Tacit Knowledge and Decision Making Practices in the Context of Family Businesses

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Abstract

Decision-making practices in family business are crucial and usually involve several stakeholders. To determine the decision-making mechanism in the family business, qualitative research approach was carried out. 30 semi-structured interviews were conducted involving family owners and non-family managers. Thematic analysis was used to analyze data. Three themes such as Business sense, consultation with elders, and ceremonial approval of the board were generated. Study reveals that decision-making is informal and based on tacit knowledge. Study emphasizes the codification of tacit knowledge, the codification will make decision-making more formal and institutionalized.

Keywords: Decision making practices, tacit knowledge, business sense, informal

Introduction

The long-term viability of family businesses is important not just for their owners, but also for the economy. Based on the survey of Census Bureau (2022), 90 percent of American businesses are family businesses - ones controlled by two or more family members simultaneously or sequentially. In the U.S., half of the employment and half of the gross national product is generated by companies ranging in size from two-person partnerships to Fortune 500 corporations. Same pattern is observed all over the world. Family businesses believed to be the dominant source of employment globally (HBR, 2021)

However, the three-generation myth appears in many forms in the context of family businesses. The phrase "shirtsleeves to shirtsleeves" implies that the money made by one generation of entrepreneurs is lost by their grandchildren. A similar saying is found in many countries, "Rich father; noble son; poor grandson."

Yew (2021) and Daspit *et* al (2017) state that implicit and tacit knowledge are the most important building block of family business, the family business rely heavily on tacit knowledge , it is considered an important intangible asset of family business . But sometimes these businesses fail to transfer this knowledge to the next generation. Thus, failure to disseminate tacit knowledge becomes another reason for the high unsuccessful rate of family businesses.

It has been observed that limited number of management accounting tools are used by family businesses and very few businesses have established specialized departments for management accounting practices (Neubauer et al., 2012). Therefore, family business owners does not have access to vital and up-to- date information about existing risks, this may lead to under performance in particular domains of the business.There are many family businesses which pass on tacit knowledge from one generation to another through value system or tradition instead of writing it in organizational memory. According to Giovannoni *et* al. (2011) potential cure for lack of strategic/ succession planning, inadequate operational planning, poor dissemination of tacit and implicit knowledge lies in the proactive use of management accounting. Management accounting practices are hardly utilized by family-owned businesses, because of their low formalized and highly flexible nature of conducting business. But highly informal and inflexible nature allows them to deliver competitive products and avoid cost intensive overhead.

Organization' strategic and competitive decisions depend upon knowledge and intellectual resource. The difference between explicit and tacit knowledge is one of the most known typologies of knowledge. Tacit knowledge "held by individuals" usually lie at the heart of the knowledge creating process, it initiates at the individual level and moves to the collective level and then to organizational level (Letonja & Duh, 2015). Due to lack of codifying tacit knowledge, informal governance mechanism is being used in family business. This informal mechanism is employed in decision making process. However, it is argued that if management accounting practices related to decision making are used then formal decision making may be observed in family businesses. So on the basis of above discussion, a research question was formulated.

What is decision making practices used in the context of family businesses.

Literature Review

According to studies of Chand & Dahiya (2010) and Durendez et al. (2011) the precise and accurate information help all types of family business to make decision about their performance improvement. But in family business decision making system is more dependent upon family expectations/values and the system is presumably more centralized. Moreover, it is difficult for managers and professionals to override decisions which are taken by family owners/ managers (Bisogno and Giovanni, 2017).

Alsharari et al (2015) argue that though use management accounting especially related to decision is not in infancy it is gradually gaining importance but academics and professional organizations are confused to) due to lack of liaison between practice and theory.

Rickards et al. (2021) sum up the previous findings on MAPs in emerging countries. The findings suggest that the use of contemporary practices is lacking in the four countries under examination China, Indonesia, Malaysia and Taiwan. In some organizations, traditional and contemporary practices are used simultaneously. The possible reasons for this can be: a dearth of knowledge about new techniques; absence of expertise; most importantly absence of top management support. Nair et al. (2018) state that external environment, user attitude (lack of knowledge, ability to take risk), cost saving mechanism and firm size (as larger firms are more willing to make an investment in advanced MAPs) may have an impact on the use of advanced practices in Malaysia.

