UNIVERSIDAD DEL CEMA
Buenos Aires
Argentina

Serie
DOCUMENTOS DE TRABAJO

Área: Negocios

SIMPLE TECHNIQUES TO ENHANCE THE GOVERNANCE OF A FAMILY BUSINESS

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Agosto 2013
Nro. 517

ISBN 978-987-1062-88-1
Queda hecho el depósito que marca la Ley 11.723

www.cema.edu.ar/publicaciones/doc_trabajo.html
UCEMA: Av. Córdoba 374, C1054AAP Buenos Aires, Argentina
ISSN 1668-4575 (impreso), ISSN 1668-4583 (en línea)
Editor: Jorge M. Streb; asistente editorial: Valeria Dowding <jae@cema.edu.ar>

Yacuzzi, Enrique Antonio
Simple techniques to enhance the governance of a family business. - 1a ed. - Buenos Aires : Universidad del CEMA, 2013.
42 p. ; 22x15 cm.

ISBN 978-987-1062-88-1

1. Negocios.
CDD 650

Fecha de catalogación: 02/09/2013

SIMPLE TECHNIQUES TO ENHANCE THE GOVERNANCE OF A FAMILY BUSINESS

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ABSTRACT

The use of simple governance techniques at a hypothetical family business (called ABC) will be beneficial. Good governance leads to a better relationship among stakeholders, increases the effectiveness of family institutions and board work and activates unknown potential at the firm through better principles and practices.

Tools proposed are: (1) A new and flexible family business governance indicator, developed for this paper; (2) *Hoshin* management; and (3) Effective meeting technology. The three techniques interact in a systemic mode. The indicator allows measurement of how family business governance evolves through time in a company and facilitates comparison between different companies´ governance. Most importantly, it is a checklist and roadmap to better governance. Hoshin management is a generic planning method that can be used to build a governance improvement plan. Effective meetings facilitate planning and control and in this sense they are a tool for governance improvement.

This paper is mainly based on the following sources: IFC (2008), Yacuzzi (2005 b, 2007, 2008, 2012), Yacuzzi et al. (2011), Naiberger & Yacuzzi (2009). To an important extent, the paper´s organization is based on Yacuzzi (2012).

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* The authors' views are personal and do not necessarily represent the position of the Universidad del Cema.

I. INTRODUCTION

Corporate governance is a field of study and application that deals with corporate by-laws, statutes, codes of good practices, management of interest conflicts among stakeholders, and accountability of the firm, among other themes.[1] Family business governance has specific problems, and specific ways to define, measure, and approach them. In order to have effective governance, companies must translate concepts into actions that transform the company and its environment according to governance concepts.

In this paper I propose a few simple tools to improve family business governance in a relatively short time if led by an active management group. In particular, I believe that they can be applied to any family business like ABC.

I show key concepts of the proposed tools and how they could be applied to enhance governance at ABC by converting abstract concepts of family business governance into concrete operating systems that conduct daily aspects of governance. These tools are: (1) A newly developed family business governance indicator –based on the structure, although not the contents– of the Japanese Deming Price; the indicator serves as a monitoring mechanism, as a checklist of governance keypoints, and as a roadmap and benchmark to better governance; (2) *Hoshin* management, with a well-tested methodology; *hoshin* management aims at short-term planning focusing on a few objectives, called *hoshin*[2], to overcome key problems in the context of a long-term plan; and (3) A system of effective meetings, based on the experience of a leading Japanese shipyard; the system organizes the *hoshin* planning process and strengthens company governance. If appropriate, all three tools can be used in the context of a TQM-like system and its quality methods.[3] When systematically applied to a family business, they become operative and put in action governance concepts.

The family business governance indicator (FBGI) was developed for this paper, based on Yacuzzi (2008). Hoshin management has been previously used in several Argentine firms, as described in Yacuzzi (2005 b) and Yacuzzi et al. (2011). The meeting system is described in detail in Yacuzzi and Naiberger (2009).

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[1] Apreda (2003).
[2] In Japanese there is no plural form for names; thus ´hoshin´ will be used in all cases.
[3] TQM means Total Quality Management.

II. MAIN FEATURES OF FAMILY FIRMS AND TECHNIQUE RELEVANCE

Most family firms share common characteristics around the world: a long-term perspective, strong commitment to the business and its strategy and a clear identity; they minimize agency costs; the family is involved in the top management of the company and creates a working environment associated with employee care and loyalty; conflicts and succession issues are key concerns, as well as governance issues such as whether the CEO belongs to the family and, in general, the board's behaviour and composition.

In addition, studies show that an important challenge faced by family firms is strategy formulation, as well as staff employment and succession from one generation to the next, in the context of conflict management and resistance to change. Classical issues confronted by family firms are: (1) The ability of family members to effectively and professionally manage the business, specially when there is the transfer of ownership or management from one generation to the following; (2) The lack of a succession plan and the confusion that this lack generates when the generation in charge leaves the business scene; and (3) Corporate governance, in particular, those issues related to the protection of minority shareholders' interests that are rather isolated from the decision making process of the firm. In addition, tighter regulation and intense competition, both domestic and foreign, force family business to adopt modern tools and philosophies.

The tools I propose are particularly apt to enhance family business governance, as they allow a consistent treatment of strategic issues, including adaptation to a changing environment and succession, and governance issues such as minority stakeholders´ problems and board's effectiveness. In particular, *hoshin* management helps to reduce intra-company conflict and systematically promotes change. In addition, the tools are flexible, of low cost, and rapidly effective, all attractive qualities for firms in a difficult environment.

These methods are very simple to learn and use. Simplicity is a highly regarded value in basic sciences such as physics, although not necessarily in management theory. However, simplicity promotes the diffusion of ideas across organizations and helps to consolidate change through a company-wide movement. Simple tools facilitate the participation of a great number of members of an organization, leading to easier implementation of plans, better use of collective wisdom, and an increased identification of employees with company goals and means. Table 1 indicates how key problems of a company like ABC and its environment could be addressed by the proposed governance tools and provides operating mechanisms.

Governance-related aspects of family business and their environment	**Applicable tools to address them**	**Operating mechanisms**
Economic uncertainty	HM, FBGI.	HM can draw specific plans with objectives of quick effect. The FBGI measures and enhances board work.
Regulation	FBGI.	The FBGI measures the quality of the relationships with the stakeholder government and enhances board work.
Competition, strategy formulation at the board	MS.	The meeting system is a framework to collect collective wisdom of owners and employees for competitive strategy formulation as a board's formal duty. In coordination with family institutions, the board strengthens its strategy-related actions.
Willingness to minimize resources to develop a governance architecture	HM, FBGI, MS.	All three tools have an extremely low implementation and maintenance cost, and they become the axis to create a family business governance architecture.
Need for a long term perspective and the formulation of a clear strategy	HM, FBGI, MS.	HM develops a plan for the first year of a long-term plan (usually, of five years). The FBGI measures and enhances board work and family institutions, the visible creators of long-term strategies. The MS collects collective wisdom.
Strong commitment to the business	MS, FBGI.	The MS leads to a regular treatment of all business-related matters; in parallel, family issues are thoroughly treated. The FBGI measures and enhances relationships with diverse stakeholders and evaluates and motivates the board.
Family members in top management, succession issues	FBGI, MS, HM.	The FBGI measures and evaluates the effect of governance principles, related to a family protocol, for example; in addition, it evaluates and motivates adequate board work. At the MS, family concerns can be systematically dealt with. HM can include succession-related objectives.
Employee care and loyalty, staff and family member employment	FBGI, MS.	The FBGI, in its stakeholder section, measures employee relationships and can serve to improve them; in particular, the family governance area deals with family member employment policies; in addition, in its principles section, the indicator approaches transparency, thus strengthening employee´s care and loyalty. Employees could participate in some meetings, with the same effect. These mechanisms facilitate, over the medium and long term, firm reputation and staff employment.

Table 1. Governance-related aspects of ABC's and their environment, applicable tools to address them, and main operating mechanisms. FBGI: Family business governance indicator, HM: *Hoshin* management, MS: Meeting system.

