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Interorganizational Familiness: How Family Firms Use Interlocking Directorates to Build Community-Level Social Capital[1]

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We draw on the concept of community-level social capital and apply it to the situation of a family-controlled public corporation. While traditional agency theory argues that agency costs are minimized in a family-controlled business (FCB) due to an improved alignment of owner and manager interests, we argue instead that FCBs endure additional agency costs uniquely related to the family firm organizational structure. To mitigate these additional costs, we propose that FCBs use board interlocks to build and maintain community-level social capital. That is, the intercorporate network of FCBs generates shared understandings, values, problem solving techniques, and approaches to dealing with family issues. Further, the network generates a level of social support for family business owners and managers grappling with challenges endemic to family control of public corporations. We generate a number of propositions that can be used in future research to test the theory developed here. We conclude with the assertion that the community-level social capital generated by the network of FCBs is an important reason for the survival and persistence of individual family firms, despite the existence of additional family-related costs.

Long discounted by both scholarly researchers and the business press (e.g., McCarthy, 2004), the topic of family business is reemerging with new vigor (e.g., Anderson & Reeb, 2004; La Porta, Lopez-de-Silanes, & Shleifer, 1999; Villalonga & Amit, 2006).[2] While family ownership in large U.S. corporations is quite pervasive and

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1. An earlier version of this work was presented at the Theory of Family Enterprise Conference, University of Alberta, June 2005.
2. Many of these studies do not differentiate between entrepreneur-controlled businesses (ECBs) and family-controlled businesses (FCBs). However, in our view, the distinction is critical. ECBs, by definition, have only a single owner-manager involved in the business, and are far less likely to have any intention to pass the company on to subsequent generations. While many FCBs start out as ECBs and make the transition only after the founder passes, for the purposes of our study, ECBs are not "family businesses" (Miller, Le Breton-Miller, & Lester, 2005).

common across a broad range of industries (Schulze, Lubatkin, & Dino, 2003), many of these firms also appear to have survived, often intact, over longer periods of time than their nonfamily counterparts (Miller et al., 2005).

While recent scholarly discourse focuses largely on performance differentials, we are more interested in examining the perpetuation of the family firm structure. How is it such firms are able to maintain their family status over time, given the obvious difficulties and costs associated with this form of ownership? Our interest lies in examining family firms in which two or more persons with kinship ties work as executives in the business, have the power to determine the composition of the board of directors, and have the objective of passing the firm to the next generation of family members. Throughout this article, we will refer to these organizations as family businesses or family-controlled businesses (FCBs).

We begin with the notion that public corporations structured as family businesses confront more, or at least different, challenges than similar, nonfamily, corporations. These differences exhibit themselves in a number of ways, at times clearly in line with firm survival and shareholder interests and at other times not. Gersick, Davis, Hampton, and Lansberg (1997) suggest these costs and issues arise from distinctions made between family, ownership concentration, and business issues. We can think of many related and intersecting issues when a family firm is viewed in such a context: e.g., succession, cousin consortiums, sibling rivalry, free riding, and unprofessional or unprepared management.

Accordingly, we do not attempt to parse the differential nature of family costs into categories and, while we recognize their existence, leave the latter for other research. Suffice it to say that while all corporations must deal with business and competitive concerns, and all public corporations have an additional burden of meeting the regulatory restrictions of public ownership, family corporations must also deal with an additional matter—family issues (Miller et al., 2005; Paisner, 1999). Miller et al. (2005) describe this second set of complexities, noting the parallels and differences between the agency costs created by the traditional separation of ownership and control, and the so-called costs of conflict, referring to the problem of dispute resolution among powerful family owners. If these additional family costs rage out of control (and there are many examples), the end result can be of significant damage to the corporation and *all* of its owners.

As an example, previous work on family firms has concluded that: (1) Two thirds fail in the transition to second generation (Handler, 1990; Ward, 1987); (2) they experience slower growth (Chandler, 1990); (3) they are often characterized by vulnerability and inertia in decision making (Meyer & Zucker, 1989); (4) they endure high agency costs (Morck, Shleifer, & Vishny, 1988); and (5) they can fall victim to predatory managers (Morck & Yeung, 2003). How then do family firms[3] maintain their status over long periods of time?

