’ goals with BauZentral’s long-term goals.

To accomplish their goals of increased employee participation within their new organizational structure, Pieter and Jens needed to consider the potential impact these decisions would have on the firm’s decision-making. Pieter and Jens had started discussions with the family shareholders regarding increasing employees’ participation. Although the family shareholders did not reject the idea, Pieter and Jens knew that the proposal would need to take into account the family’s overall goals as outlined in the family constitution, which had been updated following the passing of Pieter’s father (more details on the firm’s family constitution can be found in Exhibit 3):

As a family company we are part of society, we are very aware of our surroundings, our position and responsibility. . . . We act in accordance with this responsibility and make sure we share the value we create, in the right balance, with our customers, employees and all other stakeholders. We have created this sustainable value for over 70 years and we are determined to make a difference for years to come.

Subject to some constraints:

It is our aim that our company remains independent as long as that is possible within the continuity thought. The family does not need to have 100% of the shares, the family always wants to retain control. As a family we want to continue to determine the direction.

To be able to transfer our business to future generations, we balance entrepreneurship with a responsible approach to risk. We see it as a strength that some of us are very entrepreneurial while others pay more attention to the risks.

Although it was clear that the family constitution provided some guidance,[[3]](#footnote-3) these goals were not easily measurable, and Pieter and Jens recognized the need to be thoughtful in their evaluation of the different alternatives. The different priorities and values across all of these stakeholders clearly meant that trade-offs would be required. For the next family meeting, Pieter and Jens had promised to present a set of alternatives to increase employee engagement going forward and an analysis of their pros and cons.

Alternatives to Increase Employee Engagement

Some of the potential alternatives that needed to be evaluated were a pension-based employee stock ownership program, long-term incentive plans, restricted stock units, short-term incentives, better working conditions, and continuing education opportunities.

Pension-based Employee Stock Ownership Program

A pension-based stock ownership program would give the employees ownership in the firm as part of their compensation or pension plan, so they could feel more connected to the firm and jointly benefit as the firm grew and increased in value. The shares that could be added to the pension fund could be real shares or phantom shares.[[4]](#footnote-4) The costs to the firm of such a plan could be mitigated if the shares were deposited into a pension plan and thus could be classified as a pension expense. BauZentral could also grant different shares for each region if the company wanted to allow for different returns in different markets. By having the shares in a pension plan, the employees would have less direct control over the shares, as the votes for the shares might be helped by pension fund trustees, who could be family members of the owners, so the employees could feel disconnected from the ownership. They would, however, benefit financially if their decisions increased the value of BauZentral.

Long-Term Incentive Plans (LTIPs)

Long-term incentive plans (LTIPs) had a long-term focus and directly rewarded employees for their performance.

Restricted Stock Units (RSUs)

Restricted stock units (RSUs) could be either shares or phantom shares. As above, the shares could be for different business segments or markets. If the employees owned RSUs, a market would need to be set up to allow employees to sell the shares they had received for good performance, and the price would need to reflect the changes in company value the employee had been involved in generating.

Options, stock appreciation rights, and performance-based shares also fell into this category. These alternatives would be similar to shares but would have a value only if the value of the firm increased. The employee would receive the cash value of the increase in the stock price over the life of the security.

Short-term Incentives

Short-term incentives directly rewarded employees for their recent performance. These incentives were typically in the form of cash bonuses given directly to the employees for meeting the company’s current targets. Such incentives aligned employees’ short-term interests with the interests of the firm, but it was unclear whether this option (short-term incentives) represented a long-term incentive. This alternative avoided issues with ownership rights but could lead to a short-term focus in decisions.

Better Working Conditions

Better working conditions included child care, nicer surroundings, shorter hours, and more flexible hours. These factors could make employees more dedicated to the firm and happier, which was a good thing, as happier employees usually meant a lower turnover rate and greater commitment to the firm; however, it was unclear whether this would mean employees would be more likely to make decisions as if they were owners.

