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A Neglected Factor Explaining Family Business Success: Human Resource Practices

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A Neglected Factor Explaining Family Business Success: Human Resource Practices

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Over 600 family firms were involved in this examination of the impact of human resource management (HRM) and professional governance practices on family business success and survival. Our findings identified some of the most prevalent family firm HRM practices and found significant positive correlations among HRM practices, gross firm revenues, and CEO personal income levels. The results support prior arguments for competitive advantage in the marketplace gained through effective use of HRM practices. An interesting additional finding was that while boards of directors, strategic planning, and frequent family meetings were correlated with business longevity over multiple generations, succession planning was not. Such practices are important for current competitive advantage and may also be crucial to the longevity of the business.

With over 90 percent of all American corporations being family owned or family controlled and accounting for about 40 percent of the gross national product, surprisingly little attention has been paid by researchers, scholars, and consultants to this unique organizational configuration (Wortman, 1992; Hollander and Elman, 1988; Beckhard and Dyer, 1983). The available empirical evidence on family firms is dominated by "armchair articles, experiences, folklore, and stories," according to Wortman (1992), who pleads for new systematic research streams on this organizational entity.

There is much anecdotal evidence that suggests family firms are different from nonfamily firms. Whiteside and Herz Brown (1991) suggest that a family business is a particular type of system that is different from either a business system or a family system. Furthermore, they imply that merely discussing the overlaps of business and family systems is an inappropriate way to characterize family businesses and can lead to important misunderstandings. Others indicate that relationships between the management of the firm and the family increase the complexity of organizational and management problems and issues exponentially (Tagiuri and Davis, 1992; Kepner, 1991; Holland and Boulton, 1984; Beckhard and Dyer, 1983). It is the unique qualities of a family business system seen by many as an overlap between the institutions of family and business that make the generic human resource management tasks of employee selection, compensation, appraisal, and development such volatile concerns in the professional management of the firm. Although this institutional overlap has the potential to contribute positively to organizational success (Brokaw, 1992; Kets de Vries, 1993), often this key interface damages both entities. It is no wonder that few family firms survive the founders' average tenure of 24 years (Beckhard and Dyer, 1983).

The argument that today's organizations must gain competitive advantage through more effective utilization of their human resources (Peters, 1992; Cascio, 1992) appears to put family firms under even greater stress. Competitive advantage can be established through financial, strategic, and technological means, but the most enduring, and the most difficult to achieve, source of competitive advantage comes from the improved organizational capability of people (Ulrich and Lake, 1990). Organizational capability is "a business's ability to establish internal structures and processes that influence its members to create organizational-specific competencies and thus enable the business to adapt to changing customer and strategic needs." (Ulrich and Lake, 1990, p. 40). Limited organizational capability may be one key factor contributing to the short lifespan of family firms in an increasingly competitive global market.

With people costs representing approximately 55 percent of operating budgets across all U.S. industries (Cascio, 1991), it is important that there be more research focus on organizational capability and human resource practices in family businesses. Because of the pervasiveness of strong family values (Aronoff and Ward, 1994) and family commitment to the firm (Astrachan and Lansberg, 1989), family firms would appear uniquely capable of harnessing the component elements that Ulrich and Lake (1990) define as essential to the establishment of organizational capability: shared mindset, capacity for change, leadership, and human resource practices.

In recent empirical assessments and reviews, human resource management practices and systems have been linked to organizational competitive advantage, increased productivity, higher quality of work life, and greater profitability (Cascio, 1992; Schuster, 1985). These studies did not explore family businesses as a separate cohort, leaving a need for empirical evidence to guide family firm human resource practices, choices, and options. A recent comprehensive review of family-owned business research by Wortman (1992) does not include human resource practices in its new conceptual paradigm to guide family-owned business research. Although most of the existing empirical support for the effectiveness of human resource practices has been based on studies of large corporations, no investigations of the 126 family-owned or family-controlled firms in the *Fortune* 500 have compared their human resource practices with those of other firms (Mullen, 1992).

In a comprehensive review of family business literature and publications, Desman and Brush (1991) reported that only 4.2 percent of the 202 citations reviewed dealt with the development of human resources through education and training, but 6.6 percent focused on the topic of management succession. To date, the dominant human resource activity receiving widespread attention by writers and researchers has been top leadership and ownership succession (Welsch, 1993; Wortman, 1992; Handler, 1990). That focus has overlooked other important human resource activities associated with recruitment, selection, development, compensation, and performance evaluation that affect every employee in family firms.

