

# [Comparative analysis of family business management and corporate governance essay...](https://assignbuster.com/comparative-analysis-of-family-business-management-and-corporate-governance-essays-example/)

[](https://assignbuster.com/)[Business](https://assignbuster.com/essay-subjects/business/), [Company](https://assignbuster.com/essay-subjects/business/company/)

## Abstract

Family businesses are managed in a centralised system and process. Corporate governance on the other hand refers to an impersonal system of managing and directing firms through a series of rules that promotes transparency and systems. This paper examines the two concepts and synthesizes them in relation to how they relate to each other.   
The paper identifies that family businesses are not bad. Rather, they promote efficient and effective internal controls that lead to very good performance profiles. However, the study identifies that in cases where the firm expands and grows significantly locally and globalises, there is the need for the corporate governance to be integrated. This promotes the competitive profile of the business in order to control capital, technology and other resource controls to achieve better results in the face of expansion and growth.

## Introduction

Corporate governance has become an important aspect of the world of business since the major corporate collapses involving Enron and Lehman Brothers. This trend has shown that corporate governance is important and vital to the success. Family owned businesses benefit significantly from corporate governance.   
The purpose of this paper is to critically review and analyse the extent to which corporate governance influences and affects the development and growth of family-owned businesses. To this end, the paper will critically review and analyse the concept of corporate governance and its essence in dealing with family businesses and the expansion of such businesses.

## Essence of Corporate Governance

In the UK, the essence and importance of good governance and the proper directing of companies was emphasised in the Cadbury Committee Report of 1992 which stated that proper governance was an antidote to fraud and a catalyst for efficient management of companies. Subsequent reports including the Hampel Committee report, Smith Committee Report and the Higgs Committee report showed that the state had to play a major role by regulating corporate governance and making it a part of corporate law to ensure that directors carried out a set of minimum functions and also disclose some vital requirements.   
The core requirement and importance of corporate governance is in the fact that there is the need for proper control of the firm to be carried out. This is because corporate control is a function of residual rights that are meant to carry out a bargaining decision in each situation and context. Therefore, corporate governance involves a set of mechanisms that ensures that there is a consistent and optimal approach utilised by firms to consider issues and also control important aspects of operations.   
Corporate governance ensures proper management of the property of an organisation and the optimal distribution of corporate power as well as the handling of legitimacy crisis in an organisation. In other words, corporate governance is about the methods and measures that promotes and enhances the optimisation of resources in a given organisation.   
“ Corporate governance is a term which covers the principles that should ensure honesty in business.”. Therefore, corporate governance is about the means through which actions and processes are filtered in an organisation to ensure that the staff and workers meet all expectations and requirements. The main pointers of corporate governance include:

## Transparency;

Accountability &   
Protection of the interest of stakeholders.   
Family Businesses & their Nature   
There are some features that are inherent in family businesses. This is because they are owned by the same people who manage them and it is mainly because the owners and shareholders run the businesses without much of an external intervention. This has implications for governance and control.   
Family governance is characterised by unification of management, ownership and control which is direct and straightforward. This means that there are few or limited complications and difficulties that guide the way things are done. Things are mainly based on the requirements and expectations of the owners. This is in contrast with traditional corporate governance which is focused on appointing external directors who might own very little or no shares in the company.   
One major difference between family governance and corporate governance is the way and manner in which controls are created. Family governance structures and directions are based on the regulations and rules of the owners. On the other hand, corporate governance sets metrics and standards that are used to guide firms and organisations.   
There are many differences and complications that come with the two approaches of corporate governance. First of all, family businesses are able to absorb market risks, allocate capital significantly and reduce uncertainty and transaction costs by being directly involved. This is not the case in other firms and organisations that have and utilise corporate governance models with directors who have little or no direct connection to the issues on the ground.   
Flexible management is in place in family businesses because there are no impersonal rules and regulations. Rather, there are direct and specific controls and management and this is complemented by a few handpicked supportive employees who work hard to complement the vision of the firms.   
Also, owner diversity is linked to the family system, industry structure and business growth. This means that there is a better strategic fit that almost always manifests in better firm performance. However, the main risk and inherent challenge with family business structures have to do with the fact that owner-manager decisions could be highly subjective and lead to major problems and issues.   
On the other hand, evidence shows that family business governance models are highly constrained in areas of internationalisation and large-scale expansion. This is because internationalisation in the 21st Century means more than operating in a few countries as it was in the 19th Century, where expansion as only about moving a firm from Europe to one or two countries. Internationalisation today implies expanding to a wide array of nations. And it is important for a family business to delegate authority rather widely than it would have done a century or two back.

