Succession Problems in Family-Owned Businesses: An Example from the Czech Republic

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Key words
Succession, family-owned businesses, case study, SME, Czech Republic

Abstract

The aim of this paper is to present a particular example of Czech small retail family-owned firm which is currently facing the succession and generational transition problem. Due to their nature, family-owned businesses face a number of specific problems. The most demanding task for them is succession and generational exchange when an incumbent leaves the business and has to pass on his or her position to a successor. Succession is a very important moment for every family-owned business, particularly for small one, because there is a lack of successors. This moment has an essential influence on the eventual failure of a family-owned firm. The author of the paper made use of secondary data from a bachelor's thesis which he supervised in his research which described small retail family-owned firm. Secondary data are supplemented by a theoretical context and the specialised evaluation of the author.

Introduction

This paper studies particular small retail family-owned businesses in the Czech Republic and attempts to demonstrate certain problems which all small family-owned businesses have to generally face. Small and medium-sized enterprises (SMEs) are a very important part of each economy and play a significant role in the national economy. The European Commission (2013) is right when it states that following the daily news, it is easy to gain an impression that the European economy is dominated by large, multinational companies. Their multi-billion Euro takeovers, global expansion plans or, more recently, risks of mega bankruptcies dominate the headlines. What usually becomes lost is the fact that more than 99 % of all European businesses are, in fact, SMEs. They provide two out of three of the private sector jobs and contribute to more than half of the total value-added created by businesses in the European Union (EU).

Micro-firms dominate the SME sector in the Czech Republic. Unlike large enterprises, the number of which has been dropping since 2008, the number of micro-firms rose up until 2010, and performed better as regards jobs than SMEs. The total number of SMEs has been growing and has been consistently above the EU average. Nevertheless, there are currently approximately 3000 fewer SMEs in the Czech Republic than there were last year. There were approximately 930,940 SMEs in the Czech Republic in the year 2012 which makes up 99.9% of all the enterprises. (European Commission, 2012)

Prior to presenting a particular example of a small retail firm from the Czech Republic and their specific problems related to succession and generational transition, it is also important to provide an accepted definition of small and medium-sized enterprises, in light of the fact that American and European definitions of SMEs might be different.

The European Commission (2003) defines the category of micro, small and medium-sized enterprises as "enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million. Within the small and medium-sized enterprise category, a small enterprise is defined as an enterprise which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million. Within the small and medium-sized enterprises category, a microenterprise is defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million." Due to an eventual international comparison with other studies, we will make use of the definition recommended by the European Commission.

Methodology

It is very important for family business research to present examples from different countries thereby allowing us to learn and look at the succession issue in various surroundings and from other perspectives.

A case study presenting particular example of small retail family-owned business was chosen for the research methodology. The secondary data was obtained from a bachelor's thesis (Záhorovská, 2012) which the author of the article supervised. The data are supplemented with up-to-date information from research focused on family businesses and planning of succession. The author of the bachelor's thesis is one of the daughters of a business man and thereby had the opportunity to truly examine the company in depth. The second neutral perspective of the author of the article combined with specialised sources both serve as the advantages of the entire research and article.

Remenyi (2012) states that making use of case study research for an academic degree or for research to be published in a peer reviewed journal is challenging. He also presents two different types of case studies. In his view the term case study is used in two different ways in order to mean quite different activities. He further argues that research should be clear concerning the meaning of the term case study within the context in which the researcher encounters it. A teaching – learning case study was chosen for the purposes of this research wherein a situation was according to Remenyi (2012) described in a certain detail for use in a classroom, to stimulate discussion which will lead to those present learning about the subject of the case study.

The main objective of this paper, involving presenting a particular example of a small retail family-owned business from the Czech Republic, is to share ideas and knowledge from different part of the world and provide possible solutions.

