

Concept Paper on
Family Business Owners and Their Employees

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Theoretical Underpinnings and Previous Research

Extant theories related to family-owned home businesses and their employees come from economic, business, and sociopsychological writings.

Labor Inputs of the Self-Employed. General labor market theory assumes a framework of two functionally distinct interests: the employer and the employee. The employer is a mediator between the supply and demand factors of production. The employee's interest is in maximizing the return to labor; correspondingly, his or her position in relation to the firm's profitability is limited and passive at best. Self-employment constitutes one person performing both functions (Aronson, 1991). Casson (1991) suggested that the labor market forces become internalized, and, therefore, labor market imperfections can be avoided. He noted that "internalization of a market occurs when a transactor buys a good from himself or sells a good to himself" (Casson, 1991, p. 193).

The advantages of internalization are many and include lower transaction costs, absence of price negotiation, absence of physical or tangible exchanges, lower default risk, possible secrecy, and avoidance of private or public demands by third parties or governments (Casson, 1991). The major disadvantages are lower opportunities to gain from possible specialization or division of labor among multiple players. Theory suggests that internalization of markets only makes sense when the lower benefits are more than offset by the eliminated market costs (Casson, 1991). "Do-it-yourself" projects by household members are common examples of internalization of markets. Such projects make sense only when the benefits outweigh the costs of performing the work.

Thus, labor market theory suggests that self-employment is chosen when higher level of utility can be gained from such work than from wage and salary employment. Historical trends tend to prove otherwise. At times, self-employment had declined even though the self-employment wage was higher than other employment choices (Blau, 1987). In contrast, the recent surge in self-employment has occurred despite the fact that self-employment wages are currently lower than other choices (Aronson, 1991; Blau, 1987 U.S. Small Business Administration, 1991). These trends suggest that labor market theory does not fully address the dynamic nature of self-employment. Aronson (1991) suggested that other nonmonetary aspects of these work arrangements, such as the desire for autonomy and independence, and external factors such as job trends, must play important roles in influencing a worker to engage in self-employment.

Labor Inputs of Others in Building Firms. Although Aronson (1991) argued that the majority of the self-employed are creating jobs mainly for themselves, as small business owners the self-employed also create a major segment of the job base in the economy. Within the family firm, the internalization mechanism operates for the self-employed worker's family in much the same way as for the self-employed worker (Casson, 1991).

The process of internalizing labor markets can include involvement of family members and relatives in the business or self-employment situation (Casson, 1991). Immediate family members may be sought first because they are most dependent on the self-employed person or business owner. Such family workers are easily located and may be easier to manage and control (Aronson, 1991; Casson, 1991). The least likely to be internalized are the family members who have higher status than the self-employed person or business owner, such as nonresident family members or other relatives.

This internalization of the labor market can have its drawbacks. Use of family workers limits the range of skills available to the self-employed worker or business owner. This may be especially true in the case of decision-making and specific jobs skills. Casson (1991) suggested that families are typically too small to substitute for access to the general labor market.

Relatively little research has been conducted on the interior dynamics of family-owned business. Rosenblatt, de Mik, Anderson, and Johnson (1985) found that slightly over one-third of the family businesses in their study demonstrated tensions over compensation and work load in the case of family workers. Compensation ranged from only the approval of others to ownership shares in the business. Kinship often interfered with the ability of family members to leave a family business when desired, resulting in feelings of resentment and of being used.

In Rosenblatt, de Mik, Anderson, and Johnson's (1985) study, the supervision of family workers was often avoided by hiring nonrelated individuals to perform this task. In some cases, the supervision of a spouse or offspring was more moderate, even though the family worker may not have viewed this supervision in this light. Austere supervision of offspring usually occurred because of a desire to downplay favorites, a feeling of greater freedom to judge relatives, and a strong parental drive to help offspring achieve. Clarity about the division of labor and individual autonomy for the family worker result in the best relationship between two family members if one is the worker and one is the supervisor.

