

EMPIRICAL STUDY ON THE BOARD WORKING STYLE IN FAMILY BUSINESS

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Abstract The purposes of this paper are to explore the relationship between the board working style and the board role performance. Based on the analysis results of 107 Chinese family businesses, the results shows that board's working style affect the board role performance. Board of directors' knowledge and skill, good relation with CEO, and formalization of formal board routines are important for the board's ability to perform its control and service roles effectively. However, the board's family affaire role is mainly influenced by the ratio of family member in the board. This study empirically supports the arguments about the importance of good and clearly defined working style in the board of family businesses.

Key words Boards of directors; Board's working style; Family business; Board role

1 Introduction

It has become increasingly common for family businesses to set up a board of directors. At the same time, the boards of family businesses are attracting increasing attention from the academics[1]. Although many scholars believe that an efficient board has a positive influence on the performance of the business, practical results show that our understanding remains extremely limited in the workings of the boards of non-listed family businesses[2][3], particularly the effects of the board's working style on the board performance in Chinese family businesses. This paper will examine the influence of working style of board directors on the role of the board. The research targets non-listed small and medium-sized family businesses in China, as such businesses represent the majority of Chinese business at present and it is meaningful to investigate them. The contribution of this paper is not only that it tries to explore the processes in the board, but also that it pays attention to the formal working structures that exist to maximize board performance. This research will enrich related theories of family businesses and corporate governance. Meanwhile, the results will help family business managers to work out an effective resolution to the problems encountered in growth business.

2 Literature Review

2.1 Board's role

The views and expectations of a board' role or task performance in a business depend on who evaluates board performance[4]. Some businesses have different stakeholders, and they influence the decision-making of the board[5]. From the shareholders' perspective, the role of the board is to supervise the performance of the business. However, as far as the CEO and the management team are concerned, they hope that the board can play a greater role in helping them fulfill their tasks. For a family business, one of the roles of the board is to be involved in the management and arrangement of family affairs and to coordinate their relationship with company management[6]. In this study, the role of board refers to control, service, and family affair.

Garbrilsson and Winlund suggested that board task performance are correlated with three variables, including contingencies, board demography, and board working style[4]. To keep a focus on the relationship between the working style variables and board task performance, this paper concentrate only on the one-way influence perspective, where the main predictors are board's working style and the criteria variable in board task performance.

2.2 Board working style

Adapting the definition of Gabrilssonand and Winlund, board's working style is related to (1) the involvement of the board members. The degree of board member involving is related to the director's knowledge and skills, preparations and commitment to the board meeting, and independence towards the management. and (2) the existence of board structures. The board working structures refer to the dimensions of the board's organization and focus on the rules that exist to make the board work more efficiently[2]. These mechanisms include the formal board routines, the frequency of board meetings and the existence of a formal evaluation of the board-room performance [4][7].

2.2.1 Board member involvement

The directors' knowledge and skills have earlier been recognized as an important attribute in the board's strategic work[7]. Increased expertise on the board can enhance the director's involvement in the decision and make the board more active in its service and control roles. About the director's role of family affair management, Carlock and Ward emphasis the importance of director's experience and skill on board's role of family affair management[6]. This gives us the following hypothesis about the director's knowledge and skills:

Hypothesis 1: The director's knowledge and skill are positively related to board task performance. The higher degree of knowledge and skills among the directors, the more involved are the board in its control, service, and family affair roles.

The activity of the directors on the board is considered to be an important predictor of board outcomes. The importance of good preparation before the meetings is emphasized. Without proper preparation and commitment during the meeting, there is a risk that a board can not effectively provide the control and service functions[8][9]. Hence, well-prepared and committed directors should not only be of help in controlling the development of the business, but also in helping and supporting the management of firm and family affairs when facing an uncertain future[4]. Hence, we have:

Hypothesis 2: the director's preparations and commitment are positively related to board task performance. Better-prepared and more committed board members are more involved in the board's control, service, and family affair roles.

The director's independence towards the management is another issue considered to be important for increased board performance[4]. It has been argued that the board needs to be independent and judgment free from the bias of self-interest to effectively fulfill its responsibilities[10]. Independent boards should be better informed and thereby better able to support the management with advice and information. Finally, Carlock and Ward suggested that independent boards will play better in the family affair management and arrangement when the interest of family and firm are conflicted[6]. These arguments give us the following hypothesis about board independence:

Hypothesis 3: The director's independence is positively related to board task performance. The higher of the degree of independence, the more involved the board are in its control, service, and family affair roles.