A family-owned business

Despite the fact that we unconsciously know what a family firm consists of and what does not, there is no existing unified and generally accepted definition of a family firm. Family business researchers provide several approaches as to how to properly define a family business or firm. They are unable, however, to reach an agreement on the width or content of the definition. Countries where family businesses play an important role have attempted to describe or define family firms in a definite manner. The European Union has also tried to clearly define a family business, but has not as yet agreed upon a clear definition as is the case with SMEs. The aim of this article is not to precisely define a family firm, but to instead present a concrete example of a family firm and demonstrate the problems they are generally faced with. Family firms are extremely varied and differ in terms of size, structure and legal form. What family firms do have in common, however, is a high dedication to work on the part of the family members. Family firms are also highly flexible as concerns work and time. Families can often dedicate all of their time to the firm, this being something a developing business requires. Families are also able to adjust the financial needs of the family to the needs of the firm. Long-term goals prevail over short-term, one-time, approaches in terms of management of family firms and family businesses are also able to react in a much more flexible manner to unexpected changes on the market. Each family firm has its own company culture which is given by the visions and goals of the founder of the firm. Since many family business entrepreneurs carry out business under their own name or actually bear the name of the family, they tend to be justifiably proud of the business. Entrepreneurs are also motivated to maintain the best possible reputation for their business amongst their trade partners and customers and also are interested in producing the best possible products and providing quality services. The weak point of the firm can consist of emotional conflicts as well as also the issue of succession.

The succession problem in family-owned businesses

Cadieux, Lorrain, Hugron (2002) define succession as a dynamic process during which the roles and duties of the two main groups of individuals involved (the predecessor and the successor) evolve interdependently and overlap with the ultimate goal being the transfer of both the management and ownership of the business to the next generation. Hnátek (2012) has identified the difficulty of dealing with generational transition and succession planning as the major problem threatening the existence of family firms. The passage of a family business from one generation to the next, and the change of leadership it involves, is a process that can be fraught with difficulty. (Leach, 2011, p.13) Succession is not a one-time event, but consists of a lengthy process which should be smooth, natural and first and foremost thought-out. (Hnátek, 2012) Cadieux, Lorrain, Hugron (2002) argue that during the first phase, the owner-manager is often completely and solely in charge of the daily affairs of the business. Although the successor does not visibly hold a position in the business, it is during this time that he or she is introduced to the business and develops a positive perception of his or her parent as a manager. The successor begins to show interest in the business and the owner implicitly chooses who will take over. The second phase begins when the predecessor brings the successor into the business giving him or her part-time job or summer job. This is considered a learning period. The third phase, considered a transitional step in the process, differs from the first two phases primarily in that it marks the official entry of the successor into the business as a successor. The predecessor and the successor work side by side, thereby ensuring a transfer of responsibilities and authority until the successor is able to make business decisions on his or her own. The final step in the process is the complete transfer of responsibilities and ownership. Succession should be planed and prepared well in advance. Leach (2011, p.146-147) states that planning for transition cannot start too early and that the entire process needs to be carefully managed. He sees family business succession as a two-stage process involving the transfer of management and ownership of the family business. Unfortunately with parents often willing to maintain certain rights in management, it does not take place at the same time. Many entrepreneurs are occupied with operative management of the family firm and do not have a long-term plan or strategy. Failure to act concerning succession is often disastrous for family companies. (Leach, 2011, p.147) Worldwide statistics are clear, where it is estimated that approximately 70 % of family-owned business do not survive into the 2nd generation and 90 % no longer controlled by the 3rd generation of the family. Many entrepreneurs are aware, however, that they cannot manage a company forever and that they have to begin thinking about who will take over their position. According to Leach (2011, p.146), the willingness of family business owners to plan for their succession is often a decisive factor determining whether the business survives or fails. Family business research and professionals should therefore assist family firms in planning succession and overcoming problems connected with this issue. Succession between generations in family businesses is less straightforward than it used to be. Today's generation is growing up in a commercial culture which is radically different from that in which earlier family members took on responsibility. (Leach, 2011, p.73) It is consequently important that contemporary owners and entrepreneurs be educated in this area with a particular focus on their successors who need to be aware of their future roles and responsibilities.

