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Family Business in Times of Crisis: A Call for Interdisciplinarity for Future Research

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ABSTRACT: Family business is a dynamic field that is now attracting growing interest among researchers, theorists, investors, policymakers, practitioners, and many others. Recent research has shown that family businesses perform very well. Whether measured by their results, shareholder value creation or their ability to create jobs. Family businesses outperform their non-family counterparts. The turbulence caused by global hyper-competition has also brought home the fact that speed, sustainability, flexibility, product and service quality, branding, customer relationships, employee focus, patient capital, and the integration of smart new technologies are real sources of competitive advantage. These advantages are often pursued through idiosyncratic business strategies deployed by family-owned and family-controlled businesses. While family businesses face significant challenges, they also often possess unique advantages born of a unique and dynamic interaction between the family and the business.

KEYWORDS: family business, innovation, culture, governance

1. Introduction

Family businesses are extremely important to the well-being of the world's free economies. Between 80 and 95 percent of businesses in the United States and Latin America and more than 80 percent of businesses in Europe and Asia are still owned and controlled by families. These same businesses, large and small, young and old, account for more than 50 percent of the gross domestic product of the world's most advanced economies and employ a majority of the population.

Quality research in the established periodical literature is sure to generate more knowledge about the unique challenges and benefits of family businesses in the face of new challenges in the digital transition, with the prospect of useful implications for practice. The fact that family business is becoming the focus of research in management, economics, law, behavioral sciences, engineering, and other disciplines also bodes well for the possibility of positively influencing the currently dismal survival statistics.

Most family businesses (about 67%) do not survive beyond the founding generation under the control of the same owning family, and only about 12% make it to the third generation. Therefore, in this paper, we will try to identify a number of characteristics of family businesses for future research.

2. What about the family business?

Because of the diversity of business profiles, the definition has proven to be more difficult to pin down. In a comprehensive study of family businesses, Chrisman, Chua, and Sharma found 21 different definitions of family business in their review of 250 research articles (Chrisman 1996).

Family businesses come in many forms: sole proprietorships, partnerships, limited liability companies, S corporations, C corporations, holding companies, and even publicly traded, albeit family-controlled, companies. As a result, estimates of the number of family businesses operating in the U.S. economy range from 17 million to 22 million. Globally, estimates of all businesses considered family-owned range from 80% to 98%.

In a large-scale study of the role of family contractual relationships in the Spanish newspaper industry, a firm was considered a family firm if the last name of the CEO and/or editor-in-chief was the same as that of the owners (Gomez-Mejía 2001). Another empirical study considers family firms to be theoretically distinct from other closely held firms due to the influence of altruism on agency relationships (shareholder-management relationships). The authors of this study went on to say that family firms are distinguished both by the active involvement of the family in the management of the firm and by the intention of family members to retain ownership of the firm. They ultimately defined a family business as one in which two or more family members own 15% or more of the stock, family members are employed in the business, and the family intends to retain control of the business in the future (Schulze 2001). Another article attributes the uniqueness of a family business to the very different influence the family has on ownership, governance, and management participation through strategic direction, direct family involvement in day-to-day operations, and/or maintaining voting control (Astrachan 2002)

Taking into account this comprehensive body of research and analysis, this third edition of Family Business considers family businesses to be the set of firms in which a next-generation entrepreneur or CEO and one or more family members exert significant influence on the firm. They influence it through their participation in management or the board of directors, their control of ownership, the strategic preferences of shareholders, and the culture and values that family shareholders transmit to the company.

Participation refers to the nature of family members' involvement in the business as members of the management team, the board of directors, as shareholders, or as supporting members of the family foundation. Ownership control refers to the rights and responsibilities that family members derive from significant ownership of voting shares and governance of the agency relationship. Strategic preferences refer to the risk preferences and strategic direction that family members set for the company through their participation in executive management, the board, the board of directors, shareholder meetings, or even family councils. Culture is the set of values, defined by behaviors, that are embedded in a company through the leadership of family members, past and present. The family unit and the nature of the relationship between the family and the business also define this culture.