## Corporate Governance and Family Businesses

“ Decision-making is very different when it’s your own money that’s at stake,” . This is very relevant to the dichotomy and approach utilised by family business owners and directors who are involved in corporate governance. There is the agency constraint and the agency problem which creates a risk of the digression in the utilisation of the organisation’s resources in the best way and manner possible.   
It is noted that “ family firms tend to have a long-term commitment to jobs and local communities, which gives a significant but often under-rated”. However, corporate governance makes major changes to the approach and methods that are used to conduct business, especially when the size of the firm expands and goes beyond the previous scope.   
Brenes et al (2011) identify the core feature of corporate governance and its structures are to help improve strategy and integrate control mechanisms on family businesses. This is because corporate governance creates a system through which communication and relationships are built between the family owners and the business executives. Therefore, there could be communication and relationship issues between family owners and business owners. Therefore, there is the need for some kind of protocols to be developed that blends formal and informal communication systems and channels to prevent conflicts and challenges in relation to corporate governance in family businesses.

## There are three prominent areas that are of importance in blending corporate governance and family business management/control which are:

Principal-agent theory;   
Stewardship theory &   
Resource-based view of the firm   
These set the parameters in areas including the agency costs, competitive advantage and the governance structure which determines the extent to which a firm can carry out its activities and blend all the management and control issues. Therefore, there is the need for careful interactions and connection and blending of family business systems and corporate governance.   
In terms of international expansion, there are many variables that ought to be put in perspective before a family business can appropriately expand. This includes the examination and evaluation of five main things - institutional differences, principal-principal differences, families, business and groups and minority interests, principal-principal conflicts in emerging countries. These pointers help to institute and apply important elements and aspects of corporate governance in the operations of a business that was previously ran solely by a family.

## Recent Trends and the Need for Evolution from Family Governance to Corporate Governance

In the practical sense, family governance and corporate governance can only be examined and reviewed in the constructive sense on the basis of recent trends in corporate governance in the family businesses. Therefore, this section of the research will draw on research and studies conducted into the elements of family businesses in the 21st Century.   
Studies indicate that the dominant trend in contemporary family businesses include longer-thinking and broader perspectives in carrying out activities and processes. This includes a more critical and thorough analysis of opportunities and threats before decisions are taken. This includes a careful and sceptical review and assessment of information through conservative methods and measures before a decision is taken. This creates a more conservative trading posture which ought to be preserved even if the firm expands and grows.   
Also, due to the lack of bureaucracy and impersonal rules and regulations, there are quicker and more flexible approaches to decision making. This includes the use of various simple and flexible traditions that are used to take decisions and also get decisions approved or authorised. This culminates in a tradition of running leaner and less dense organisational structures. Hence, things are achieved quicker and more efficiently. Thus, there is a general sense of concern in introducing corporate governance which might complicate a functioning system and process.   
Evidence also shows that survival and succession are interlinked in the success of modern family businesses. This is because most family businesses pass on to close family relations. Therefore, there is the need for the succession plan of a family to be guaranteed and this is not always the case when family businesses are set up. However, in some cases, there could be minority interest clauses in the articles of incorporation that could guarantee some aspects of corporate governance in these situations.

## Relevant Highlights of Family Businesses & Relevance to Corporate Governance

Surveys and studies into family business show that there are some relevant issues that ought to be reviewed and evaluated into the years 2017. This includes the need for family businesses to focus on financial and social sustainability requirements for the growth of businesses like family businesses.   
Additionally, there is the need to retain and maintain centralised control and the introduction of family members to ensure the transfer of family businesses to the next generation. And in this process, family image, reputation and status are important and must be retained in all situation and contexts. There are numerous elements and features of concern that stands in the way of applying and integrating elements and aspects of corporate governance.   
However, there are some elements of important processes and procedures that ought to be put in place in order to achieve the best results in terms of corporate governance. This includes major trends and processes that ought to be put in place to achieve the best of results.   
First of all, the economy is a major cause of concern to all family businesses today. There is the need for proper and in-depth examination and prediction of economic change in the 21st Century. Therefore, there is the need for corporate governance systems and processes in order to achieve the best and most appropriate approaches and methods of evaluating and assessing important changes in the economy in order to objectively position the firm without any major strategic gaps and issues. Thus, corporate governance is important in many ways and positions in achieving these ends and goal.   
Secondly, globalisation is an important and vital end for the achievement of corporate strategic goals in family businesses today. This includes the fact that global expansion come with complications and requires the raising of a lot of funds to carry out expansion and also the involvement of other interest groups in foreign countries. The process is such that it must be done through cooperation and a corporate governance system that cannot be modified or changed in any way or form. Therefore, all companies that are ran as family businesses will need to present some degree of accountability and transparency to prove sceptics wrong and guarantee the highest and best levels of results and operations.   
The creation of corporate governance standards also opens the door for more innovation in order to achieve competitive advantage. This is because the survey of Pricewaterhouse shows that technology and its control thereof is a major aspect of achieving survival in the corporate world for these family businesses. Hence, the growth and expansion into technological arenas and processes will help to promote and enhance business and will allow a firm to invest significant portions of their capital in capital to power and aid the expansion plans a family business might need to survive the competition.   
Finally, there is the need for talent to be attracted and sustained in a family business. Family businesses often prefer to hire a few people and maintain a lean production system. However, for proper expansion to achieve its goals and requirements, there is the need for a family business to evolve and integrate important aspects and elements of human capital and its management. This is about the process of attracting talented workers and competing with other firms in the industry for the best.   
Risk management and control of external risks are an important and vital part of corporate governance. This includes the fact that corporate governance involves the presentation of important goals and strategies to the firm in dealing with its risks and issues. This is done by the examination and evaluation of external risks as an inherent part of management and this must be done in a way and manner that promotes transparency and accountability. This is something that most family businesses do not do. However, the integration of corporate governance will help family businesses to critically assess and analyse issues in the markets and position the firm properly.   
Corporate governance on the other hand does not normally mean that succession systems of family businesses will end. There could be many situations where the succession plans of family businesses can be retained. And one of them is to integrate it into the articles and corporate governance rules and regulations.