Continuing Education Opportunities

Continuing education opportunities helped to increase both the value of the employees and employee commitment to the firm. However, it was unclear how long-term the commitment to the firm and its success would actually be.

To evaluate these alternatives, it was important to understand the trade-offs. Satisfying each stakeholder group had both monetary and non-monetary costs and benefits. Some key considerations for the final proposal were 1) the proposed alternatives had to provide equal treatment for all employees; 2) a well-prepared solution (as a participation scheme could be introduced only once); and 3) protection for employees against themselves.

Some issues to consider

Pride of Ownership

Entrepreneurs often shared ownership with key members of management to give them a stake in the company’s success, to provide incentives to retain them, and to add to their compensation without adding to payroll. Members of management usually took pride in ownership, and strove to build the value of the enterprise for both their benefit and that of the other shareholders. A tax-deferred wealth enhancement was often involved, as it allowed for capital gains to be postponed until the divestiture of the assets. However, sharing ownership with others came at a cost and with risk—the decision-making process needed to consider more shareholders. To mitigate the risks of ownership, BauZentral could use options such as pensions or trusts to hold the shares or phantom stock plans. These plans allowed employees to benefit from the appreciation of the company’s value but it did not confer ownership and control rights to the employees.

Control

Adding shareholders to a closely held company came with risks. New shareholders had a right to have access to sensitive information and a vote on key corporate decisions. This may have led to disagreements among owners at very sensitive times such as mergers and corporate restructurings. During times of great opportunity or distress from having additional shareholders could make it more difficult to successfully navigate the opportunities and risks. However, for employee stock ownership plans (ESOPs) to be effective, the employees would need to have detailed information on the firm’s operations, feel their opinions and decisions have been listened to, and be able to see the impact of their decisions, all of which had been missing in the previous attempt at employing an ESOP.

Stock but Not Stock

Phantom stock was a form of equity-linked compensation where the holder had the right to receive cash at a future point in time where the amount was based on the value of the company’s stock after the date the phantom stock was granted. Stock appreciation rights (SARs) were close cousins of phantom stock since their cash value was based upon the change in the stock price from the time the SAR was granted. In both cases, the payment was made in cash but the amount of cash was based on the stock price performance of the firm.

The cash payments were equal to the cash the recipients would have received if they had owned the same percentage of the corporation’s stock (or the appreciation in value of an equivalent amount of stock). Some plans also included the PS or SAR holder receiving dividends that would have been paid to shareholders between the time of granting and the vesting of the PS and/or SAR. Implementing a phantom stock plan should have cost less in legal and accounting fees than a formal stock option plan, but more than simply selling stock to an employee. It had, however, the advantage that no shares and thus no voting rights were given to the employees. Phantom stock offered a way to share in the financial success of a business while avoiding the risks inherent in having additional shareholders.

Valuation

An important but thus far neglected aspect of these discussions was how to value the shares. It was important to value them in a way that was deemed fair and equitable on all sides. The valuation of shares was relatively simple for publicly listed companies: use the stock price on the relevant day. However, as long as the company remained private, no public source was available for a “fair market value” of the shares. Instead, different models would need to be used to determine value.

Internally, the family used the formula shown in Exhibit 4 to establish the value of the shares if a family member wished to buy or sell shares at any point in time.

The valuation was currently 34.146 million × 1.8568 = CHF63.4 million or an enterprise value of CHF74 million (using 2015 debt levels). This valuation gives an Enterprise Value ÷ Earnings before Interest, Taxes, Depreciation, and Amortization (EV ÷ EBITDA) of approximately 7.9 times. This valuation was below the average multiple for its publicly listed peers (see Exhibit 5). Given that BauZentral was smaller than its peers, privately owned, and controlled by the family, a significant discount in its valuation was to be expected, compared with more widely held, larger publicly listed firms.

