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Family Business – The New Potential for Further Business Development in the Czech Republic

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Abstract

The paper deals with the findings from research activities in the field of family businesses in the Czech Republic. It focuses on the field research and the findings as far as the transition between generations of family companies is concerned. The authors pay attention to the family business from several perspectives. Later they provide an outline of possible options for the development of a family business with regard to the risks for family and individual companies.

1. Introduction

Family business is an important factor in economic development throughout the world, particularly in countries changing from a socialist social-economic model to a market economy model. More than ever in the Czech Republic, where free enterprise had been suppressed for decades, it is a very hot topic, because about 25 years ago new private enterprises were established in these countries, whilst the majority of them were the family type. Now is the time to transfer these companies into the hands of successors and followers of the family tradition of entrepreneurship.

At Business School Ostrava there have been prepared on this issue a number of professional and research work. The paper presents the lessons learned by authors that are undervalued in the literature, especially in terms of dilemmas arising from the transition between generations of family firms.

2. Definition of a Family Business

Defining the term *family business* is quite complicated. Individual professional literatures have specific definitions, however their nature is intertwined, and in many respects matches. For instance, they point out to the following characteristics of a family business: *the company is owned by the family, there is an exchange of generations in the course of business (among owners or employees), the company operates a higher number of family members, the influence of the family is manifested on the strategic management of the company, or even there is the desire to pass the business into the hands of generations of family members.*

Late last century for the reason Joseph H. Astrachan and Melissa Carey Shanker provided three definitions of the family business, which differ from one another to the

degree of family involvement in the business¹. Chua, Chrisman, and Sharma state that: "... just a family concern of business is what has resulted in differences between family and non-family business." ²

The first definition of the authors is referred to as a *broad definition*, which describes *the influence of the family on the strategic development of the business, but does not have a stake in the company. Owners have the idea of keeping the business in the family.*

The second definition is called a *medium broad definition*, where there is a crucial *share of ownership (shares) of the founder or his/her family successors.*

In the third referred to as a *narrow definition several family members generationally diverse are involved in business. Ownership and control (management) functions lie directly in families.*

It is necessary to realize that the theoretical models (concepts) of a family business are in specific conditions modified under the influence of traditions and culture of the region and the Church, political, global trends etc. Generally what applies is that: *"The family environment is characterized by the fact that it creates a feeling of security and stability. The behavior of individuals and their relationships can then be based on subconscious performing rituals. However, the purpose of the company is to show a profit, and this goal should be directed to the behavior of people in the business".* ³

Currently, when often the successors (the new owners) of originally family businesses are not blood relatives, *such as a family business is understood the business that maintains the values, style and the spirit of the original family business of the family.* Due to factors of spreading globalization, the development of "family culture" (in the Czech Republic and other Central European countries), and trends in the development of the family business, the family business can be loosely defined as *"Family undertaking in the broadest sense is understood by all enterprises, regardless of whether or they are not owned or controlled by generations of descendants of its original founders, provided that they maintain the spirit and philosophy of business and management style, along with possessing the family of the original founders of the company."* ⁴

In the Czech Republic in the legislation, there is a new concept of a "family enterprise." After several decades for the first time in the new Civil Code as part of the family, the family business has been defined (§ 700-709): *"As the family enterprise is considered such an enterprise where spouses work together, or at least one of the spouses and their relatives*

*up to the third degree or those with husbands who have become brothers-in-law up to the second degree and which is owned by some of these people. Those of them, who are constantly working for the family or for a family enterprise, are viewed as family members involved in the operation of a family enterprise."*⁵

A new Civil Code (§ 700-709)⁶ as well as the Business Corporations Act⁷ offer a broader range of legal means of developing the family business as of 1.1.2014.

3. Succession in the Family Business

Family business is fraught with specific problems that are caused by linking family and business constituents. One of the problems is, for example, the generation change. Korab (2008) states that only a third of family businesses survives the first generational change and of this part then only half of family businesses manage to implement the second generation replacement.