Governance-related aspects of family business and their environment	**Applicable tools to address them**	**Operating mechanisms**
Corporate governance issues, conflict management	FBGI, MS, HM.	The FBGI is an overall guide to treat various governance issues, including conflict management. The MS is a space to deal with problems. HM can fix some objectives addressed to solve specific conflicts.
Parallel development of family and business structures. Consolidation of family institutions	FBGI, MS, HM	The FBGI provides elements to control this development. MS and HM allow easy interaction and mutual improvement of family structures, specifically, family institutions, and business structures.
Need to manage professionally and monitor the effectiveness of governance practices	FBGI, MS, HM.	The FBGI suggests that professionalization starts at the board. The MS can include training and educational activities, starting at the board members. Some hoshin can be related to professionalization. All three tools help to monitor the effectiveness of family governance practices.
Need to continue on a sustainable path to governance improvement	FBGI, MS, HM	The indicator serves as a roadmap to governance improvement as well as a basis for improvement control, the MS is a sounding board to new governance initiatives, HM helps planning and control of these initiatives.
Need to strengthen the work of board committees	FBGI, MS, HM	The FBGI serves as a control mechanism of the development and effectiveness of audit, remuneration, nomination, change management and perhaps other committees. The MS facilitates the interaction board-committees. HM helps committees action plans and control.
Need to create an adequate policy for succession planning for family members in senior management positions	FBGI, MS, HM	FBGI helps monitoring this policy. HM is an adequate framework to develop succession planning for family members in senior management positions, at all levels, individual, family, shareholders, board, family institutions, etc. MS facilitates discussion and implementation of decisions on succession of senior management.
Need to establish a policy for family member employment and remuneration	HM, MS, FBGI	HM can include among its objectives the establishment of these policies. MS serves as a place to discuss the issues. FBGI acts as a control and internal benchmark tool of the policy development.

Table 1. Governance-related aspects of ABC's and their environment, applicable tools to address them, and main operating mechanisms. (Cont.) FBGI: Family business governance indicator, HM: *Hoshin* management, MS: Meeting system.

III. KEY IDEAS ON FAMILY BUSINESS GOVERNANCE. AN INDICATOR

"To measure is to know."

"If you can not measure it, you can not improve it."

Lord Kelvin

Table 2 shows fundamental themes of family business governance and its indicator. The table integrates main elements from IFC´s Family Business Governance Handbook IFC (2008), and from a questionnaire (Yacuzzi, 2007, 2008) that provides a quantitative evaluation of SME[1] governance.

Area	Themes
General principles of governance (70)	Explicit consideration of governance (10)
	Provision of information (30)
	CEO duality (30)
Family governance (330)	Family protocol (60)
	Family governance institutions (100)
	Family policies (50)
	Conflict of interests (30)
	Content of communication (20)
	Communication and meeting system (70)
Boards (230)	Advisory boards (15)
	Board of directors, general aspects (70)
	Board of directors' routine (40)
	Board of directors' ability and compromise (40)
	Board of directors' composition and behaviour (35)
	Board of directors' control and monitoring (15)
	Board of directors' advice and networking (15)
Senior management and succession (170)	Senior management (70)
	CEO and senior management succession (100)
Stakeholders (200)	Shareholders' position (80)
	Employees' position (20)
	Customers' position (25)
	Position of banking and non-banking creditors (10)
	Suppliers' position (25)
	Position of government (10)
	Position of society and the environment (30)

Table 2. Areas and themes of the family business governance concept and its indicator. For more information, please see the Appendix I. Numbers between brackets indicate the maximum number of points potentially assigned (Total = 1000 points). Maximum number of points was established by utility theory. Please see Appendix II.

[1] SME means Small and Medium-Sized Enterprise.

The complete set of areas, themes, dimensions and elements that give shape to the family business governance indicator are presented in the Appendix I. Appendix II provides a detailed explanation of how the maximum number of points for each area, theme, dimension, and element were calculated by means of utility theory.

Please notice that the maximum number of points is tentative and reflect the author´s utility functions, his governance-related preferences. The indicator is flexible: its structure, contents and values can be modified to show ABC´s management utility functions.

Governance principles are a list of a minimum set of prescriptions for action that emerge from the adopted governance design. Family governance is the indicator's key area, and closely follows IFC (2008). The same considerations apply to the area of senior management and succession. The stakeholders´ area is given much space among the elements that define family business governance and its measurement. Clarkson (1994)[1] characterizes the firm as a system of stakeholders operating within the larger system of the host society; the stakeholders provide the legal and market infrastructure for the firm's activities. The firm creates wealth or value for its stakeholders by converting their stakes into goods and services. Margaret Blair adheres to the position that considers firms as institutional arrangements regulating relationships among all the parts that contribute to wealth creation with specific assets.[2] The area of boards rests on studies such as Gabrielsson (2003), which present directors' work as value-creating tools that improve SME performance.

Although the proposed indicator is easy to use, it looks complex, due to its large number of elements. A simpler measurement instrument would be ideal, but it is not available today. The literature shows a great number of complex indicators used in management and finance theory. Following Lord Kelvin, a key idea behind these indicators is that 'things that matter must be measured; if they were not, things could not be improved´ and, even if improved, no one would realize it for sure. In short, National Quality Awards-type indicators define measurement criteria and suggest the need for a number of metrics, both financial and non-financial.

[1] In Clarke, (2004), p. 195.
[2] Blair (2004), p. 182.

IV. HOSHIN MANAGEMENT[1]

Hoshin management (or policy deployment) is a management style that coordinates an organization's activities to achieve key objectives, called '*hoshin*', and quickly react to environmental change. *Hoshin* management involves the whole company and integrates strategic management with daily management; to do this, *hoshin* management links top management *hoshin* with lower level *hoshin*, in a process of cascade deployment that goes all the way down to reach daily management.

Hoshin management is a systemic process. A partial application of its tools becomes suboptimal, as ends-means relationships are not properly managed. Due to its nature, which aims at integration of company activities, *hoshin* management can be considered as a framework for TQM, in which strategic activities are readily linked to operational activities; objectives are set at all levels; people are motivated; changes are planned; and results, controlled.

Hoshin is the Japanese word for magnetic compass; as a second meaning, it means policy, in a general sense. Each top-management objective, as well as lower objectives that are generated cascade-style, are called *hoshin*. *Hoshin* plans are detailed and mutually accepted by all members of an organization; they are developed and implemented with simple tools that lead the organization to its objectives while it learns in the process.

Let us look at a simple model of *hoshin* practice. Assume a firm with the following structure, similar to ABC's: (1) Board of directors, (2) CEO, (3) Directors, (4) Section chiefs, and (5) Employees, working individually or as a group. *Hoshin* management starts by adapting the corporate vision and (five year) long-term plans to changes in the economic and social environment. From that adaptation, (two year) medium-term plans and annual plans are devised for each one of five levels. The *hoshin* and the annual action plan for each director's office, section chief's office, and employee is obtained by deploying the CEO's *hoshin* and key action plans.

About two months prior to the start of the year, the CEO informs his managers about the *hoshin* he plans to apply and about key elements in the action plan. Directors receive those *hoshin* and key elements and, on that basis, prepare their own preliminary *hoshin* and action

[1] This section is based on Yacuzzi (2005 b).

plans, through negotiation with his subordinate section chiefs. Section chiefs, in turn, prepare preliminary *hoshin* and action plans that respond to the action plan of each director. Likewise, groups and individuals prepare their preliminary *hoshin* and action plans according to each section chief's guidelines.

Hoshin deployment involves frequent catchball activity. Catchball is a kind of negotiation founded on the analysis of objectives, schedule and resources of different areas that creates a high level of trust among participants. *Hoshin* (objectives) are realistic and emerge from catchball, which deals with means and ends and employs physical units (such as number of trucks or square meters) rather than monetary units. The consistent use of catchball and physical units are among the main differences *hoshin* management has with other planning methods such as management by objectives. Another difference is that (annual) *hoshin* plans are part of a long term plan, usually a five-year plan.

In general, *hoshin* planning covers a calendar year; over the first six months, top level management's *hoshin* are deployed through catchball toward lower levels. During the process, upper level managers explain to lower level employees the details of *hoshin* deployment. During the second half-year, a final agreement between levels, from bottom to top, is reached through catchball; the agreement implies commitment to the devised plans, thus closing the annual planning period.

During the *hoshin* and plans design process, ends-means relationships are thoroughly and explicitly discussed. At all levels, goals, metrics (preferably quantitative) and timetables are established. Quantitative goals inspire more confidence than simple qualitative goals. Tasks to achieve goals start and improvement activities are carried out.

Goals are the basis of control. Goals and their control method are established during the planning cycle, after defining *hoshin* and assigning resources to achieve them. This is an application of the continuous improvement cycle (Plan-Do-Check-Act, or PDCA) to the management process. Each member in the firm must have goals. Without goals, the PDCA cycle cannot be closed, as the checking step cannot be accomplished.

At the end of the planning period, *hoshin* and key action plans are informed to the company. From there on, the CEO interacts with managers and employees to inquire about their advances and difficulties to execute the plans. Formal control systems are not enough: personal interaction is constant.

The correlation between the above description of the *hoshin* management process and real cases has been documented in the literature. Moreover, I have had the opportunity to participate in the implementation of hoshin plans, during a period of four years, at a leading Japanese shipyard.

Let’s show an initial scheme of how hoshin planning would apply to ABC. The process is depicted in Figure 1. Possible CEO´s hoshin and preliminary action plans for ABC are shown as Figure 2 and Figure 3. Hoshin follow guidelines issued by the Board of Directors and are initially relatively vague, but they become more concrete as the process advances downstream and hoshin become preliminary action plans. Figure 4 shows a second instance of the hoshin deployment. It corresponds to the Action plans for the Administration and Finance´s Director. Column titles are self-explanatory.