We adapt the notion of community-level social capital (Bourdieu, 1983; Putnam, 1993) as an important mechanism through which family owners protect and nurture their family businesses. Many readers are more familiar with the instrumental approaches to social capital, characterized by the works of Burt (1979, 1980, 1992) or Nahapiet & Ghoshal (1998). The instrumental approach emphasizes network position, and how network position influences the information flows among individual network members, as well as individual-level benefits that accrue. In contrast, a community-level approach emphasizes concepts such as shared values, trust, norms of reciprocity, and social support

3. We, as do others (e.g., Chua, Chrisman, & Steier, 2003), subscribe to the notion that family firms, as compared with nonfamily firms, are more likely to view success in terms other than purely economic.

shared broadly among members to a community, and it is much less concerned about network position except as an indicator of particular characteristics.[4] In our study, the executives, directors, and owners of family businesses form the community under study.

Our article is organized as follows. We first review recent information about the existence and persistence of family companies in the United States. Then, we discuss the concept of community-level social capital, and provide some early clues as to its application and appropriateness for the family business setting. In the third section, we review the theory of interlocking directorates, as we believe that director interlocks will form an important mechanism for information sharing and the creation of community-level social capital among family business owners. Finally, we apply these theories to family corporations, emphasizing the situation in which the family business is publicly traded. Discussion and conclusions end the article.

Family Control of Public Corporations

Recent research has indicated that family control of large public corporations is widespread in the United States. Family ownership constitutes approximately 35% of large publicly traded firms in the United States and is evident across a broad spectrum of industries and firm sizes (Anderson & Reeb, 2004; Gomez-Mejia, Larraza-Kintana, & Makri, 2003; Schulze et al., 2003). Additionally, much of the wealth owned by the richest families in North America is corporate wealth (Allen, 1987). This wealth is often created through substantial stockholdings in a single corporation and through management of that corporation by members of the founding family or its descendants. Kinship ties tend to bind family members together. Yet those same ties can become disruptive influences or distractions when there are sharp disagreements among family members. As noted earlier, Miller et al. (2005) describe the costs associated with intra-family conflict—costs that are not endured by nonfamily businesses.

Although there are few theoretical treatments of agency theory dealing with the costs of intra-family conflict as we have defined them,[5] a perusal of scholarly research on FCB suggests that most authors assume these costs are substantial. Put differently, most authors seem to believe that family control of large businesses is inherently inefficient. This should not come as a surprise, given that traditional assumptions about market competitiveness, coupled with the tendency to perceive managerial interests as sharply divergent from shareholder interests (Lane, Cannella, & Lubatkin, 1998) contrast sharply with those few authors who view family firms as stewards of resources (Schulze, Lubatkin, Dino, & Buchholtz, 2001). Indeed, the very persistence of family companies seems to challenge the notion of market competitiveness, as FCBs face challenges comparable to all other firms and often must additionally deal with costly intra-family issues. If they outperform regular public corporations, the logical conclusion would seem to be that they are better governed than regular public corporations—a hard pill to swallow for free-market economists.

Of course, the existence of public corporations was also a difficult thing to acknowledge until it was better understood. Our article argues that the social capital generated by family business linkages to one another is an important reason for the survival and

4. In the community-level approach, network centrality can indicate "ideal type" status. One of our propositions builds on this notion.

5. For exceptions, see Chrisman, Chua, and Litz (2004); Miller and Le Breton-Miller (2003); Miller et al. (2005); and Schulze, Lubatkin, and Dino (2002).

prosperity of this organizational form. Through these linkages to other firms, family businesses develop a strong identity, core values, and knowledge about how "family businesses" respond to challenges, both intra-family and competitive. This is not to argue that the mechanism is perfect—there are numerous examples of poorly run family firms, and family firms in which the family, or some of its members, looted the company. Yet, the three large-sample studies of family business in the United States that we are aware of have consistently concluded that family businesses outperform nonfamily businesses (e.g., Anderson & Reeb, 2003; Miller et al., 2005; Villalonga & Amit, 2006).[6]

Community-Level Social Capital

Social capital can be used to bond members of a group, social or otherwise, with a shared identity. Additionally, it may facilitate cooperation among groups, but may also be used to exclude those who are not considered "like us" (Healy, 2004). Likewise, community-level social capital is a term we employ to describe a phenomenon whereby firms invest in social capital through norms of behavior and access to resources such as mutuality, trust, and respect for one another. In this regard, the social capital that is captured at a community level is one that yields corporate well being. These benefits accrue from knowledge sharing, lower transaction costs due to improved communication, and a coherence of action. Community level social capital, in our context, is akin to the works of sociologists such as Coleman (1988) and Portes (1998), who emphasize a bounded form of social capital, one that largely exists between specific groups of people. Through joint identities and mutual interests, collectives of people and organizations develop common bonds which may be used to achieve joint ends (Gold, 2002). From a community-level view, it is the community that structures action and provides the frame of reference for community members.

