UDC 005.41:334.722.24(497.11)
CERIF: S 144
DOI: 10.51204/Anali_PFBU_23404A

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CORPORATE GOVERNANCE IN SERBIAN FAMILY-OWNED COMPANIES: IDLE OPPORTUNITIES

This paper aims to contribute to legal research on family-owned companies, focusing on Serbian law. This company type is the focus of Part Two of the Serbian Corporate Governance Code, which contains various specific corporate governance mechanisms, such as succession plans, family general meetings, family councils, and family protocols and recommendations aiming to achieve responsibility, transparency, continuity, efficiency, and fair treatment of all shareholders.

The paper presents existing possibilities and explores whether a specific Serbian corporate governance regime dedicated to family-owned companies can be accommodated into a general company law regime. This paper aims to further promote the use of specific mechanisms designed for family-owned companies, paying particular attention to the importance of drafting family protocols. These protocols can regulate not only typical corporate governance issues but are also suitable to include the family-owned company's vision and mission as a sustainable, balanced, and long-term viable business organization.

Key words: *Corporate governance. – Family-owned companies. – Family protocol. – Family general meetings. – Serbian Corporate Governance Code.*

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1. INTRODUCTION

Even though the issue of specific corporate governance for family-owned companies has already been widely explored in contemporary comparative company law, Serbian theory, as well as practitioners, usually remain silent on the subject. This is particularly surprising, bearing in mind that in Serbian law there are various opportunities to introduce specific corporate governance mechanisms to family-owned companies. Among them, the most important is Serbian Corporate Governance Code (CGC), in which the whole second part is dedicated exclusively to this company type.[1] A number of principles and recommendations are developed and defined particularly for family-owned companies. The Serbian CGC advocates for the introduction and inclusion of mechanisms that are suitable for the specific needs of this type of companies, pointing to family protocols, family general meetings, and family councils. All of these are still not very common in Serbian business practice, since their usage is exceptional, while expertise among practitioners remains at a rudimental level, being thus far limited or undeveloped.[2]

It will be explained that the most common closely held form of business organization in Serbian law by far is the limited liability company. This form is also typical for establishing and conducting a family business (after the sole proprietor, which is not in the focus of this research). The same is the case in comparative law. The organization of a family business can also be structured in the form of a joint-stock company, including a public company, while using its advantages to offer securities on the regulated markets. Nevertheless, in Serbia this is still not the case. This is due to the fact that after the privatization of socially owned enterprises to joint-stock companies, in the past three decades only a limited number of them became family owned. Also, in recent years very few joint-stock companies were established, and many among them even converted to limited liability companies.

Being the most commonly used form for the organization of a family business, a limited liability company offers many important advantages over the other company forms. The company's (family) members have many

1 Kodeks korporativnog upravljanja [Corporate Governance Code, CGC], *Official Gazette of the RS* 99/2012. (English translation available at *https://www.ebrd.com/documents/ogc/serbia.pdf,* last visited 26 October 2023)

2 There are, nevertheless, some exceptions. See, for example, Family Business Advisory Consultants, *https://www.porodicnekompanije.com/porodicni-protokoli* (last visited 25 September 2023); or Adizes Southeast Europe – Centre for promotion of family companies, *https://adizes.eu/biznis-transfer/* (last visited 25 September 2023).

possibilities in organising the company's affairs, its structure, and internal issues, due to the vast party autonomy, particularly characteristic of this closely held form of company. Therefore, apart from specific principles and recommendations developed for family-owned companies in the Serbian Corporate Governance Code, general provisions of company law may provide a solid background in order to accommodate the CGC principles and recommendations, and to further promote their establishment and functioning. However, even though Serbian law offers many opportunities for tailor-made corporate governance in family-owned companies, many of them remain thus far unexploited.

Family ownership in companies does not have a long tradition in Serbia, becoming common only after the introduction of the market economy during the 1990's. According to unofficial data, the majority of Serbian family-owned companies are less than 20 years old, while 34.5 per cent are less than 10 years old. According to information from the Chamber of Commerce and Industry of Serbia, the majority of family-owned companies are first-generation companies, only 11.9 per cent of them are in the second generation of a family, while only 3 per cent have been acquired by a family.[3] It is still rare to plan succession in family firms, while problems relevant for family firms in the second, third, or next generations are problems Serbian companies will become increasingly aware of in the near future. Therefore, many problems family-owned companies face will become evident only in the years to come.

It is the aim of this paper to shed more light on various opportunities offered by existing corporate governance provisions in Serbian law. They can be introduced in family-owned companies, making them more efficient and productive and less prone to conflicts, while helping them to survive through the years. After a short presentation of the advantages and disadvantages of this type of business, the paper will provide an overview of the Serbian corporate governance provisions aimed at family-owned companies, focusing on the recommendations to introduce various mechanisms, including a succession plan, family protocol, family general meeting, family council, and communication and conflict management. We will discuss how these mechanisms can provide better corporate governance, on the one hand, and

3 This data, claimed to be sourced from the Serbian Chamber of Commerce cannot be confirmed by any official source, and therefore should be used provisionally. Still, it cannot be far from the truth, in particular considering the fact that the majority (if not all) family businesses could have been established only after the introduction of the market economy in the 1990s or were acquired by families after the privatizations during the same period. See the statistics referred to in the results of the Project of European Business Association (n.d.).

fit into the general regime of corporate governance and law, on the other. We will also reflect on the difficulties that might arise in their practical implementation. This is particularly the case with family protocols, which must find a proper place in the hierarchy of legal acts applicable to the family-owned company. Therefore, the proper designation of their contents and of the legal nature of their provisions can lead to their appropriate use.

The legal research in this field is, unlike abundant research in management and economic studies, still insufficient even in comparative law. According to our knowledge, no theoretical legal study on this topic exists in Serbian company law. This paper is, therefore, only a starting point or introduction, with the purpose of promoting further legal research in the field.