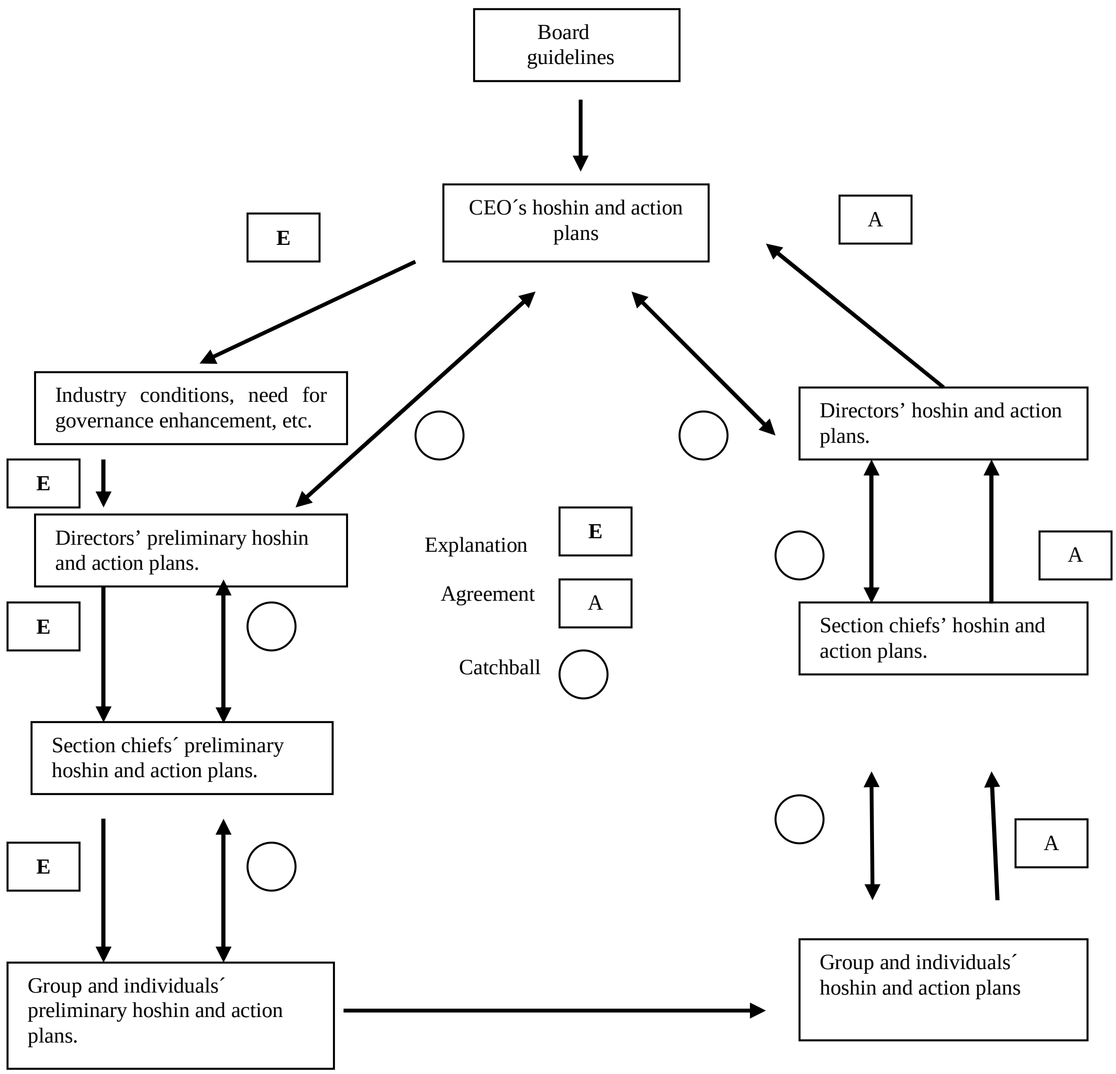

Figure 1. Hoshin and action planning process. Rectangles for directors, section chiefs, and groups and individuals represent a multiplicity of such entities.

Hoshin 1: Develop a sound meeting and communication system

ABC deserves to have a meeting system that channels the information exchange through a formal process of meetings and communication. This process would allow the provision of timely data to all interested parties.

Hoshin 2: Transform the board of directors

ABC's board is to be transformed in order to:

- To appoint non-executive, independent board members;
- To enhance monitoring activities;
- To develop a senior management succession plan.

Hoshin 3: Develop a strong change management effort

The enhancement of family business governance at ABC requires a systematic change management activity involving a great many senior managers, other managers, and key family members and the main family institutions.

Figure 2. Possible CEO's hoshin for ABC. The name of each hoshin is followed by a brief explanation or justification. There might be up to four or five hoshin in a year. Some of them might involve operative areas and functions such as operations, marketing or finance and administration.

Hoshin 1: Develop a sound meeting and communication system

1. Evaluate with all interested parties the current system and its problems.
2. Through a benchmarking activity and through a literature search, examine possible models for improvement. (For example, please see Yacuzzi and Naiberger (2009).)
3. Discuss these models with all interested parties and choose one for implementation.
4. Implement the chosen model.

Hoshin 2: Transform the board of directors

1. Establish initial conditions for change, through education on specific governance issues. ("Field preparation").
2. Select one of the most urgent (and not too conflicting) areas for transformation, such as board monitoring activities.
3. Decide improvement activities related to it and implement them.
4. Choose a second (perhaps more conflicting) area and replicate the procedure. Etc.
5. Evaluate the results and provide feedback.

Hoshin 3: Develop a strong chance management effort

1. Set up a change management committee with board and family members.
2. Evaluate with top managers the attitudes toward organizational change of key actors and detect possible forces for change.
3. Train key executives in change management.
4. Develop a change management plan concentrating on resistance to change and ways to overcome it using Organizational Development tools.
5. Implement the plan.

Figure 3. Possible CEO's action plans for ABC. The hoshin name from Figure 2 is repeated and preliminary action plans are described.

For all other levels and functions, the cascade deployment process is continued until all the organization´s levels and functions are covered. At the end of the downstream cascade, the approval cycle covers all levels from bottom to top, as shown on the right hand side in Figure 1.

Hoshin	Key elements	Concrete actions	Responsible person	Object-ive	Timetable											
					2013									2014		
					4	5	6	7	8	9	10	11	12	1	2	3
Evaluate with all interested parties the current system and its problems (From CEO´s action plans for hoshin 1, Figure 3)	1. Consultation with reporting areas.	1. Set up meetings with a clear agenda (meeting system and its problems).	HR manager	To be completed in one month.	x											
		2. Organize interarea consultations to enrich the findings.	HR manager	To be completed in two months.	x	x										
	2. Write a memory of findings and proposals for improvement of the meeting system.	1. Collect benchmark information as background to the memory.	HR manager	To be completed by month 3.	x	x	x									
		2. Write findings and preliminary proposals, to be discussed with other areas.			x	x	x									
Improve the board's monitoring activities (from CEO´s action plans for hoshin 2, Figure 3)	1. Monitoring of decisions on education, recruitment, career planning and other HR areas.	1. Apply adequate indicators.	HR manager	To be completed through months 4 to 6.				x	x	x						
		2. Provide feedback to interested parties.		To be completed through months 4 to 6.				x	x	x						
	2. Write appropriate procedures for monitoring activities.	1. Consultation with external experts.	HR manager	To be completed through months 4 to 6.				x	x	x						
								x	x	x						

Figure 4. Possible action plans for the Administration and Finance director.

V. A SYSTEM OF EFFECTIVE MEETINGS[1]

A third important tool for family business governance is a system of effective meetings. *Hoshin* management assumes the existence of such a system, through which planning activity is deployed and controlled. In this sense, the *hoshin* system and the meetings system are part of the same governance architecture. Likewise, the family business

[1] This section is based on Yacuzzi & Naiberger (2009).

governance indicator is integrated in the system, and used throughout the year in the context of meetings and *hoshin* plans, as a tool for learning, orientation and control.

A system of effective meetings is a hierarchical structure of regular meetings in an organization. For example, let us assume a firm integrated by the following levels (the structure is similar to ABC´s): (1) CEO, (2) Directors, (3) Section chiefs reporting to directors, (4) Employees (reporting to section chiefs).

Its meeting system would be a pyramid. The pyramid is an ideal structure that is used recursively. Information flows smoothly through it, from top to bottom and vice versa, at least twice a month. As soon as it is designed, the pyramid is an empty structure that is filled out with two elements: (1) Systematic search for important governance problems; and (2) Methods to solve them. During meetings we emphasize two things: (1) Team work and (2) A scientific approach to problem-solving, based on data and facts.

