

What Constitutes a Family Business?

What do we mean by the term *family business*? Its definition is not as easy to come by as you might think.

- In a comprehensive study of family businesses, Chua, Chrisman, and Sharma cited 21 different definitions of family business found in their review of 250 research articles.
- 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. That is why estimates of the number of family businesses operating in the U.S. economy range between 17 and 22 million. IN the free economies of the world, estimates of all enterprises considered family businesses range between 80 and 98 percent.
- In a large-scale study of the role of family contractual relationships within the Spanish newspaper industry, a business was considered to be a family business if the last name of the CEO and/or the editor was the same as that of the owners.
- Another recent empirical study took the position that family firms are theoretically distinct from other closely held firms because of the influence of altruism on agency relationships (relationships between shareholders and management). The authors of this study went on to say that family firms are differentiated by both the active involvement of family in firm management and the intent of family members to retain ownership of the firm. They ultimately defined a family business as enterprise where two or more family members hold 15 percent or more of the ownership, where family members are employed in the business, and where the family intends to retain control of the firm in the future.
- A more recent article ascribed the uniqueness of a family business to the very different influence that family has on ownership, governance, and management participation; the experience reflected in the generation in charge; and the organizational culture embedded in the enterprise.

Taking into account this full range of research and analyses, this text considers family businesses as constituting the whole gamut of enterprises where an entrepreneur or later generation CEO and one or more family members influenced the firm. They influence it via their participation, their ownership control, their strategic preferences, and the culture and values they impart to the enterprise. Participation refers to the nature of the involvement of family members in the enterprise, whether as part of the management team, as board members, as shareholders, or as supportive members of the family foundation. *Control* refers to the rights and responsibilities family members derive from significant voting ownership and the governance of the agency relationship. *Strategic preferences* refers to the direction family members set for the enterprise through their participation in top management, consulting, the board of directors, or even family councils. *Culture* is the collection of values, defined by behaviors, that become embedded in an enterprise as a result of the leadership provided by family members, past

and present. Family unity and the nature of the relationship between the family and the business also define the culture.

[The authors] adopt an inclusive theoretical definition of a family business that focuses on the vision, intentions, and behaviors, vis-à-vis succession, of the owners. Ownership structure aside, what differentiate family businesses from management-controlled businesses are often the intentions, values, and strategy-influencing interactions of owners who are members of the same family. The result is a unique blending of family, management, and ownership subsystems to form an entire family business system. This family-management-ownership interaction can product significant adaptive capacity and competitive advantage. Or it can be the source of significant vulnerability in the face of generational or competitive change. This 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 manner that is potentially sustainable across generations of the family or families.”

Thus, we arrive at a working definition of a family business. A family business is a unique synthesis of the following:

1. Ownership control (15 percent or higher) by two or more members of a family or a partnership of families
2. Strategic influence by family members on the management of the firm, whether by being active in management, by continuing to shape the culture, or by serving as advisors or board members
3. Concern for family relationship
4. The dream (or possibility) of continuity across generations

The following characteristics define the essence of the distinctiveness of family firms:

1. The presence of the family
2. The owner’s dream of keeping the business in the family (the objective of business continuity from generation to generation)
3. The overlap of family, management, and ownership, with its zero –sum (win-lose) propensities, which render family businesses particularly vulnerable during succession
4. The unique sources of competitive advantage derived from the interaction of family, management, and ownership, especially when family unity is high

Poza, Ernesto J. Family Business. Mason: South-Western, 2004.