

3.2: Family Business - An Overview

Learning Objectives

1. Explain what a family business is.
2. Understand the role that family businesses play in the US economy.
3. Explain the advantages and disadvantages of family businesses.

“Family businesses are different.” “Focusing on Business Families,” BDO, November 2009, accessed October 8, 2011, static.staging.bdo.defacto-cms.com/assets/documents/2010/04/Focusing_on_business_families.pdf.

BDO 2009 Report: “Focusing on Business Families”

There is no agreed-on definition of a family business. The percentage of ownership, the strategic control, the involvement of multiple generations, and the intention for the business to remain in the family are among the many criteria that experts use to distinguish family businesses from other types of businesses. Joseph H. Astrachan and Melissa Carey Shanker, “Family business’s Contribution to the U.S. Economy: A Closer Look,” *Family Business Review* 16, no. 3 (2003): 211–19. For the purposes of this chapter, however, a **family business** is defined as a business that is actively owned and/or managed by more than one member of the same family. “Family Businesses,” *Entrepreneur*, 2010, accessed October 8, 2011, www.entrepreneur.com/encyclopedia/term/82060.html. A family business can also be defined as the result of someone’s dream:

The story of every successful family business starts with someone who has the passion, confidence and courage to put his [or her] money where his [or her] mouth is...[These entrepreneurs] work incredibly hard, make things happen, are positive without being unrealistic and possess the resourcefulness to overcome all sorts of hurdles. They are also socially adept, capable of communicating effectively and good at inspiring others...“Making a Difference: The PricewaterhouseCoopers Family Business Survey 2007/08,” *PriceWaterhouseCoopers*, November 2007, accessed October 8, 2011, www.pwc.com/en_TH/th/publications/assets/pwc_fbs_survey.pdf.

Family business owners know that their roles are different from that of shareholders in companies owned by many public investors. In addition, “employees in family businesses know the difference that family control makes in their work lives, the company culture, and their career. Marketers appreciate the advantage that the image of a family business presents to customers. And families know that being in business together is a powerful part of their lives.” Kelin E. Gersick et al., *Generation to Generation: Life Cycles of the Family Business* (Cambridge, MA: Owner Managed Business Institute, Harvard Business School Press, 1997), 1.

Market and Employment Presence

Because of the private nature of most family businesses, it is difficult to obtain accurate information about them. Joseph H. Astrachan and Shanker, “Family business’s Contribution to the U.S. Economy: A Closer Look,” *Family Business Review* 16, no. 3 (2003): 211–19. Complicating the situation is that most data sources do not distinguish between small family businesses, such as the local pizza parlor or deli, and large family businesses, such as Walmart, Mars, and Ford. “The reality is that family-based operations are represented across the full spectrum of American companies, from small businesses to large corporations.” “Family Business Statistics,” *Gaebler.com: Resources for Entrepreneurs*, October 10, 2010, accessed October 8, 2011, www.gaebler.com/Family-Business-Statistics.htm. Within this context, the following has been observed: “Family Business Statistics,” *Gaebler.com: Resources for Entrepreneurs*, October 10, 2010, accessed October 8, 2011, www.gaebler.com/Family-Business-Statistics.htm; and Stacy Perman, “Taking the Pulse of Family Business,” February 13, 2006, accessed October 8, 2011, www.BusinessWeek.com/smallbiz/content/feb2006/sb20060210_476491.htm.

- Family businesses account for a staggering 50 percent of the gross domestic product (GDP).
- Although it may seem that this GDP contribution comes from thousands of small operations, 35 percent of the *Fortune 500* companies are family companies.
- Family businesses account for 60 percent of US employment and 78 percent of the new jobs created.
- Family businesses represent one of the fastest growing sectors of the economy because their new job requirements outpace their current employment rates when compared to other types of businesses.