A meeting system includes the following elements: (1) Organization of the pyramid, which is dynamic and usually done by trial and error; (2) Objective determination, that is, what are the most important themes to be dealt with; (3) Determination of objective measurement criteria and problem solving methods; for a system to work, methods for analysis and problem resolution are required; (4) Clarification of manager and employee responsibilities regarding the meeting system.

A complete meeting system for ABC could include regular meetings such as those shown in Figure 5.[1]

[1] The frequency of these meetings, as well as their main agenda items, key participants, and other details such as responsibilities for the agenda and minutes, will vary; some meetings will be held every two weeks, others, twice a year. Information between brackets, although tentative, suggests possible frequencies for ABC´s meetings.)

Meeting	Possible frequency and observations
Meetings related to family governance and institutions	Every two weeks at first, then with less frequency.
Board meetings	At least, every two weeks.
Planning and control meeting for education and training	Once or twice a year.
Strategy meeting	Twice a year.
Meeting with key suppliers	Once a year. Could include preparation for supplier development.
Meeting with key clients	Twice a year, regularly, or when needed.
Functional meetings. (These functional meetings should closely interact with board meeting and provide feedback from one board meeting to the next).	Once a week.
Meeting of the change management committee	The committee could operate during the first months of the change effort; later, it could stop its functioning based on results.
Meeting of the board committees	Once a month.

Figure 5. Possible meetings for ABC.

VI. OTHER TOOLS AND THEIR INTEGRATION

The family business governance indicator can be considered to be a quality tool (after all, it is a kind of checklist). Likewise, the meeting system is a vehicle for teamwork, another quality tool. Quality tools are an integrated system. This implies, if the company so wished, the potential use of classic tools of quality management, such as the PDCA cycle, the seven classic tools, and the seven managerial tools. Classic tools interlink with newer and more general methods. For example, the PDCA cycle is an integral part of *hoshin* management, as we saw above. On the other hand, well-known TQM tools can be used in problem solving during the *hoshin* process, the meeting system, and the evaluation of governance through the family business governance indicator. The three main techniques presented in this article are themselves closely integrated, as shown in Table 3.

	FBGI	*Hoshin* management	Effective meeting system
FBGI	X	The FBGI provides guidelines to potential *hoshin* and serves to control implementation.	The FBGI is analyzed at meetings on a periodic basis and serves to design policies.
***Hoshin* management**	*Hoshin* (objectives) can become new items in the FBGI.	X	The *hoshin* plan is elaborated and controlled at meetings.
Effective meeting system	The effectiveness of the meeting system is analyzed with appropriate indicator items.	The meeting system is a source of ideas for the *hoshin* plan.	X

Table 3. How the FBGI, *hoshin* management, and the effective meeting system conform a system.

VII. A POSSIBLE APPLICATION OF THE TOOLS TO A CONCRETE GOVERNANCE ACTION AT ABC

How can we integrate our tools to enhance family business governance at ABC? One of the characteristics of the techniques is the freedom to mix them in various ways. Freedom applies to the order in which tools can be used, to the field of application, to the greater or lesser intensity in control activities, to the scope of trials, and so on. Each organization should decide how to use the tools, as a function of its purpose, its resources, the time of implementation, and other factors.

Nonetheless, there are universal guidelines. If we assume that the proposed tools are to be applied at ABC to family business governance, the starting point should be a governance-enhancing plan. The plan could be part of a more general long-term plan, of which the *hoshin* plan would be the first-year plan. There are various ways in which *hoshin* management could be applied to the enhancement of family business governance. This is not surprising, as a *hoshin* is an objective to be met and, as long as this objective is important, it is possible to introduce it in a *hoshin* plan.

For instance, ABC could activate the work of its board and include this activation as one of the company's annual *hoshin*, as I proposed in hoshin 1, Figures 2 and 3. Thus, 'all' areas would became aware of the value and importance of using board resources to the limit. I highlight the word ‘all’ as all areas and employees have the chance and obligation to use the opportunities of an active board. If board activation consists, say, in hiring an external director, all managers and employees will have access to the experience of this director in solving company problems in different contexts.

In addition, all personnel, one way or another, should have access to the new director to learn as much as possible from his experience. Access and interactions, moreover, should not be casual or random, but rather the result of a systematic plan to integrate the new board member with all levels in the organization. The plan would be in line with *hoshin* management ideas.

Problems in which the new director could operate are those associated with concrete governance actions, such as the following: Awards to management performance; actions to enhance company culture, values and mission, as well as leadership at all levels; implementation of an ethics code; and monitoring of managerial actions. These actions could be followed by applying the family business governance indicator in the context of a meeting system. Thus, from a concrete governance action, *hoshin* management would become operative, as well as its associated meeting system and its family business governance indicator, which would act as a signal of the direction set by the enterprise and as a vehicle of organizational learning and control.

VIII. THE ROLE OF CULTURE

The proposed tools have the hallmarks of Japan and frequently we hear references to the difficulty of applying them in other cultures, as they would be products of a unique social and cultural environment. I do believe, however, that the socio-cultural view is limited; it assumes that socio-cultural values are the explanatory variables while management methods are the dependent variables. In practice, however, socio-cultural values evolve and it would be inconsistent to assume that the reality of management is determined by culture alone. There might be some features in Japanese culture, such as discipline and groupism, which cannot easily be transported to other cultures, but the key to effective learning from the Japanese consists in adopting technological tools that transcend culture and history and can be applied in foreign cultures.

By consistently applying them, a new culture can be created through a large-scale company-wide effort. Systematic adoption of the governance tools proposed in this article implies what Shiba et al. (1993) call ‘a mass movement’, that is, a set of activities and change actions that reach everyone in the company.[1] For the mass movement to take place, the role of the CEO and middle managers in leading and implementing change is key, as any practical change theory would maintain.

IX. CONCLUSIONS

Good family business governance is the confluence of good concepts and good practices. Good concepts are provided, among others, by IFC (2008) in its handbook. I sincerely believe that the techniques presented in this article can serve as a solid framework for implementation and control of a family governance concept application at ABC.

In order to be successful, management tools, such as the ones here proposed, should be kept simple. If necessary, the techniques should be made easier to understand and should be shared by as many people as relevant at ABC. Shared knowledge acts as a powerful glue that leads the organization to success through better motivation, coordination, and transparency.

Much effort is devoted in this article to governance measurement through a quantitative approach that resembles in its structure the National Quality Awards, with dozens of items. The proposed indicator is flexible and can accommodate different preferences and, equally important, new developments in the governance and management fields, such as sustainability, a topic displaying a strong impulse today.

At this point, please let me quote Lord Kelvin once again:

> *“I often say that when you can measure what you are speaking about, and express it in numbers, you know something about it; but when you cannot measure it, when you cannot express it in numbers, your knowledge is of a meagre and unsatisfactory kind; it may be the beginning of knowledge, but you have scarcely in your thoughts advanced to the state of Science, whatever the matter may be."*

Needless to say, most improvement efforts must include both quantitative and qualitative tools, such as those from Organizational Development. Finally, the hoshin and meeting systems, as long as they are kept simple, provide an excellent field in which the

[1] Shiba et al. (1993), p. 307.

organization can arrange its human, physical, and information resources for governance improvement and control.

APPENDIX I

THE STRUCTURE OF THE FAMILY BUSINESS GOVERNANCE INDICATOR

Indicator´s dimensions and elements. Numbers show the maximum score allowed for each area, theme, dimension and element. Appendix II shows how each score was calculated. This structure could become a questionnaire for measurement.

Area	Themes	Dimensions	Elements
General principles of governance (70)	Explicit consideration of governance (10)	Documental (5)	Explicit document on the importance of governance 2
			Section on governance in the annual memory 3
		Organizational (5)	Adoption of a code of good practices 3
			Appointment of a person to follow-up governance measures 2
	Information provision (30)	Transparency criteria (20)	Actualization of accounting criteria 10
			Information on future performance objectives 10
		Organizational (10)	Appointment of a person responsible for information provision 5
			Existence of a mechanism to answer inquires from stakeholders 5
	CEO duality (30)	CEO duality (30)	Whether the CEO is a permanent director 15 Whether the CEO is concurrently chairman of the board 15