2.2.2 Board structures

The formal board routines are a general term for the rules concerning the board agenda, rules concerning the summons to the meetings, accurate protocols, and formal clearly stated divisions of the work among the various directors. Demb and Neubauer found that both the procedure of having formal, clearly stated divisions of the work among the various directors and proper mechanisms for informing the outside directors can enhance board effectiveness and improve board outcomes[8]. The existing formal board routines may help to make good information flow possible between the management team and the board, and enhance board effectiveness and improve board outcomes on the roles of control, service, and family affair. Gabrielson and Winlund's empirical study indicated that the formal board routines significantly affect the board task performance[4]. This results in the following hypothesis:

Hypothesis 4: the degree of formal board routines is positively related to board task performance. The higher the degree of formal board routines, the more involved is the board in its control, service, and family affair roles.

The directors serving on the board must be given adequate time to make effective decisions. Consequently, the frequency of board meetings is recognized as important for the board to have any possibility of performing its functions and fulfilling its legal responsibilities such as control role[8]. In boards with a majority of inside directors the frequency of board meetings may be considered to be of less importance. However, this makes the management risk losing their objectivity and long-term focus. Increased board activity can thus give the inside directors, such as family directors, a unique focus on strategy [11]. However, the number of meetings may not affect the possibility that the board will perform its various service and family affair roles. Many aspects of the service roles can be performed outside the board room between the regular meetings. These arguments give us the following hypothesis:

Hypothesis 5: The more frequent the board meeting, the more involved is the board in the control and service roles, but not the family affair role.

Several studies show that good board outcomes demand an evaluation of boardroom performance which includes the evaluation of board and individual directors[5][8]. It is argued that an evaluation of boardroom performance helps to define the director's tasks and strengthen the relationship between the management and the board[12]. It also enables all directors to contribute with ideas for improvement, thus committing them to make changes in processes. This appraisal can possibly make the board more efficient and active in performing both the control and service roles[3][12]. However, empirical evidence shows that there is no significant correlation between formal board evaluations and task performance[4]. The arguments lead to the following hypothesis:

Hypothesis 6: The existence of formal board evaluations is positively related to the board's control and service roles, but not related to the family affairs role.

3 Research Design

Data used in this research has been obtained from questionnaires surveys conducted by the author in April and May 2006 in China. The samples in this search are non-listed small and medium-sized privately owned firms. Surveys targeted chairmen or director/general manager of businesses with a board of directors. A total of 212 questionnaires were recovered, and 117 of them were classified as valid after screening.

The surveyed businesses had average annual sales of RMB 135.91 million and an average workforce of 551. Of these businesses, 83% were in the manufacturing industry, 6% in the service industry, 11% in other

industries. The majority stakes of 81% of the businesses were held by families, and the boards had an average of five members. All sample boards had directors who are family members, and on average, 62.5% of the board members were family directors.

The question that described the board's control and service roles comes from the research by Gabrielsson and Winlund[4]. The 5-level Likert Scale was used for measurement. The board's control role primarily describes its supervisory function and consists of five questions, with a Cronbach's alpha of 0.7436. The service role consists of seven questions, with a Cronbach's alpha of 0.8567. The family affair role was measured by two questions that describe the extent of board's involvement in management and arrangement of family affairs.

The director's use of knowledge and skills was measured using a scale consisting of the mean of three items (Cronbach's alpha=0.7118), along a five-point scale. The board member involvement variables were measured using a scale consisting of 2 questions[4][5][8]. The correlation coefficient was 0.657 ($p=0.000$). Independence was measured as the mean of two items. The correlation coefficient was 0.7333 ($p=0.000$). The formal board routines variable was measured as the mean of four items (Cronbach's alpha=0.823). A five point scale was used to measure the various items. The board structure variables were measured as follows: annual board evaluation and regular board evaluation were measured by dichotomous dummy variables. Two variable's correlation coefficient was 0.819 ($p=0.000$). Finally, there are two questions to measure the number of board meeting one year and the lengths of the average board meeting.

In the analysis, five variables were used as control variables: the number of directors, the ratio of family board directors, the size of the firm, the firm's technology level, and the family ownership of the firm. Family director ratio was measured as the number of family directors divided by the total board size and used to measure the board independence. The firm size is measured by using the mean of the natural log of number of employees and the natural log of total sales. Technology was measured by a dichotomous dummy variable where the firms were categorized high-tech or non high-tech in the firm. Family ownership was used to measure the extent of influence of family on the business.

4 Analysis and Results

The following steps were taken during the data analyses. First, a correlation analysis was undertaken to explore the intercorrelation among the variables in this study. Then multiple regressions was used to test hypothesis 1-6.

4.1 Correlation analysis

Correlation analysis result is list in Table 1. The results indicated there is no significant influence of the size of board on the board working style and control and service roles. However, the size of board is negatively correlated with the board role of family affair management and arrangement. This seems understandable, as smaller boards have a stronger relationship with family member and more actively involve in family affair management.