In terms of the family business and succession process it is necessary to include the conscious intention of handing over an existing enterprise to succeeding generations and focusing on the future development of the company. ⁸ In the process of the generational change, it is important to plan well in advance the method of transmission of ownership and the procedure of conferring management and business management. Specifically, it is appropriate to focus on the following three areas:

- managing the biggest amount of capital by involved family members
- creating order in the area of ownership and management for the future generation
- ensuring fair compensation to the excluded successors.

According to Koráb: *"...the entrepreneur should inside his/her family create and nurture the desire to undertake the management of the family business long before he/she actually starts to think about his/her retirement."*⁹

Generational change in the family business is accompanied by many complications from the position of the current owner, but also in relation to family relationships (socio-psychological factors, which are an essential part of family groupings). The owner should focus on the issue of selecting an adequate successor, the appropriate time and method of generational change. ¹⁰

⁵ Act no. 89 dated March 26, 2012. In: *New Commercial Code 2014*. Ostrava: Publ. house Sagit, 2012, Act no. 89/2012 Coll. § 700 Article 1.

⁶ The so called "family enterprise" is defined in §700–707. Act no. 89 dated March 26, 2012. In: *New Commercial Code 2014*. Ostrava: Publ. house Sagit, 2012, p. 320. ISBN 978-80-7208-920-8.

⁷ Act no. 90 dated March 1, 2013. In: *Business Corporations Act 2014*. Ostrava: Publ. house Sagit, 2012, p. 112. ISBN 978-80-7208-921-5.

⁸ VALKOVA, Dagmar, MIKOLAS, Zdenek et al. *Family business: theory and examples from practice*. VSP Ostrava and VSEMVS Bratislava, 2013/14, p. 13.

⁹ KORAB, Vojtech, HANZELKOVA, Alena a Marek MIHALISKO. *Family business: methods of financing family businesses, managing family businesses, successful succession handover*. Brno: Computer Press, 2008, p. 133.

¹⁰ Ibidem, pp. 130–131, 140.

¹ KORAB, Vojtech, HANZELKOVA, Alena a Marek MIHALISKO. *Family business: methods of financing family businesses, managing family businesses, successful succession handover*. Brno: Computer Press, 2008, p. 20.

² ODEHNALOVA, Pavla. *Advantages and limitations of family business*. Brno: Masaryk University, 2011, p. 18.

³ VALKOVA, Dagmar, MIKOLAS, Zdenek et al. *Family business: theory and examples from practice*. VSP Ostrava and VSEMVS Bratislava, 2013/14, p. 16

⁴ VALKOVA, Dagmar, MIKOLAS, Zdenek et al. *Family business: theory and examples from practice*. VSP Ostrava and VSEMVS Bratislava, 2013/14, p. 13–14.

