

THE ADDED VALUE OF GOVERNANCE BOARDS IN SMALL AND MEDIUM-SIZED FAMILY FIRMS

Ilse A. Matser^{a,} and Dirk F. Gerritsen*

Abstract

This paper explores a possible relation between governance boards in small and medium-sized family firms and performance indicators of the firm. Following the legal framework in The Netherlands, firms can have an advisory and/or supervisory governance board next to the top management. The resource based view is used to discuss the possible valuable resources of family SMEs, including the governance board. Two relevant board functions within SMEs are the contribution of resources and the aid to the strategic process. If a governance board is a valuable resource, the establishment of it should ultimately lead to a better defined strategy and possibly a higher performance. Hypotheses were tested on a sample of 330 Dutch family SMEs. Our results show that governance boards positively affect the existence of written strategic plans and the expected marketability of the firm, while there is no relation with the expected short term sales growth.

Keywords: Boards; Governance; Family Firms; Strategic Planning; Performance

* Corresponding author: Utrecht University School of Economics, Janskerkhof 12, 3512 BL Utrecht, the Netherlands; telephone: +31 (0) 30 253 7118; fax: +31 (0) 30 253 7373; e-mail: i.matser@econ.uu.nl

1 Introduction

In this explorative paper we assess the research question whether the existence of a governance board in small and medium-sized family firms (family SMEs) accounts for direct and/or indirect effects on the performance of a family business.

There is a growing interest in corporate governance, resulting in the issuance of various corporate governance codes worldwide. In the Netherlands the Code Tabaksblat was put into practice in 2003. For that reason, firms should install a supervisory board according to this code. Installing a board besides the top management is a key feature of the two-tier governance system. This code only applies to listed companies. However there is a big gap between governance practices in listed firms and governance practices in non-listed and small and medium-sized firms (SMEs). This paper describes governance practices in Dutch family SMEs and focuses in particular on the possible benefits of governance boards in family SMEs. Relatively little research has been conducted on governance in SMEs (Van den Heuvel, Van Gils and Voordeckers, 2006). The aim of this paper is to make a contribution to this field. An important cause for the big gap between governance practices in large firms and SMEs is the focus on monitoring within the governance framework. This focus stems from the view that the firm's goal is to optimise shareholders wealth. Because of the separation between ownership and management in large firms, shareholders must monitor the managers to be assured that they receive an optimal return. This last argument stems from the

agency theory (Jensen and Meckling, 1976). The stewardship theory takes a very different approach. The basic assumption for the stewardship theory by Davis, Schoorman and Donaldson (1997), lies in their 'model of man': "the model of man is based on a steward whose behaviour is ordered such that pro-organizational, collectivistic behaviours have higher utility than individualistic, self-serving behaviours" (Davis et. al, 1997). Therefore managers are likely to be collectivistic, pre-organizational and trustworthy. If this is true then governance mechanisms should not be based on control but on trust. Given the nature of family firms, the stewardship approach is likely to be more applicable for family SMEs.

Uhlaner (2008) stipulates that the objective of governance mechanisms is to enable entrepreneurship in firms. The firm is able to thrive and grow due to the support received by the board.

Instead of choosing one absolute theoretic perspective, Lynall et al. (2003) argues that various theories can be applied to governance issues. The key is to identify which theory is more applicable. This depends on certain conditions, such as the ownership structure and the legal framework. The focus of this article is on the existence of governance boards. The key question addressed in this paper is whether governance boards are a valuable resource for small and medium size firms. Therefore the resource based view (RBV) will be the used for the theoretical framework of this paper.

This paper proceeds as follows. The next section will discuss the resource based view which is the theoretical framework of this paper. Attention will be given to "familiness" which is a distinctive feature of

family firms. Subsequently governance in family firms will be discussed, and attention is given to differences between family and non family firms with respect to governance. Also the different functions of governance are considered in this section. The literature discussion will be concluded with the life cycle theory, which elaborates on the differences in firm complexity varying with the age of the firm. The theory is followed by the hypotheses, after which we present our sample and the methodology. Then we present our main findings and consequently our conclusions and the discussion.

