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“THE EMPLOYEES ARE ALL EQUAL... BUT SOME ARE MORE EQUAL THAN OTHERS”. ALTRUISM, OPPORTUNISM AND DISCRIMINATION IN FAMILY SMEs

Filippo Ferrari¹

Abstract

This article provides empirical evidence to support the Agency Theory as applied to small and medium-sized family firms. The research, conducted on a sample of SMEs (N = 88), has investigated the main elements of the Agency Theory (type of contract, agent autonomy, mechanisms of resource distribution, the match between job assignment and worker skills, the overall level of perceived organizational justice), using a qualitative method.

The literature suggests that altruism of the Principal as a parent and widespread opportunistic behavior by the Agent are confirmed phenomena typical of family SMEs. In addition, the research highlights the implications in terms of agency costs and perceived organizational justice on the part of employees who are not members of the family. Finally, this article suggests the causes and reasons for such altruistic and opportunistic behavior.

Key Words: Family Business; Agency Theory; Organizational justice; Opportunistic Behavior.

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INTRODUCTION

Early work on the Agency Theory (Jensen, Meckling, 1976; Ross, 1973) attributed a specific situation favorable to the family firm. The sense of belonging of family members would protect the company from the opportunistic behavior of its members, to the benefit of the overall agency costs. This position has been challenged by the economy of the family (Becker, 1981): family firms are characterized by opportunistic behavior and altruism expressed by parents (the Principal), generating costs related to adverse selection (eg, selection of their children according to criteria of belonging and not of expertise: Lansberg, 1983; Schulze, Lubatkin, Dino, 2003; Chirsman, Chua, Litz, 2004; Schulze, Lubatkin, Dino, Bucholtz, 2001). Also, the little empirical evidence available relating to the Italian SMEs (Gagliano Spina, 2000; Biasseti et al, 2009) emphasizes the limited diffusion of managerial practices in the SMEs themselves. These practices (accounting control, total quality management, management by objectives, use of rewards and incentives) would allow the Agent's behavior (family or not) to be monitored and to align his objectives with those of the company. On the other hand, an alternative approach based on the *stewardship theory* (Davis et al, 1997) suggests that workers who are members of family firms feel that they own and pursue non-economic objectives of the company (Corbetta, Salvato, 2004). The literature offers little empirical evidence for the difficulty of direct study of worker behavior in family businesses, especially SMEs. Among the few studies, that of Chrisman et al (2007) seems to show that workers' family members act as agents, contrary to the expectations of the stewardship theory and the first formulation of the Agency Theory. Hence the need, recently made explicit (Pieper, 2010), to integrate the perspective founded on the agency relationship (considered too 'rational') in a model that takes into account other psychological variables rather than economic ones, able to explain behavior such as adverse selection or opportunism of the agent in SMEs family.

1 THE THEORETICAL MODEL

The Agency Theory describes the exchange relationship between an actor (the Principal) which delegates to another actor (the Agent) the discretionary power (i.e., decision-making responsibilities) to act on behalf of the Principal for reward (Jensen, Meckling, 1976; Ross, 1973). This report aims to align the objectives of the Agent to those of the Principal, in order to reach the desired effectiveness (for a review, Eisenhardt, 1989). The Agency Theory also makes it possible to identify the most efficient type of contract in terms of organization costs, which are determined by the remuneration that it is necessary to give the Agent to induce him to accept the risk. This theory is considered to be a powerful model for explaining the relationship between the parts of an organization (Jensen, 1983) but it is also considered dehumanizing and even ' dangerous ' (Perrow, 1986). In regard to the application of this model to the family firms, the literature suggests that the trade- off between Principal and Agent is affected by several factors, which can in turn improve or diminish its efficiency .