Over the years the valuation formula had changed, but the changes were minor, as the family felt the formula provided a good average that was both stable and representative. A key concern was that both Pieter and Jens recognized that this formula did not represent a fair market valuation (a condition required under some shareholder plans). Internally, some felt that even more important was having stability in the valuation (i.e., the lack of sensitivity to time and market conditions).

Conclusion

As the firm continued to work on integrating its recent acquisitions, Pieter and Jens needed to consider the best way to move forward with more actively involving employees in the company and providing the employees with the opportunity to benefit from their efforts.

Exhibit 1: BauZentral Balance Sheet, 2015–2017 (IN CHF)

|  |  |  |  |
| --- | --- | --- | --- |
|  | **2017** | **2016** | **2015** |
|  |  |  |  |
| Assets |  |  |  |
| Fixed assets |  |  |  |
| Intangible assets | 1,344,381 | 1,531,280 | 1,556,056 |
| Tangible fixed assets | 18,870,898 | 19,092,841 | 23,287,294 |
| Financial fixed assets | 1,283,774 | 1,071,011 | 1,633,464 |
| *Total fixed assets* | 21,499,053 | 21,695,132 | 26,476,813 |
| Current assets |  |  |  |
| Stock |  |  | 19,885,117 |
| Trade debtors |  |  | 11,385,267 |
| Loans to affiliated companies |  |  | 7,732 |
| Other debtors, prepayments, and accrued income |  |  | 2,551,805 |
| *Total current assets* | 37,774,751 | 35,008,623 | 33,829,921 |
|  |  |  |  |
| Cash and cash equivalents | 2,959,334 | 2,772,546 | 2,750,212 |
|  |  |  |  |
| Total assets | 62,233,138 | 59,476,301 | 63,056,946 |
|  |  |  |  |
| Liabilities |  |  |  |
| Group equity |  |  |  |
| Shareholders’ equity | 30,978,013 | 28,384,730 | 28,068,541 |
| Minority interests | 3,168,226 | 2,369,309 | 2,515,572 |
| *Total group equity* | 34,146,239 | 30,754,039 | 30,584,113 |
| Provisions | 4,165,118 | 4,224,844 | 4,832,096 |
|  |  |  |  |
| Non-current liabilities | 3,661,619 | 5,259,725 | 5,687,487 |
| Current liabilities |  |  |  |
| Amounts payable to credit institutions |  |  | 1,407,098 |
| Mortgages and other loans |  |  | 2,407,636 |
| Creditors |  |  | 8,001,602 |
| Other liabilities, accruals, and deferred income |  |  | 10,136,913 |
| *Total current liabilities* | 20,260,162 | 19,237,693 | 21,953,249 |
| Total liabilities\* | 62,233,138 | 59,476,301 | 63,056,946 |

Note: \*This is the sum of Total group equity, Provisions, Non-current liabilities, and Total current liabilities. The Total Liabilities are 30,754,039 + 4,224,844 + 5,259,725+19,237,693 = 59,476,301.

Source: Company documents.