Empirical Research on Sole Proprietorships. Earlier studies have examined characteristics of the self-employed, including gender, age, race and ethnicity, education level, occupational distribution, hours worked, and income. Men outnumber women in the ranks of the self-employed; however, women are a faster growing segment of the self-employed (Cromie, 1987; Hagan, Rivchun, and Sexton, 1989; Hisrich and Brush, 1986). Blacks historically have experienced the lowest rates of self-employment, closely followed by Hispanics (Aronson 1991). Self-employed persons are generally substantially older than wage and salary workers (Becker, 1984; Fuchs, 1982; Quinn, 1980) and have higher levels of education (Aronson, 1991, Evans and Leighton, 1989; Fredland and Little, 1981). The occupational distribution of the self-employed shows larger numbers of self-employed among white-collar occupations and skilled crafts.

The incomes of the self-employed vary widely, with significant numbers of individuals in both the high- and the low-income classes. On average, they earn less per hour than their wage-earning counterparts and tend to work longer hours for lower wages (Aronson, 1991). About 14 percent of all business owners earn less than the minimum wage. Self-employment can, however, generate capital gains as well as wage earnings. These capital gains and the longer hours worked by the self-employed may account for the findings of some studies that the self-employed tend to receive a higher rate of return on educational investments, despite their lower earnings per hour. These findings also suggest that business owners may experience nonmonetary benefits, expect relatively high future incomes, or place a high value on their self-employment (U.S. Small Business Administration, 1991).

One group of self-employed who earns slightly more than their wage counterparts is incorporated businessmen. Haber, Lamas, and Lichtenstein (1987) studied business owners using nationally representative data from the survey of Income and Program Participation. In their study, business owners accounted for 11.9 percent of persons working in nonagricultural industries during the last half of 1983. About 70.8 percent of businesses were sole proprietorships, while 18.3 percent were incorporated businesses. The nature of business ownership exhibited differences by gender. Men were more likely to work full-time at businesses than were women; but women were more likely than men to be engaged in casual and side businesses. Although underreporting of business earnings appeared to be an issue, median annual earnings ranged from about \$3,700 for female sole proprietors to \$24,000 for male owners of incorporated businesses. In addition to the employment of the business owners themselves, these small business owners employed, at a minimum, 28.5 million workers or slightly over 25 percent of all workers. Clearly, self-employment, including family-owned business opportunities, offers flexibility and adaptability in the economy, adds diversity not only to employment choices but also to the available mix of services and products, and increases the country's productive capacity.

Research on Home-Based Businesses. Horvath (1986) suggested that, in general, home-based work, including business ownership, allows for more effective combinations of work and family roles. Others have found a lack of similarity between family demands and home-based work (Ahrentzen, 1990; Christensen, 1985; McLaughlin, 1981; Olson, 1983).

A general profile of home-based workers, including self-employment, has been provided by Heck (1988, 1991), using household data obtained from the 1984 Panel Study of Income Dynamics. This sample of home-based workers consisted of 6,744 individual workers, approximately two-thirds of whom were self-employed. The likelihood of being involved in home-based work was positively related to age, absence of children, presence of children under age six, self-employment, and farming. Decreased participation was associated with minority status, high total family labor income, a high school education or less, and long working hours.

In a comparison of home-based business owners to home-based wage workers, business owners were more likely to own their homes and to be involved in seasonal work (Masuo, Walker, and Furry, 1992). Gender, marital status, and work hours per week were not significantly related to business ownership. Business owners were older, had less education, had a larger household size, had lived longer in the community, had been engaged longer in their employment situation, and had lower incomes than wage workers. The business practices and economic outcomes of family-owned businesses have been examined by Rowe, Heck, Haynes, and Bentley (1993).

Specifically, the factors related to business income, management behavior, and satisfaction with the business were studied. Gender differences in relation to family-owned businesses were the focus of research conducted by Walker, Furry, and Masuo (1993). In our study, we examined the number and types of workers utilized by sole owners of family home businesses and the effects of these workers on business outcomes.

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