2 Theoretical background

2.1 The Resource Based View

The existence of governance boards is based on different theories. Given the existence of boards, the added value will be analysed using the resource based view of the firm (RBV). This view is one of the most influential theoretical frameworks in the strategic management field (Barney, Wright and Ketchen, 2001; Newbert, 2007). Wernerfelt (1984) introduced the notion that firms can be analysed by looking at the resources of the firm. A resource is defined by Wernerfelt as "anything which could be thought of as a strength or weakness of a firm". The key objective of the RBV is to establish a causal relationship between resources and a long-term competitive advantage. Barney (1991) argued that resources should have four characteristics to establish a competitive advantage. They should be: valuable; rare; inimitable; and non-substitutable. Barney based the RBV on two assumptions: resources should be both heterogeneously distributed among firms and imperfectly mobile. These assumptions allow for differences in firm resource endowments to exist and persist over time. Both assumptions thereby allow for a resource-based competitive advantage.

There is an ongoing debate about the RBV framework. A focus on processes led to new approaches within the RBV (Newbert, 2007). Firstly, there is the notion that besides the existence of resources, firms should be capable of exploiting the full potential of these resources. Barney (1991) named this the implementation skill set of the firm. Concurrent with Barney, Teece, Pisano and Shuen proposed dynamic capabilities framework. This dynamic capabilities framework is "the firm's ability to integrate, build and reconfigure internal and external competences to address rapidly changing environments" (Teece et al. 1997). Valuable resources alone are not enough to create a sustainable competitive advantage. Resources should be managed effectively and adjusted to the changing environment of the firm (Sirmon and Hitt, 2003).

The RBV is being increasingly tested as a theoretical framework in empirical research projects. The results of a number of empirical researches are discussed in two meta-analytical reviews (Barney and

Arikan, 2001; Newbert, 2007). The empirical results are mixed. Barney and Arikan (2001) conclude that only 2 percent of the presented results are partially inconsistent with the RBV theory. Newbert (2007) found that only 53% of the 55 empirical tests support the RBV, and that the degree of support varies considerably. Notwithstanding, since the introduction in 1984 the RBV has become a very important theory in the field of strategic management (Habbershon and Williams, 1999). The RBV has also proven its value as an appropriate theoretical framework in the field of family business research (Chrisman, Chua and Zahra, 2003).

'Familianness' can be valuable resource. The RBV can be used as a theoretical framework for assessing the possible competitive advantage of family firms (Habbershon and Williams, 1999). Family firms have several unique resources that have been referred to as the familianness of the firm (Sirmon et al. 2003). Familianness is described by Habbershon and Williams (1999) as the unique bundle of resources created by the interaction of family and business. Dyer (2006) refers to the 'family effect' when explaining the effect the family can have on firm performance via variables as governance, management and firm characteristics. Habbershon and Williams (1999) stipulate a potential problem caused by a generic approach to assessing family firm advantage. Competitive advantage of a firm has to be discussed with referring to the underlying resources, specific strategies and skills. For instance, a strong family leader is not per se beneficial to every firm, as certain companies may become too dependent on its leader. It is not one specific advantage that is held by all family firms. The question to be answered then is why does one family firm utilise its familianness better than the other? This is also emphasised by Nordqvist and Melin (2007) when they discuss the institutionalization of the family firm. Overemphasizing the similarities between family firms and thereby downplaying the differences can lead to a too simplistic view on family firms. The RBV offers the possibility to focus on the distinctive resources and to look for the firm's uniqueness as to explain the competitive advantage.

Which resources are possible assets to create long term competitive advantage? Various authors discuss the possible sources of competitive advantage (Carney, 2005; Eddleston, Kellermans and Sarathy, 2008; Habbershon and Williams, 1999; Miller and le Breton-Miller, 2006, Miller, Le Breton-Miller and Scholnick, 2008; Sirmon and Hitt, 2003). There is a common understanding of the valuable resources which can exist in family firms. Sirmon and Hitt (2003) discuss for instance five possible family firm specific resources with the following positive outcomes:

- Human capital stands for the acquired knowledge, skills and capabilities of an individual. The positive attributes include extraordinary commitment, warm relationships and the potential for deep firm-specific tacit knowledge;

- Social capital is composed of three dimensions: structural, cognitive and relational. The first dimension is based on network ties, the second one on shared languages and narratives and the third one on trust, norms and obligations. All these components are embedded in the family and can lead to the development of human capital;
- Patient financial capital is capital that is invested without the threat of liquidation for a long period. The generational outlook provides a focus on a long time horizon instead of on short-term results;
- Survivability capital represents the pooled personal resources that family members are willing to loan, contribute, or share for the benefit of the family business. This will help the firm through poor economic times;
- Governance structure: the mutually-shared objectives, trust and family bonds reduce governance costs.