What this means is that family businesses continue to be a powerful economic force, no matter what their size and no matter how they are defined. “Family firms are the most common form of business structure; they employ many millions of people; and they generate a considerable amount of the world’s wealth.” “Making a Difference: The PricewaterhouseCoopers Family Business

Survey 2007/08,” *PriceWaterhouseCoopers*, November 2007, accessed October 8, 2011, www.pwc.com/en_TH/th/publications/assets/pwc_fbs_survey.pdf.

The focus of this chapter is on the small family business.

Video Link 3.2.1:

Mothers and Daughters Partner in Family Business



Advantages and Disadvantages of the Family Business

There are benefits to a family business, but there are disadvantages that must be considered as well. Starting a family business is not for everyone.

Advantages

A family business offers the following advantages:

- One of the popular misconceptions about family businesses is that they are unable to adapt easily to increasing competitiveness and technological progress. The reality is that family businesses frequently have the advantage of entrepreneurial spirit, flexibility, and opportunism. “Myths and Realities of Family Business,” 2002, accessed October 8, 2011, www.insead.edu/discover_insead/publications/docs/IQ03.pdf.
- It is believed by some that family firms are “too soft” and rarely reach their potential. The reality is that family businesses actually outperform public companies. Oftentimes, the marketplace forces public companies to make short-term decisions, whereas a family business has the advantage of having more freedom to make its decisions. Family businesses can adapt to market fluctuations more easily because they can afford to be patient. They have common goals, shared values, and a commitment to brand building. “Myths and Realities of Family Business,” 2002, accessed October 8, 2011, www.insead.edu/discover_insead/publications/docs/IQ03.pdf.
- Family-owned businesses are often seen as ideal because family members form a “grounded and loyal foundation” for the company, and family members tend to exhibit more dedication to their common goals. “Having a certain level of intimacy among the owners of a business can help bring about familiarity with the company and having family members around provides a bui .html.
- The culture of a family business is very different from that of a company you will find on Wall Street. “Family businesses frequently take a very long-term point of view. They’ll make investments that they don’t expect to pay off for 5 or 15 or 25 years...Culture in a family business is more frequently based on very personal and emotional values. It’s stronger because there are deeper roots and closer connections to the history of the company.” Margaret Steen, “The Decision Tree of Family Business,” *Stanford Graduate School of Business*, August 2006, accessed June 21, 2012, www-prd-0.gsb.stanford.edu/news/bmag/sbsm0608/feature_familybiz.html.
- Family businesses are becoming more and more attractive to undergraduate business students who face a bleak job and salary outlook for new grads. These undergrads are choosing to return to their family businesses directly after graduation instead of trying to find a job in corporate America or on Wall Street. Alison Damast, “Family Inc.: The New B-School Job Choice,” *Bloomberg BusinessWeek*, April 12, 2010, accessed October 8, 2011, www.BusinessWeek.com/print/bschools/content/apr2010/bs20100412_706043.htm.