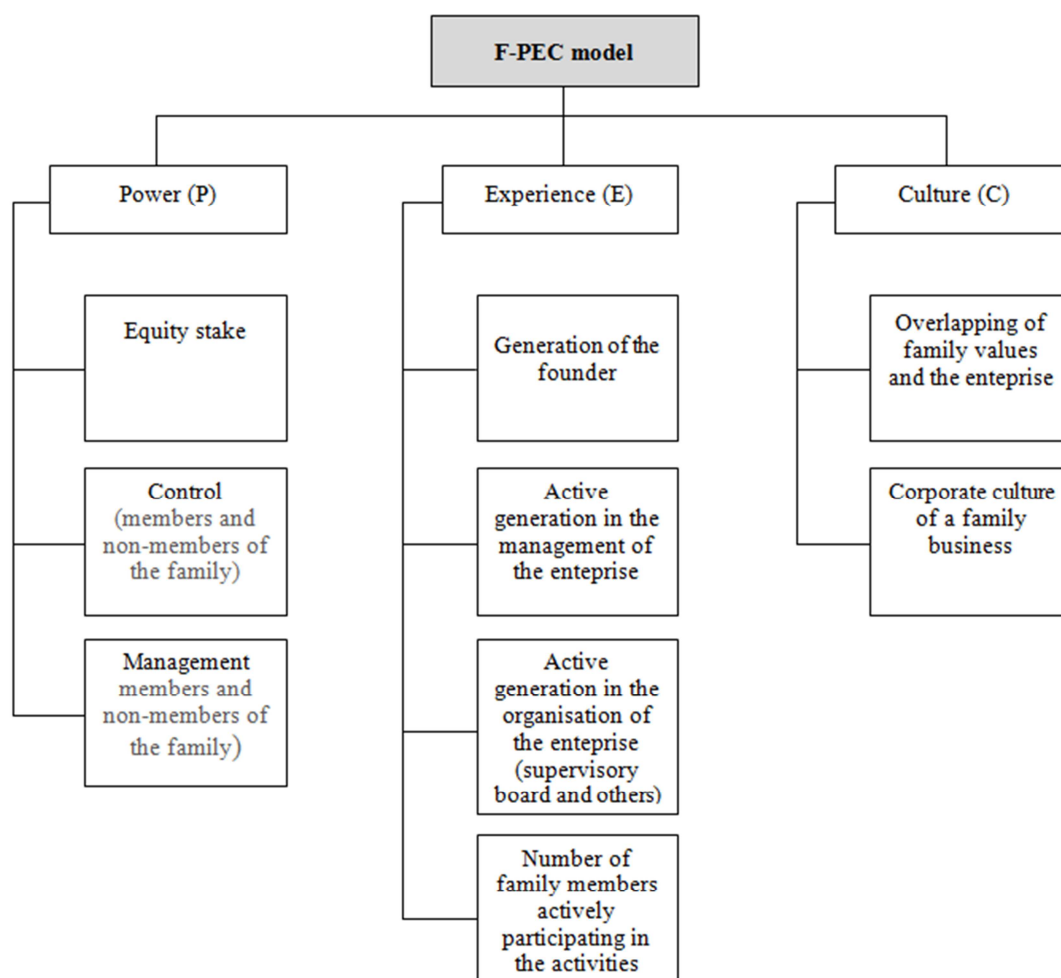


Figure 1. F-PEC model.

Source: KORÁB, Vojtech, HANZELKOVA, Alena a Marek MIHALSKO. Family business: methods of financing family businesses, managing family businesses, successful succession handover. Brno: Computer Press, 2008, 23 p.

4. Field Research

The team of authors had conducted a series of field research in family businesses in the Moravian-Silesian Region (Czech Republic). Very interesting and the latest findings was brought by the study of family businesses (i.e. the holding of family businesses) developed by D. Valkova and Z. Mikolas¹¹, or J. Mikolasova.¹²

During three years (2013 - 2015) more than 100 family businesses were examined in the regions of eastern Bohemia, southern and northern Moravia and Silesia (Czech Republic). The size of the companies investigated was in the range of 3-30 employees. A smaller number of research activities (around 10) was implemented in Poland and the Slovak

Republic.

The main research methods were based on personal contacts of researchers with family businesses. The first phase of the research was based on observations, surveys and interviews with owners and employees of companies, followed by specially oriented monitoring, analysis (relational, causal, financial, business, SWOT analysis etc.). Based on the information and knowledge gained incidence matrices, network diagrams and applied network analysis were processed. Simple statistical indicators and graphical representation were used at the end of the research in the interests of visual interpretation of the information obtained.

The research is based on the concept of *F-PEC* (Family influence through Power, Experience and Culture) by Astrachan, Klein and Smyrnios.¹³

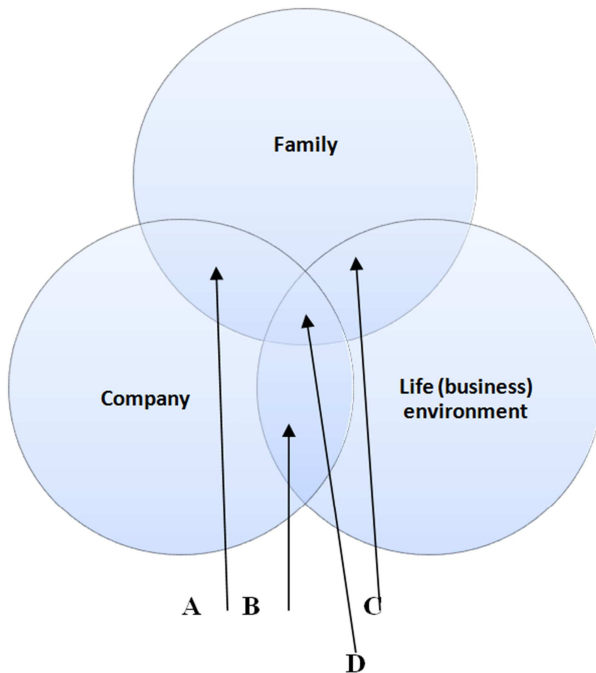
The research team developed the above stated concept

¹¹ VALKOVA, Dagmar, MIKOLAS, Zdenek et al. *Family business: theory and examples from practice*. VSP Ostrava and VSEMVS Bratislava, 2013/14.