However there is a commonly accepted understanding that the familiness is not always positive. Taguiri and Davis (1996) defined an important feature of family firms: the bivalent attributes. These attributes can be the cause of high performance but can also turn into disadvantages, hence the term bivalent.

Patient financial capital is good illustration of this bivalency. It often leads to a conservative financial strategy, which can have a negative impact on the firm's growth.

The management of resources may be a possibility to influence the effect of the attributes (Sirmon et al.2003). The availability of appropriate resources is necessary but insufficient to achieve long-term competitive advantage. Resources must be managed effectively. Whether governance mechanisms can be a method to manage this "familiness" effectively will be discussed in the next section.

2.2 Governance in family firms

Dyer (2006) named firm governance as one of the common determinants of firm performance. However, to date there is no convincing evidence that governance practices will positively affect firm performance (for instance Klein, Shapiro and Young, 2005, Uhlaner 2008). Abor and Adjasi (2007) draw attention to the disadvantages of governance structure. The introduction of a governance structure in a firm will lead to additional roles in audit, remuneration and nomination committees. Furthermore new and more directors have to be hired and paid – they stipulate that governance structures cost money. Put it differently: governance should be seen as an investment, hence it is a legitimate question to ask if this investment offers a sufficient rate of return. Before we discuss this further it is important to establish what we regard as firm governance.: "Corporate governance is about the understanding and institutional arrangements for relationships among

various economic actors and corporate participants who may have direct or indirect interest in a corporation" (Letza, Sun and Kirkbride, 2004).

Firm governance in family firms can be different from non family firms. The agency theory can be useful for explaining the possible advantages and disadvantages of family firms in comparison with non-family firms. The agency theory focuses on the principals (owners) and the agents (managers) of a business. Jensen and Meckling (1976) define agency costs as the sum of the principals' monitoring expenditures, the agents' bonding expenditures and the residual loss. The outcome of the agency theory for the family firm can be twofold. Agency theory is often used to argue that family firms will have relative low agency costs as compared to non family firms. One of the causes is that the owner of a family firm is quite often the same person as the manager, in which case there is no need for monitoring the agent. Another aspect is that the family effect can lead to common goals, high trust and shared values among the principal and the agent which reduces the need for costly governance practices (Dyer, 2006) Research (e.g. Chrisman, Chua and Litz, 2004) supported the view that the family effect can lead to lower agency costs which subsequently potentially enhances firm performance. In this way the relative low agency costs can be viewed as a positive outcome of the familiness of a firm.

On the other hand there is a lot of attention for disadvantages. Altruism is an important aspect that has been investigated by Schulze, Lubatkin and Dino (2003). Altruism can create agency problems. For example, family incumbents have an incentive to be generous. However, that generosity may cause the successors to free ride, shirk and/or remain dependent upon their incumbents.

Another aspect discussed in the literature of agency theory is entrenchment. Poza, Hanlon and Kishida (2004) argued that goal incongruity between the CEO and the rest of the family lead to costs associated with executive entrenchment. Avoidance of strategic planning, lack of career opportunity for non-family agents and avoidance and/ or reduction of business risk are costs found by Gomez-Meija, Nunez-Nickel and Gutierrez (2001).

Governance can have different functions within firms. In the academic debate on corporate governance most attention goes towards the monitoring function of corporate governance. The objective is the maximization of shareholders wealth. In this approach "managers have to be monitored either directly, indirectly via a board of directors or through formal contractual approaches designed to hold management accountable." (Uhlaner 2008). This focus is often not relevant at all for small and medium-sized family firms. Consider for instance the case when the owner is also the manager. However, governance has more aspects than monitoring the managers. Filatotchev, Toms and Wright (2006)

distinguish three functions of governance: monitoring, resource and strategy.

The resource function states that resources from outsiders can be helpful in reducing uncertainty, increasing the firm's ability to raise funds or increasing its recognition (Bennett and Robson, 2004). Resources include business contacts, networks, tacit knowledge, et cetera. The strategy function – also known as counselling or advisory role – of governance has a link with the resource function. Outside directors are widely recognised as being a means of providing a source of expertise that may otherwise be lacking (Bennett and Robson, 2004). This expertise can be valuable in the strategy formulation process.