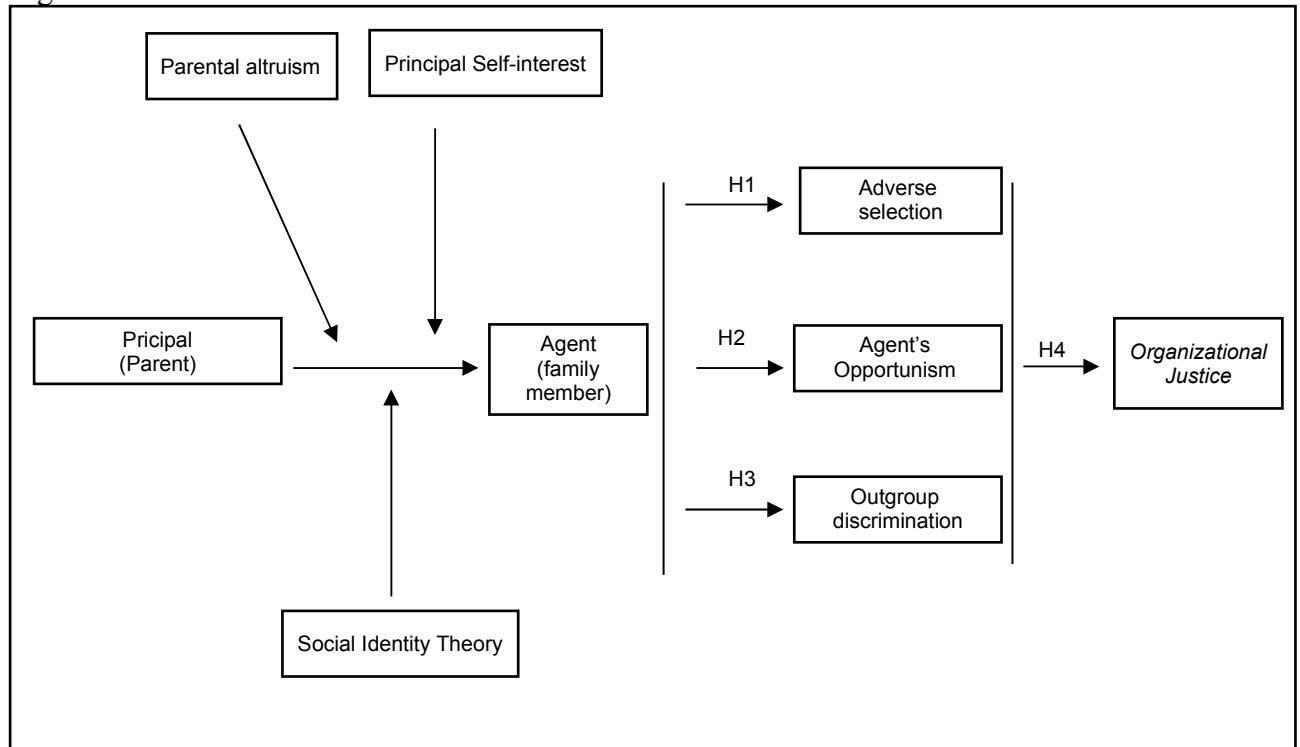
First, family firms, especially SMEs, are characterized by the overlap between ownership and management. This *institutional overlap* (Landsberg, 1983) brings the Principal (the entrepreneur, i.e., the parent) to act in a conflict of interest, since the role of control exercised by an external property is lacking, and exposes Principal to the risk of decisions functional to the pursuit of non-economic objectives but of business interest. Parental altruism (Schulze, Lubatkin, Dino, 2003; Karra el al, 2006; Lubatkin, Durand, Ling, 2007) is a second variable to take into consideration in the traditional model of the agency theory. The parent-child relationship is characterized, even in business contexts, by attitudes and acts of generosity on the part of the older generation, according to a universal model of the relationship of care and help. This feature makes the Principal run the risk of acting once again in a functional manner in the pursuit of non-economic objectives. Altruism can generate different types of problems