Human contributions to the bottom line in a family business can only increase when that resource base is identified, managed, and developed. Although family members have always provided labor to the firm, optimization of that contribution has received little research attention or interest. Clearly, some family businesses have gained competitive advantage by developing and managing their human assets as well as their cash flow. But identification and validation of those critical human resource practices has lagged in the family business sector. External validity of empirical family firm research has been hampered by an overreliance on case studies and the generally small samples used in previous family firm research. The largest sample size in Wortman's (1992) comprehensive review of family business research was 265 firms. The generalizability of the prescribed human resource practices is suspect when applied to the diversity within the 12.9 million family business firms in the United States (Mullen, 1992; Dreux, 1990).

Study Purposes

Our study empirically examines the relationships between human resource practices and critical family firm success and survival outcomes. This exploratory investigation attempts to validate for the first time the contribution of human resource management practices to firm effectiveness across a large and diverse group of family businesses. The following basic research questions were addressed in this study: (1) What are the most frequently employed human resource management (HRM) practices in family business firms? Efforts to manage the human resource base in family firms can include traditional HRM activities, such as performance appraisals and compensation planning, and more fundamental management governance practices, such as written business plans. (2) Do human resource management practices contribute to family business success and survival? A positive relationship between the use of HRM practices and indices of family firm success/survival would confirm the importance of developing this organizational capability in family businesses. (3) What business owner characteristics (education, age, sex) can explain the use of human resource management practices in family firms? In other words, are there any individual difference variables associated with a stronger focus on HRM practices in family businesses?

Methodology

To address these research questions, a large national sample of family businesses was needed. Research support was provided by Massachusetts Mutual, an insurance company, as part of its ongoing research program to better understand family businesses.

Sample. Perhaps nothing is more critical in conducting family business research than the definition of family firms. Consistent with Handler's (1989) definitional criteria for a family firm, business ownership and management had to be established in this study. Using a random listing derived from Dun & Bradstreet and Survey Sampling data bases, an initial telephone inquiry was used to establish whether or not the firm met the Handler (1989) criteria.

In this study, the specific criteria used to classify a business as a family firm are as follows:

Family ownership of more than 50 percent of the business for private firms (99 percent of the final sample) or more than 10 percent of the stock in public companies
More than one family member works in the business *or* the owner anticipates passing the business to the next generation of family members *or* the owner identifies the firm as a family business
Ten or more employees
Annual revenues exceeding 2 million dollars
At least ten years of continuous operations

Furthermore, because of the lack of family businesses in the following heavily regulated industries, the business could not be a nonprofit organization, a public utility, bank, insurance carrier, a personal investment company, or involved in the health, legal, educational, or social service fields. The extensive efforts applied to sample identification and qualification were deemed necessary to maximize the generalizability of the study's findings.

Participants in this study had to hold CEO, president, or owner positions within the family firm. Table 1 presents a demographic profile of the respondents, including gender, age, race, household income, and education, along with profiles of the family firms sampled including their annual gross revenues, number of full- and part-time employees, and the number of generations the business has been in the family.

Data Collection. Structured telephone surveys were used to collect the data. This method was selected over written or mailed questionnaires because it permitted timely data collection, higher respondent involvement levels, follow-up questioning and clarification, and administrative control. However, perhaps the greatest advantage of structured telephone interviews lies in sampling controls (Churchill, 1991). These sampling control concerns were very important given the need to direct the inquiry to our designated respondents (founder, owner, CEO) and to help secure that person's cooperation.

Table 1. Respondent and Family Firm Profiles

Respondent age	
Under 50	48%
50–64	38
65 and older	13
Respondent gender	
Male (n = 504)	82%
Female (n = 110)	18
Respondent race	
White	92%
Hispanic	3
Asian American	2
African American	1
Other or refused to reply	2
Education	
Some high school or less	5%
High school graduate	24
Some college/trade school	24
College graduate	33
Postgraduate work/degree	13
Refused	1
Household income	
Under $50,000	14%
$50,000–$100,000	30
$100,000–$250,000	31
Over $250,000	17
Refused	8
Revenues	
Under $10 million	84%
$10–25 million	6
$25–50 million	3
$50–100 million	1
$100 million or more	1
Missing	5
Mean number of full-time employees: 50	
Mean number of part-time employees: 15	
Number of generations business has been in the family	
One generation	50%
Two generations	26
Three generations	18
Four or more generations	5

Note: n = 614.

The Gallup polling organization collected the data using a structured telephone interview format during August and September 1993. Five attempts were made to contact a given interviewee. Those not participating most often cited a lack of time as a reason. Of those who were qualified to participate in the study (family businesses), 78% chose to participate in the study, yielding a final sample of 614 family businesses.

A structured telephone interview protocol insured standardized response conditions and limited any order effects in the questioning. An introductory description of the purpose and goals of the research was shared with subjects to verify their role in the business and secure their cooperation for the 20- to 40-minute interview period. Subjects indicating an inability to meet that time estimate were recalled.