Family governance (330)	Content of communication (20)	Communication of values, etc. (7)	Whether values, mission and long term vision are communicated to all family members. 7
		Communication of accomplishment, challenges, strategies (6)	Whether family members, especially those who are not involved in the business, are kept informed about major business accomplishments, challenges, and strategic directions. 6
		Communication of rules and decisions (7)	Whether the rules and decisions that might affect family member´s employment, dividends, and other benefits they usually get from the business are communicated. 7
	Communication and meeting system (70)	Communication system (15)	Whether formal communication channels that allow family members to share their ideas, aspirations and issues exist. 15
		Regular meeting system (40)	Whether the family comes together regularly and makes any necessary decisions. 40
		Fair communications (15)	All family members have the same access to family business information, regardless they work at the family business or not. 15
	Family protocol (60)	General aspects (60)	There exists a family constitution, or family creed, or family protocol, or family strategic plan, or statement of family principles, or family rules and values, or family rules and regulations. 60
	Family policies (50)	Family member employment policies (30)	There exist clear and written employment policies that establish suitability for the job and other terms and conditions of family employment within the firm. 10
			Whether the written employment policies are fair in covering the treatment of family member employment as well as the employment of non-family employees. 10
			Whether the written employment policies are made available to all family members to clarify expectations. 10
		Family member shareholding policies (20)	There exist clear shareholding policies that set the right expectations among family members regarding shares´ ownership rights (for example, whether in-laws are allowed to own share or not). 5
			Whether an existing set of policies define the mechanisms that allow family members to sell their shares. 10
			Whether there exist a Shares Redemption Fund or a similar institution in order to buy back any shares that family members would like to liquidate. 5

Area	Themes	Dimensions	Elements
Family governance (Cont.) (330)	Conflict of interests (30)	Conflict of interests among different kinds of family shareholders (30)	Whether there exist conflicts of interests between family members who work at the firm and those who do not. 30
	Family governance institutions (100)	Existence of institutions (40)	There exists one or several family governance institutions, such as the family assembly, the family council, or the family office and other various committees (education, shares redemption, career planning, family reunion and recreational committee), that help strengthen the family harmony and relationships with its business. 40
		Information to family members (30)	Whether family members are well informed about the purpose and activities of established family governance institutions. 15
			Whether family members distinguish between the role of family governance institutions and the governing bodies of the business, such as de board of directors and senior management. 15
		Written procedures (30)	Whether there exist written procedures for family governance institutions and they are shared with all family members. 30
Boards (230)	Advisory boards (15)	Consideration of advisory boards (15)	Regardless of whether there exists an advisory board or not, the organization has evaluated the advantages and disadvantages of advisory boards. 15
	Board of directors, general aspects (70)	Resources (10)	Directors have sufficient resources to oversee management and other family members. 10
		Independent directors (50)	There exists in the board one or more independent directors (free of links to management, the family and others that could influence his/her judgement. 25
			Whether the chairman of the board is an independent director. 25
		Directors' representativeness (10)	The CEO or his/her family occupy positions on the board. 5
			Whether the CEO and the chairman of the board belong to the same family or group of control. 5
	Board of directors' routine (40)	Meetings (10)	Meeting frequency. 3
			Presence of top management at meetings. 4
			Existence of fix rules for meeting call, agenda distribution, preparations, etc. 3
		Division of labor (10)	Division of labour among directors. 3
			Directors act as guides to strategy and decisions, but do not perform day-to-day management activities, which are reserved to management. 4
			Division of labour between the board and the CEO. 3
		Evaluation and follow-up (20)	Existence of rules on evaluation and follow-up of the board´s decisions. 7
			Existence of annual evaluation of the board´s work. 7
			Existence of evaluations of the board´s work after each meeting. 6
	Board of directors' ability and compromise (40)	Knowledge (10)	Ability in areas of knowledge relevant to the firm. 4
			Familiarity with industry conditions. 3
			Familiarity with firm operations.3
		Compromise (20)	Preparation for board meetings on the part of directors. 10
			Compromise during board meetings. 10
		Information (10)	The board searches for strategic information by itself, in addition to that received from top management. 5
			The board makes acute questions to top management on their proposals. 5
	Board of director´s composition and behaviour (35)	Conflicts of interest (15)	Cases of conflicts of interest in a transaction that involves directors. 15
		Disciplinary measures (10)	Disciplinary measures against the board or the management in the last three years. 5
			Disciplinary measures against directors for violating their fiduciary duties in the last three years. 5

Area	Themes	Dimensions	Elements
Boards (Cont.) (230)	Board of director´s composition and behaviour (Cont.) (35)	Management evaluation (10)	Managers´ salary is linked to their performance. 5
			Existence of a board´s agenda on the evaluation of the management. 5
	Board of directors' control and monitoring (15)	Initiative (5)	Initiation of decisions on markets, customers, employees, products, technologies, budgets, etc. 5
		Ratification of decisions (3)	Ratification of decisions taken by managers on markets, customers, employees, products, technologies, budgets, etc. 3
		Support (4)	Support to managers for implementing decisions on markets, customers, employees, products, technologies, budgets, etc. 4
		Monitoring (3)	Monitoring of decisions on markets, customers, employees, products, technologies, budgets, etc. 3
	Board of directors' advice and networking (15)	Advice (10)	Advice on issues related to administration, legal, economic, financial, technical, marketing aspects, etc. 10
		Lobby and corporate image (5)	Influence on important parts of the environment to reduce uncertainty. 3
			Influence on important parts of the environment to support the firm and enhance its image. 2

Senior management and succession (170)	Senior management (70)	Professionalization (40)	Senior management positions are occupied by experienced and qualified professional managers, regardless whether they are family members or not. 8
			The organization has designed a formal structure and clearly defined the roles and responsibilities of all senior managers, present and future. 8
			The organization strives to have the best available people running the organization, be them family or non-family. 8
			The organization has evaluated the skills and qualifications of all senior managers. 8
			The organization has replaced or hired senior managers, as a comparison between needs and realities indicated. 8
		Strategic issues (30)	Decision making and approval powers at all levels are well defined. These powers are linked to the roles and responsibilities of managers and no to their ties to the family. 8
			The company develops an internal training program that allows skilled employees to be prepared for taking on senior jobs in the future. 8
			Establishing a remuneration system that provides the right incentives to managers based on performance and responsibility and not on their ties to the family. 7
			Senior managers use business resources strategically and clearly separates business and family assets and set plans and budgets. 7
	CEO and senior management succession (100)	Awareness of its importance (20)	The family firm is aware that CEO and senior management succession is a key issue for all kind of companies, family and non-family. 20
		Sound succession plan (50)	Whether the family strives to set a sound formal succession plan for the family firm´s CEO and senior managers. 13
			Whether the selection process of the next CEO starts as early as when the current CEO is appointed. 13
			Whether the family gets advice from the CEO, the board members, the family council or other sources to help the succession process. 12
			Whether a consensus is reached about the future CEO among key stakeholders including the board of directors, and senior management, family or non-family. 12

Area	Theme	Dimension	Elements
Senior management and succession (Cont.) (100)	CEO and senior management succession (Cont.) (100)	Career development and transition (30)	Whether there exists a career development system for the best possible candidate that prepares him or her through education, training and periodic feedback on performance. 15
			Whether a clear transition process for both the current CEO and the successor is developed. 15

Stakeholders (200)	Shareholders' position (80)	Search for economic benefit (20)	Search for value creation. 7
			Search of benefit for the shareholder. 7
			Search for future income. 6
		Information transparency to shareholders (30)	Information that goes beyond that required by law. 10
			Scope of accounting and other information. 10
			Reports requested by minority shareholders. 10
		Lack of complaints (15)	Lack of complaints from shareholders not in the board. 15
		Control rights (15)	Minority shareholders take part in setting agenda. 8
			Veto rights of minority shareholders. 7
	Employees´ position (20)	Salary (4)	Frequency of salary discussion at the board. 2
			Average difference, in percentage, between company´s salary and industry´s salary. 2
		Job security (4)	Rate of new job creation. 2
			Turnover rate. 2
		Working conditions (5)	Indicators of safety and occupational health. 1
			Working hours. 1
			Benefits. 1
			Cafeteria at the plant. 1
			Recreation area at the plant. 1
		Training (3)	Average number of job-related training hours per year per employee. 2
			Average number of job-unrelated training hours per year per employee. 1
		Information (2)	Existence of information channels for exclusive use of employees: newsboards, newsletters, etc. 1
			Utilization of information channels: yearly number of informative actions of prioritary or exclusive interest to employees. 1
		Feedback (2)	Existence of systems for transmission of employee complaints and opinions. 1
			Degree of utilization of complaints and opinion system. 1
	Customers´ position (25)	Quality (8)	Product and service quality. 4
			Guarantee policy and after sales service try to achieve customer´s royalty. 4
		Price (6)	Least possible price. 3
			Truthful publicity. 3
		Information (6)	Complete information on products and services. 3
			Existence of complaints. 3
		Feedback (5)	Existence of complaints. 1
			Existence of lawsuits against the firm. 2
			Existence of a system for handling claims. 1
			Existence of a system to know customer opinion. 1
	Position of banking and non-banking creditors (10)	Economic competence (3)	Annual gross sales. 3
		Cash flow management (2)	Application of modern techniques. 2
		Financial and other information (3)	Broad, updated, transparent. 1
			Available on Internet. 1
			Possibility for creditors to participate as observers at meetings. 1
		Complaints and law suits (2)	Existence of lawsuits from creditors against the firm. 1
			Existence of complaints from creditors against the firm. 1