The situation in the Czech Republic

The Czech Republic was established in 1993 after the dissolution of Czechoslovakia, when the Czech Republic and Slovakia became independent states. Family businesses in the Czech Republic do not have a long tradition and unfortunately family firms which have been owned and managed by one family over several generations do not exist. This is a result of the fact that private businesses in Czechoslovakia were nationalized and became state companies after World War II (Hnátek, 2012). Genuine Czech family businesses came into being after the economic and political changes in the year 1989. The 1990s in the Czech Republic were marked by bold business activity whereby young people full of euphoria from the social changes threw themselves into businesses without any experience. The situation stabilized over time and at present more than 20 years after these pioneer days, entrepreneurial thinking has matured concerning how to approach a building and stabilizing business.

There is therefore no experience with succession and generational transition. At present, the first Czech family firms are beginning to encounter this situation whereby they have to deal with the problem of succession. The first small and medium-sized companies are beginning to move from the hands of the founders into the hands of their children, thus the businesses begin to be managed by a second generation. The rest of the world has much more experience with family businesses and with generational transition. The situation, however, is not all that conducive and generational transition is an extremely demanding process. (Hnátek, 2012)

Family businesses are not as yet controlled by a specific law in the Czech Republic. The first initiative from the side of the legislative consists of the new civil code which is in effect as of 1 January 2014 and which, among other things, will newly introduce a so-called "family plant". According to the code, this will consist of firms where a couple work together or another law which will define relations which as family members working in a family business will have the right to share revenue as well as items obtained from that revenue. The law does not otherwise focus on family businesses or control it in any fashion.

An example from the Czech Republic

The example from Czech society which is currently solving the problem of succession consists of a small retail limited company with its seat in the regional capital of Zlín with approximately 75,000 inhabitants in the east of the Czech Republic. This company is specialised in retail involving complete furnishings of bathrooms.

The historical context and development of family-owned firms

TomášBaťa, one of the most successful Czech entrepreneurs of his time and the founder of the family industrial empire Bata Shoes Company currently bearing the name Bata Shoes Organization with its headquarters in Switzerland, also come from the town of Zlín where our analysed small retail family-owned firm also comes from. TomášBaťa (3 April 1876 – 12 July 1932) holds a similar position as world renowned industrialists such as Thomas Alva Edison and Henry Ford. Thanks to his industrial activities, TomášBaťa built up the town of Zlín providing it with a specific industrial architecture which the town has preserved up until the present. Despite the fact that the company was nationalized after the year 1945 and given a different name Svit in the year 1948 by Communist functionaries, the entrepreneurial spirit of the town is still apparent. Many local entrepreneurs view TomášBaťa as their model for business success.

The analysed small retail family-owned firm has been registered in the Trade Register as of September 2004. The actual history of this firm, however, dates back to the year 1990 when the founder of the family firm worked as a natural person using his business license. The small retail family-owned firm is involved in the sales of complete furnishings for bathrooms. 4 employees are currently actively employed in the firm in all out of which 3 are members of one family. 80 % of the business is owned by the founder while a 20 % share is owned by his wife who works in the firm with him. The founder, in a similar manner as other entrepreneurs, made use of the political-economic changes and business opportunities the beginning of the 1990s. This initially, however, only consisted of side earnings while working full-time at another job. The founder of the business invited his wife's brother to join the firm in the year 1992 and opened a small shop out of their home. The entrepreneur gave up his job in the year 1994 and began to focus on his business full-time. He hired another employee as a stock clerk in the year 1997. The shop moved to new facilities in the year 1999 and became the largest shop of its kind in the region. The wife of the entrepreneur also became fully involved in the business in the year 2000 in the position of chief accountant. The entrepreneur along with his wife founded a limited company in the year 2004. The wife's brother who was not interested in contributing financially to the business remained as a normal employee in the family firm.