As an example, Granovetter (1995b) emphasized the value of network-based social capital as an underlying success factor for various groups of ethnic entrepreneurs. He showed how, by maintaining strong ties within and weak ties without, these ethnic groups were able to sustain advantageous economic relations. Others (Light & Bonacich, 1988; Porter, 1987; Zhou, 1993) have also found that community networks may be a source of vital resources such as access to capital, tips about business operations, and access to markets. We follow the lead of those who argue that social capital exists within social networks, rather than a less precise society-wide formulation or a more precise, individualistic view (Coleman, 1988; Granovetter, 1995a; Lin, 2001b; Portes, 1998). However, social capital researchers do not necessarily agree on this boundary, nor its merits or definitions.

For example, Bourdieu (1983, p. 248) defines social capital as "the aggregate of the actual and potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance and recognition." Bourdieu argues, through this definition, that social capital is not possessed by any single person, but exists in shared form among a relatively large community of individuals. Put differently, Bourdieu states that social capital is first a resource of individuals connected with group membership and social networks (Siisiainen, 2003), and these individuals accrue benefits through participation in groups (Portes, 1998). Huysman and Wulf (2004) noted

6. Again, we emphasize that only Miller et al. (2005) differentiate between family businesses (as defined here) and entrepreneur-controlled businesses—a distinction we believe is critical.

that this approach implies a world characterized by its own capitalists—those who accumulate relationships, networks, and contacts. Further, those more central in this social capital network are likely to be more influential. In slight contrast, Putnam (1993) describes social capital as a shared resource characterized by the level of civic engagement. He perceives civil society as created and maintained by the direct social relationships that people of the society share on a more or less regular basis. Here, norms of trust, shared language, etc., are important determinants of the ease with which cooperative activities can be achieved. In Putnam's view, the level of civic engagement is a key indicator of the health of a community.

A less often discussed outcome regarding social capital is the potential for negative outcomes. Less desirable consequences, such as restrictions on members' freedom to innovate, downward leveling norms, and exclusion of outsiders (Portes, 1998) suggest that the network also affects its members. According to Rumbaut (1997, p. 39), "family ties bind, but sometimes these bonds constrain rather than facilitate particular outcomes." Thus, strong intergroup relations, such as those found in highly unified communities, may give rise to unintended consequences (Portes, 1998).

Despite differences in definitions and usage, a consensus seems to be growing that social capital represents the ability of individuals or groups to secure advantages through membership in social networks or other such social structures (Portes, 1998). For those in family businesses, the community of other family firms likely provides social support and information about how to deal with issues germane to their often unique situations. Understanding that others have successfully dealt with similar situations provides a certain level of social support and trust for the members of the family business community. Further, the broad network of family businesses may provide answers to important questions in much the same way that instrumental social capital functions in employment and promotion situations (e.g., Burt, 1980). Certainly, issues such as intrafamily disputes, the role of in-laws in the business, handling a problem employee who is also a family member, and leader succession are important problems that any family business must confront and overcome in order to survive over the long run. We therefore argue that family firms use mechanisms, such as a board of directors, to build, maintain, and draw upon community-level social capital in an effort to resolve these and similar problems.

Interlocking Directorates

The typical conceptualization of an interlocking directorate is when two firms share one or more directors. Early research was based on the theory that interlocking directorates reduced competition, but since the prohibition of interlocks among direct competitors (adopted in 1914), there is little consistent evidence that interlocks have any dampening effect on competition (Mizruchi, 1996). However, much research suggests that interlocking directorates facilitate the flow of information (Mills, 1958; Stanworth & Giddens, 1975) or co-opt powerful actors in the environment for the purpose of coordinating behavior (Mintz & Schwartz, 1981; Pfeffer & Salancik, 1978) or achieve interfirm coordination and control (Fitch & Oppenheimer, 1970). More recently, research on interlocking directorates suggests that this phenomenon might influence a broader range of firm behaviors such as political action committees, public policy group memberships, and organizational structure changes, as well as involvement in mergers and acquisitions (Mizruchi, 1996).