This paper therefore adopts a comprehensive theoretical definition of the family firm that focuses on the vision, intentions and behaviors of owners with respect to strategy, succession and continuity. Beyond the ownership structure, what differentiates family firms from management-controlled firms are often the intentions, values, and interactions of family owners that influence strategy. The result is a unique blend of the subsystems of family, management, and ownership to form an idiosyncratic family business system. This interplay between family, management and ownership can produce significant adaptability and competitive advantage. It can also be the source of great vulnerability to generational or competitive change. Dominant decisions in a family business, according to this inclusive theoretical definition, are "controlled by members of the same family or a small number of families in a way that is potentially sustainable across generations of the family or families" (Chua 1999).

Thus, we arrive at a working definition of the family business as a unique synthesis of the following elements:

- Ownership control (15% or more) by two or more members of a family or family partnership.
- Strategic influence of family members on the management of the business, whether by being active in management, continuing to shape the culture, serving as advisors or board members, or being active shareholders.
- Concern for family relationships.
- The dream (or the possibility) of continuity between generations.

The following characteristics define the essence of family business distinctiveness:

- The presence of the family
- The intertwining of family, management and ownership, with its zero-sum (win-lose) propensities that, in the absence of business growth, make family businesses particularly vulnerable during succession.
- Unique sources of competitive advantage (such as a long-term investment horizon) derived from the interaction between family, management, and ownership, especially when the family unit is high.
- The owner's dream of keeping the business in the family (the goal being the continuity of the business from generation to generation).

3. The dilemma between intergenerational situations and the sustainability of the family business

Family businesses are unique in that succession planning plays a key and very strategic role in the life of the business. Because competitive success, family harmony and ownership performance are all at stake at the same time in the business, careful orchestration of the multi-year process of succession between generations of owner-managers is a priority. There are hundreds of reasons why organizations fail, but in family-owned and family-controlled businesses, the most common reason is failure to plan for succession. Whether it is incompetent or unprepared successors, unclear succession plans, a tired strategy unable to contain competitors, or family rivalries and power struggles, if a family business is to survive, it must get its succession process right.

One study identified three types of inefficient succession (Miller 2003):

- Conservative: Although the parent has left the business, the parental shadow remains, and the business and its strategies are locked in the past.
- Rebellious: In what is often an overreaction to the previous generation's control of the company, the next generation initiates a clean slate approach to the organization. As a result, traditions, legacies and even the business model or its "secret to success" are destroyed or discarded.
- Hesitation: The next generation is paralyzed by indecision, unable to adapt the company to current competitive conditions, and unable to assert itself and its leadership effectively.

The study concludes with the thought that the patterns have been observed so frequently that many family businesses will likely have to struggle with these syndromes in order to ensure the continuity of the family business between generations of owners.

4. The sustainability of family businesses: the future of interdisciplinary research on these entities

Without the vision and leadership of two generations of family members and the use of selected family, management and governance practices, the future is bleak for family-controlled businesses. The blurring of the lines between family ownership, family management, and family ownership puts family businesses at risk of confusion, slow decision-making, and even business paralysis. The inability to adapt to changes in the competitive marketplace or the inability to manage the relationship between the family and the business ultimately undermines the business. As a result, a family business that lacks multigenerational leadership and vision can hardly position itself to retain the competitive advantages that made it successful in a previous, often more entrepreneurial generation.

It takes an ongoing dialogue between generations of owner-managers about their vision for the business to build a family business so that it lasts. Family businesses that have been built to last recognize the tension between preserving and protecting the core of what made the business successful on the one hand, and promoting growth and adapting to changing competitive dynamics on the other (Porras 1997). Family businesses that are sure that each generation will responsibly bring a different but complementary vision to the business have a foundation on which to build continuity.

4.1. Sustainability and family and socio-cultural constraints

In leading family businesses, employment in the company is a birthright. The stereotype of nepotism, which still dominates most people's views of family businesses, stems from this not-so-rare sub-optimization of the family business system. It is clear that if employment is based solely on the candidate's last name, merit and other important criteria in selection and succession processes are devalued or totally irrelevant. Understandably, non-family managers with high career aspirations are often reluctant to join family businesses out of concern for their prospects. Unless due diligence assures them that their career ambitions will not be thwarted by a lack of family ties, high-potential nonfamily managers may choose never to join family-owned or family-controlled businesses.