2.3 Importance of the firm's life-cycle

Filatotchev et al. (2006) argue that it is necessary for a firm to identify where the company stands in the corporate governance life cycle in order to establish an effective governance structure. The corporate governance life-cycle is dependant on the firm's phase in the life-cycle. Based on two variables, 'the organisational resource base' and the 'transparency/accountability', firms can be classified into four quadrants. These quadrants can help define the governance functions suitable for specific firms. For small and medium-sized family firms it is suggested that the monitoring function should be low, resource function high and the strategy function high as well. This is consistent with Van den Heuvel, Van Gils and Voordeckers (2006) who found that CEOs of small and medium-sized family firms perceive the board's service role as more important than the control role.

This life-cycle approach is consistent with Steier's argument on the importance of trust (2001). Steier argues that trust and relational contracting are both prominent features of the governance of family firms in the early stages of their development. But firm owners should realise that the transfer of ownership and/or control could become very difficult when the source of competitive advantage stems solely from the existence of trust in the family firm. Governance systems in firms should evolve in line with the life-cycle phase the firm. This could mean an increase in the formal aspects of the governance model when the next generation has taken over the leadership of the firm.

Summarizing, in order to study the influence of governance on performance it is important to take into account several aspects. Above we discussed briefly the influence of the organizational context, the ownership structure and the life cycle-phase of the firm. Firm performance is influenced by various aspects; examples are familiness, state of the human capital and the position in the life-cycle. A governance board may be an important means to optimise these aspects within the firm.

3 Hypotheses

The empirical focus of this paper is on potential benefits of the establishment of a governance board within SMEs. Theoretically, board functions within SMEs are centred on the contribution of resources and the strategy enhancement. Ultimately these two functions could lead to a higher performance of the firm. As noted earlier, existing research offers no clear answer to the question if an investment in governance has a positive effect on the performance of a firm (e.g., Bennett and Robson, 2004, Uhlaner et al., 2007).

Brunninge et al. (2007) articulate this with two arguments. Firstly strategic change is necessary before performance can improve. Secondly multiple goals prevail in SMEs instead of a sole focus on profit maximization. Rather than focusing only on an overall governance effect we first isolate the strategy function of a governance board. Can we find evidence that a governance board fulfils a strategy function? Van den Heuvel et al (2006) performed research on the importance of the various board tasks as perceived by the CEO. They found that the task 'formulate/ratify organizational strategy' came second after 'building organizational reputation'. In case the strategy function of a governance board does exist, there should be a relationship between the existence of a governance board and strategic planning activities (Blumentritt, 2006). Blumentritt (2006) investigated if a family firm is more engaged in strategic planning and succession planning when the firm has a board of directors or an advisory board. His analysis shows that more planning activities took place in firms equipped with an advisory board than in firms with a board of directors. This leads to the first hypothesis:

Hypothesis 1: Family SMEs with a governance board will more often engage in strategic planning activities than family SMEs with no governance board.

A governance board may not only influence the strategic process, but could also influence firm performance. This can be explained by relating it to the bivalent attributes of family firms (Taguiri and Davis, 1996). Bivalent attributes being the reasons for high performance that sometimes turn into drawbacks. Can an effective governance board prevent this from happening? In this instance the added value of a governance board lies in risk mitigation.

This can be illustrated by using the leadership role as an example of a bivalent attribute. (Miller et al., 2006). Family executives often have the status and ownership position to make courageous decisions aimed at long-term benefits. But strong command could also make the firm too dependent on the leader. Guaranteeing optimal use of the resource 'leadership' can be the added value of a governance board, by safeguarding firms not to become too dependent on the family executive. This dependency will most

likely make the firm more difficult to sell or transfer to the next generation. If this argument holds then firms with a governance board should be easier to sell or transfer than firms without such a board.

Summarizing, the dependency on critical success factors could decrease due to the instalment of a governance board. Hence, continued long-term performance is safeguarded and the continuity of the firm will increase at the same time. The continuity is especially important because of the greying of the owner population. Research confirms a steadily aging ownership in the Netherlands but also in Europe as a whole (Uhlener, 2008). The European Commission (2002) fears that 30 percent of the firms that face⁵ a transfer will not succeed in leading the firm to the next phase. Hypothesis 2b thus states:

Hypothesis 2a: Family SMEs with a governance board will show a higher continuity than family SMEs with no governance board.