¹² MIKOLASOVA, Jana. *Family business with a focus on the company Hostinec a Pivovar U Konicka*. Thesis. Ostrava: VSB-TU, 2015.

¹³ ODEHNALOVA, Pavla. *Advantages and limitations of a family business*. Brno: Masaryk University, 2011, p. 18-19.

according to the main bodies of the development of a family business (see Figure 2).



Source: own processing

Figure 2. Model of the main bodies of a family business.

The research team categorized the obtained knowledge into five groups according to the research objectives and interactions of the main bodies of a family business:

D - Key synergistic factors of a contemporary family business in the Czech Republic

A - Key factors of the management and administration of family businesses (critical relationships of a family and a company)

B - Key factors of the interaction of a company with the business environment

C - Key factors of the interaction of a family and the environment (incl. social, cultural, ideological and legal environment)

E - Other factors not included in the recorded set of factors A to D (the figure shows residual parts of the sets - family, business, life / business / environment).

From the field research published a lot of stimulating information has come up that can be generalized for transition countries (transitioning from a socialist to a capitalist socio-economic model) in Central Europe (e.g. The Czech Republic, Slovakia, and Poland):

- The basis for the development of family businesses is *strong family relationships between family members*, especially between parents and children, supported by a unified moral foundation of value.
- The owners of family businesses surveyed *have never relied on the theoretical sources describing the business, or the family business*, and did business intuitively from the very beginning and often their decisions were supported by the *deep emotions without logical*

considerations and calculations. This finding supports the notion that the business plans of small and medium-sized businesses are not always necessary. More important is creativity, perseverance and diligence of family members.

- *The vast majority of the revenue from business has been reinvested; families surveyed were non-luxury and basically did not change lifestyle after starting a business. Therefore, they did not play their socioeconomic role: although they owned a company, and worked in the company as self-employers, yet they did not profile the role of capitalists, or rentiers.*
- *The goal of doing business is mainly personal satisfaction of the family members with a well done job of satisfied clients etc. The profit from the business is a prerequisite for the economic development of the company, not as a business objective.*
- *Relations between family members and employees are not privileged, they can be described as harmonious - an essential criterion for the management of the family business is the spirit of a family business.*
- *In business activities of families surveyed quite progressive elements appear without business owners' knowledge of their theoretical definition (families involved in doing business "used the common sense" when applying technical, technological, organizational and other innovations).*

5. An Outline of Possible Options for the Development of a Family Business with Regard to the Risks for Family and Enterprise

Based on the findings from analyzes we can outline possible options for the development of the family business in the Czech Republic with regard to the risks for the family and the individual enterprises of the family business in the next 3-5 years.

In the specific conditions of the region of the Czech Republic (in the northern part of the Moravian-Silesian Region), where the studied family businesses operate, there is a philosophical conflict between the standard objective of business - *profitably* and fairly conservative values of *solidarity, relationships between parents, children, etc.* resulting primarily from Christianity (which in this area is deeply rooted both in the form of Catholic and evangelical, Orthodox and other churches).