Exhibit 2: BauZentral income Statement, 2015–2017 (IN CHF)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  |  |  | **2017** | **2016\*** | **2015** |
| Net turnover |  |  | 101,662,509 | 98,114,246 | 88,659,032 |
| Changes in inventories of finished products and work in progress |  |  | (2,401,129) | 2,679,790 | - |
| Other operating income |  |  | 642,332 | 1,465,064 | 1,099,309 |
| Total operating income |  |  | 99,903,712 | 102,259,100 | 89,758,340 |
|  |  |  |  |  |  |
| Cost of raw materials and consumables |  |  | 38,156,929 | 43,902,851 | 35,759,065 |
| Cost of outsourced work and other external costs |  |  | 22,447,149 | 20,760,825 | 21,317,629 |
| Wages and salaries |  |  | 24,030,062 | 22,349,143 | - |
| Social security and pension charges |  |  | 5,994,286 | 5,459,479 | 5,195,110 |
| Amortization of intangible fixed assets |  |  | 526,997 | 660,240 | 519,000 |
| Depreciation of tangible fixed assets |  |  | 2,993,235 | 3,976,083 | 3,313,153 |
| Other operating expenses |  |  | 101,024 | 182,740 | 20,053,882 |
| Total operating expenses | | | 94,249.682 | 97,291.362 | 86,157,852 |
|  |  |  |  |  |  |
| Operating result | | | 5,654.030 | 4,967,738 | 3,600,488 |
| Interest receivable and similar income |  |  | 29,359 | 25,061 | 20,634 |
| Interest payable and similar charges |  |  | (448,753) | (424,900) | (469,900) |
| Exchange rate differences | | | (201,668) | (149,526) | (48,710) |
|  |  |  |  |  |  |
| Result on ordinary activities before tax |  |  | 5,032,968 | 4,418,351 | 3,102,463 |
| Taxes on result from ordinary activities |  |  | (692,315) | (940,200) | (1,242,540) |
| Result on ordinary activities after tax |  |  | 4,340,653 | 3,478,147 | 1,859,924 |
| Minority interests | | | (797,705) | (382,700) | (47,690) |
| Net result |  |  | 3,542,948 | 3,095,409 | 1,812,237 |

Note: \*Due to an accounting change in 2016, some numbers in 2015 and 2016 are not entirely comparable.

Source: Company documents.

EXHIBIT 3: EXTRACT FROM FAMILY CONSTITUTION

1. VALUES IN THE FAMILY AND IN THE COMPANY

As individuals and as a family we have many values we use in our daily lives. We have inherited rules of life from previous generations and we want to live them and pass them on to future generations. As such, the following “values” guide us in the daily conduct of our business:

Responsibility

This concerns our responsibility towards the company, the responsibility of the company towards us as well as responsibility towards society in general.

Passion and fun

Respect and Tolerance

For each other’s differences in character as well as culture.

Integrity and Reliability

This includes both acting honestly and keeping appointments.

Creativity and Entrepreneurship

Ambition to grow both personally and as a company.

Prudence and Thoughtfulness

To ensure that no unreasonable risks are taken and that continuity is not compromised.

2. OBJECTIVES FOR OUR COMPANY

Out of respect for and pride in previous generations and their efforts, we want to manage our company as “good stewards.” We want to maintain, develop and transfer the company to future generations.

It is our aim that our company remains independent as long as that is possible within the continuity thought. The family does not need to have a 100% of the shares, the family always wants to retain control. As a family we want to continue to determine the direction.

3. IMPORTANT PRINCIPLES OF CONTROL

3.1. Respect and dialogue in our governance

We have set up the governance of our company anticipating the development of our family and our company. As a family we have an important role in the governance of our company, for example, by monitoring and living our values.

We respect each other’s roles. Dialogue is essential for good control on the basis of this model.

3.2 Balance between family and business

The welfare of our families and harmony in our family, we find very important. Nevertheless, we will not make decisions that go against the interests of the company.

Given the scale and required professionalism in our company, our company needs external directors.

3.3 Balance between entrepreneurship and continuity/preservation of heritage

To be able to transfer our business to future generations, we balance entrepreneurship with a responsible approach to risk. We see it as a strength that some of us are very entrepreneurial while others pay more attention to the risks.

Source: Company documents.

EXHIBIT 4: Family formula to establish the value of the shares

Share Value = Intrinsic Value × Multiplier, where the Multiplier = (1 + A)4 × (1 + MR + RP)4

A = Profitability Ratio = Average Profit or Net Income from the Income Statement over the Past 3 Years ÷ the Intrinsic Value or the Book Value of Equity from the Most Recent Balance Sheet

MR = Market Interest Rate = Long-term Deposit Rate + 1.25%

RP = Risk Premium = 4%

Currently this formula would lead to the following valuation:

A = 8.79% (2015 to 2017 Profit from the Income Statement / Intrinsic Value for That Year as Total Group Equity from Balance Sheet)

MR = 1.30% (20 year LIBOR on CHF) + 2% = 3.3%

RP = 4%

= (1 + 8.79%)4 × (1 + 3.30% + 4%)4 = 1.8568

Source: Created by the author.