- There is a common misperception that family businesses are less professional and rigorous in their behavior because of the relational nature of the businesses. “American Family Business Survey,” *Mass Mutual Financial Group*, 2007, accessed October 8, 2011, www.massmutual.com/mmfg/pdf/afbs.pdf. However, like all other businesses, family businesses face global competition and rapidly changing markets. This creates more pressure on those who join to make sure that they produce. “This emphasis on professionalism has made family businesses both more daunting and more attractive—and has created new interest in them, from family members, outsiders, and business school students.” Margaret Steen, “The Decision Tree of Family Business,” *Stanford Graduate School of Business*, August 2006, accessed June 21, 2012, www-prd-0.gsb.stanford.edu/news/bmag/sbsm0608/feature_familybiz.html.
- Many family-owned businesses tend to be stable and optimistic, even when economic times are uncertain. They seem to be better able to weather economic difficulties and stabilize the economy than their nonfamily counterparts. “American Family Business Survey,” *Mass Mutual Financial Group*, 2007, accessed October 8, 2011, www.massmutual.com/mmfg/pdf/afbs.pdf. However, this is a function of the industry and the size of the business.
- In general, family businesses feel that they are stronger because family members are involved in their activities. Family owners believe that their family members can be trusted, will work harder, and care more. “The Family Business Survey 2008/2009,” *Praxity*, 2009, accessed October 8, 2011, praxityprod.awecomm.com/News/...essSurvey.aspx. This can help create competitive advantage in the marketplace.
- Family businesses may be more open to flexible or part-time schedules or choosing your hours. This presents a very attractive work environment for people who need to tend to children, parents, or other family members in need. Alexis Writing, “Pros and Cons of Family Business,” *Chron.com*, 2010, accessed October 8, 2011, smallbusiness.chron.com/pros-cons-family-business-409.html.
- Family businesses tend to operate more ethically. In fact, many family businesses believe that their ethical standards are more stringent than those of their competitors. In addition, family businesses are often deeply embedded in their communities, and this proximity is seen as an important factor that increases the likelihood of ethical decision making and moral behavior. “American Family Business Survey,” *Mass Mutual Financial Group*, 2007, accessed October 8, 2011, www.massmutual.com/mmfg/pdf/afbs.pdf. As members of the local community, any ethical problems with a family business will be quickly visible.
- Family businesses also exhibit more social responsibility than their competitors. This has been attributed to their concern about image and local reputation “American Family Business Survey,” *Mass Mutual Financial Group*, 2007, accessed October 8, 2011, www.massmutual.com/mmfg/pdf/afbs.pdf, as well as their closeness to the community.
- Family businesses may incur lower costs because of the greater willingness of family members to make financial sacrifices for the sake of the business. Accepting lower pay than they would get elsewhere to help the business in the longer term or deferring wages in a cash-flow crisis are examples of family altruistic behavior. “Advantages of Family Businesses,” *Business Link*, accessed October 8, 2011, www.businesslink.gov.uk/bdotg/action/detail?itemId=1073792650&type=RESOURCES.
- Family businesses, in general, have greater independence of action because they have less (or no) pressure from the stock market and less (or no) takeover risk. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.
- Family businesses tend to be more resilient in hard times because they are willing to plow profits back into the business. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.
- Family businesses are less bureaucratic and less impersonal, which allows for greater flexibility and quicker decision making. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.
- Family businesses offer the possibility of great financial success. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71. This can manifest itself in interesting ways. “As the family of a media conglomerate once mentioned, ‘The name I have has certainly helped me to get access to top executives of companies, persons who under other circumstances would have kept their doors shut.’” Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.
- Family members have the chance to learn the business early. This extensive expertise can create an important competitive advantage. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71. “One executive recalled how as a child he would take long walks with his father, during which they would visit stores to look at competitor’s products. Afterwards, his father would ask him which

products he liked most, and this would lead to lengthy arguments about each product's quality. This man felt that the expertise he gained during those informal outings proved invaluable later in life." Manfred F. R. Kets de Vries, "The Dynamics of Family Controlled Firms: The Good and the Bad News," *Organizational Dynamics* 21, no. 3 (1993): 59–71.

Video Link 3.2.2:

The future of family business



Why Family Businesses Are So Special

"If family businesses are so common, how can they also be special? When Freud was asked what he considered to be the secret of a full life, he gave a three-word answer: '*Lieben und arbeiten* [to love and to work].' For most people, the two most important things in their lives are their families and their work. It is easy to understand the compelling power of organizations that combine both. Being in a family firm affects all the participants. The role of chairman of the board is different when the company was founded by your father and when your mother and siblings sit around the table at board meetings, just as they sat around the dinner table. The job of a CEO is different when the vice president in the next office is also a younger sister. The role of partner is different when the other partner is a spouse or a child. The role of sales representative is different when you cover the same territory that your parent did twenty-five years earlier, and your grandparent twenty-five years before that. Even walking through the door on your first day of work on an assembly line or in a billing office is different if the name over the door is your own." Kelin E. Gersick et al., *Generation to Generation: Life Cycles of the Family Business* (Cambridge, MA: Owner Managed Business Institute, Harvard Business School Press, 1997), 2–3.