Governance boards may also add value in the short run. Experts taking place in the board keep track of the changing business environment and can thus signal potential problems and opportunities for the owner-manager. Short term flexibility may be enhanced due to the establishment of the board, and consequently short term performance may be improved. Hypothesis 2b is stated as follows:

Hypothesis 2b: Family SMEs with a governance board will show a higher expected short term performance than family SMEs with no governance board.

4 Research Methodology

4.1 Sample

The empirical data used in this paper originate from a study exploring the current status of good governance and succession in Dutch family firms. The Dutch family research centre *Centrum van het Familiebedrijf*, in collaboration with the Utrecht University, set up a questionnaire consisting of 27 questions divided into three parts: succession, governance and characteristics of the firm and the owner manager. A web survey tool was used and 20,000 owner-managers were by email asked to participate in April 2007. We have targeted firms with more than 10 employees. After a reminder, in total 857 surveys were returned (a response rate of 4.3 percent). There is no agreement between scholars

about the definition of a family firm (Chrisman, Chua and Sharma, 2005) As a consequence there is a variety of definitions used in research projects. To establish if a firm is a family firm we asked the owner manager whether he or she regards the firm as a family firm. After removing cases with missing values, non family firms and firms larger than 250 employees, we ended up with a final sample of 330 small and medium-sized firms. All variables and results used in the study are based on this database.

Thorough checks were made to assess the representativeness of the sample. The sample is representative for the average Dutch population with respect to age of the owner-manager, the sector and the size of the firm.

4.2 Methodology

Our primary objective is to determine the effects on strategic planning and performance caused by the instalment of a governance board. We use the availability of a written strategic plan as an indicator of the engagement of a firm in strategic planning. Two different measures are used a proxy for performance. The first measure – used a proxy for continuity – is the expected marketability of the firm. Respondents could indicate this on a 4 point scale. The second measure – used as a proxy for the short term expected performance – is the expected sales growth for 2007 as compared with 2006. This is being measured on a 5 point scale.

With respect to the explanatory variable we distinguish two kinds of firms with respect to governance: firms with and firms without a governance board

Four control variables have been included in the regression model. Firstly the variable “firm size”. When a firm grows, the complexity will increase and it becomes more likely that professional management practices are required (Voordeckers et al. 2007). Firm size is measured in 3 categories: 10-19 employees, 20-99 employees and 100-259 employees. Secondly, as an indicator of firm age the variable “founder of the firm” is used. Steier (2001) and Filatotchev et al. (2006) stipulate the relation between governance practices and the generation of the family which is involved in the firm. The higher the number of the present generation, the more complex the organization will become and the more governance generally is needed. Therefore we included the item founder of the firm which measures whether the present family in the business is in its first or in a later generation.

We included the existence of a “strategic plan” as a third control variable in hypothesis 2 as we expect a high correlation between the performance indicators and the availability of a written strategic plan. For the same reason, “marketability” was included as a control variable in hypothesis 1 regarding the regression model for “sales growth”.

⁵ In the same study by the Centrum van het Familiebedrijf (Matsers and Gerritsen 2008) 56 percent of the business owners expected a transfer within the family and 32% expected a sale of the firm or a Management Buy Out. These figures show the importance of a marketable firm.

4.3 Data description

This research confirms the research done by Hessels and Hooge (2006) that most SMEs do not have a board installed at all. 31.2 percent of the owner-managers confirmed to have a governance board whereas 68.8 percent did not have a board. Just over half of the owner-managers with a governance board indicated to have something different than a supervisory or an advisory board. Responses included family members, a private advisor and a family council. This reflects the broad variance in governance boards in Dutch family SMEs and creates an interesting topic for further research.

49.2% of the firms in the sample have 10-19 employees. Another 43.5% have in between 20 and 100 employees. Only 7.3% of the respondents indicate to have more than 100 but less than 250 employees.

The data show a strong relation between firm size and governance boards. 71 percent of the firms with more than 100 employees have a governance board, 30 percent of the firms with 20-100 employees have a board, while only 19% of the firms with 10-20 employees have a board.

With respect to the generation of the owner, 24 percent of the respondents are the founder of the firm.

The descriptive statistics and correlations among the variables used to test the hypothesis are provided in table 1. The correlation table indicates a high correlation between the existence of a governance board and the marketability of the firm. Interestingly, there is only a moderate correlation between marketability and sales growth. This suggests that these performance indicators are distinct. The correlations show a stronger relation between the board and marketability than with the sales growth. There is only a small correlation effect between governance board and strategic planning.

