

Corporate Governance and Family Business Performance

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In principle, the board of directors instills a sense of professionalism and a norm for governance in a company. Three Costa Rican researchers, Esteban Brenes, Kryssia Madrigal and Bernardo Requena conducted a research study to evaluate the effect of a professional board of directors on the firm's performance. They selected a set of Latin American family businesses some of which had developed a family protocol or formalized a corporate governance structure. They conducted a survey among the members of the owning family and each non-family director or executive to study the governance structure in their respective companies and the firm's performance.

The authors found in their research that the role of boards of directors in family firms goes through transition as the businesses grow. This transition could be broadly classified into three stages as following:

Initial Stage - In the early stages of board formation, its members play the role of advisors to the company and the family. They provide objective advice and support decision-making. In some cases, they also oversee the transition of shareholding to the successors.

Maturity Stage - As the business matures, the role of the company's board becomes that of a catalyst between the family and the business. It helps create bodies and mechanisms for managing the family - business relationship and ensures effective and regular communication with the family on business matters. The board also protects the interests of the company and its shareholders, thereby that of the family as well.

Professionalisation Stage - When the company adopts professionalisation, the role of the board undergoes another transition. The board ensures effective administration and operations in the company. It sets the standards for goals and investment decisions for the business. It evaluates the decisions taken by the company's management with regard to investments and profitability. It assesses the managers' business analyses and their assumptions while ensuring that good creative ideas are not stifled. In many cases, the board also formulates a capital allocation strategy taking into account various requirements of the family and the business.

The authors found that setting up a formal board of directors, helps improve the business performance. Moreover, effective evaluation of board performance leads to better performance of the family business firm compared to its competitors. The findings also suggested that the board enriches the company management by bringing in objectiveness to the firm. Inclusion of independent, non-family members on the board improved transparency and confidence with

respect to business operations of the company especially among the non-participating family members. The authors found that family and non-family members brought complementarity on the company's board - while family members brought knowledge, experience, family values and culture, non-family members brought objectivity and professional approach to business.

The study found that about 60% of the business families had established some family government body, either a business council or a family council. Family governance was found to be more relevant for larger families as they had many non-participative members. The larger families preferred to have business councils since those were considered more effective mechanisms for conflict resolution. In case of smaller families, family councils were preferred as means of resolving conflicts and promoting family interests.

The authors concluded that establishment of formal governance bodies such as a professional board of directors, a family or a business council helps improve the business performance of the family firms. Most importantly, in many family businesses, the non-family board member takes on the role of a conciliator in resolving business/family conflict. This provides peace of mind to the members of the owner family. Resentments and viewpoints often clouded by emotions cleared when dealt with the objectiveness of an outsider. This contributes to family unity and business sustainability.

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