Disadvantages

As attractive as family businesses are on many fronts, they have the following disadvantages:

- Family businesses tend to be stable organizations. Although this is a good thing in many instances, stability can also make it difficult to change. A new, younger family member coming into the business will find tradition and structure. Changing that is not simple. The key to changing a family business lies in defining tradition in terms of the company's core values, not in specific ways of doing things. Margaret Steen, "The Decision Tree of Family Business," *Stanford Graduate School of Business*, August 2006, accessed June 21, 2012, www-prd-0.gsb.stanford.edu/news/bmag/sbsm0608/feature_familybiz.html.
- Family closeness can lead to sibling rivalry or problems when both the parent and the child want control. By the third or fourth generation, with many cousins possibly sharing ownership, governance can become very complicated. Margaret Steen, "The Decision Tree of Family Business," *Stanford Graduate School of Business*, August 2006, accessed June 21, 2012, www-prd-0.gsb.stanford.edu/news/bmag/sbsm0608/feature_familybiz.html.
- There may be times when the interests of a family member conflict with the interests of the business. One family member may want to expand the business, but other family members may not share this person's desire. The needs of the business are not in sync with the needs of the family.
- Family ties have a downside. Family members will frequently be expected to work harder, make more of a commitment, and get paid less than other employees in the business. "The Family Business Survey 2008/2009," *Praxity*, 2009, accessed October 8, 2011, praxityprod.awecomm.com/News/...essSurvey.aspx.

- Family business owners may automatically promote someone from the family or give family members a job even if they do not have adequate skills for the job. A nonfamily employee may be better qualified. Alexis Writing, “Pros and Cons of Family Business,” *Chron.com*, 2010, accessed October 8, 2011, smallbusiness.chron.com/pros-cons-family-business-409.html. This can cause dissension and resentment among other employees.
- Relationships between parents and children or among siblings have a tendency to deteriorate due to communication problems. “This dysfunctional behavior can result in judgments, criticism and lack of support.” Alexis Writing, “Pros and Cons of Family Business,” *Chron.com*, 2010, accessed October 8, 2011, smallbusiness.chron.com/pros-cons-family-business-409.html.
- The family business may be a breeding ground for jealousies, resentment, anger, and sabotage. Family problems may spill over into the workplace. “Advantages and Disadvantages of a Family Business,” September 6, 2009, accessed October 8, 2011, pinoynegosyo.blogspot.com/2009/09/advantages-and-disadvantages-of-family.html.
- The business may be plagued with managerial incompetence, the lack of exposure to other businesses, and the inability to separate family and work. “Advantages and Disadvantages of a Family Business,” September 6, 2009, accessed October 8, 2011, pinoynegosyo.blogspot.com/2009/09/advantages-and-disadvantages-of-family.html.
- Some family businesses may have difficulty attracting and keeping highly qualified managers. “Qualified managers may avoid family firms due to the exclusive **succession**, limited potential for professional growth, lack of perceived professionalism, and limitations on wealth transfer.” David G. Sirmon and Michael A. Hitt, “Managing Resources: Linking Unique Resources, Management, and Wealth Creation in Family Firms,” *Entrepreneurship Theory and Practice*, Summer 2003, 339–58. Succession refers to passing the business to the next generation.
- Family businesses have limited sources of external capital because they tend to avoid sharing equity with nonfamily members. David G. Sirmon and Michael A. Hitt, “Managing Resources: Linking Unique Resources, Management, and Wealth Creation in Family Firms,” *Entrepreneurship Theory and Practice*, Summer 2003, 339–58. Having less access to capital markets may curtail growth. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.
- Not all children of owner-managers may want to join the business. According to one study, Sue Birley, “Attitudes of Owner-Managers’ Children towards Family and Business Issues,” *Entrepreneurship Theory and Practice*, Spring 2002, 5–19. 80 percent of those who did not work in the family business did not intend to go into the business. This reluctance comes from several directions, such as the following:
 - My parents would not want me to join.
 - I could not work for my parents.
 - There are already too many family members in the business.
 - I am not interested in this particular business.
 - The business is too small for me.
 - The business would not allow me to use my talents.
 - The business would not allow me to use my training.
 - I can earn more elsewhere.
 - I am not interested in a business career. Sue Birley, “Attitudes of Owner-Managers’ Children towards Family and Business Issues,” *Entrepreneurship Theory and Practice*, Spring 2002, 5–19.