Most scholars seem to believe that interlocks are created to serve organizational interests or the interests of the executives who manage the interlocked corporations. For example, resource dependence theorists believe that interlocks are a means for the firm to reduce the uncertainty in its environment (Burt, 1980; Pfeffer & Salancik, 1978). The same logic is drawn upon by hegemony theory, which suggests that interlocks indicate the influence and importance of capital structure and the management of capital (Kotz, 1978; Mintz & Schwartz, 1981). This sits in some contrast to social class theorists who believe that interlocks exist to support the structure of the capitalist class differentiated by various familial relationships or other such social ties (Useem, 1979, 1984). Research about corporate elites has long recognized that they are not a monolithic class. While Baltzell (1958) was among the earliest to suggest ways in which individuals within the upper class may be differentiated from others, the idea has been picked up by other researchers (Isaacs, 1974; Zweigenhaft & Domhoff, 1982). For example, Domhoff (1970) categorized elites based on religious and ethnic affiliation. Another source of internal differentiation in the capitalist class stems from the economic interests of particular families (Allen, 1974; Pittman, 1977). Consequently, it is likely that the members of the elite family corporate class may compensate for their numerical inferiority by becoming sources of information, contacts, and reciprocity for each other.

In alignment with a resource-dependence perspective (Pfeffer & Salancik, 1978), our view is that family firm interlocks provide resources to the firms involved, helping each other to navigate uncertainty in the environment (Kono, Palmer, Friedland, & Zafonte, 1998). Others (Bourdieu, 1983; Palmer & Barber, 2001; Useem, 1979) argue that manager-specific resource needs, rather than firm-level resource needs, drive corporate interlocks. For example, corporate managers may seek to protect their own jobs and reputations (Lorsch & MacIver, 1989) as well as augment their salaries (e.g., Westphal & Zajac, 1997) through board-level ties to the community of corporate elites. However, owner managers (particularly family business executives) are typically quite secure in their positions. Therefore, we expect that family business executives will seek interlocks for reasons other than entrenchment and self-preservation. A central thesis of our article is that family business executives will seek advice and counsel from others who have experiences relevant to their unique situations (Hillman & Dalziel, 2003).

Moreover, we take exception to the Jensen and Meckling (1976) model, as do others (e.g., Chrisman et al., 2004; Schulze et al., 2002). That model asserts that family firms have so little managerial opportunism within their organizational structure that the need for internal governance mechanisms, like a board of directors, is negated. Recent theory suggests, however, that boards serve more than a governance function (e.g., Hillman & Dalziel, 2003; Johnson, Daily, & Ellstrand, 1996). In this more recent tradition, we perceive the board of directors as a resource used by family firm owners to assist family executives (less so than to monitor them) and reduce within-family agency costs (not create them). The board then is a means in family firms, unlike in their nonfamily counterparts, to build community-level social capital as a resource capable of sustaining and preserving their unique organizational structure. Additionally, family members, as large owners, are relatively free from the threat posed by the market for corporate control. We suggest this provides them some additional latitude in developing board interlocks relative to other types of managers.

There has been some empirical support for this notion. In a seminal work regarding the formation and history of Scottish capital, Scott and Hughes (1980) provide evidence that kinship ties were a means of a sustained continuity of control over firms through a network of interlocking directorates. The propertied class of family firms were interlocked

in a large number of companies and constituted a prominent pool from which directors for other firms were recruited (Scott & Hughes, 1980, p. 263).

Our perspective suggests a theory of "interorganizational familiness" whereby status in a community of family-controlled corporations provides a mechanism that, in addition to kinship ties, serves to extend and maintain family control and influence over their organizations and reduce the likelihood of firm failure due to the family's inability to effectively deal with disputes and differential agency costs. We additionally argue that interorganizational familiness can have positive side effects for nonfamily owners, as the firm's strategy and performance are likely enhanced. Accordingly, we posit a number of areas in which family firms utilize community-level social capital to their own and their organizations' advantage.