2. FIRST GLANCE AT THE SERBIAN COMPANY LAW AND CORPORATE GOVERNANCE OF FAMILY-OWNED COMPANIES

The primary law to deal with corporations and partnerships in the Republic of Serbia is the Law on Commercial Companies. The first law to introduce a modern company law regime in Serbia was enacted in 2004.[4] The 2004 Law followed the needs of practice by introducing, among others, general forms of limited liability companies and offered at the time advanced corporate governance for them. This law was replaced in 2011 by the new Law on Commercial Companies (LCC 2011).[5] The 2011 LCC was expected to improve certain inconsistent or unpractical solutions, but aimed to keep the basic concept and most important characteristics of previous provisions, including modernization.[6] Even though modern in approach, and following all trends

4 Zakon o privrednim društvima [Law on Commercial Companies, LCC], *Official Gazette of the RS* 125/2004.

5 Zakon o privrednim društvima [Law on Commercial Companies, LCC], *Official Gazette of the RS* 36/2011, 99/2011, 83/2014, 5/2015, 44/2018, 95/2018, 91/2019, and 109/2021. (English translation available at *https://www.paragraf.rs/propisi/companies-act-of-serbia.html* (last visited 26 October 2023)

6 Serbian laws, especially in this area, have a notable tendency to change often. This is understandable bearing in mind the major reasons for these changes. First, many provisions and norms typical for a market economy were introduced after almost fifty years of their exclusion from Serbian law, with the introduction of the market economy. It is understandable that many of them are still new, and that business practice, theory and case law are still attempting to accommodate certain company law instruments and fit them into the legal system. Second, developments in this area were significant in company laws in many countries and within the EU and were sometimes too eagerly followed in Serbian company law by way of harmonization and legal transplantation. These developments particularly include

of contemporary corporate governance in comparative law, following the adoption of these acts Serbian company law did not distinguish a separate category (type) of a family-owned company, but followed the traditional path by recognising four general business organization forms with legal personality: joint-stock company, limited liability company, partnership, and limited partnership. It also distinguished public companies in defining special rules (the majority of which is mandatory in nature) applied only to this company type, while for all the other closely held companies vast party autonomy. Even though partnership and limited partnership are also available forms to serve for organization of a family-owned business, their specific features – particularly joint and several liability of partners – make them unattractive in business practice.[7]

A similar path was followed in the issues of corporate governance. The Chamber of Commerce and Industry of Serbia adopted the Serbian Corporate Governance Code (CGC) first in 2006 and more recently in 2012. Intended for all companies of capital – companies with limited liability of its members – it is applied on a voluntary basis with the aim of improving the corporate governance systems of those companies.[8] The rules contained in this Code supplement the legal framework prescribed by the law, and are usually applied to issues where provisions are of either a dispositive (permissive) nature, or where there are no provisions at all, if party autonomy is allowed.

While the Law on Commercial Companies promotes the introduction and application of corporate governance codes on the 'comply or explain' basis, especially for public companies, their voluntary but recommended implementation applies to all other companies.[9] However, the low level of Serbian corporate governance tradition involving joint-stock companies, as well as in closely held companies, still points out to further promotion and wider application of these principles of good business practice (Vasiljević 2013, 30). The same is especially the case in limited liability companies, where adoption and application of these principles is almost non-existent. This is also the case with Part Two of the Code which is particularly aimed

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modernization and introduction of new technologies, development of financial markets, etc. They also include modernization efforts in corporate governance, including board structures, increased transparency, and further simplification of capital requirements for closed companies. On the Serbian Company Law in general see particularly Vasiljević, Jevremović Petrović 2022, 147 ff.

7 For this reason they will be left out from this research.

8 According to the CGC they are especially recommended to limited liability companies, members of the Chamber of Commerce and Industry of Serbia. CGC, Introduction.

9 LCC 2011, Art. 368.

at family-owned companies. Even though only the second part of the Code is specific to this company type, other parts of the Code, especially Part I Chapter I, aimed at all limited liability companies, and other special chapters, if applicable (Chapter II: Big Corporations and Public Joint-Stock Companies, and Chapter III: Additional Recommendations for Public Joint-Stock Companies), are also encouraged for family-owned companies, on a case by case basis and their independent assessment.[10]

Even though many provisions of the Law on Commercial Companies can be emphasised to promote family-owned businesses or could be of particular use to them, in further sections we will focus only on those specific mechanisms developed in the Corporate Governance Code for family-owned companies. Therefore, numerous provisions of company law that could be analysed from the perspective of family-owned companies (including specifics on the establishment, organization and choice of form, particular rights or duties of shareholders, transfer of parts or shares, conflict management, and specific financing of these companies) remain outside the scope of this paper.[11]

3. DISPERSION AND TYPICAL FORMS OF FAMILY-OWNED COMPANIES IN SERBIA

It is estimated that 80 to 95 per cent of all business in the US are family owned or family controlled (Alderson 2015, 140). In Europe, they are estimated to represent around 60 to 80 per cent of all companies.[12] There is not much statistical data on the number of Serbian family-owned companies.

10 CGC, Introduction.

11 An excellent example of provisions of general company law that is of interest to family-owned businesses, relates to establishing and maintaining control of the company. Namely, there has been much discussion on introducing loyalty parts or shares in these types of companies. In jurisdictions where it is allowed, loyalty parts or shares leave the possibility for family shareholders to maintain control of the company, even though they can go public and seek external funding. On the positive effects of the introduction of loyalty shares in Italian public family-owned companies see Bajo *et al*. 2020. In contrast, on the many restraints of external financing through capital markets for family-owned businesses, due to loss of control, see Schammo 2015, 152.

12 In the Final Report of the Expert Group on Family Businesses, produced for the European Commission, it was estimated that family businesses account for 60 per cent of all European companies (European Commission 2009), while the European Family Businesses organization estimated them to represent 65 to 80 per cent of all European companies.

The general trend of many continental European countries, where closely held companies with concentrated ownership are predominant, is typical for Serbia as well.

Many closely held companies are established in the form of limited liability companies, while there are few closely held companies in the form of partnerships and especially limited partnerships (if at all for latter). While not numerous, joint-stock companies play an important role in the economy, even though most of them were created following the privatization of socially owned enterprises during the 1990s and few were created afterwards. Even among them, the significant trend of conversion from a joint stock company to a limited liability companies must be pointed out.[13]

Some of the former socially owned enterprises followed an insider privatization scheme, whereby companies were privatised to current and former employees by free distribution of shares. Others were excluded from this general approach and became subject to 'special privatization programs' carried out by the government. In those cases, many companies were sold to major investors, with a chance of concentration of ownership and establishment of privately (family) owned companies. Finally, some of them still have the state as a controlling shareholder, while in a few of them ownership is widely dispersed among the population. Therefore, the majority of large (joint-stock) companies have concentrated ownership, but the number attributed to family-owned companies cannot be significant, especially compared to the prevalence of limited liability companies in practice.