In Their Own Words

Why Some Children of Owner-Managers Do Not Want to Join the Business Sue Birley, “Attitudes of Owner-Managers’ Children towards Family and Business Issues,” *Entrepreneurship Theory and Practice*, Spring 2002, 5–19.

I see the pressure my dad is under—this does put me off slightly. I want to enjoy my job as well as enjoying life outside work.

A larger factor when working under a relative is the problem of self-worth. It is hard to feel like you are worth something when your father is an MD.

A business relationship with your father makes your family relationship harder.

I do not look to go into the family business straight away, as I feel this is giving a commitment to work there for the rest of my life.

I would join only because I am genuinely qualified, not because I am the owner’s daughter.

The difference in my father’s education and mine is a factor affecting why I have decided not to go into the business. I have more choice over what I want to do as a career, and my personal interests would not be met by my father’s company. I am sure it would not have been his choice had he had the same educational choices as me.

As much as the route into the family business is seen by outsiders as an “easy route to wealth and inheritance,” in my case it was also a liability. At 17, was I to be the fourth generation after 100 years that could not keep the company going?

- The “spoiled kid syndrome” often occurs in a family business. The business owner may feel guilty because his devotion to the business takes away from the attention he should be giving to his children. Out of a sense of guilt, he or she starts to bribe the children, “a kind of pay-off for not being available emotionally or otherwise.” Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.
- Financial strain emanating from “family members milking the business and a disequilibrium between contribution and compensation” Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71. can have a significant negative impact on the business.
- Nepotism that results in the “tolerance of inept family members as managers, inequitable reward systems, [and] greater difficulties in attracting professional management” Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71. can easily lead to low morale among nonfamily members of the business, and it can ultimately result in business failure.
- Family businesses frequently have a confusing organization, with “messy structure and no clear division of tasks.” Authority and responsibility lines are unclear; jobs may overlap; executives may hold a number of different jobs; and the decision-making hierarchy may be completely ignored, existing only to be bypassed. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71. This can create a dysfunctional working environment.
- Family businesses frequently have paternalistic or autocratic rule that is characterized by a resistance to change, secrecy, and the attraction of dependent personalities. Manfred F. R. Kets de Vries, “The Dynamics of Family Controlled Firms: The Good and the Bad News,” *Organizational Dynamics* 21, no. 3 (1993): 59–71.

KEY TAKEAWAYS

- Family businesses account for 50 percent of the GDP, 60 percent of US employment, and 78 percent of the new jobs that are created.
- A family business offers both advantages and disadvantages. It is important to understand both.

EXERCISE

1. In Chapter 2, Robert Rainsford was introduced in the *Frank's All-American BarBeQue* case. He has returned to the family business and is very enthusiastic about expanding the business. He has identified four options: (a) expanding the restaurant either at its current site or elsewhere in Fairfield; (b) opening several similar-sized restaurants in nearby towns; (c) using the Internet to expand sales; and (d) expanding the sales of Frank's sauces from a local store to a regional supermarket chain. Any one of these ideas would represent a change from his father's business model. Given that he had not expressed any interest in the management of the business, how should he go about approaching his father with these ideas? If the company expands, should Robert approach his sister and her husband about taking a more active role in the business? What should their roles be?

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