in the agency relationship, which decrease efficiency. First, parental altruism and conflict of interest can lead to *adverse selection*, and thus to staffing incompetent family members, with obvious negative impact on performance. Second, parental altruism can lead to assigning benefits (economic and otherwise) to family members, regardless of their merit, laying the groundwork for future deviant behavior (Eddleston, Kidwell, 2010), and at the same time discriminating against non-family members. In both cases, it also generates a disutility for the firm. Also, since the literature describes altruism as asymmetrical (Bergstrom, 1989), the Agent (the family member) can trigger opportunistic behavior, again generating costs for the firm. Third, in the presence of workers who are not family members, parental altruism can generate favoritism toward relatives and discrimination towards others, with a negative impact on perceived organizational justice (see below). Social psychology provides a third element to be introduced into the model: the categorization of oneself as a member of a group (Tajfel, Turner, 1986). Ample literature, almost exclusively psycho-social (with the exception of De Massis, 2012), describes the mechanisms and conditions under which individual behavior is determined not by individual characteristics but by those of the group to which it is believed to belong. This condition raises the risk of the Principal (and for all members of the family working in the company) to favor the *ingroup* (the members perceived as belonging to the same group) and at the same time to discriminate against the *outgroup* (those who considered to belong to groups outside one's own). Behind it all, then, there seems to be a phenomenon of social categorization (Tajfel, 1970, 1971), a mechanism under which the social world is divided and sorted into categories. But the categorization, in itself, would not justify favoritism towards the *ingroup* (i.e., the category to which one feels he belongs): it is necessary for the categorization to be based on the individual's Social Identity Theory (SIT), which consists in his conception of himself as a member of a group. And since people tend to have a satisfactory self-conception (to protect their self-esteem), then comes favoritism. In these terms, an intergroup conflict is a competition for prestige as much as for material resources.

Organizations are economic institutions, but not only, and to neglect this aspect may have undesirable effects (Cropanzano, Bowen, Gilliland, 2007). The exclusive pursuit of efficiency and effectiveness can be counterproductive for an organization. The members of an organization obviously want the benefits, economic and otherwise, but also something else: they want *organizational justice* (organizational justice, henceforth OJ, which is the perception of the moral quality of how they are treated by the organization and by other members. OJ has been much studied in recent years, and was the subject of two meta-analyses at the beginning of the century (Cohen-Carash, Spector, 2001; Colquitt et al, 2001). Cropanzano, Bowen and Gilliland (2007), based on the existing literature, point out that the members of an organization assess, with regard to justice, three different aspects: criteria for the distribution of resources (distributive justice); procedures relative to distribution of resources (procedural justice) and justice arising from interpersonal relationships (relational justice). The three dimensions tend to be related, and may be considered as three components of the same construct (Ambrose, Arnaud, 2005; Ambrose, Schminke, 2007). But, although related, they have different antecedents, and thus it is useful to treat them separately. One hypothesis of this article is that family-firms differ from non-family ones as regards the level of OJ, lower in the former than in the latter. The primary source of organizational injustice in fact seems to be the overlap between family and business (Lansberg, 1989). Family and firm are two institutions with different objectives (the welfare and protection of their family members the former, profit the latter), goals that may conflict. The literature also describes the impact on the perception of injustice in phenomena such as nepotism (Padgett, Morris, 2005), authoritarianism (Tagiuri, Davis, 1992), management practices, discrimination towards non- family staff members (Barnett, Kellermans , 2006; Lubatkin et al, 2007; Schulze

et al, 2001), the perception of non-members as 'foreign' (Barnett, Kellermans, 2006; De Massis, 2012), organizational culture centered on the founder (Schein, 1983), and little recourse to delegation (Kelly et al, 2000).

Figure 1: Theoretical model



In addition, since the family-owned company also pursues non-economic objectives, these can increase the perception of injustice by non-members, since these goals are not of interest to them (Chrisman, Memili, Misra, 2013). However, at the moment there is little empirical evidence (Barnett, Kellermans, 2006; Carsrud, 2006; Sieger, Bernhard Frey, 2011). In particular, recent research suggests (Bassanini et al., 2011; Block et al, 2013) that family members are more satisfied than non-members, and have a greater sense of security (linked to the tenure of the job) but receive lower wages, with the exception of the females, who, if family members, have wage levels higher than 'foreign' females (about 5% more: Block et al, 2013). The theoretical model (represented in Figure 1) is then defined in the following formal terms.