It is for this reason that a general regime of corporate governance will be further explored for all types of companies with limited liability. However, a particular focus will be on the limited liability company form and the scope and limits of party autonomy in its corporate governance.

13 According to official data from the Business Registers Agency (2023), on 4 October 2023, there were 136,326 registered commercial companies. According to the official data from the Central Securities Depository and Clearing House, there is data for 917 joint-stock companies, while in the register of financial instruments there are 923 issuers of shares (which is reserved only for joint-stock companies). According to the Central Securities Depository and Clearing House (2023) statistical overview of ownership structure of registered companies, legal persons are predominant (84 per cent), while ownership by natural persons who own less than 5 per cent accounts for 13 per cent, while natural persons who own above 5 per cent account for only 1 per cent.

4. DEFINITION OF A FAMILY-OWNED COMPANY

Finding the exact definition of a family-owned company is not a simple task, because they come in variety of business forms and can be of different sizes (Uffmann 2015, 2443). The typical definition of a family-owned company is the one based on the *control of the company by family members*. Family control can be achieved through major shareholdings but is usually combined with control through direct management or board position(s) of family members. In order to investigate which performs better, Miller *et al*. (2007) introduced distinction according to the *number of family members included in the family business*. Namely, they distinguished single-member companies – where a single member was usually the founder of the company and categorised it as a *lone-member firm* – from those with several family members – *true family firms*, which included companies with several family members over time (Miller *et al*. 2007, 831). Even if not of high importance for economic research, single member companies can be of particular importance to succession issues and are included in legal research, providing additional corporate governance mechanisms in family-owned companies.

In addition to these, many other important features of family-owned business are used as criteria to identify them. The European Family Businesses Organization, as well as the European Commission use variety of these other, auxiliary criteria in defining family businesses, including establishment, decision-making, share capital holding, involvement of family generations in the company, and representation in the management of the company.[14] Still, the definition should be relaxed by specific circumstances, including the time frame, and the fact that companies can be fluid between family and non-family ownership.[15]

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14 According to a definition of the European Family Businesses organization (n.d.), as well as the European Commission (2009, 4), a firm is a family businesses if: 'the majority of decision-making rights are in the possession of the natural person(s) who established the firm, or in the possession of the natural person(s) who has/have acquired the share capital of the firm, or in the possession of their spouses, parents, child or children's direct heirs; the majority of decision-making rights are indirect or direct; at least one representative of the family or kin is formally involved in the governance of the firm. Listed companies meet the definition of family enterprise if the person who established or acquired the firm (share capital) or their families or descendants possess 25 per cent of the decision-making rights mandated by their share capital'.

15 In the same line: European Commission 2009, 9.

Serbian law defines the family-owned company in the Corporate Governance Code as 'a company in which the majority of voting rights belong to the family controlling the company, including the company founder intending to transfer the company to his/her descendants and make the company operation sustainable down through the generations of this family'.[16] Also, succession is defined as 'the transfer of management and ownership in a family-owned business, or of the control over a family-owned business, from one generation to another'.[17]

The complex wording of the term 'family-owned company' is a first feature of this definition. Also, this complicated definition provides a list of various requirements for a 'family-owned company'. Among them, the most important ones are voting rights and control, as well as (the intention of) transferring the company to descendants. Nevertheless, succession includes the transfer of not only ownership of the business, but also management, while retaining (and separating) the control criteria.

The interpretation of this provision must be the most benevolent one, given the voluntary implementation of the Code's recommendations and principles by companies that meet the family-owned company criteria. Thus, understanding of the offered criteria must be that they are put *alternatively* – they are applicable if any of them is fulfilled. Therefore, a family-owned company can be the one where family members have the majority of voting rights and/or control in the company. Also, a family-owned company can be one with only one founder when he intends to transfer the company to descendants, or to make it sustainable down through generations of the same family. Finally, issues covered by succession can be related to ownership, management, or control over a family-owned business.

5. CORPORATE GOVERNANCE IN FAMILY-OWNED COMPANIES

In one of the first studies to cover family firms and family behaviour within these organizations, Tagiuri and Davies (1996, 199) developed the renowned '3-Circle' model of family business, showing how family firms incorporate three essential elements: family, business, and ownership. Shortly afterwards, various management and empirical research on this issue emerged. Anderson and Reeb's (2003, 1303) empirical study of large US public firms at the end of last century demonstrated that family

16 CGC, Glossary.

17 *Ibid*.

ownership was an effective structure of business organization: family firms performed better than other, non-family firms. Also, when family members served as CEOs, performance was better than with outside CEOs (Anderson, Reeb 2003, 1303). This finding opposed previous prevailing findings in the US literature, where it was argued that controlling shareholders used public firms in order to pursue private goals and extract private benefits while they underperformed (Anderson, Reeb 2003, 1301–1302).

Similar results were shown in large European companies (Andres 2008, 431–445). In his analysis of German family-owned listed companies in the early 2000s, Andres (2008, 431–445) concluded that all benefits regarding better firm performance in family firms, particularly compared to other blockholders, were correlated with the involvement of family members in the company's management or supervisory boards.

At the time of the first publication of empirical research in the field and until recently, legal writings on the topic were sparse. Nevertheless, this is changing, while legal research is constantly emerging, especially in the past decade, and is complementary with the trend of putting more focus on small and medium enterprises. The focus of legal analyses is on specific corporate governance issues of family-owned companies (Fleischer 2018, 11–20; Fleischer, Recalde, Spindler 2021, 1–302; González-Cruz *et al*. 2021, 3139–3165; Braut Filipović 2021, 9–28), even though other issues, including adequate funding, remain significant.