[Insert table 1 here]

Additional information regarding the composition of the governance boards can be found in appendix 1.

We will make use of a t-test for comparing means and regression analyses to analyse the hypotheses.

5 Main findings

5.1 Strategic planning

The first hypothesis states that family SMEs with a governance board will more often engage in strategic planning activities than family SMEs with no governance board. This is operationalised by testing if a family firm with a governance board more often has a written strategic plan, as opposed to family firms without a governance board. Does the existence of a governance board increase the likelihood that a family

SME has a written strategic plan? To test this hypothesis an independent t-test has been conducted. On average, family SMEs with a governance board more often have a written strategic plan (Mean (M) = 0.56; Standard error of the mean (SE) = 0.05) than family SMEs with no governance board (M = 0.38; SE = 0.03). This difference was significant $t(190) = 3.14$; it represented a medium sized effect ($r = 0.22$). This result is consistent with earlier research (Blumentritt, 2006).

5.2 Performance

In hypothesis 2a a positive relation was expected between the existence of a governance board and the continuity of family SMEs. A regression analysis was conducted to test this hypothesis. This has led to the following results.

[Insert table 2 here]

The results indicate a significant and robust relation between the existence of a governance board and the expected marketability of the firm. Also significant but less strong is the relation between the expected sales growth and the expected marketability. This relation is the same as shown in the first regression model. No other included variables showed a significant relation with expected marketability. Interestingly, the availability of a strategic plan has a small adverse relation with the expected marketability.

Hypothesis 2b states that family SMEs with a governance board will show a higher expected short term performance than family SMEs with no governance board. To test hypothesis 2b a regression analysis was conducted to test the relation between the existence of a governance board and the expected short term sales growth. The results of the model indicate no significant relation between governance boards and expected sales growth. However the model shows a significant relation between sales growth and the availability of a strategic plan, the expected marketability of the firm and the fact that the founder is the owner manager of the firm.

[Insert table 3 here]

Summarizing, the empirical results strongly supports hypothesis 1 and 2a while giving no support to hypothesis 2b. This analysis, therefore, indicates that the existence of a governance board is related to the expected marketability of the firm and the availability of a written strategic plan.

With regards to the expected sales growth three other variables turned out to be significant. Two of them are related to the existence of a governance board, hence there may be an indirect effect.

5 Conclusion and discussion

In the context of the discussion on the relevance of good governance in small and medium-sized family firms, this study is an attempt to underpin the relevance of comparing firms with a governance board with firms that did not invest in such a contractual governance mechanism. This study is a first step that should ultimately lead to practical advice for owner managers in small and medium-sized family firms. Should a firm invest in a governance board and how should that investment be carried out? This study leads to some tentative conclusions concerning the first part of this question.

Our hypotheses that governance boards affect the existence of a written strategic plan and the expected marketability are confirmed. That a governance board has an effect on expected sales growth was not confirmed by our data. Overall our findings support the argument that a governance board can have an added value for the firm. The upside potential of governance boards for firm performance is found in the relation with the availability of written strategic plans. Beside the upside potentials, a governance board may also serve as an insurance against downside risks by facilitating the establishment of for example an emergency succession plan. This could be the reason for the strong relation we found with the expected marketability i.e. the positive effect on the continuity of a firm. Firms with a governance board can mitigate the risk of becoming too dependent on the owner-manager(s).

The next step would be to gather more information about the way in which various governance boards function. This way we can learn more about what type of board is effective, and in which situation. Today, most research is focussed on best practices of governance in large firms. This makes sense from an efficiency and monitoring perspective. Looking at SME firms, governance best practices are more likely to be the result of attention to resources, advice and strategy. It is interesting to see which effective governance best practices are transferable to other SMEs. For example, the added value of advisory boards is broadly recognised in high tech start-ups (Morkel and Posner, 2002). The knowledge from these start-ups' advisory boards can help making governance boards in other (family) SMEs more effective.

This study has some limitations which could be improved with further research. Our study was confined to Dutch family SMEs. Furthermore it relies heavily on the self-judgement of the family executives/ respondents. There are also some concerns with respect to the low response rate and possible interaction effects. Lastly, there is the question of causality. There are at least two ways of interpreting the relationship between, for instance, governance boards and expected marketability. Do owner managers invest in a governance board because

they think that it will be valued by potential buyers of the firm? Or are potential buyers more interested in firms with a governance board because they value these boards?