Managing a family firm

Small family-owned firms are intuitively managed by the founder of the business who does not have specialised managerial education and who instead tends to make use of his or her practical long-term experience. Záhorovská (2012) in her work argues that the primary strong side of the analysed family firm specifically consists of the entrepreneur's long-term experience in the area of business and long-term solid relationships with both his suppliers and customers. These good relationships are built upon the personality of the founder of the firm. According to Záhorovská (2012), the entrepreneur has moved with all of his business activities toward his established goals which have never, however, actually been formulated and which are therefore not even fully known by his other employees or family members.

The employees are aware of the values, visions and goals of the firm via the business culture which the entrepreneur has created. The firm, however, is not managed in a strategic fashion, but is instead more of a reaction to the existing situation as opposed to long-term goals. The entrepreneur does not conceal his interest in passing on the firm to his children, but is not currently taking any steps towards an organised planned succession. The entrepreneur has two daughters. The older daughter has already completed university and is married. The younger single daughter is studying at university with a focus on management and economics. Neither of them, however, is significantly involved in the family business, but only occasionally assist with administration or serve as persons who the entrepreneur consults marketing activity with.

In light of the variety of work activities on the part of the current entrepreneur, the intuitive operative management on the part of the current entrepreneur will be extremely difficult to replace and the operations of the entire firm could be seriously threatened if a sudden indisposition should occur.

Záhorovská (2012) makes mention of the minimal marketing expenditures and attempts to save money in this area as ranking among the weak points of the analysed firm, despite the fact that the business could by this means increase its sales. This approach could stem from a lack of trust on the part of the entrepreneur in marketing tools which he perceives as a cost as opposed to an investment which would increase sales. The weak side of the firm is in her view the number and work positions of the employees. 4 employees work in the firm in all as has been mentioned earlier: the founder of the firm and his wife, the wife's brother and one employee who is not a member of the family. This consists of a small firm from the perspective of small and medium-sized companies, or to be more exact a micro-firm. In light of the low number of employees in the firm, written communication does not exist and everything is merely a question of spoken communication and personal meetings at the workplace. The employees are not fully involved in their work on a balanced level over the long-term. A lower number of employees, according to Záhorovská (2012), would not be possible, however, as no one would be able to replace the work position and react flexibly to the arising situation in case of illness to one of the employees. The actual problem of the family firm is instead too large a connection between the firm and the family. At present the shop is actually situated in their house which is owned by the father of the wife of the founder and her brother. This house is also inhabited by the family of the entrepreneur, the family of the wife's brother along with their parents. At present, when the entrepreneur is considering the possibility of future development of the firm and handing it over to the next generation, selling the firm as one of the possible solutions to the succession problem appears problematic. The entrepreneur developed the firm, however, from the beginning with the idea that the business would one day be handed over to his children. For this reason the entrepreneur is unwilling to sell the firm. The founder and his wife have two daughters while the wife's brother has a daughter and a son. As has already been mentioned, they are not significantly involved in the operations of the firm which serves to complicate their successor position. All of the offspring have an extremely positive relationship to the firm and everyday interaction with it as a result of their presence in the house.