What makes corporate governance in family-owned companies distinct? According to economic and management research in the field, in family-owned companies family members are usually focused on 'their' company and do not diversify their investment portfolio, which is usually closely connected to their family wealth, making them more engaged (Anderson, Reeb 2003, 1304; Andres 2008, 433). Therefore, the change of (family) members is much less common here than in other types of companies, transferability of parts and shares is usually subject to stricter provisions, while control of the company (in terms of ownership, as well as management) is one of the most important features of this company type.[18] The specific interests of family-owned companies also include stability and long-term investment, company growth, technological innovation, and sustainability. They often have particularly close connections with employees, as well as

18 In this context, the term 'control' is used within its widest possible meaning. It includes not only control through ownership and other criteria prescribed in LCC, 2011, Art. 62, para. 5, but also other control mechanisms, including informal control.

with other stakeholders, suppliers, and customers. Family members commit themselves to the company and are personally more involved in its success, they promote loyalty, cohesion, and cooperation.[19]

Still, family-owned companies face various limits, including specific conflicts, different scopes of application of provisions on duties towards the company, and even more pronounced minority oppression issues. Family-owned companies usually have poor and underdeveloped corporate governance, without much influence of independent, internal control within the company bodies. Finally, they are limited in regard to survival.[20] Also, specific problems are related to the financing of these companies, because equity finance and fear of losing control usually make these companies not suitable for external financing, particularly on the capital markets (European Commission 2009, 13–14). Therefore, they are usually financed through private (family) equity, while external funding is predominantly provided by bank loans (Allotti, Bianchi, Thomadakis 2021, 7). Therefore, typical funding of family-owned business, as a small or medium enterprise, remains limited and more expensive than more efficient sources of funding, affecting potential for survival and growth.[21]

6. SERBIAN CORPORATE GOVERNANCE PRINCIPLES AND RECOMMENDATIONS FOR FAMILY-OWNED COMPANIES

Serbian Corporate Governance Code set its goal 'to provide family-owned companies with support and guidelines on their path of transformation from a small family corner store into a company that is a serious regional player'.[22] Nevertheless, its contents are not limited solely to the growth of the family-owned company, nor does it deal with company funding, but

19 On the stewardship theory and positive altruism effects in interaction between family relationships with family firm performance, see in particular Eddleston, Kellermanns 2007, 550–551.

20 Tagiuri and Davies (1996, 200) reported that family-owned companies survive to the second generation of family owners in only 30 per cent of cases, while their average lifespan is 24 years.

21 On the inclusion of the family-owned companies as typical SMEs in capital markets and the challenges they have in this regard, see Jevremović Petrović 2022, 197–200.

22 Introduction to Part Two CGC: Additional Principles and Recommendations for Family Corporations.

rather encompasses various mechanisms aimed at corporate governance improvement, conflict management resolution, and especially the ability of the company to survive to the next generation(s).

According to the CGC, family-owned companies are guided by three main organizational requirements: the skill to recruit and retain the best people for the family business, the capacity to develop a culture of trust and transparency, as well as the capability to define a logical and organizational structure.[23] Therefore, the CGC underlines that various mechanisms of corporate governance – including responsibility, transparency, continuity, efficiency, and fair treatment of all family and non-family shareholders – must be ensured.[24] Still, one must not forget that it is not only up to family members to recognise the necessity to adopt specific corporate governance tools and mechanisms for their business. Namely, the national legislator and government in general have the important task of making progress and further promoting already adopted acts, programs, and strategies. The European Commission (2009, 18) insists that in family-owned companies entrepreneurship training, as well as management-specific skills, should be encouraged by national governments and strategies. Also, it is important that general provisions of company law, financing, labour law, inheritance and tax law create a climate in which family firms can thrive.

The Serbian Corporate Governance Code developed five general principles, with additional recommendations.[25] As will be shown, their content does not fall only within the scope of company law, or law in general, but is also related to management, organization, economy, and even psychology matters. They include: 1. planning of the transfer of governance (management) of the company to following generations; 2. establishment of a family general meeting; 3. establishment of a family council; 4. adoption of a family protocol; and 5. introduction of methods of communication and conflict resolution. We will briefly review these principles and recommendations and point out how one should accommodate them to general provisions of company law, leaving aside other branches of law that are beyond the scope of this paper.

23 CGC, Introduction to Part Two.

24 *Ibid*.

25 CGC, Part Two.

6.1. Continuity and Succession in Family-Owned Companies

Succession is one of the most important issues for a family-owned company's viability and life cycle. It is very common for family members to think about succession issues too late or not at all, impairing the existence and future prosperity of the company. According to the Serbian Corporate Governance Code, the first principle for family-owned companies insists on *careful and timely planning of the transfer of governance (management) of the company from one generation to another*. Therefore, there are several important aspects of succession that have to be taken into consideration if this principle is to be adopted: the first is succession (or more generally transfer) of parts or shares in family-owned companies, and second is the continuity of family management of the company, and the issue of employment or other engagement of family members from more than one generation.

The Serbian CGC is not focused solely (nor even foremost) on the legal context and regime of the succession of parts and shares, and continuity in management. It does not contain a particular legal mechanism on how succession or continuity should be achieved but leaves these issues to the general regime of company law (and other legal branches). Nevertheless, the limitations and scope of these general provisions should be taken into consideration when following the CGC recommendations.

Serbian law generally allows for the succession of parts or shares of a company, even though this regime depends greatly on the form of the company. Certain restrictions regarding succession make such transfer of parts overly difficult or even impossible in certain company (or business) forms (Vukotić 2018, 167, 175–178, 185–186, 189).[26] Still, even with various company law restrictions, depending on the legal form, a majority of them remain permissive in nature and can be contracted around, in accordance with the needs of family members. This is especially the case in limited liability and joint-stock companies, where succession of parts or shares is generally allowed.[27]

Succession, as defined in the CGC, should also encompass other forms of succession of parts or shares in family-owned companies, including modalities of transfer of parts or shares from one family member to other

26 LCC 2011, Art. 119 which was in part amended in 2018, and strongly criticized by certain authors regarding the (later amended) provision of compensation (Jovanović 2012).

27 LCC 2011, Arts. 172 and 261.

member(s) of the family during their life, with or without compensation. Also, transfer of parts or shares in order to provide family succession should also be possible through various dispositions of property with similar effects in inheritance law (such is testamentary disposition), use of private endowments, investment funds, or various life insurance modalities of property disposal.[28] Nevertheless, even though contractual disposition and transfer of property during life of a family member could be carried out in order to provide family succession, succession contracts, including disposition of property after the death of a family member, are not allowed in Serbian law (Đurđević 2015, 246), and should be kept in mind in succession planning.[29]

To emphasise the importance of succession planning, the CGC developed a number of recommendations. They specify the necessity to develop a *succession plan in the company, as well as an emergency succession plan* (in the event of unpredicted situation when it is important to act with short notice). *The plan of succession must regulate not only company law related issues* – such as the transfer of shares, selection of family members for key management positions etc. – *but must also consider other important implications of this succession*, in terms of substantive and procedural aspects in the field of finance, inheritance and tax law.