Area	Theme	Dimension	Element
Stakeholders (cont.) (200)	Suppliers´ position (25)	Contractual conditions (10)	Payment according to contract terms. 5
			Search for a long-term relationship. 5
		Supplier development (8)	Supplier development programs. 4
			Training of suppliers to improve quality. 4
		Complaints and lawsuits (7)	Existence of lawsuits from creditors against the firm. 4
			Existence of complaints from creditors against the firm. 3
	Position of government (10)	Job creation (2)	Existence of an explicit policy of job creation. 2
		Facilitating government action (6)	Adequate supply of information requested by government organs. 3
			Facilitation through publicity campaigns of government actions aimed towards general welfare (for example, towards heath care). 3
		Enhancing industry transparency (2)	Supply of relevant information to strengthen free competition in industry. 2
	Position of society and the environment (30)	Facility and operational safety (10)	Resource investment to strengthen facility and operational safety. 4
			Collaboration with insurance companies and industry chambers to improve safety and occupational health. 3
			Consultation with experts on industrial safety and its social impact. 3
		Information (6)	Provision of information to authorities on health and safety. 3
			Provision of information to the public on topics of general interest. 3
		Environment (7)	Savings in natural resources and sustainability. 4
			Campaigns to avoid damaging the environment. 3
		Initiatives of corporate social responsibility (7)	Diffusion of social policies to protect the environment. 3
			Existence of a policy of corporate social responsibility. 2
			Concrete actions of corporate social responsibility. 2

To a great extent, the methodological aspects of the Appendix I follow Yacuzzi (2007, 2008).

APPENDIX II

CALCULATION OF THE SCORES FOR THE INDICATOR´S STRUCTURE

In this appendix the method used for maximum score calculation of the indicator´s structure is explained. So far, the questionnaire has not been written, but the procedure can equivalently be applied to the tables in Appendix I. The appendix starts with considerations on measurement in the social sciences, where a large number of variables is usually necessary. Next, scores for each item are determined using utility theory.

A.I. MEASUREMENT IN THE SOCIAL SCIENCES[1]

Some variables, such as temperature and area, can be objectively and precisely measured. In management research, however, there are hundreds of variables, such as compromise or leadership, which are subjective and difficult to measure. How do we handle such abstract concepts and measure them? We analyze abstract concepts along their dimensions and elements, in what is called "operationalization".

Operationalization of variables

Variable operationalization, which leads to the measurement of abstract concepts, is achieved by looking at the concept incorporated in each variable from its different dimensions and elements—observable and measurable. Let us examine, for example, the operationalization of the concept "position of the employees in the firm."[2] This concept is part of our indicator and tries to measure the degree of consideration than the position of employees ocuppy in the mind of a director. We consider that directors concerned about their employees will share the following general dimensions:

(1) **Salary.** They will be concerned about their employees´ salary level.

(2) **Job security.** They will think about providing job security to current employees through time.

[1] Yacuzzi (2007) is followed in this section.
[2] Sekaran (1992) is followed in this section.

(3) **Working conditions.** They will be concerned about offering working conditions that are attractive and, at least, comparable to those offered by other industry competitors. Obviously, they will consider safety and occupational health.

(4) **Training.** They will allocate important resources to train employees.

(5) **Information.** They will keep their employees informed about company-related themes of potential interest to them.

(6) ***Feedback.*** They will promote the creation and maintenance of systems that collect personnel opinions and complaints.

Governance dimensions at family business

Dimensions (1) through (6) above describe the agenda of a director concerned about her employees as stakeholders. They explain the meaning of "employee position" to the eyes of a director, but measuring them requires further examination. One way to examine a dimension is to divide it in its constitutive elements. Constitutive elements are aspects in which dimensions show up as human behaviour or administrative facts and can be measured more easily than dimensions. For example, if we take the *salary* dimension, directors' concern about salary is an abstraction, while one of its possible constitutive elements, "the number of times per year salary level is considered at board meetings", is an easily measurable element. Other elements that might be part of the salary dimension include a percentage comparison between average salary paid at a firm for a given position and the average salary paid at the industry level for the same position. And so on.

Dimensions can be measured by means of a questionnaire with appropriate scales. The questionnaire, not written as yet, would be based on Appendix I and would be similar to that in Yacuzzi (2008). For instance, a question about the salary dimension might be: "Please indicate the degree of validity for your firm of the following statement, using the scale provided: 'Salary level is a major concern of top management in our company.'" And the question would be answered by choosing a value from a five-point scale, ranging from "Absolute disagreement" to "Absolute agreement". The same reasoning applies to items in the structure of Appendix I.

Appendix I presented a list of items for our family governance indicator. Its columns are: areas, themes, dimensions, and elements. The table contents could be deployed with great detail in the future questionnaire, on the basis of which governance scores would be calculated.[1] Generally speaking, each question corresponds to one element, although there might be some exceptions. Notice that the dimensions of the concept of family business governance cover five areas: General principles of governance, family governance, boards, senior management and succession, and stakeholders. Appendix I can be analyzed by variable operationalization. The relevance of all its areas cannot be overlooked.

A.II. DETERMINING THE SCORES FOR EACH ITEM

Let us analize in greater depth item scores. Even if every element were perfect and free from measurement errors (impossible features), and even if all important dimensions and elements were included, and irrelevant ones excluded, we still would have to deal with the hard problem of assigning importance to each item and to the sections in which items cluster. In other words, in designing a measurement instrument, proper weight must be given to score graduation.

In this work we calibrate maximum scores in each section by using a preference function with multiple attributes. This method, even though it does not completely eliminate arbitrary scoring decisions, is based on systematic questioning to decision makers and governance experts about their preferences. The objective of the indicator could be, in the last instance, to establish a hierarchical order among firms, according to the quality of their governance. The order would be established on the basis of scores assigned to each firm.

Let us consider the major areas that define the concept of governance. We must determine the weight of each area and, to that end, a preference function is built. At this stage we aim at finding weights for each of the five areas; analogously, we will find weights for themes, dimensions, and elements in Appendix I.

Maximum scores assigned to each area will depend linearly on the values assigned in a preference function. This function will finally establish the hierarchical ordering of firms on

[1] The indicator´s structure is fundamentally based on the following sources: IFC (2008), CEF (ca. 2005), Gabrielsson (2003), Blair (2004) and Clarke (2004 b).

the basis of their governance quality. The basic procedure to determine this preference function is described, and then we apply it to the assignment of scores to our structure.[1]

Step 1. Preference function determination

Preference function P is assumed additive, with the form:

$$P(v_1, v_2, v_3, v_4, v_5) = w_1v_1 + w_2v_2 + w_3v_3 + w_4v_4 + w_5v_5 \qquad \text{(Equation 1)}$$

where P is preference, the v_i are the values that the governance expert assigns to the areas of the questionnaire, and the w_i, weights for each area. Weights and value functions are scaled in such a way that

$$\sum w_i = 1, \ \ 0 \le w_i \le 1 \quad \text{and}$$
$$v_i(best\ level) = 1$$
$$v_i(worst\ level) = 0, \text{ for i = 1 to 5, where i is the area.}$$

A frequent doubt is related to the legitimacy of this additive model. We believe that it is sufficient to check the *difference independence* condition for each area. This condition establishes that the magnitude of the difference in the intensity of the preference between two levels in area i does not change when fixed levels in other areas change. Let us assume, for instance, that a decision maker is given two values, v_1 = 0.1 and v_1 = 0.7, where values 0.1 and 0.7 are taken from a 0-1 scale that measures the value assigned to the strength of the area "principles of governance" in a firm; 0.7 is higher than 0.1. The decision maker is asked to answer if the intensity of her preference to go from 0.1 to 0.7 is influenced by the fixed levels at other areas. (In other words, she is asked whether she would be conditioned, in choosing a firm with better governance principles, by the levels of areas "family governance", "boards", "senior management and succession" and "stakeholders".) If the levels of other areas do not affect the first area considered, then this area is considered *difference independent* from the rest.

If the area does not pass the test, we can choose a model that takes into account interactions among areas, or else areas can be redefined so that *difference independence* is

[1] The procedure follows in general that described by Buffa and Sarin (1987), with minor changes in the way to calculate unidimensional values.

achieved. In our work, we follow the criteria of just one expert (the author), and the rationale to justify *difference independence* follows.[1]

"In the first place, let´s look at the relationship between the areas "principles of governance" and "stakeholders": a firm with good governance must have solid principles of governance, regardless whether it adopts an attitude favorable to its shareholders, employees, creditors, etc. In the second place, let us examine the relationship between the areas "principles of governance" and "boards": the boards could function properly, regardless of the existence of (explicit) solid principles of governance. In the third place, let us consider the relationship between the area "stakeholders" and "boards": a board could function properly, be involved with its work and follow a reasonable routine of control and networking, regardless of how the firm, by its philosophy of governance, considers the position of stakeholders. And so on with the remaining areas.