## Internationalisation and Corporate Governance

The surveys of major corporate firms indicated that corporate governance is an important part of the expansion and growth of family businesses. One of the family businesses had a representative who said “ corporate governance standards are an issue – if we want to grow then our standards will need to be up to speed with international best practice”.   
Therefore, corporate governance and its rules are important and vital in the expansion of family businesses. The cycle of family businesses included the following four steps:

## Entrepreneurship

Growth   
Governance &   
Maturity.   
This includes the formulation of the firm and the growth of the firm. In this process, the governance of the family system was central and important. However, when a family business gets to the mature state, there was the need for corporate governance information and rules to be adopted and integrated into the family business to help it to grow. Growth is about internationalisation and there is the need for this to be integrated and instituted in these family businesses.

## Conclusion

The study shows that corporate governance operates almost always in the larger entities and organisations. Family businesses use a centralised system of communication and this helps to govern and control the companies. However, when the family business grows and expands, corporate governance is the best and most appropriate system to ensure a disciplined system of growing and controls.   
However, family businesses are well run and efficient. In this process, there are mainly centralised and they focus on operating under the rules of the managers and owners. In spite of this, when they grow to a certain point, the only solution is to grow and expand the business to meet its obligations.   
Corporate governance helps to predict and forecast and align a family business into the broader context of growing a company. There are also issues with globalisation which requires more control and the building of trust through a democratic approach and system. Corporate governance creates the avenue to acquire more talents in the industry and using technology and innovation in order to achieve competitive advantage.   
In spite of this statement, there is a stronger case for the creation of family businesses and running them in a lean and centralised system. The limit of this is the fact that corporate governance is the only system through which extreme expansion and internationalisation can be controlled and managed properly.

## References

Arregle, J. C., Naldi, L., Nordqvist, M. & Hitt, M. A., 2012. Internationalization of Family-Controlled Firms: A Study of the Effects of External Involvement in Governance. Entrepreneurship Theory and Practice, 36(6), pp. 1115-1143.   
Brenes, E. R., Madrigal, K. & Requena, B., 2011. Corporate governance and family business performance. Journal of Business Research, 64(3), pp. 280-285.   
Carney, M., 2010. Corporate Governance and Competitive Advantage in Family Controlled Firms. Entrepreneurship Theory and Practice, 29(3), pp. 249-265.   
Credit Suisse, 2012. Family Businesses: Sustaining Performance. [Online] [Accessed 6 July 2015].   
Dewan, S. M., 2011. Corporate Governance in Public Sector Enterprises. Delhi: Prentice Hall India.   
Du Pleiss, J. J., Margovan, A. & Bagaric, M., 2010. Principles of Corporate Social Responsible. Cambridge: Cambridge University Press.   
Epstein, J. & Buhavac, A. R., 2014. Making Sustainability Work: Best Practices in Managing and Measuring. 2nd ed. San Francisco, CA: Berrett-Koehler.   
Goel, S. et al., 2012. Strategy, ownership, governance, and socio-psychological perspectives on family businesses from around the world. Journal of Family Business Strategy, 3(2), pp. 54-65.   
Kouzmin, A., 2014. Refounding Corporate Governance: The Metaphysics of Corporate Leadership. 2nd ed. London: Bentham Science.   
Pricewaterhouse Coopers, 2012. Family Firm: A Resilient Model for the 21st Century. [Online] Available at: http://www. pwc. com/fambizsurvey[Accessed 5 July 2015].   
Siebels, J. F. & Knyphausen-Aufseß, D., 2012. A Review of Theory in Family Business Research: The Implications for Corporate Governance. International Journal of Management Reviews, 14(3), pp. 280-304.   
Sison, A. G., 2014. Corporate Governance and Ethics: An Aristotelian Perspective. Surrey: Edward Elgar.   
Young, M. N. et al., 2008. Corporate Governance in Emerging Economies: A Review of the Principal-Principal Perspective. Journal of Management Studies, 45(1), pp. 196-220.