An issue of great consequence in regard to succession plans, from a company law perspective, is related to its legal nature. Namely, the CGC recommends that *a succession plan should be a part of the family protocol* (which will be discussed in detail below). Nevertheless, it should be emphasised here that if a succession plan is contained in a contract or in a similar legal transaction, it can have only a general civil (contract) law effect.[30] Only when and if a succession plan is defined as a part of the articles of incorporation (or statute, in the case of a joint-stock company) it can have

28 See, for example, certain forms of capital investment plans through life insurance, including 'tontine insurance', Zakon o osiguranju [Law on Insurance], *Official Gazette of the RS*, 139/2014, and 44/2021, Art. 8, para. 1 under 6. On various alternative investment funds see in particular Zakon o alternativnim investicionim fondovima [Law on Alternative Investment Funds], *Official Gazette of the RS*, Art. 2 para. 1 under 3, 5 and 6. Dudás recommends the introduction of fiduciary transfer and management of property (Dudás 2014, 223–224), which could be applicable in this case.

29 Zakon o nasleđivanju [Law on Inheritance], *Official Gazette of the RS*, 46/95, 101/2003, and 6/2015, Art. 179.

30 It can be also signed by two or more members of the company – as a members' (shareholders') agreement, with an *inter partes* effect between those members who signed the contract (see LCC 2011, Art. 15).

important company law and statutory/institutional effects (as accepted in Serbian legal theory, see Jevremović Petrović 2019, 26–27; Vasiljević, Jevremović Petrović, Lepetić 2020, 47; Jovanović, Radović, Radović 2021, 110).[31] This is important because a succession plan may be validly argued against company, as well as all present and future members of the company, only if it is part of the articles of incorporation (or statute, in the case of a joint-stock company).

The second aspect of continuity in family-owned companies is related to a succession plan, which should also *include criteria for the selection of candidates among family members for management positions*, considering market requirements, applicable in the same way as to non-family professionals. *The same should also apply to management contracts with a family member*, who should be in the same position as those who are not family members.

In this aspect, the CGC resorts not only (nor exclusively) to regulate issues of succession, but rather focuses on continuity in management and employment by family members. These mechanisms serve the purpose of improving professionalism in the management of the company and should stimulate family members to meet professional and personal characteristics required in the labour market. Unlike previous issues concerning the succession of parts or shares, which are related to the position of company members or shareholders and can be dealt with by articles of incorporation, planning for management positions and employment usually stays outside of its scope. Namely, many other issues of management planning remain outside the substantive scope of this act and are limited by provisions on the competences of the company's bodies. Particular rights of members, including the right or obligation to perform work or services, could be provided by the articles of incorporation, with the abovementioned effects, which is also the case regarding the criteria for selection of the company's body members, etc.[32]

Finally, the CGC recommendations suggest that *the succession plan should include the employment policy of the family-owned company* which would provide better corporate governance in family-managed companies. This recommendation is intended to improve the employment policy of the family-owned company, by making it as objective as possible. Furthermore,

31 LCC 2011, Art. 11. On the possibility of the succession plan with company-specific rules on share succession being part of the incorporation document, see Marjanski, Dudás 2021, 123.

32 For limited liability company see LCC 2011, Art. 141 para. 1 under 8, 152, 200, and 224.

employment, as well as policies regarding management recruitment, is additionally important to family members in order to prevent internal (family) conflicts. As a final remark, we would like to emphasise the conclusions in this regard made by the European Commission (2009, 17), which claims that family-owned companies are usually associated with prejudice in the labour market. Therefore, the employment policy is important not only to improve corporate governance within the company but also has important side effects: attracting lower, as well as higher positioned non-family employees. Still, problems related to prejudices against family-owned companies in the labour market must be improved not only from within the company – thorough various family-owned company employment policies, but also through public campaigns and other public influence (European Commission 2009, 17).

6.2. Family General Meetings

Family firms exhibit specific dynamics in management, organization, and supervision decision-making. Family members, as controlling shareholders, can be in a specific conflict of interest situation, among themselves as well as with others. We will discuss internal conflicts within the family in detail below. When it comes to others, family members can have conflicting interests with 'their' company, which are particularly prominent in regard to minority non-family shareholders, employees, or other typical 'outsiders'.

Also, family members effecting active control – by holding the CEO position, being board members or performing other managerial tasks and duties – can face even more conflict-of-interest situations, because in this case there is no typical separation of ownership and control.[33] Even if not performing managerial duties, controlling shareholders can make managers less independent and influence their decision-making to pursue the family members' interests. Some authors argue that family members holding active control can undermine the company's performance by excluding more competent, professional managers, while also not being accountable, in comparison with professionals or outsiders (Anderson, Reeb 2003, 1306–1307). In this context, strict adherence to the best corporate governance practice, including equal treatment of members and shareholders, information rights and disclosure, efficient management organization, introduction of

33 On the typical conflict-of-interest issues and separation of ownership and control see classics in this topic: Kraakman *et al.* 2017, 29 ff; Easterbrook, Fischel 1982, 700 ff.

professional and/or independent board members when not required by imperative requirements, additional mechanisms of internal control within company, protection of minority rights, etc., remains prominent and can be perceived as being equally important as in other companies, particularly those with controlling shareholders.[34]

On the other hand, family members of the family-owned companies distinguish themselves in many positive features from other company's members. They are more willing to promote the firm's success and its reputation, they relate to the company on a long-term basis; also, they can more easily identify with the company's interests (Anderson, Reeb 2003, 1306–1307). Finally, family members are not only and prevalently motivated by adequate immediate or short-term compensation and firm performance benefits. This is why family-owned companies often promote long-term, sustainable goals which are not only profit oriented (López-Pérez *et al.* 2018, 3–4). These advantages can be more important than the possible inefficiency, lack of knowledge, expertise, and professionalism of family members in management positions. For this reason, it is important how corporate governance mechanisms further promote positive features of family-owned companies.