Even though this reasoning is preliminary and could be confirmed by better qualitative and quantitative analysis, Buffa and Sarin (1987, p. 702) maintain that additive preference functions are quite robust and, in most situations, will produce small errors, even when there is a moderate interaction among areas.

Step 2. Construction of unidimensional value functions

An important problem is that of assigning values to governance areas, themes, dimensions, and elements. In what follows, we introduce a method to evaluate the value function v_i belonging to area i. Similar reasoning would allow us to study value functions for themes, dimensions, and elements of the concept. It is common to establish a 0-1 scale, where 0 indicates the worst level, and 1, the best level. These values emerge from utility functions that will depend on each decision maker or, in the case of a general use indicator, on the consensus of the comunity of family governance experts at a given moment and place. For this work, we propose the utility functions shown in Figures 6, 7, and 8.

The utility function of "general principles of governance", shown as table and graph in Figure 6, was built so as to reflect the decision maker´s way of thinking. For the lower degrees of principle consolidation, the utility (or value) increases linearly, at a rate that is higher than that for upper degrees; for upper degrees, the growth rate flattens. This implies

[1] Future versions of this indicator should include opinions of a qualified group of governance experts. See Yacuzzi (2007, section V.2 Appendix V).

that (relatively speaking) the decision maker values more small efforts towards family business governance than more advanced enhancements. The meaning of different degrees is shown in Table 4. This table is important, since it provides some objectivity to the search for a preference function.

Degree of principle consolidation	Degree, in number	Assigned value
Null	0	0
In development	1	0.4
Partial	2	0.7
Total	3	0.9
Level of excellence	4	1

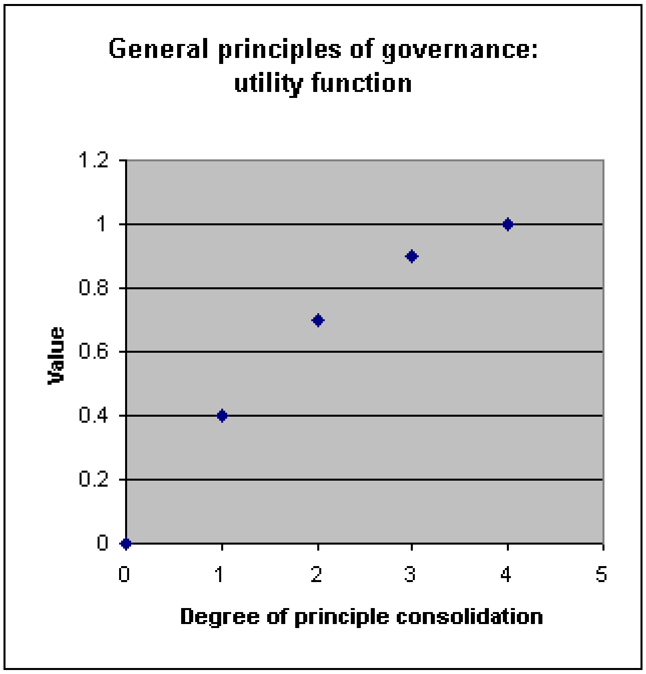

Figure 6. General principles of governance: utility function.

Degree	Meaning
Null consolidation	Governance principles are either unknown or not mentioned at the firm. There are no references to them in director´s or manager´s daily discourse; at the most, there are isolated references.
Consolidation in process of development	The topic of governance principles starts to be developed, with some systematic order. For example, ad-hoc documents are issued, or some people are trainned in governance themes, or responsible persons are assigned to governance themes, or the organization works on a code of good practices. Issues such as the management of information is given explicit attention.
Partial consolidation	There are evidences of a significative degree of implementation in all themes and dimensions of the governance concept. For example, a code of good practices has been enforced, and an accounting expert has been contracted to update the delivery of information to markets.
Total consolidation	The company displays knowledge and application of solid governance principles at all levels. Internal and external documentation related to governance is up-to-date and available; transparency prevails in accounting and operational areas.
Excellence level	The company has not only totally consolidated its governance principles, but it also exhibits its achievements to the industrial community, thus becoming a nacional and international model. In order to maintain governance principles, methods similar to those of continuous improvement in quality management are applied.

Table 4. General principles of governance: Meaning of its degrees of consolidation.

Figure 7 shows the utility function for the stakeholders area. It is a linear function, that so reflects a "democratic" perspective concerning the importance of stakeholders: all stakeholders are important, and the scores add value whether they are assigned when considering shareholders or any other stakeholder. The meaning of the degree of consideration of stakeholders is presented in Table 5.

Degree (Scope) of considered stakeholders	Degree, in number	Assigned value
Null	0	0
Mínimum	1	0.25
Medium	2	0.5
Large	3	0.75
Maximum	4	1

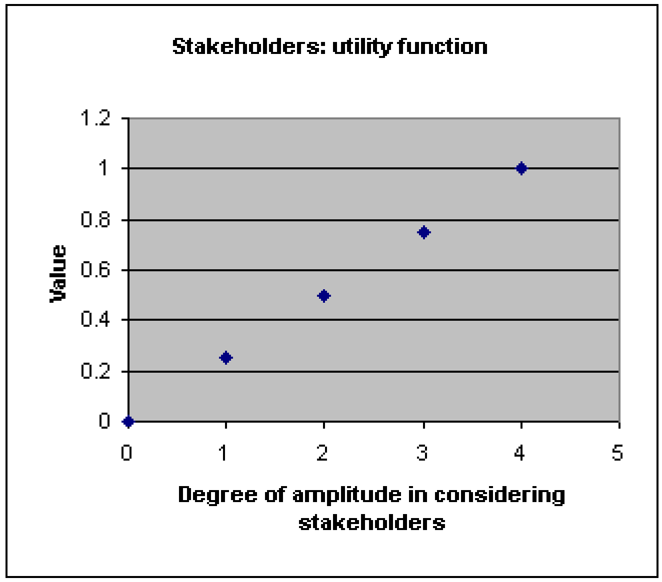

Figure 7. Utility function for the stakeholders area.

Degree	Meaning
Null amplitude	Concern for shareholders holds absolute priority. In spite of that, there is little or null information transparency, and little or null opportunities for dissatisfied shareholders to manifest themselves or enforce their rights in the context of the firm.
Minimum amplitude	Concern for the shareholder holds priority, but other stakeholders, such as customers or suppliers, are considered as well. Aside from the shareholder, stakeholders only get partial attention: for example, employee training is properly performed, but salary considerations or quality of working life are ignored.
Medium amplitude	Several stakeholders receive attention from top management, including shareholders, employees, customers and suppliers. In addition, for each stakeholder, one or more dimensions are considered.
Large amplitude	At least five out of seven stakeholders are closely attended to. Attention, in this context, means that, for each stakeholder, at least two or three dimensions are properly taken care of, and, in each dimension, a plurality of elements is considered.
Maximum amplitude	All stakeholders are considered in all dimensions. For each dimension, all elements receive at least some degree of consideration. At all levels in the firm there exists a "culture of stakeholders".

Table 5. Meaning of the degrees of amplitude in the consideration of stakeholders.

Finally, Figure 8 exhibits the utility function for the boards´ work. The first points are not too highly valued: after all, there are certain routines that all boards, no matter how shallow its work, must adhere to. However, values growth with greater slope when the percentage increases, in order to highlight the importance of a board that performs tasks that go beyond the minimum practice. Table 6 shows the meaning of the degree of effectiveness of the boards' work.

Degree of effectiveness of the board's work	Degree, in number	Assigned value
Null	0	0
Minimum	1	0.1
Medium	2	0.25
Large	3	0.6
Maximum	4	1

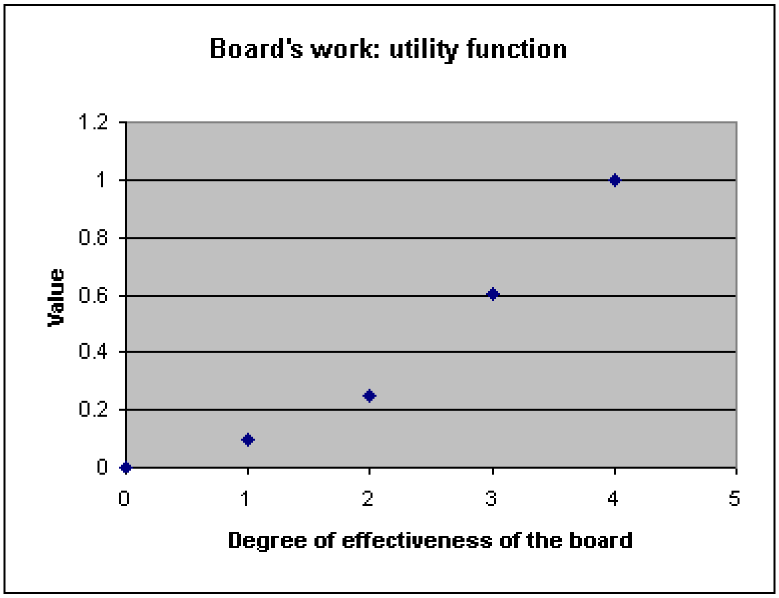

Figure 8. Utility function for the board´s work.