Given the *null hypothesis H0: no difference in behavior, in a family firm, to family members than non-members*, on the basis of the above considerations, it is possible to make four working hypotheses:

- H1: family firms are characterized by adverse selection of family members*
- H2: family firms are characterized by opportunism of family members*
- H3: family firms are characterized by discrimination against non-family members*
- H4: In family firm, non-family members have low levels of perceived organizational justice*

The literature provides extensive evidence of the negative impact of such mechanisms (adverse selection, opportunism, discrimination) on the cost of management and on organizational justice. In particular, the literature provides evidence of specific effects such as: 1) higher costs due to inefficiencies in the transfer of risk (e.g., a higher rate of pay for

non-family members: Block et al, 2013), 2) higher costs due to Agent opportunism, 3) worse professional performance due to the mismatch between skills possessed and skills required by the job, as a result of adverse selection, and 4) perceived organizational injustice generates a higher rate of resignation on the part of family members due to lower job satisfaction, 5) lower organizational citizenship behavior (OCB) and finally 6) a lower level of work commitment by non-family members. In conclusion, the empirical literature does not seem to be able to provide direct evidence on the benefits (economic and otherwise) received by members rather than non- members. Also missing is evidence about unequal treatment of female and male members within the family, and its impact on job satisfaction, and, finally, from the literature it can be expected that most 'professionalized' family firms are less affected by distorting mechanisms than by others, but this is a fact that still does not emerge from the literature. It seems, in fact, very difficult to obtain data of this nature, and often the elicited responses are distorted, if not explicitly denied. For these reasons, this study used a qualitative protocol, collecting interview data that would otherwise have been difficult to obtain through other means (such as a questionnaires).

2 THE RESEARCH

The research was conducted over a period of 4 years (2009-2013), on a sample of family SMEs of Emilia Romagna (N = 88), using a qualitative protocol. The research was based on interviews with the Agent family member, where at least one Agent did not belong to the family. The interview focused on elements typical of the Agency Theory: contract type, kind of supervision, agent autonomy, mechanisms of resource distribution, consistency between skills required and those possessed, and the overall level of perceived organizational justice. We chose a clinical approach because of the nature of the data, which discouraged the use of a quantitative method, such as self-reported questionnaires. It was feared that by using a self-reported questionnaire respondents would not provide truthful information, given the nature of the information sought, the existence of discriminatory behavior against non-members, the level of perceived organizational justice by non-members, mechanisms for the selection and career not based on merit, etc.). It is therefore felt that, methodologically, the collection of data through direct conversation in extreme confidentiality is the most effective choice, thanks to the professional secrecy which is required of the interviewer. Furthermore, to prevent resistance and defense mechanisms by participants, the data were collected within already existing consultancy and tutoring activities, but formally with different purposes (such as, for example, actions to design and facilitate generational transmission or actions to improve the management of processes and policies Quality in SMEs). Despite the use of qualitative methods, we tried to follow scrupulously the literature guidelines (McCollom, 1990; Chenail, 2009), in order to: produce generalizable data about the universe of SMEs (external validity); achieve an epistemologically unobjectionable process of intervention; keep under control the distortion costs of the researcher; ensure a methodologically consistent system (internal validity).

1.1 The sample

The survey was conducted on 88 small and medium-sized family firms in seven Provinces of Emilia Romagna (PR 10, RE 26, MO 26, BO 6, RA 2, FC 10, RN 8). Little significance is attached to the average size of the sample (34 workers), in light of the high deviation standard (DS = 41), and so the median was calculated, as a more dependable measurement, which was equal to 16.