In order to tackle these problems, the second principle in Part Two of the Serbian Corporate Governance Code for family-owned companies introduces the *family general meeting as an advisory body of the family-owned company, with the aim of bringing together all family members to discuss business-related and other family issues* related to their company. Its purpose of *fostering unity among family members, facilitating exchange of knowledge and familiarization of all family members with the company's affairs, while keeping family issues apart from the company*, is particularly important in the second and subsequent generations. According to the recommendations, all issues pertaining to the establishment of this body, decision-making, purpose, meetings, agenda, etc. should be stipulated in the family protocol (as will be discussed below). Therefore, the most important goal of the establishment of the family general meeting should be to prevent or diminish internal family conflicts related to company's management and business conduct, while promoting best corporate governance practices. It should serve to make a more prominent distinction between the family and its interests on the one side, and the company and its own, separate interests, on the other side. This is emphasised by the recommendation to *keep family issues apart from the company*.

34 In this regard, see other CGC principles and recommendations, in Part One, which can be applied in this context.

In order to separate the family from the company, *family general meeting should bring together only family members*. Among them, management professionals recommend introduction of particular 'generational meetings' (Alderson 2015, 151), bringing together the second, third etc. family generations together. This is a particularly suitable mechanism involving those family members who are not at the same time members of the company but are involved in another way – as managers or, more often, employees of the company – with those staying outside the company but with important informal influence over its functioning.

The first general remark from the perspective of general provisions of company law in this context is emphasis on the fact that there is no equivalence between the terms 'family general meeting' and 'general meeting of members or shareholders'. Therefore, a family general meeting can be an informal gathering of family members, outside the companies' bodies. Also, it can be introduced as an informal (but nonetheless, according to the CGC recommendation) *advisory body* in the structure of a limited liability or joint-stock company. Its features, including composition and competences, can be determined in the articles of incorporation (or statute for the joint-stock company). Nevertheless, if so, its competences cannot be in contravention with the prescribed organization structure, duties, and competences of the company's bodies, which to a great extent are of the imperative nature in a joint-stock company, but with vast party autonomy in relation to almost all internal issues between the company and its members, as well as among members themselves in limited liability company.[35]

This far-reaching party autonomy allows a limited liability company to be adapted to the individual needs of its members and has important consequences on its internal organization. It can also accommodate various modalities of family general meetings into the internal organization of the company. Because of this flexibility, this form can be more attractive to family members than a joint-stock company, making it more adaptable to family needs. This is especially the case of family-owned companies where all shareholdings are in the hands of a family. Nevertheless, the separation of the competences with this family meeting from a general meeting of members or shareholders is the first step in the best corporate governance practice. It is even more important when there are not only family, but also

35 LCC 2011, Art. 140, 246–247.

non-family members in the company, when the company's interests and their protection must be imperative guidelines for best corporate governance practice in family-owned companies.[36]

6.3. Family Council

The establishment of the family council, provided in the case *when the family general meeting becomes too large*, is envisaged as the third principle for family-owned companies.[37] Its main task is to simplify communication between the company and the family, specifically management structures (board of directors, supervisory board, and executive directors) with the family general meeting. This should be done when the family general meeting becomes too large (for example more than 30 members) for the purpose of effective communication with the management of the company. They can be particularly useful in second, third and other generations of the same family.[38] The main task of the family council is to connect family members with the management of the company, not replace the management or other formal body in the company (Braut Filipović 2021, 11). Also, it reduces costs of other intermediaries in the company, and keep affairs 'within the family'.

Even though the Serbian Corporate Governance Code particularly emphasises that *family members may not give instructions to executive directors except through these formal governance bodies*, special care must be taken in order not to contravene the mandatory provisions on the competences and duties of company bodies.[39] It is particularly true for the joint stock company where explicit provisions regulate communication between shareholders (general meeting of shareholders and various rights of shareholders, such are rights related to the convocation of the general meeting, information rights, etc.) and management and supervisory bodies, as well as permit transfer of competences between bodies.[40]

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36 Many provisions dealing with the conflict of interest in general company law can be of importance here. Apart from composition and competences of the companies' bodies (as discussed above) it refers, above all, to duties owed to the company (LCC 2011, Art. 61–80).

37 CGC, Part II, Principle 3.

38 See data in various European countries on the involvement of family councils in Alderson 2015, 150.

39 CGC, Part Two, Principle 3, Recommendation 5.

40 With similar conclusions for Croatian law, see Braut Filipović 2021, 17–18.

Less strict provisions exist for limited liability companies, allowing various possibilities regarding competences and even delegation of powers from the general meeting to other bodies, and *vice versa*, according to party autonomy.[41] That provides more space for the family bodies to be involved more closely in the management of their company, according to their specific needs. Party autonomy could be used in various mechanisms by arranging that the internal affairs of the company, through the family council, can deal with problems related to shared control, unanimity, or high level of agreement in decision-making. Family councils could also be useful in facilitating various restrictions on the disposal of company's shares by promoting communication with current, prospective, and non-family members of the company in the event that they are numerous. The family council could also impact specific types of diversified company's management and control and could introduce advisory bodies to include and accommodate family members and their interests.

Members of family councils are family members, elected by the family general meeting, while the most important provisions on the composition, meetings, agenda etc. should be defined in the family protocol. *Other family bodies may be also introduced, depending on the family size and complexity of the company, to review, manage and decide on certain delegated issues*. Specifically mentioned are so-called *family offices*, usually in charge of investment services and activities for family members and their (family) assets. Nevertheless, this also should be done within the party autonomy in different forms of the family-owned companies.

Besides communication between a family and the company's management, the other important *task of a family council is to approve the family protocol, as well as other decisions on company and family assets*. Here, the family council serves as the main communication, as well as informal dispute management body, and is of particular use in numerous families that have several generations involved in the family-owned business.

41 Art. 141 para. 2 LCC 2011 explicitly introduces the permissive nature of provisions on companies' bodies competences. It provides that '[i]f the memorandum of association does not contain provisions on competences of the company's bodies, the company's bodies have competences provided by this Act'.