In this context, let us state just three key proposals related to the rational development of family businesses:¹⁴

- 1) Caring for the physical and mental health of family

¹⁴ In the article, we have presented key factors of the Segment A - key factors in the management and administration of family businesses (critical relationships of the family and the business) that had the greatest frequency of occurrence (most families reported them).

members

Family members in the first five to ten years of building family businesses usually spend from 10 to 15 hours a day working in the company (each family member), i.e. during a week for at least 60 hours. This situation leads to long-term stress, mental burnout and a loss of motivation, increased morbidity (mental disorders, sleep disorders and concentration, increases in blood pressure, diabetes etc. illness). *Health care of family members, time management, and the delegation of competencies for employees are the key moments of rational family business.*

2) Transition of parents – from founders of the family business to business retirement

The field research shows a clear recommendation to the descendants (daughters, sons, grandsons) to conclude with parents (grandparents) written agreements as for securing their economic, social and other needs after their business retirement. It could be a written record of "reserved property"¹⁵, which would be based on family and moral values. It should not be a problem in families, if they have a world-view orientation to a strong relationship between parents and offspring (e.g. the Christian concept of the family). Space for the definition of "reserved property" is offered in the new Czech Civil Code section on family (especially in terms of § 700-709).

Should this written obligation not be met by the descendants and the parents, moral or other wrongs could occur under certain circumstances (the influence of strangers, distant relatives etc.) as far as original owners (parents) and the founders of family businesses are concerned and other moral wrongs, e.g. a decline in living standards in old age, a loss of social contacts, etc.

3) Proprietary differentiation of descendants

It is obvious from the field research that the present family holding companies are companies which have the same growth potential. In this situation, the property relations and the growth of property differences between siblings tend to change very quickly, which usually manifests itself in a conflict between family members of the third generation (i.e. the grandchildren). The implied risk could lead to a threat to family relationships and family business. Therefore it is recommended that each family business should well in advance discuss this informally "growth" risks as well as set up a "joint family" plan which would compensate for the risks outlined by the socio-economic differentiation of the extended family, especially future generations (the grandchildren, great-grandchildren). It is about e.g. creating a system of payments for the family brand into the family "solidarity" fund, building mutual funding system services to a wider family (system of social solidarity), implementing joint investments, creating a joint financial fund, which would generate resources for grandchildren, family members etc. in sickness, old age, etc.

Socio-economic implications of the departure of the

founders of family firms to "entrepreneurial retirement" and the socio-economic stratification of followers (followers in a family business) are critical moments in the further development of family business not only in the Czech Republic.¹⁶ This problem can be very painful for the founders of family businesses that they had built from "scratch" through their diligence, creativity, personal victims of time, often health etc. A great inspiration may be the principles arising from the foundations of the Jewish, Christian or Muslim socio - economic thinking that we have known for two or more millennia (e.g. a Christian socio - economic system Mandragora, a Jewish kibbutz, etc.).

6. Conclusion

Family businesses in the Czech Republic are neither theoretically nor practically (legislative and economic policy of the state, activities, regions, municipalities etc.) sufficiently supported. Usually they are referred to as small and medium business, without paying attention to whether this is a family business or other type of business, which is a considerable debt to the institution of the family business entrepreneurs.

Family businesses, as revealed by the practical analysis, have more benefits than the "non-family business." The family business has an impact on the cultivation of family life, maintaining the value system and lifestyle on the one hand and to stabilizing the business on the other.

During the examination of the family business there have been identified some findings that are not described in the available literature. In particular, it is the fact that *employees can continue the family business provided that they maintain the "family spirit" of the original founder of the company.*

There are also risks of a family business. It was found that the family must take care of the physical and mental health of its members to take over the long-term extra burden and thus avoiding breakdowns in health, mental burnout etc. Families must also address the fundamental ethical questions of future family relations: *in particular, the way descendants will secure socially and economically parents' and grandparent's life standard and (the founders of family firms), after going to the "business retirement".* Another potential challenge for the future is *a different level of economic growth of individual enterprises managed by family members. Thus equity ratios of offspring in the future may be different, if there is no "ethical agreement" on property redistribution ("settlement") within the wider family.*

Family businesses have a great potential to enhance the development of both the country's economy, but also have a significant hub for the development of culture, traditions and values of a healthy modern harmonized society.

¹⁵ Putting it bluntly.

¹⁶ It should be noted that the available scientific literature has not clearly and unequivocally presented the above stated findings. Therefore, we consider the findings published in this article as a shift in the understanding of family businesses in the Czech Republic.

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¹⁷ The second monograph in the context of international research: „Development and status of small and medium enterprises in the Czech Republic and the Slovak Republic, “VŠP Ostrava and VSEMVS Bratislava.