Overall, with regard to dimension, more than 60% of the sample is less than or equal to 25. The data on the universe (the complex of active enterprises in Emilia Romagna, including artisan firms and individual entrepreneurs), indicate that 53.6% had only one employee,

92.3% have up to 15 employees, large companies (> 250 employees) are 0.1% (Istat, 2011). Then this sample is characterized by a median size greater than the reference population. This is due, of course, to the sample used (which includes only minimally small businesses and individual entrepreneurs).

1.2 Methodology

Through an interview a job analysis and skills assessment of the family member was carried out (in terms of required skills, autonomy, use of resources, etc.). For each company involved, at least two interviews were carried out: of a member belonging to the owner's family and, if present, of a non-family member, such as an internal customer. The data, although qualitative, were collected and coded with a grid structured to detect the dimensions shown in Table 1. As defined above, data collection was carried out in already activated programs of counseling and mentoring, but formally with different purposes (such as, for example, programs financed to facilitate generational passage or to improve quality management processes and policies quality in SME's). These acts focused on job analysis and skills assessment, using both interviews that and analysis of available documentation (e.g., the Quality Manual). Each interview was repeated until complete collection, and this process had a duration from a minimum of 6 hours up to a maximum of 24 company hours.

1.3 Results

Regarding the composition of the sample by gender, 50 males and 38 females were interviewed as family members. Almost all (82) are children of the business ownerships, the remaining 3 are in-laws, especially the wives of the owners. At the time of the interview, 20 were department/division heads, 21 employees/operationals, 3 were finally placed as interns or freelancers. All were included in the company with a permanent contract, except for 2 interns and a temp. With regard to career path, 34 respondents joined the company straight after school, nine held other jobs in different sectors, one working in another company in the same sector. The match between CV (skills, experience) owned and skills required is on average partial (0.9): in particular and interestingly, the average matching of the male members of the family is 1.3, that of females 0,4.

Table. 1: Results

Dimension	Scale used	Average value
Career path of the respondent	0 = only in the family, 1 = in other companies in the same sector, 2 = in other companies in other sector	0**
Match between job characteristics and CV	0 = no, 1 = partial, 2 = total	0,9
Job relevance	0 = none, 1 = poor, 2 = high	1,5
Job autonomy	0 = poor, 1 = partial autonomy, 2 = full	1,9
possibility of participation in training	0 = no formalities, 1 = discussed each time, 2 = only determined from the property	1,9
use by the respondent of capital goods	0 = never, 1 = sometimes, 2 = always	1,4
use by the respondent of corporate human resources	0 = never, 1 = sometimes, 2 = always	0,1
level of shared goals/organizational strategies	0 = none, 1 = in exceptional cases, 2 = regularly	0,5
the level of access to information	0 = none, 1 = in exceptional cases, 2 = regularly	0,4
perceived level of discrimination experienced	0 = no discrimination, 1 = sometimes subject to discrimination, 2 = always discriminated against	0,9
level of perceived organizational justice	0 = unfair situation, 1 = neither just nor unjust, 2 = very fair	0,9

*average values in the perception of internal customer

****Median**

The importance of the organizational task being performed by the members of the family is systematically higher in the perception of the owner with respect to the partner (on average 1.5 and 1.0, respectively). The data also shows that the autonomy of the job and the discretionary nature of the time management is much higher for family members than non-members of the same task (1.9 to 0.2), and for female than male (1.9 to 1.6). Similarly, with regard to the opportunity to participate in courses and training activities without any formalities (on average 1.9 family members, 0.3 for the others). In addition, members of the family have greater freedom to use for their own private purposes items such as capital goods company car, phone, tablet, etc. (on average, 1.4) compared to non-family members, who in fact are not permitted use of these things, unless as exceptions (mean, 0.1). Human resources, however, are almost never used for purposes unrelated to work or by family members or others.