Exhibit 5: Valuations of Comparable, Publicly Listed Firms

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Company Name** | **TEV/Total Revenues LTM – Latest** | **TEV/EBITDA LTM – Latest** | **TEV/EBIT LTM – Latest** | **P/TangBV LTM – Latest** |
| **Schneider Electric S.E. (ENXTPA:SU)** | 1.7x | 10.8x | 12.5x | NM |
| **Eaton Corporation plc (NYSE:ETN)** | 1.9x | 11.7x | 16.4x | NM |
| **Atlas Copco AB (OM:ATCO A)** | 3.4x | 15.2x | 18.1x | 30.6x |
| **Siemens Aktiengesellschaft (DB:SIE)** | 1.4x | 11.4x | 15.4x | 40.6x |
| **NKT A/S (CPSE:NKT)** | 0.9x | 13.4x | 23.9x | 3.9x |
| **Legrand SA (ENXTPA:LR)** | 3.1x | 14.2x | 16.3x | NM |
| **Alstom SA (ENXTPA:ALO)** | 0.8x | 13.1x | 13.3x | 3.2x |
| **Johnson Electric Holdings Limited (SEHK:179)** | 1.0x | 7.8x | 13.3x | 2.9x |
| **Rockwell Automation, Inc. (NYSE:ROK)** | 2.9x | 14.4x | 16.7x | 26.2x |
| **Emerson Electric Co. (NYSE:EMR)** | 2.7x | 12.8x | 15.1x | 13.1x |
|  |  |  |  |  |
|  |  |  |  |  |
| **ABB Ltd (SWX:ABBN)** | 1.5x | 11.7x | 15.4x | 28.0x |
|  |  |  |  |  |
| **Summary Statistics** | **TEV/Total Revenues LTM – Latest** | **TEV/EBITDA LTM – Latest** | **TEV/EBIT LTM – Latest** | **P/TangBV LTM – Latest** |
| **High** | 3.4x | 15.2x | 23.9x | 40.6x |
| **Low** | 0.8x | 7.8x | 12.5x | 2.9x |
| **Mean** | 2.0x | 12.5x | 16.1x | 17.2x |
| **Median** | 1.8x | 13.0x | 15.9x | 13.1x |

Note: TEV = total enterprise value; LTM = last twelve months; EBITDA = earnings before interest, taxes, depreciation, and amortization; EBIT = earnings before interest and taxes; P/TangBV = price to tangible book value; ENXTPA = Euronext Paris; NYSE = New York Stock Exchange; OM = Nasdaq Nordic; DB = Deutsche Borse; CPSE = Central Public Sector Enterprise; SEHK = Stock Exchange of Hong Kong; SWX = SIX Swiss Exchange

Source: CapitalIQ – search ABB, QuickComps.

1. Renato Panichi et al., *S&P Global Ratings: Industry Top Trends 2019—Building Materials*, Standard & Poor’s Financial Services LLC, November 14, 2018, accessed March 9, 2021, www.spratings.com/documents/20184/5670590/Industry+Top+Trends+2019+-+Building+Materials/912d0b2c-1117-e17b-2b2b-94d300d67d24. [↑](#footnote-ref-1)
2. CHF = Swiss franc; CHF1 = US$1.0319 on June 12, 2017; all currency amounts are in CHR unless otherwise indicated. [↑](#footnote-ref-2)
3. Shareholders did not state anything on the required financial returns. Continuity was their main priority. [↑](#footnote-ref-3)
4. Phantom shares were contractual agreements between the firm and employees that gave the employees the right to a certain cash payment in the future wherein the value of the cash payment was based on the value of the firm’s stock price. The employee therefore would receive the financial benefits of stock ownership (i.e., dividends and capital gains) but would not receive the benefits of stock ownership associated with having control or a voice in decision-making. [↑](#footnote-ref-4)