Measures. The interview questions focused on how the business got started, the family's involvement level over time, succession planning, the use of select human resource management and governance practices, and the importance of various financial goals. (A list of the 52 interview questions is available from the authors.) In addition, several biographical and demographic characteristics were collected, such as respondent gender, age, educational attainment, number of full-time and part-time employees, the firm's gross revenues, and annual personal income levels. All respondents were promised feedback on the study's results and potential future follow-up study involvement.

Human resource management practices. Six interview questions assessed the use of various common human resource practices in these family firms. Respondents were asked if they used written job descriptions, had formal compensation plans, conducted formal employee performance reviews, had a written employee manual, had a written succession plan, and whether the firm had specific entry requirements. A human resource management practice (HRMP) scale was computed, representing the number of aforementioned human resource practices used in the firm. The six items, the percentage of family firms using each human resource management practice, and the HRMP scale average value are presented in Table 2.

Firm governance practices. In addition to the HRMPs assessed, more basic business practices dealing with management governance processes that could contribute to increased organizational capability were investigated. Three interview questions measured the use of formal management governance practices in the sample firms. Interviewees were asked if their firm had a written business plan, held regularly scheduled family business meetings, and held regular board meetings. A firm governance practices scale was similarly calculated to capture the total number of governance practices used in each family firm. The three items, the percentage of family firms using the practice, and the summary scale average value are also shown in Table 2.

Family business survival and success outcomes. Five interview items dealt with common measures of family business success/survival and served as out-

Table 2. HRMP and Family Governance Items

Human Resource Management Practices (for family and nonfamily employees)	
Do you have a formal and regular employee review process?	59%
Do you have set compensation plans?	57
Do you have a written employee manual?	56
Do you use written job descriptions?	53
Do you have a written succession plan?	21
Does your business have formal and established entry requirements for family members who want to work in the business?	16
Summary HRMP Scale (mean = 2.63, SD = 1.66)	
Governance Practices	
Do you hold regularly scheduled meetings with family members involved in the business?	51%
Do you have a written business plan?	42
Do you hold regular board meetings?	42
Summary governance scale (mean = 1.36, SD = 1.05)	

Note: $n = 614$. Percentage of affirmative responses shown above.

come measures in this study. The questions assessed the number of generations as a family firm, the firm's gross revenues, reported access to capital, the personal income of the CEO, and number of full-time employees. The descriptive statistics for these items are presented in Table 3.

Analysis and Results

Basic descriptive statistics and Pearson product-movement correlations were utilized to examine the three research questions anchoring this empirical investigation. Table 2 shows the percentage of family firms, indicating their current use of specific human resource management practices and basic management governance practices. A paired comparison *t* test was used to test whether these percentages are significantly different from one another. In other words, were certain HRMPs used significantly more than others within the family firm?

The results in Table 2 confirm that certain HRMPs are used more frequently than others. Employee reviews, compensation plans, written employee policy manuals, and written job descriptions were used significantly more frequently in family firms than written succession plans or formal entry requirements for family members($p \leq .05$). The less frequently used succession planning finding is consistent with the authors' experiences. In regard to family business governance practices, results show that family meetings are used significantly more often than written business plans or board meetings ($p \leq .01$) in the family businesses sampled. In general, firms that used one HRMP were likely to use others as well, with the exception of succession planning.

Table 3. Means, Standard Deviations, and Correlations of Study Variables

				Correlations								
Variable	*n*	*Mean*	*SD*	*1*	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*
Gender	614	1.18	.39									
Educational level	609	3.74	1.57	–.14**	1.00							
Respondent birth year	608	1942.67	11.87	.10**	.02	1.00						
HR practices scale	597	2.63	1.66	–.12**	.06	–.02	1.00					
Governance practices scale	610	1.36	1.05	–.05	.10**	.01	.51**	1.00				
Number of generations business in family	216	1.83	1.08	–.09	.16**	–.01	.03	.12*	1.00			
Full-time employees	604	49.86	122.44	–.12**	.19**	–.06	.20**	.17**	.02	1.00		
Gross revenues	581	1.22	.68	–.09*	.18**	–.05	.16**	.15**	.01	.77**	1.00	
Reported access to capital	609	1.83	.90	.01	.05	–.01	–.14**	–.03	–.15**	–.09**	–.12**	1.00
Respondent personal income	557	2.56	.96	–.17**	.18**	–.13**	.21**	.04	.15*	.25**	.25**	–.28**

Notes: Gender: 1 = male, 2 = female. Educational level: 1 = some high school, 2 = high school graduate, 3 = some college, 4 = college graduate, 5 = postgraduate. Gross revenues: 1 = under \$10 million, 2 = \$10–25 million, 3 = \$25–50 million, 4 = \$50–100 million, 5 = more than \$100 million. Respondent personal income: 1 = under \$50,000; 2 = \$50,000–\$100,000; 3 = \$100,000–\$250,000; 4 = over \$250,000.