Furthermore, it seems overall very poor practice to involve or at least even inform employees who are not non-family members with regard to strategies, development programs, major investments, with the exception of when they are part of the property, participate in governance bodies or hold positions of responsibility. The perception of these elements is substantially identical between families and non-families, (0.5 and 0.4, respectively). The overall level of discrimination perceived by non-members is average (0.9): non-members sometimes feel discriminated with respect to members, but that seems to have no particular effect on perceived organizational justice. The majority of non-members of the family respondents consider the company where they work as neither just nor unjust, but basically balanced. Results are shown in Table 1.

3 FINDINGS

First, the vast majority of junior members of the family go right into the company, with no work experience, or in the same sector (at a major supplier's, customer's) or in any other sector. With some differences, however, in relation to gender: a third of the daughters (32% versus 12% of males) first try another path, in a different industry, with a decision to join the family that comes a little later, or even as something to fall back on. This is also consistent with the findings in relation to the match between personal skills and competences required. The sample shows that the male members have a significantly better fit than female (1.3 compared to 0.4): the calculated chi-square with 2 df is equal to 14.41, much higher than the critical chi-square for $\alpha = 0.05$ is equal to 5.991. This allows us to reject the null hypothesis of independence of the variables, and establish an initial body of evidence: the family firms have a high level of adverse selection, a level that becomes even greater (about three times more) if a daughter is to enter the firm. So, there is confirmation of the hypothesis *H1: family firms are characterized by adverse selection of family members*, in particular as regards the females. The organizational relevance (in terms of strategic output) of the work performed by family members is placed in doubt by the perception of colleagues. The widespread lack of management by objectives and the exclusive use of permanent contracts on an hourly basis does not allow a proper measurement of the output produced by the owner of the job. Another critical factor thus appears: family members very often hold jobs of dubious value, often designed ad hoc to find a place in the workforce for a son / daughter / relative. Family members enjoy privileges relating to the management of their work (e.g., time) and benefits such as the use of instrumental resources for private purposes, with a difference between males and females: the latter enjoy greater freedom (especially due to child care). They can also be absent from work to attend training, conferences, seminars during working hours. Since employment contracts are based on the hourly rate of pay in a fixed salary, these data

seem to provide evidence which supports the hypothesis *H2: family firms are characterized by opportunism of family members*. The difference with non-members is, in fact, equal to the entire rating scale (1.9 versus 0.2), i.e., for non-members any possibility of flexible working hours is precluded beyond the provisions of the work contract. Participation in training events is usually subject to the approval of a superior, if not rigidly managed by it. The data show no difference between family members and non-members as to the type of contract in place. So, there is no evidence that family members have access to additional monetary resources or other rewards as opposed to non-members, or that wage differentials are present for equal work (for example, the superminimum). Thus, based on these data, hypothesis *H3 is partially confirmed: family firms are characterized by discrimination of non-relatives*. This discriminatory behavior is related to organizational aspects (time management and schedules) but not to other aspects such as pay and incentives. Finally, hypothesis *H4 is not confirmed: family firms are characterized by low levels of organizational justice, as perceived by non-family members*. Family firms are considered to be neither just nor unjust, but balanced.