Figures 6, 7, and 8, show then three different functional forms, corresponding to the criteria of a decision maker or governance expert. For the remaining two areas, "senior management and succession" and "family governance", the figure and table for "boards" will be used. On the basis of these utility functions, the expert can build tables and assign values. Other decision makers might have other criteria, and these could become explicit in other different utility functions.

Degree	Meaning
Null effectiveness	The board has no work routine. Directors do not even have a clear consciousness about their role. They do no meet beyond what the law establishes and they present an insignificant level of ability and compromise with the organization. The board does not evaluate management and, even if there are no conflicts of interest, the board´s behaviour is negative or null. Directors do not perform tasks of control, monitoring, or networking, nor do they provide advice to managers.
Minimum effectivenes	The board understands the importance of its role, but this understanding does not translate into innovative action or control behaviour, due to a limited level of ability and compromise from directors. Just two or three themes of the board´s work are treated, albeit insufficiently, in one or two dimensions each.
Medium effectiveness	The board is reasonably competent and is involved in all dimensions of the "ability and competent" theme. In addition, it takes forward a regular routine, and duly exercises monitoring and control activities. The board develops advising and networking tasks, but unsystematically.
Large effectiveness	All themes related to the board´s work are considered: routine, ability and compromise, composition and behaviour of the board, control and monitoring, and advice and networking. In addition, at least three dimensions are covered for each theme.
Maximum effectiveness	All themes and all dimensions are properly considered. A culture of continuous improvement is alive, applied to the board´s work. There are even written procedures to evaluate the board´s effectiveness.

Table 6. Meaning of the degrees of effectiveness in the board´s work.

Step 3. Determination of important weights for each area (w_i)

The most important area is identified first. This is an arbitrary decision, although it reflects a philosophical position towards family business governance; if necessary, the effect of this choice can be evaluated through sensitivity analysis. Let "family governance" be our area of greatest importance. In order to evaluate weights we ask the following question: "Consider firm A, with the worst level in its "principles of governance", $v_1 = 0$, and the best level in "family governance", $v_2 = 1$. Consider now another firm, B, with $v_1 = 1$, the best level for its "principles of governance". What should be level v_2 for this firm B so that you would be indifferent (as an external expert that evaluates this firm´s governance) between choosing A or B?

Assume that the answer is $v_2 = 0.8$[1], i.e., decision maker at firm B is willing to trade-off part of family governance consideration in order to have perfect principles of governance. By using equation 1 this situation is presented as:

[1] This means that $v_2 = 0.8$ emerges objectively from the utility function and the description of degrees in Figure 8 and Table 6. Taking intermediate values is legitimate.

w_1v_1 (worst level of principles) + w_2v_2 (best level of family governance)=

= w_1v_1 (best level of principles) + w_2 x 0.8

$w_1 \times 0 + w_2 \times 1 = w_1 \times 1 + w_2 \times 0.8$

Rearranging this expression, we have:

$0.2\, w_2 = w_1$ Equation 2

Next we pose analogous questions for the remaining areas. “Consider firm A, that has the worst level in its boards´ work, $v_3 = 0$, and the best level in “family governance”, $v_2 = 1$. Consider now another firm, B, with $v_3 = 1$, the best level in its boards´ work. What should level v_2 be for this firm B so that you were indifferent (as an external expert that evaluates this firm´s governance) between choosing A or B?” If your answer to this question were $v_2 = 0.3$ then:

w_3v_3 (worst level in board´s work) + w_2v_2 (best level in family governance)

= w_3v_3 (best level in board´s work) + w_2 x 0.3

$w_3 \times 0 + w_2 \times 1 = w_3 \times 1 + w_2 \times 0.3$

Rearranging this expression, we get:

$0.7\, w_2 = w_3$ Equation 3

Analogously, for the areas “senior management and succession” (area 4) and “stakeholders” (area 5) , we get:

$0.5\, w_2 = w_4$ Equation 4

and

$0.6\, w_2 = w_5$ Equation 5

The sum of weights must equal unity, i.e.:

$w_1 + w_2 + w_3 + w_4 + w_5 = 1$ Equation 6

Therefore, with equations 2, 3, 4, 5, and 6:

$0.2\, w_2 + w_2 + 0.7\, w_2 + 0.5\, w_2 + 0.6\, w_2 = 1$

$3\, w_2 = 1$

$w_2 = 0.33$,

and, as a consequence:

$w_1 = 0.07$; $w_3 = 0.23$; $w_4 = 0.17$; $w_5 = 0.20$.

And we take these five estimates as our importance weights w_i, i = 1 through 5.

Step 4. Global values calculation

Equation 1 allows us to calculate our preference for a given firm as a function of its governance quality. We will have, for instance:

$$P(v_1, v_2, v_3, v_4, v_5) = w_1v_1 + w_2v_2 + w_3v_3 + w_4v_4 + w_5v_5 =$$

$$= 0.07 \times 0.75 + 0.33 \times 0.70 + 0.23 \times 0.45 + 0.17 \times 0.75 + 0.20 \times 0.8 = 0.6745$$

This value is multiplied by 1000 in order to generate an indicator that covers the range from 0 point through 1000 points. This operation is a simple arithmetic step that does not affect comparisons made with the governance indicator.

Step 5. Sensitivity analysis

The previous line of reasoning might be affected by subjectivity. Subjectivity covers both the selection of weights for each area and the assignment of its values. In order to increment confidence in the indicator´s performance, sensitivity analysis could be performed. A possible way to conduct this analysis is the following:

- take a set of firms and evaluate its governance with the developed indicator, with the base values;
- establish a ranking for these firms on the basis of the results obtained with the indicator;
- obtain other (or others) indicator (or indicators) by changing values (utility functions) and weights in steps 1 through 4 above;
- establish a new ranking of firms with the new indicator;
- compare results. If they agree, our level of confidence in the indicator will increase; otherwise, it would be convenient to make a more profound study of the philosophy of governance and look for more information, in order to find a more consistent indicator.

Sensitivity to the utility function used could also be measured. Yacuzzi (2007, Appendix V, shows this case). A further way to conduct sensitivity analysis is to compare the weights that different decision makers or experts assign to different governance areas, by following steps 1 through 4 above. If weights are approximately equivalent, our confidence in the indicator will increase. Important differences would reflect different understandings of governance, as shown in Yacuzzi (2007, Appendix V, second section).

A.III. APPLICATION TO THE COMPLETE STRUCTURE

In the previous section we have shown how weights can be systematically assigned to the five areas of governance. Something similar can be done to assign weights to different themes in each area; to different dimensions in each theme; and, finally, to different elements in each dimension (although in this work we follow a different way to assign weights to the elements).

Likewise, weights for themes and dimensions were calculated: please see Appendix I, where the results are reflected (multiplied by 1000, as explained below). The following criterion is adopted for the elements: If a dimension is made from just one element, then, the weight of the element is equal to the weight of the dimension; if the dimension is made from n elements, the weight of each element is (1/n) times the weight of the dimension. We could have calculated each element´s weight by using a preference function as we did with areas, themes, and dimensions but, for practical reasons, we chose the laplacian criterion that gives equal weight to each element in a given dimension.

We are ready to assign points to each element. Following the National Quality Award scoring standard, we assign a total number of points in the range from 0 point to 1000 points. Given the weights of the governance areas, points are assigned as follows:

- General principles of governance: w_1 * maximum score to be assigned = 0.07 * 1000 = 70 points.
- Family governance: w_2 * maximum score to be assigned = 0.33 * 1000 = 330 points.
- Boards: w_3 * maximum score to be assigned = 0.23 * 1000 = 230 points.
- Senior management and succession: w_4 * maximum score to be assigned = 0.17* 1000 = 170 points.
- Shareholders: w_5 * maximum score to be assigned = 0.2 * 1000 = 200 points.

In a similar way points are assigned to themes in each area. Calculations are not shown, but their results are included in Appendix I, in each cell and between brackets. Notice, finally, that in this work the concept of utility function is used in two related but different contexts: on the one hand, it is used to assign values (utilities) to the degrees of consolidation, amplitude, or effectiveness of diverse areas, themes and dimensions (see, for example, Figures 6, 7, and 8); this use allows assigning points to the indicator´s areas, themes and dimensions; on the other hand, the concept will be used in the future questionnaire to assign points to different possible answers in a multiple choice setting (Yacuzzi, 2008).[1]

[1] Reflections on measurement and considerations on the indicator as a roadmap to good governance can be read in Yacuzzi (2008).

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