*$p < .05$.

**$p < .01$.

Table 3 presents the means, standard deviations, and intercorrelations for each study variable. The human resource practices summary scale was significantly correlated with four of the five family firm success/survival outcomes assessed: owner/respondent personal income ($r = .16, p \leq .01$), number of full-time employees ($r = .20, p \leq .01$), firm gross revenues ($r = .21, p \leq .01$), and reported access to capital ($r = -.14, p \leq .01$). No support was found for the link between HRMPs and the number of family business generations. These results confirm the important relationship that human resource practices play in family firm success and survival.

It is also interesting to note that business governance practices and HRMPs were significantly related ($r = .51, p \leq .01$). Governance practices were also positively associated with organizational survival across family generations ($r = .12, p \leq .05$). The relationships between family governance practices and the five outcomes were much weaker, with only the number of full-time employees ($r = .17, p \leq .01$) and gross revenues ($r = .15, p \leq .01$) related to the governance scale.

The final research question concerned the relationship between business owner characteristics and the prevalence of human resource management practices in their family firms. The results show that only gender was related to HRMP ($r = -.12, p \leq .01$) with male owners/CEOs more likely to have HRMP in place. In addition, owner/CEO educational level was the only individual characteristic studied that was significantly related to the prevalence of business governance practices ($r = .10, p \leq .01$), with more highly educated owners more likely to use such governance practices in their firms.

Discussion

This exploratory investigation supports the important role that human resource management practices, along with professional governance practices, play in the success and survival of family firms. It provides empirical evidence, albeit perhaps circumstantial, for the long-standing prescriptive and anecdotal arguments concerning the critical contribution of sound human resource practices in family businesses that Lansberg (1983) and others have made in the past. Furthermore, this study's near pure random sample selection and large sample size permit greater confidence in the generalizability of these findings to family firms than most past family firm research efforts.

We urge caution in interpreting these findings to suggest a causal link between business success and survival and HRM and governance practices. Causality was not studied and the correlations reported in this study are low enough to allow for many other factors in addition to HRMPs that also account for long-term survival and success. However, we believe that such policies and practices are indicative of many other elements that are also needed for survival and growth, such as the ability to discuss and evaluate business policies, practices, and visions.

Before this study, the only significant human resource management practice studied in family firms focused on succession planning efforts (Welsch, 1993). Our findings provide the first insight into the actual prevalence of six common human resource management practices in family firms, thus meeting the first goal of our research. Formal employee reviews, set compensation plans, written employee manuals, and use of written job descriptions were found to be the most widely used HRMPs in the family firms studied.

The second objective of this study focused on examining the relationship between HRMPs and family firm success and survival. Positive associations were found between HRMPs and gross firm revenues and the CEO/owner's personal income level. These results are consistent with the "organizational capability" logic proposed by Ulrich and Lake (1990), where firms establish competitive advantage in the marketplace by developing and leveraging their human resource base.

This empirical support for more professional management practices in family firms was also reinforced by findings regarding family firm governance practices. The positive association found between governance practices and business survival (number of generations family firm) and firm success (gross revenues) was supported in our data. Overall, better management practices apparently yield significant payoffs for family firms. Thus, Welsch's (1993) finding that family firms do not seem to involve HRM experts in the business to the extent that nonfamily firms do may represent an opportunity cost to family businesses.

The practical implications of this research point to the need for family firms to implement the HRMPs and governance practices studied here. Family business success and survival outcomes were empirically linked, for the first time, to a set of HRMPs in a large sample of diverse family firms. Ignoring the importance of these sound management practices could provide other firms in one's industry with an opportunity to gain competitive advantage (Peters, 1992).

Related study findings were no less significant. When the correlation between the use of written succession plans and the number of generations the business had survived in the family was examined, no empirical linkage was found ($r = .04$, n.s.). This finding challenges prior arguments (Handler, 1990; Beckhard and Dyer, 1983) that written succession planning permits family firms to better survive across generations as a family entity. It seems that strategic planning, boards of directors, and families that meet regularly are more important to long-term survival and success. Such practices may be indicative of open family and business relationships as well as common understanding of goals, which can aid long-term survival.

Family business researchers should modify their conceptual frameworks and paradigms to include specific aspects of professionalization of business practices, such as the role of HRMPs and governance practices. The "organizational capability" provided by better development and utilization of the existing employee resource base is worthy of study as a potential competitive advantage for family firms. Additional studies should explore the independent contribution of various types of human resource practices to family firm success, industry-specific HRMPs, longitudinal case studies (Welsch, 1993), and the causal process of how HRMPs affect key outcomes. Future research should seek to validate the findings of this exploratory research.

We hope others will investigate whether these findings represent the "tip of the iceberg" in the study of human resource practices in family firms or a limited avenue for family firm development and growth. Our evidence points to the former.

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