4 CONCLUSION

The opportunistic behavior of family members seems grounded in family SMEs. When daughters were questioned about it ("Don't you think that the fact that you are free to manage your work almost as you want might generate discontent in others?"), they often explained their opportunistic behavior as obvious ('the company is mine, after all, the business risk is ours'), considering it an intrinsic element in the situation. This is consistent with some evidence in the literature, such as the greater satisfaction of women (Cohen-Carash, Spector, 2001; Barnett, Kellermans, 2006), due to job flexibility (getting to work, leave leaving or being absent according to the needs and health of school children). The data shows a clear inability to separate organizational aspects from personal ones, to distinguish family relations as hierarchical relationships. And this is the source of the economic costs described by the Agency Theory: moral hazard, adverse selection, opportunism of the agent. Employees who do not belong to the family are poorly informed about decisions of strategic importance, unless they belong to management. Sometimes they feel discriminated, but these two elements do not seem to have an impact on the perception of organizational justice: the company is perceived as neither just nor unjust, but basically balanced. In the light of the existing literature, this is quite surprising. Evidently, even by non-members it is considered correct (in terms of of procedural and distributive justice) to resort to the criterion of need, rather than merit or equality, to get benefits: flexible work hours or 'use of corporate assets (telephone, car) for private purposes. All this seems contrary to what is predicted by the SIT. The research findings do not support the relationship between identification with the *ingroup* and intergroup differentiation: not always is there a bias towards the *outgroup*. So the assumption is that the basic processes of social identity are more complex than Tajfel argues (1978; 1981; 1982), and worthy of further investigation within the organization. For example, opportunistic behavior toward a family-owned by the family itself, which emerges from the research, takes the form of *ingroup* favoritism, and then in contrast to the SIT. Not surprisingly, for some years the psychosocial literature has raised criticisms of the SIT (Brown, ref?): The author reports the fact that, especially in field studies, *outgroup* discrimination is far from being an automatic phenomenon. Indeed, there is a possible occurrence of favoritism towards the *outgroup*, or the same group favors the *ingroup* of a certain size, the *outgroup* of another and none of others, again in contradiction with the SIT.

5 PRACTICAL IMPLICATIONS AND FUTURE RESEARCH

The first limitation is of course methodological: the sample size and the protocol used impose caution on the generalizability of the findings. Future research will need to validate the results on a larger scale. The second limitation is the choice to involve in research only one family member per firm, with the result of an over-simplification of the organizational reality. Often, in fact, family firms are characterized by a variety of generations but also of bloodlines (Ferrari, 2005). Future research should investigate whether the theoretical model presented here is also valid in different situations, such as those characterized by the presence of brothers and/or cousins.

This article, despite the methodological limitations due to the qualitative approach and the size of the sample, is perhaps the only empirical contribution in the field of agency costs in small and medium-sized Italian families. In a small family business, agency costs seem greater than for similar non-family SMEs. Often, children (especially daughters) enjoy freedoms that other employees do not have, hold a job for which they are not prepared and, moreover, their tasks are of dubious value to the organization. Data shows therefore greater attention to non-economic objectives than economic ones.

The findings suggest some practical implications. First, there seems to emerge the need for family SMEs to become more professional (Chua, Chrisman, Bergiel, 2009), beyond the costs that this option can represent. Only the acquisition of instruments for monitoring and managing for results can help SMEs to reduce the effects of overlapping in family-enterprises, and finalizing the behavior of family members to the business objectives of economic nature. The professionalized firm must evaluate the performance of family members and provide incentives that will motivate them to achieve the firm's goals. In addition, the evidence suggests a more critical situation for the family business when the new generation is represented by a daughter than by a male. This leads us to carefully consider the implementation of training and mentoring from high school on for SMEs whose daughters express a wish to join the family business. These courses could be organized by employer associations. *Adverse selection* is another endemic factor in SMEs family. Beyond these research findings, it would be advisable to investigate the role played by third parties belonging to the family, such as mothers: they often are formally absent from the company, but it is assumed that they have an important role in decisions to hire children in the family firm. Agency Theory characterizes self-control as an internal conflict resembling the principal-agent conflict between the owner and manager of a firm (Thaler, Shefrin, 1981). According to this hypothesis, mothers would be involved in the decision of the Principal to hire children in the family firm, a decision carried out in conditions of conflict of interest.

Finally, with regard to the phenomena of social categorization and intergroup discrimination, this article does not provide evidence that supports SIT. It therefore becomes necessary to explore other approaches borrowed from social psychology. A promising line of research for example was started some years ago by Deaux and colleagues (2011), which explores the different functions of relational processes and affective identification with the group, processes hitherto considered only cognitive. According to the author, in this context it is not to be taken for granted that the SIT will generate positive identities, and thus it is not obvious that the outcome is the identification of biological group membership (in this case, the owner family). Future research, therefore, is called for to investigate the affective, relational, motivational dimensions of these processes of identification with the *ingroup*.

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