6.4. Family Protocol

Even though *adoption of family protocols* is introduced as the fourth principle for family-owned companies, it is the most important feature of specific (Serbian) corporate governance for family-owned companies.[42] All other corporate governance mechanisms from the Code (including succession plan, family general meeting and family council) are (or can be) stipulated within family protocol, which can include numerous tasks and features.[43] Family protocols, as defined by the CGC, are based on a specific regulatory technique, so-called regulatory instructions. This regulatory technique allows the possibility of adoption of a document, in this case the family protocol, but without proposing how and with what legal instrument this should be done, or defining its legal nature, due to the diversity and specific needs of each family-owned company.[44]

Empirical studies have shown that family business with family protocol can improve their performance.[45] Their advantage is that they can reduce the opportunism of family members and create a regulatory framework in advance, while promoting professionalism, a feeling of justice between family members, and bringing other advantages to the company's purpose, vision, and performance (González-Cruz *et al*. 2021, 3134). According to Serbian Corporate Governance Code *family protocols should define family objectives and values*. This is the perfect document to include various family values, the vision and mission of the company. It should promote the family-owned company as a sustainable, balanced, and long-term business organization. If family protocols provide the vision and mission of the company – this

42 Even though rare, they are included in the provisions of some national company laws under various names (family charter, family constitution, family code). Spanish law introduced them by Real Decreto 171/2007, Art. 2 para. 1; German law introduced family protocols by Governance Code for Family Businesses (GKFU) in 2004; Italian law uses this contract as an exception to the usually prohibited inheritance contracts, while Belgian law recognizes some provisions on these contracts within the Corporate Governance Code for non-listed companies. For details, see Fleischer 2018, 13–15.

43 For similar conclusions about the importance of family protocols over other mechanisms see Arteaga, Menéndez-Requejo 2017, 5.

44 A similar approach was followed in Germany, within its Corporate Governance Code for Family Business. For those provisions see Fleischer 2018, 12. Also, on the advantages and disadvantages of this approach see Uffmann 2015, 246.

45 This study was conducted using a sample of 530 Spanish family businesses during 2003–2013, of which 265 received financial aid to introduce family protocol, over the period of 2 years following the implementation of a family protocol (Arteaga, Menéndez-Requejo 2017, 1–2).

should be considered by the management when deciding on the company's strategy. This is particularly the case when deciding on the 'best interests of the company'. Also, *family protocols define the most important mechanisms of family governance and corporate governance and their mutual relation*. It is advised that the definition of the competences and decision-making areas assigned to the family should be carefully prepared in the family protocols, so that it does not become a limiting factor for the company and its governance.

Finally, an important feature of the CGC recommendation for the family protocols is that it is *advisable* for them *to be legally binding*. This is, in our opinion, the most delicate feature of the family protocol and needs elaboration. Namely, one of the most important issues about family protocol must be whether and under what conditions it can be drafted as to have a legally binding nature (and in particular company law binding nature). Also, other general company law issues are of relevance here: what is the relation of this document to other company acts, particularly articles of incorporation and statutes. Finally, should family protocols be drafted as shareholders' (or members') agreements or as acts of another legal nature. The answers to all these questions require much more detailed research than this paper permits. Still, we will underline some important preliminary thoughts on some of these issues.

First, family protocols must be drafted specifically for each family-owned company and according to family needs. The 'one size fits all' principle is not suitable for application in this case. Particular care must be taken when adopting family protocols with a legally binding nature. They must be in accordance with all company's acts, especially articles of incorporation and statutes.[46] It must be underlined here that model articles of incorporation are not suitable for family-owned companies, especially if they are to include family protocols.[47]

In order to have a legally binding effect for the company and other members, family protocols must be concluded between all members of the company and included in the articles of incorporation (statutes), in accordance with their substantive and formal requirements.[48] It is only in

46 On these issues see also above fns. 29–30.

47 For more on this issue, see Jevremović Petrović 2019, 168–170.

48 LCC 2011, Art. 11. The Law on Commercial Companies gives the founders an opportunity to autonomously regulate numerous matters related to their organization, management, relations between the owner and his/her company, therefore creating a source of law applicable to specific and not general matters. This is especially so for closely held companies, while public companies are under stricter regime of legislative control through imperative provisions and even

this case that a family protocol becomes 'resistant' to succession and change in the family and membership status. In all other cases, the agreement (or other legal transactions, like unilateral testamentary disposal of parts or shares) would have limited (or no) effects on the company and its (present and future) members.

A negative feature of including family protocol provisions in the articles of incorporation and statute is their obligatory disclosure, which would not be suitable for all family-owned companies.[49] In this case, if disclosure is to be avoided, more suitable arrangements could be achieved by preparing and signing a contract between members of the company (including shareholders' agreements).[50] Although generally allowed in Serbian law, they have significant limitations.[51] Even though they could be kept confidential, these agreements will bind only those (family) members of the company who are also signatories to these agreements.[52] If a company is owned by family members only, this would be one of the preferable and most practical approaches to regulating their internal affairs. Still, it is prone to difficulties if there is no equivalence between family and company members. Also, even if family and company members are the same, this situation can be changed due to growing families, or in time – by families changing over generations. These issues, therefore, remain the most important deficits of family protocols being drafted as shareholders' agreements. Similar conclusions can be made – including the limited scope of rights and duties and in particular effects on the company and its members – if they are based on other civil law contracts or other legal transactions between family members.

supervision by public law bodies in certain cases. On the contents of the articles of incorporation in limited liability company, which is the most suitable form for individualisation, see LCC 2011, Art. 141. While articles of incorporation of all forms of closely held companies allow for greater party autonomy, it is much more limited in the statutes of a joint-stock companies, due to numerous imperative legal requirements regulating this company's form. See LCC 2011, Art. 246.

49 On mandatory disclosure see LCC 2011, Art. 11, para. 8.

50 LCC 2011, Art. 15.

51 LCC 2011, Art. 269, 359. On voting agreements in Serbian law and recommendations for improvement, which can be of particular importance in regard to 'connected persons' in family-owned company, see Lepetić 2019, 239–245. For more on these issues see also Vasiljević, Jevremović Petrović 2022, 352–353.

52 For similar conclusions on family protocols being part of members/shareholders' agreements in German law, see Fleischer 2018, 12.

Finally, family protocols can be of a non-legally binding nature. Even though they can promote in this case better corporate governance, principles, values and manage communication or conflict management, they are limited in their effect.