The correlation matrix showed that the family director ratio was significantly related to the length of board meeting and the degree of director's preparation and commitment. Negative relationship indicated that the boards with larger number of family members are more likely to have shorter length of board meeting and lower degree of the director's preparation and commitment to the board meeting. One of possible explanations may be that small boards with larger numbers of family directors only are more likely to use informal family meeting to instead the functions of the formal board meeting. This explanation also supported by the results that family ownership also negatively correlated to the degree of director's preparation and commitment and the degree of formal routines in the board. This seems understandable, as larger family ownership usually have more family members in the board ($r = 0.52, p < 0.01$) and the need for rules and frame-works is less apparent. Evidence also comes from the result that the family director ratio only significantly correlated with the family affair role but not the control and service roles.

Table 1 Correlation Matrix

Variables	Mean	1	2	3	4	5	6	7	8	9	10	11	12	13	14
1Firm size		1.00													
2Technology		0.11													
3Family ownership	81%	-0.17	0.19*												
4Board size	5.01	0.25**	-0.03	-											
5Family board ratio	62.5%	-0.08	0.18*	0.52**	-										
6Knowledge and skill	3.78	0.05	0.16	-0.00	-0.04	-0.04									
7Preparation & commitment	3.38	-0.05	0.14	-0.18	0.13	-0.19*	0.49**								
8Independence	3.44	-0.05	0.06	-0.15	0.11	-0.12	0.54**	0.67**							

9 Formal board routines	3.44	0.01	0.17	-0.19*	0.15	-0.14	0.51**	0.65**	0.65**			
10 Formal board evaluation	2.88	-0.06	0.29**	0.04	0.03	0.14	0.27**	0.36**	0.45**	0.58**		
11 Meeting frequency	4.45	0.11	0.13	0.11	-0.12	0.03	0.07	0.08	0.16	0.09	0.20*	
12 Meetings length	3.02	0.03	0.07	-0.14	0.09	-	0.16	0.21*	0.20*	0.19*	0.07 -	
13 Control	3.60	-0.02	0.20**	-0.04	-0.04	0.07	0.54**	0.48**	0.54**	0.56**	0.37**	0.07
14 Service	3.60	-0.08	0.24**	-0.06	0.12	-0.08	0.54**	0.52**	0.59**	0.64**	0.39**	0.13
15 Family affair	3.04	-0.07	0.22*	0.12	-0.19*	0.36**	0.23*	0.13	0.23**	0.30**	0.39**	0.09
												0.43**
												0.30**
												0.07

Notice: Significance level * $p < .05$; ** $p < .01$, two tails.

In the correlation matrix the author also found that there were no significant relationship between the family director ratio and board's independence. Gabrielsson and Winlund indicated that independence should be regarded as a way of action, where the directors are contributing to board task performance by doing a good job[4]. There is no direct relationship between board's independence and the ratio of outsider directors.

The correlation analysis matrix showed some interesting correlation between the board working style and task performances: board knowledge and skill, preparation and commitment, independence, formal board evaluation, formal board routines were significantly positive related to the board control, service, and family affair roles. This seems that board work style influence its task performance. The results also showed that a high correlation among control, service, and family affair role. Hence, boards that involved in one of the board roles are to a high degree also involved in the other role

4.2 Results of regression analysis

The hypotheses in this study were tested by multiple regression analyses. Control, service, and family affair role were the dependent. The variables were included in two steps so that the study would be able to identify the separate effects of the control variables and the traditional board variables. First, firm size, high-tech firms, family ownership, board size, and family director ratio was included (step A). This analysis are presented as I in table 2. Second, 6 working style variables (step B) were included as II. The table presents coefficients for each variable and adjusted R² and F-values. The results of the linear multiple regression are listed in table 2. SPSS 11.5 was used to analysis the equations.

4.2.1 Contingencies and board family affair role

The regression analysis result of model I showed that contingency variables do not explain much of the variation in control and service roles, and the model I was not significant. However, for the dependence variable of family affair role, the model I was significant ($F = 0.002$). The result indicated that contingency variables particularly the ratio of family board directors explain a lot of variations in board family affair role.

The differences in multiple R, R², and adjusted R² between I and II are shown in Table 2. As can be seen, with the working style variables, the model II can explain some of the variations in the board control and service roles, but not the family affair role. Hypothesis H1, H2, H3, and H4 were not supported when it related to the family affair role. The family affair role was not significantly related to the board's knowledge and skill, preparations and commitment, independence, and the board's degree of formal routines. However, hypothesis H5 and H6 were partly supported that the frequency of meeting and evaluation were not significantly related to the family affair role. In generally, the board family affair role was not affected by the board working style. This also means that the board service and control roles may be the basic task performance and were not affected by the board structure.