The possible impact of a governance board was only tested in firms with a governance board. The definition of a governance board in this paper is rather broad. It would be good addition to test if, and how, distinctive governance mechanisms interact with each other. It would be interesting to develop a scale of various contractual governance mechanisms and find out where, when and which mechanism works best. For instance, research done by Brunninge et al. (2007) found that a possible weakness of closely held SME can be overcome by utilizing outside directors on the board and/or extending the size of the top management team. Besides contractual governance there are all kinds of informal governance mechanisms, also known as relational governance. Relational governance 'relies on informal social controls based on mutual trust, a shared vision and commitment to the success of the enterprise.' (Uhlener, 2008). To get a complete view of governance in small and medium-sized family firms it is important to include this concept of relational governance.

Furthermore, as stipulated by various researchers (e.g. Van Ees et al. 2008) it is necessary to open the 'black box' of the governance board. We have to look further to shed more light on the ambiguous results found with regard to the relation between governance boards and performance. Most research focuses on the descriptives of the board: for instance the amount of outside directors, the CEO tenure and the size of the board. It is necessary to go beyond these descriptives and investigate the processes and behaviour of the board. An interesting start could be the two concepts developed by Pugliese and Wenstøp (2007): 'board working style' and 'board quality attributes'. 'Board working style' relates to organizing and conducting board meetings and reflecting board work periodically, 'board quality attributes' relates to three attributes: in-depth knowledge of the firm, board diversity and the personal motivation to participate in the board.

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Appendix

We have asked the participating firms in the survey for other characteristics as well. See table A1 for the outcomes.

[Insert table A1 here]

The descriptive statistics show that overall owner-managers are satisfied with the functioning of the governance board. There are significant but not very high correlations between the various variables.

List of tables

Table 1 descriptive statistics and correlations variables

	Mean	SD	B	M	SG	SP	S	F
Governance board (GB) 0=no, 1 = yes	0,312	,464	1					
Marketability (M) 1= very difficult, 4 = very easy	2,139	,850	,549(**)	1				
Sales growth (SG) 1= strong decrease, 5 strong increase	3,976	,787	,231(**)	,313(**)	1			
Strategic plan (SP) 0= no, 1 = yes	,436	,450	,172(**)	,108(*)	,194(**)	1		
Size (S) 1=10-19, 2=20-99,3=100-249	1,603	,631	,212(**)	,194(**)	,144(**)	,160(**)	1	
Founder (F) 0= not the founder, 1= founder	,212	,409	,050	,096	,113(**)	,096	,027	1

N=330, Spearman's correlation coefficients

* Correlation is significant at the 0.05 level (1-tailed).

** Correlation is significant at the 0.01 level (1-tailed).

Table 2: governance board and expected marketability

Explanatory variables	Expected marketability	
	Beta	T-value
Governance board	0,445	8,936 (****)
Control variables:		
Firm size	0,007	0,136
Strategic plan	-0,011	-0,218
Founder	0,023	0,475
Expected sales growth	0,200	4,064 (****)
Constant		4,476

N= 330, R²= 0,28

*significant at 0,10 level

**significant at 0,05 level

***significant at 0,01 level

****significant at 0,001 level

Table 3: governance board and sales growth

Explanatory variables	Expected sales growth	
	Beta	T-value
Governance board	0,066	1,075
Control variables:		
Firm size	0,030	0,564
strategic plan	0,138	2,592 (***)
Founder	0,104	1,994 (**)
Marketability	0,242	4,064 (****)
Constant		21,563
R-square		0.131

N=330, R²= 0,13

*significant at 0,10 level

**significant at 0,05 level

***significant at 0,01 level

****significant at 0,001 level

Table A1 descriptive statistics and correlations governance board

	Mean	SD	G	M	A
Overall grade of the board (G) <i>Grades between 1-10 (10 = perfect)</i>	7,17	1,533	1		
Frequency of the meetings (M) <i>1= once in the last 12 months 2= twice, 3= 3-6, 4 > 6</i>	2,6701	1,038	,116	1	
Advise function (A) <i>1= no advise 2= reactive advise 3= also proactive advise</i>	2,1197	,892	,254 (**)	,425 (**)	1
Family members in board (F) <i>1 = yes, 2=no</i>	,5299	,501	,199 (*)	,322 (**)	,114

Spearman's rank correlation n= 97

* Correlation is significant at the 0.05 level (1-tailed).

** Correlation is significant at the 0.01 level (1-tailed).