6.5. Communication and Conflict Resolution in Family-Owned Company

Family members overlap with the owners of the company, but quite often also with its management and employees. Because of their intertwined roles, they can also easily bring family issues to their business affairs and management of the company (Tagiuri, Davies 1996, 202). The potential of conflicts can be related to their private (family) affairs (interpersonal conflicts), but often is related to the company itself. When it comes to personal issues, Alderson (2015, 141) distinguishes between siblings' rivalry, non-working family members, divorce, interpersonal conflicts, incompetent family employees, and multi-generational succession issues as the most prominent conflicts within family-owned companies. Their specific problem is that family members are not only emotionally attached to each other and are in a (life-)long relationships, but also that they usually try to resolve their problems internally (Alderson 2015, 141). This makes conflict management and resolution not only more difficult but also very sensitive and confidential.

Family member conflicts can be related not only to different positions of family members within the company (employee, management, and shareholder), but can also be particularly problematic when they are between non-employed shareholders and companies managed by owners and can even include conflicts regarding the company's goals (Alderson 2015, 144). They can also lead to so-called 'principal–"super principal" conflicts', including conflicts between family owners and other family members not directly involved with the company in terms of ownership, management, and employment (Arteaga, Menéndez-Requejo 2017, 5). For this reason, communication and conflict resolution must be addressed with special care in family-owned companies.

The Serbian Corporate Governance Code for family-owned companies finally introduces the principle of *necessity to establish methods of communication and conflict resolution in the family*. Recommendations underline the *importance of a good communication for family-owned*

companies and insist on the complementarity of the formal as well as informal communication. The definition of other channels of communication between the family and the public are also recommended.

Even though the issue of internal conflicts is often considered the most vulnerable feature (or a cardinal problem, according to Fleischer 2014, 29) of family-owned companies, Serbian law does not offer many recommendations on their resolution. It offers regulatory instruction to regulate the matter, without suggesting how this should be done. This is slightly disappointing and should be particularly addressed in practice.

Even though many valuable conflict resolution mechanisms can be found in general provisions of Serbian company law, specifically for a limited liability company, they are usually not efficient enough or are not appropriate to individual family needs. This is why they should always be part of the articles of incorporation, members' (shareholders') agreements, or family protocols. The family protocol can above all promote or include shareholders' (or members') agreements in its part related to ownership conflicts (Arteaga, Menéndez-Requejo 2017, 5). They can be of particular importance to ownership disposal and can include put and call options, rights of first refusal, tag-along and drag-along rights, lockout clauses, buyout agreements, and others (Arteaga, Menéndez-Requejo 2017, 5). One of the proposals, specific to management conflicts, suggests the introduction of 'co-CEOs' or the revolving position of family members in previously prescribed appointment terms (Alderson 2015, 152). This could be of particular importance in conflicts of family members with management positions, but is even more prominent in generational conflicts of multiple family members, and could also be transposed to issues of family council representation, family general meetings chairpersons, etc.

It should be underlined once again that family conflicts are sensitive in nature and tend to be resolved internally and without too much interference of third parties. This is why articles of incorporation, members' (shareholders') agreements, and family protocols should include mediation and other informal ad-hoc dispute resolution mechanisms.

Currently, existing recommendations in regard to conflict management do not provide adequate instruction on the various possibilities of mediation and other alternative dispute resolution mechanisms. It is, therefore, advisable that other recommendations on specific mechanisms of conflict resolution in sensitive family-owned companies disputes should be developed and included in the CGC provisions. Until then, the existing mechanisms, including arbitration and mediation, should be publicly promoted as particularly suitable for family-owned company disputes.

7. CONCLUSION

There are many features of Serbian company law that befit family-owned companies. The majority of provisions applicable to limited liability companies make them well-suited for this type of business: the internal structure of the limited liability company makes it a good form for a family business with adaptability in terms of size, organization, and possibility of adjustment to family needs. Furthermore, the vast party autonomy in contracting between members and the company allows 'tailor-made' approach, which can satisfy the specific characteristics of each family. Serbian company law also offers another form of a joint-stock company, which, even though less flexible in its structure and organization, can satisfy the requirements and needs of more developed businesses, aspiring to growth through public funding and the benefits of capital markets.

Departing from these general provisions and in order to further promote and support corporate governance in family-owned companies, the Republic of Serbia introduced in the Corporate Governance Code several principles and recommendations with particular focus on family-owned companies. The intention is to make these companies more efficient and productive and less prone to conflicts, while helping them to survive over time.

The CGC principles and recommendations include planning the transfer of corporate governance over generations through a succession plan and an emergency succession plan. Also, they call for the establishment of various advisory bodies in companies where family members get together to discuss family issues related to their family, as well as the company's affairs. Depending on the size of the family, business, and its organization, this gathering can include family general meetings, or if a family is more complex, family councils.

The most important principles of corporate governance for family-owned companies recommend the adoption of a family protocol signed by all the family members. It is preferable that it is legally binding, so that it could provide legal certainty and have legal effects towards the company and other present and future members. Together with the best corporate governance practices, this could be the cornerstone of family businesses over generations.

Even though the Serbian Corporate Governance Code recommends the introduction of methods of internal and external communication and conflict resolution, various specific mechanisms must be promoted in this process. These involve specific instructions for communication and conflict management to be included in the company's acts, as well as other family

agreements (shareholders' or members' agreements and family protocols). They should mandate that once conflicts are inevitable, it is preferable that they are resolved through mediation and other informal ad-hoc dispute resolution mechanisms.

We conclude by acknowledging various opportunities in specific corporate governance mechanisms for family-owned companies in Serbian law. Serbian theory, as well as practitioners, so far remains mostly silent on the subject. Various advantages of preventive general and specific corporate governance are unknown and, therefore, unused by many family-owned businesses. Also, many of them seem to be ignorant of the problems that may arise in the future. For this reason, it is imperative that more knowledge on the various opportunities offered by existing corporate governance regime become more widespread. However, it is not solely up to families and family-owned businesses to recognise the necessity of adopting specific corporate governance tools and mechanisms – it is also a task for a national legislator (and government in general) to make advances related to already adopted acts, programs, and strategies. The involvement of all stakeholders in this issue will make family-owned companies more efficient and productive, and less prone to conflicts, while helping them to survive over the years.

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Article history:
Received: 10. 10. 2023.
Accepted: 29. 11. 2023.