Accounting Practices related to decision making are considered as source of refining business sustainability. Morshidi et al (2021) finds that usage of both traditional and advanced practices increased. Study reveals that in manufacturing sector, there is higher reliance on practices to cope with ever changing business environment. It concludes that management accounting acts as platform for handling changes in business with respect to its environment. So, it has been established through literature that practices have been used to offer valuable internal information, different tools, techniques for budgeting, planning and performance assessment and decision making

The literature has discussed that traditional or informal are highly irrelevant to serve the purpose of strategic decision-making, thus inducing demand for innovation in management accounting. Although response is made to call but adoption of innovative management accounting practices has remained very low (Doktoralina & Apollo, 2019).

Similarly, according to İbrahim & Duman (2020) manufacturing designs, presentation process, product and services of firms have been changed due to globalization, technological and economic developments. As a result, expectation regarding nature, scope, and amount of information have also been changed.

Global competition, particularly competitive economic situation, institutional pressure are probably considered the most commonly quoted stimuli of revolution/ advancement in practices (Gunarathne, 2021). When organizations confront substantial environmental variation, the conventional practices, encompassing ceremonial controls and reporting measures, are simply not sufficient to satisfy new and changing demands. According to Thomas (2016) practices need to be modernized and adapted consequently to get used to innovative and various informational requirements. In a summary of empirical studies carried out in different countries, Dahal (2019) identified the role played by both organizational factors such as essential competencies, downscaling, subcontracting, and customer & supplier relationships and environmental factors such as developments in information and production technologies, and globalization of markets.

A study by Sievinen et al (2020) suggests that the informal rules of family firms and their owners preserve family customs and traditions and aid in the transmission of knowledge. According to them, the informal rules used by family firm owners for decision-making reflect the experiences the family members have accumulated over time.

It is also likely that these rules will be available for owners who have no direct experience with these matters. Through these informal rules and experience families are able to exert control and influence. As explained by Ting (2020), the flexibility, informality, and mutual respect that characterize the ongoing dialogue enable family business owners to benefit from the unique business insight and understanding they have acquired through extended exposure and experience within the company.

Nevertheless, in many family businesses, institutionalized decision making mechanisms are absent for instance, board or executive committees either do not exist or do not perform in a formal manner. Therefore, business's owner-managers practice more informal mechanisms when forming decisions (Calabrò and Mussolino, 2013).

Methodology

Deductive research approach was used. A qualitative approach seems specifically suitable for recognizing and comprehending the delicacies and essential structures leading to decisions in family firms (Tudor - Locke, 2001). Semi structured interviews were conducted to gather data. Population was comprised of family firm owners and non-family workers.

In total, we w interviewed 30 family owners, non-family managers that were involved in the decision-making processes of the family businesses. Furthermore, we chose family businesses at different stages in their development, varying from founder-led business to those in the 3rd generation.

The interviews were carried out at the firms' office to guarantee a familiar environment for the interviewees. We gathered information about their culture, and made our own observation notes on-site. Furthermore, we had access to archival data including media reports, press, advertising material, firm websites, and annual reports. The saturation level was obtained through the above-mentioned data set.

Thematic analysis was used to analyze data. Open coding and then axial coding were employed at the later to identify themes.

Findings

Demographic data of participants is given below

Table-1

Summary of years of experience

Years of Experience	No of Participants	percentage
0-3	5	17
4-6	5	17
7-9	4	13
10-12	2	6
13-16	5	17
Above 16	9	30
	30	**100%**

Table-2

Summary of industries

Industry	No of Participants	percentage
Textile	5	17
Groups (Textile+Food+ IT)	25	83
	30	**100 %**

Table-3

Summary of age group

Age Group	No of Participants	percentage
20-29	5	17
30-39	5	17
40-49	10	33
50-59	7	23
60 and above	3	10
	30	**100 %**

Table -4

Summary of Gender

Gender	No of Participants	percentage
Male	27	90
Female	03	10
	30	**100%**

Table -5

Summary of Education Level

Education Level	No of Participants	percentage
Undergraduate	6	20
Graduate	24	80
Postgraduate	0	0
	30	**100%**