Since a family business exists primarily for the needs of the family, the benefits that are transferred from the business to family members are often substantial. Financial systems can be obtuse by design, and secrecy is often paramount. After all, the lack of transparency fosters the ability of family members to reap rewards beyond what would be considered reasonable under normal human resources, compensation and benefits policies. As a result, the business is often part of a lifestyle. The Rigas family and Adelphia Communications were eventually sued by the Securities and Exchange Commission (SEC) and other federal and state authorities because of a tangle of corporate and family relationships that were deemed to represent significant personal transactions for the benefit of Rigas family members.

While well-run and well-governed family businesses may have good reason to pay all members of the next generation of senior management equal or nearly equal salaries, family businesses tend to equalize compensation regardless of a family member's responsibility, performance and overall merit. Ironically, because their primary concern is the family, the level of commitment of family businesses to business continuity across generations depends on the agendas of individual family members and the levels of conflict associated with running the business.

Family businesses are likely to choose continuity only if members of the current and next generation aspire to it and if the current generation has sufficient resources in retirement to make it possible. In cases where no generation dreams of continuity or sees the value of making the business a legacy for the next generation, the business will most likely be sold at the end of a generation. And even if family members aspire to perpetuate the business, family businesses find it very difficult to ensure continuity, as the selection of successors, strategic renewal, and governance of the relationship between the family and the business all require a strong commitment to sound business management principles.

The lack of balance and clear boundaries between family, ownership and management is not always resolved by giving priority to family. On the contrary, management or ownership of the business can just as easily be prioritized in decision-making and actions, again to the detriment of the overall family business system.

4.2. The professionalization of the family business as a vector of sustainability:

Management-oriented family businesses are likely to actively discourage family members from working in the business and/or to require work experience outside the business as a prerequisite for employment. The performance of employed family members is evaluated in the same way as that of non-family managers, and human resources policies generally apply equally to family and non-family employees. Compensation is based on responsibility and performance, not position in the family hierarchy. And the company's performance scorecard is entirely business-driven; for example, the focus is on profitability, return on assets, market share, revenue growth, and return on equity. Once in the business, next-generation family members are often considered based on their ability to manage and grow the business - in other words, based on their usefulness and potential contribution to the business.

When family members meet socially, the conversation often turns to business topics. Family events - even weddings and honeymoons - are sometimes arranged, cancelled or delayed for business reasons. There is no automatic commitment to the continuity of the family business in executive-led businesses, because the business is considered a productive asset. As an asset, it can just as easily be integrated into a larger company through a tax-exempt share exchange with a publicly traded company or sold as part of an employee stock ownership plan.

4.3. Sustainability and the question of ownership: what guidelines for future research?

In family businesses where ownership comes first, investment horizons and risk perception are the most important issues. When shareholders come first, priority is given to risk-adjusted economic returns or owner's rents - for example, shareholder value, EBITDA, earnings growth rates, and debt-to-equity and debt-to-asset ratios.

Majority-owned family businesses may have shorter time frames for evaluating financial results. Just as impatient and greedy Wall Street investors, aided by analysts and the media, can push well-run publicly traded companies into short-term thinking, family shareholders who are not active in the business, and who have a poor understanding of the management and time cycles involved in new strategies or investments, can hinder the effective operation of a family-controlled business. These family members can cause the company to lose the founding culture, which valued the role of patient capital, or the long-term investment in the family business.

Patient capital - one of the key sources of competitive advantage for many family businesses - is disappearing at the hands of greedy shareholders. Siblings and cousins caught up in the high expectations of short-term returns through dividends, distributions or shareholder value creation are prone to second-guessing family members who run the business. Family leaders, who better understand the company's limited ability to deliver on the promise of high returns, are more likely to manage in the long-term interests of shareholders. If the family unit suffers from pressure from some family members for high returns and short deadlines, the result can be a loss of will and vision. The continuity of the family business may be abandoned in favor of the immediate recovery, through the sale of the business, of the value created by previous generations.

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