Discussion and conclusion

This paper has examined the issue of succession problem with the example of a concrete small retail family-owned firm from the Czech Republic. The author placed family businesses into the historical and economic context in the introduction to the article with a reference to the specific aspects of family businesses. He also described the economic situation in the Czech Republic where the tradition of family businesses was interrupted by the Communist planned economy with the result that entrepreneurs at present lack experience with planned succession. In the majority of cases, the owner of a family business is also the founder of the company with this actually being a reflection of his or her personality and visions. Hnátek (2012) argues that it is specifically the founder who decides what will be the subject of the business, who will be the customers for the business, what needs and what products or services the business will provide. These missions and visions should be written down on paper and be clearly formulated so as to express the basic strategic aims of the management and be understandable for all the employees in the company. The fact that family businesses are intuitively managed by the founder of the firm who lacks specialised managerial education and instead makes use of his or her practical long-term experience was revealed as the main problem. Handing over the firm to the offspring would be personally desirable from the side of the founder of the business who also built up the firm, however, none of the potential successors are currently significantly involved in the firm at present nor is the entrepreneur himself taking concrete steps in order to prepare his offspring to take over the business in the future. Both daughters only contribute to administrative activities, but have not expressed interest in the actual subject of business. The older daughter of the entrepreneur is already married; however, her husband is not involved in the firm in any manner and has no ambition to do so. The younger daughter is single.

The answer to the question as to which direction the business strategy should take concerning the planned succession in order to ensure that the prosperous firm be successfully passed on to the next generation and prevent it from being sold, despite the fact that the two daughters have not expressed a significant interest in the business, can be found in the dissertation by Hollerbach (2011). This work makes mention of another example from the Czech environment involving the entrepreneur Koloman Münnich who lived from 1854 to 1934 and achieved renown as a pioneer in the energy branch and amongst other things carried out business in agriculture and other areas. Münnich had five children with his wife, with these consisting of two boys and three girls. Münnich's oldest son who did not have any offspring, successfully graduated from university with a focus on agriculture and was supposed to supply the family with food. His father consequently invested in land, farming machinery and livestock. Münnich's second oldest son studied at a more technical university with a focus on electrical energy. He was hoping to become the director of the electricity plants which his father owned. This son had four children. The oldest daughter married a physician who provided the family with the essential medical needs. Her father invested into medical equipment and the pharmaceutical industry. The second daughter also remained in a branch connected with medicine when she married a pharmacist with his own chemist's. The youngest daughter married an economics specialist who worked as the director in a company supplying electricity and later became director of the entire family company when another of Münnich's son retired.

The arrival of a competent manager into the entrepreneur's family would serve as a new impulse for the analysed family business. The analysed family-owned business is intuitively managed by the founder of the firm who does not have any specialised managerial education and tends to make use of his practical long-term experience in his work. The business is consequently not managed in a strategic manner, but instead managed in reaction to the emerging situation. The management style consequently needs to be changed in order for the business to be able to function independently and not be completely dependent on the person of the entrepreneur who is clearly interested in handing over the firm to his offspring, but is unfortunately not taking any steps in order to ensure an organised planned succession. This situation has to change in order for a successful generational transition to take place in the business. The entrepreneur cannot manage this change on his own and will need assistance.

In order to generally assist family firms with planned succession, there is a need for functioning direct cooperation between family-owned businesses and family business professionals from both the private and academic environment. State institutions, which have not as yet paid any major attention to family businesses in the Czech Republic despite the fact that the economy of the entire country is linked with it and that problems within these firms would bring about problems for the entire economy, should also become involved. The task of academics is to examine the problems of family businesses in detail and consequently inform both the specialised and lay public about the issues.

Research limitations and suggestions for future research

The performed research, which arose out of secondary data (Záhorovská, 2012), brought with it extremely interesting results. The research has both strengths as well as weaknesses. The strengths include the fact that the secondary data was provided by the daughter of the entrepreneur allowing us to look in depth into the functioning of a retail family-owned business. The disadvantage, however, could be the unintentional self-control on the part of the author of the work and the provided data due to reasons of involvement in the firm. The author of the article has commented, however, on the obtained data from a neutral position and placed it into both the economic and social context, thereby supporting the strengths. The weaknesses of the research include the fact that only one firm has been selected as an example representing family businesses and problems connected with succession in the Czech Republic. In order to make generalizations from these conclusions, there will be a need to present more examples of family-owned businesses in the Czech environment and observe them over a longer time period in order to be able to evaluate in what manner they have managed or failed to come to terms with the succession problem and generational transition.

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