Table-6

Summary details of interviews

Job Title	Firm information
CFO	Conglomerate (Listed)
Project Director	Conglomerate (Listed)
Chairman	Conglomerate (Listed)
CEO	Conglomerate
Director	Conglomerate
Chairman	Conglomerate
Accounts officer	Conglomerate
CFO	Conglomerate (Listed)
HR Manager	Conglomerate (Listed)
Marketing Director	Conglomerate (Listed)
Accounts officer	Conglomerate
CEO	Conglomerate
Business Unit Director	Conglomerate
Manager	Conglomerate
CEO	Conglomerate
Procurement Director	Conglomerate
Chairman	Conglomerate
CEO	Conglomerate
CFO	Conglomerate
Chief Accountant	Conglomerate
Business unit director	Conglomerate
Auditor	Textile company
CEO	Textile company
Finance Director	Textile company
CEO	Textile company
Chairman	Textile company
Finance Director	Conglomerate
Director	Conglomerate
Business Unit Director	Conglomerate
Operation manager	Conglomerate

The results show that decision making in family businesses tend to be made on the basis of business sense, in consultation with elders and through ceremonial approval of board.

About business sense one CEO of company disclosed that

> "We observe market, our own weaknesses and strengths, which are part of our family business. Then we make decisions. However, you can say that decisions are based on experience."

He further explained

> "We try to learn from our past experiences and apply it in future decisions. E.g in past when we had to expand business, there were two option should we buy new machinery or purchase used/ second hand machinery, my decision was to purchase new one. But during second expansion phase, I realized through my experience that used/ second hand machinery was better option, so in second phase I purchased used one. Look. We learnt this from our experience"

Chairman of group of companies expressed that consultation with elders is very important.

> "We do proper market research and paperwork before making any investment. Sometimes we use techniques which you people study in universities, but we also use our experience to make final decisions. Sometimes we consult our elders although they do not have relevant expertise as I told you about my mother. But her recommendation helps us a lot."

Another CEO explained consultation with elders as

> "Our elders are rich source of knowledge which they have learnt through their experience. We take their opinions and discuss with them. "

A Director said that investment decisions are usually made through ceremonial approval of BOD and mutual consultation

> "Informal meeting and discussion have very positive impact. New ideas and suggestions are floated. Then after thorough discussion I put proposal on BOD for final approval. Then board members make decision about it."

Operation manager clarified that

> "Whole business is centralized. Chairman is more than 70 years old but he runs whole business. He has final authority to take decision. No one can go against him."

Discussion & Conclusion

It is evident from our study that that family owners use business sense to form decision, this sense is very often based on experience A study by Sievinen et al (2020) suggests that the informal rules of family firms and their owners preserve family customs and traditions and aid in the transmission of knowledge. According to them, the informal rules used by family firm owners for decision-making reflect the experiences the family members have accumulated over time. Hougaz, (2015) state that an enterprise's basic structure is shaped by its founder's philosophies, pragmatic decision-making, business acumen and values. So, making decision on basis of business acumen or business sense prevails within family business. Business and family are not just connected, they are woven into each other. Businesses and families are inextricably intertwined and dependent on each other.

According to in the first generation of a new family business, personal values are closely related to personal resources. For upcoming generation these personal values become point of reference. It acts as particular capital resource which helps in perpetuation of ancestral experiences and tacit knowledge. Second and third generation always refer back to personal values / particular capital resource in order to make decision. Although sometimes this capital contains outdated historical context and condition, even then for second and third generation it remains relatable (Hougaz, ,2015)

In previous research, family owners/directors typically perceive the board as an instrument to strengthen their control. As a result, they pressure top executives to pursue family goals. Thus, the board is viewed by the family owners or directors as a platform for justifying strategic decisions that promote the Socialemotional Wealth preservation agenda. (Gomez-mejia et al 2011; Carney et al., 2015 ; Gomez-Mejia et al 2018).

Our study infers that business sense which is based on experience & market analysis, and suggestions of elders are used. Approval from board is ceremonial. So it can be stated that decisions making is informal in family firms. This trend was observed in small, medium and larger family firms. Experience and suggestion of elders are rooted in tacit knowledge.

As deductive approach is followed so study cannot be generalized however it underpins reasons behind informal decision making which in turn is based on the use of tacit knowledge. The motive of deductive and qualitative approach is never to generalize results or phenomenon but to understand phenomenon.

The study used opinion of participant, specifically running their businesses in Pakistan. However future studies may obtain from different countries. Moreover, only manufacturing sector is used.

The study provides an insight to the scholars working in the domain of family business and policy makers to consider importance of tacit knowledge and suggest interventions to codify and institutionalize this implicit knowledge.

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