Table 2 Results of Regression Analysis

Board role	Control		Service		Family affair	
	I	II	I	II	I	II
Equation:						
Constant	3.54	0.64	2.90	-0.02	2.28	-0.25
Firm size	-0.04	-0.02	0.02	0.08	-0.07	-0.09
Technology	0.21*	0.08	0.26	0.10	0.18	0.14
Family ownership	-0.23+	-0.11	-0.09	0.05	-0.14*	-0.08
Board size	-0.02	0.01	0.08	0.12	-0.01	0.01
Family director ratio	0.17	0.26*	-0.02	0.08	0.40**	0.40**
Knowledge and skill		0.27**		0.21*		0.12
Preparations & commitment		0.14		0.08		-0.15
Independence		0.07		0.22+		-0.00
Formal board routines		0.36**		0.37**		0.31*
Formal evaluations		-0.02		-0.08		0.15
Meeting frequency		-0.03		0.05		0.01
Meeting length		-0.05		-0.03		0.01
R square	0.08	0.49	0.08	0.53	0.17	0.36
Adjusted R ²	0.03	0.42	0.04	0.47	0.13	0.27
F (F - sign)	1.77(0.12)	7.34(0.00)	1.87(0.1)	8.47(0.00)	4.18(0.00)	4.23(0.000)

Notice: significance level + $p < .10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

4.2.2 Board member involvement and control and service roles

The degree of Board member involving is related to the director's knowledge and skills, preparations and commitment to the board meeting, and independence towards the management. The study clearly indicates that board member involvement is a main element when trying to understand the board's working style. The findings indicate that the use of directors' knowledge and skill are both important for the control and service roles. Hypothesis 1 was partly supported. This result indicated that knowledgeable and skilful directors are an important issue not only for their service role, but also control role. There seems, the directors with a high degree of knowledge and skills not only strength the firm's access to competence

and contacts, but also help board of directors to control managerial behavior. However, no evidence showed directors' knowledge and skill are critical for their family affair role.

The relationship between the director's preparations and commitment and control and service roles were not found. Hypothesis 2 was not supported. This finding was different from the results of Gabriëlsson and Winlund's empirical study[4]. They found that the directors' preparations and commitment is an important factor in explaining board task performance. One of the possible explanations is that the board task performance in Chinese family business may mainly be through the informal channels such as interpersonal discussion and communication.

The relationship between the board independence and control and service roles were not found. Hypothesis 3 was partly not supported. However, the results indicated that director's independence positively related to the service role also not significantly ($p < 0.1$). There seems that directors' independence towards the management may be better informed and there by better able to support the management with advice and information[4][8].

4.2.3 Board structures and control and service roles

Board structures refer to the formal board routines, the frequency of board meetings and the existence of a formal evaluation of the board-room performance. The results indicated that only hypothesis 4 was partly supported that the formal board routines are positively related with the board task performance. This shows that the formal routines have considerable impact on the board behaviors and its outcomes. There were no significant influences of the formal evaluation and the frequency of board meetings on the board control and service roles. Hypothesis 5 and 6 were partly not supported. The correlation matrix in Table 1 showed strong intercorrelation between both regular and annual evaluation and formal board routines. This indicates that board evaluation may have an indirect effect on board task performance. Hence, the effects of formal board evaluation need further investigation[4].

5 Conclusion

It has become increasingly common for family businesses to set up a board of directors. Empirical studies conducted in Sweden and other countries showed that the board working style variables explain considerably more than the traditional board composition variables when studying variations in board task performance[4]. Meanwhile, several researchers also suggested that generalizations of these findings to other countries must only be undertaken with caution. The present study conducted in China will make some contributions to this research area. The finding in this paper support the argument about the importance of the board' knowledge and skills and the formal board routines on the board task performance.

The significantly influence of the boards' knowledge and skill on the board task performance indicated the importance of the selection of directors. Consequently, various kinds of knowledge and skills will be an important criterion to select the outside and even inside directors. Meanwhile, this study also found that the board of directors in Chinese family business frequently uses the informal channels such as interpersonal discussion and communication to accomplish the board task performance. On the hand, this result indicates that a director serving on a board needs depth in the understanding of not only the industry but also the firm. On the other hand, it seems that the directors need a good personnel relationship with the top management team in order to enhance the director's involvement in the decisions and make the board more active in its roles. This study confirms Forbes and Milliken's suggestion that the personnel relationship and similar rationale with CEO often play a critical role in the selection outside directors in the board of family businesses[10].

As the empirical result point out, the working style variables explain considerably more than the contingency variables when studying variables in board task performance. As previous studies indicated, strong influence of the formal board routines on three family board roles was found. The future development of corporate governance and boards of directors in family firms should thus be to give attention to the working styles of the boards, especially the formal routines. Both the procedure of having formal, clearly stated divisions of the work among the various directors and proper mechanisms for informing the outside directors can enhance board effectiveness and improve board outcomes[8].

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