Theoretical Development

Community-Level Linkages

The boundary of what we call "community" is defined by the network of family-controlled public corporations. More specifically, our interest lies in firms which rely upon a formal board of directors as an important source of governance. A community then, in our context, exists among firms whose interaction brings about "mutual engagement, a negotiated enterprise, and a repertoire of negotiable resources accumulated over time" (Wenger, 1998, p. 126). Wenger (1998) describes a "community of practice" whereby organizational learning and sharing suggest both a particular context and a social interaction component (Soekijad, Huis in 't Veld, & Ensering, 2004). For example, Lave and Wenger (1991) identified a group of repairmen who regularly interacted both socially and professionally, and concluded that this interaction provided an important source of solutions to problems in their work environment. Additionally, Lave and Wenger (1991) suggested that such communities exist to develop community-level capabilities through exchange, acquisition, and creation of knowledge. In a parallel way, family firms are embedded in their "communities," and through those communities are able to weave common interests and shared values into their specific environments.

Moreover, our focus on community-level social capital postulates that family influence is both developed and exercised in networks that stretch beyond the family firm's boundaries. These intercorporate connections include formal associations such as boards of directors as well as instrumental and trust relations across formal boundaries (DiMaggio & Powell, 1985). A community of interorganizational families consisting of members of family firms is likely to act cohesively through their actions on each other's boards. We expect the members of this community to share common interests and act in concert within and across the firm's boundaries (Pitelis & Sugden, 1986). While our emphasis is on community-level issues such as the diffusion of practices and perspectives from similar organizations, clearly some actions of mutual benefit to the parties are also likely. For example, business linkages among interlocked firms seem likely to be facilitated, perhaps even more so than in the case of regular public corporations.

Another common theme in community-level social capital is trust (Fukuyama, 1995). Trust, in our context of interorganizational familiness, entails a degree of risk because it is not certain that linkages with other family firms will function as expected. However, we believe that family members will, on average, "respond as expected" because of a sense of community and shared norms. Misztral (1996) argued that trust is a belief that the results of one's actions will be appropriate from one's own point of view. Therefore, a sense of community likely exists in a family firm network context. Members have shared

experiences, trust one another, and should be expected, all else equal, to act in one another's best interest.

It has been argued that family firms suffer from an increased moral hazard (Schulze et al., 2002) which increases monitoring costs. Family firms also suffer from conflicts related to expectations among family members in regards to both economic and noneconomic motives (Bergstrom, 1989; Chrisman et al., 2004; Lee & Rogoff, 1996). FCBs therefore, for both economic and noneconomic reasons, actually incur additional agency costs which increase the costs of monitoring and enforcing agreements among owners. Thayer and Shefrin (1981) describe this phenomenon as an "agency problem with oneself." Similarly, La Porta et al. (1999) argue that family firms are particularly prone to internal dysfunction, while Schulze et al. (2003) describe altruistic family behaviors not necessarily in the firm's best interests.

Our premise then is actually one of alignment concerning the way in which an FCB might opt to mitigate, to the degree possible, the additional costs of organizing as a family business. How best should influential family owners reduce these costs while also seeking organizational advantages? We argue that FCBs will align themselves in a community of like-minded organizations, namely other family firms. These communities are used to share knowledge, develop capabilities, and learn from one another. One reason we expect to observe these linkages is the trust developed by aligning with similar others. Following this logic, family firms, when seeking outside directors for their boards, will lean toward those whom they are able to trust and with whom they share a sense of community with their own interests. Therefore:

> **Proposition 1:** Family-controlled corporations will have a higher proportion of board interlocks to other family firms than will nonfamily-controlled corporations.

Geographic Linkages

Another important factor in community-level social capital is geographic proximity. While our earlier arguments imply that there is a family business elite in the United States, it is also likely that there are geographically clustered segments within the family business community. Davis and Greve (1997) found that 32% of the outside directors who were executives of other large firms came from other firms headquartered in the same telephone area code, and 39% came from within the same state. This evidence suggests that firms have a broad preference for interlocks to other firms that are nearby.

There are several reasons to expect that geographic proximity will actually be more important for family business interlocks than for interlocks among regular public companies. Domhoff (1970) maintains that metropolitan upper class social clubs are places where local members of the upper class maintain and perpetuate interpersonal ties. Scott and Hughes (1980) found that interlocks from wealthy corporate families followed prominent regional patterns. Further, these interlocks may also provide a context in which trust can be developed (Kono et al., 1998). As discussed earlier, trust is central to family business relationships involving advice and counsel, because families tend to guard their privacy, and are very careful with whom they share confidential information. Further, it is important that persons selected for board service actually behave as expected.

The broader interlocks literature, which emphasizes managerial self-interest, seems less about trust and more about social exchange reciprocity. Further, when managerial self-interest is the key driver behind director selection, we might expect to see busy people selected as outside directors, in the hope that they will not monitor too closely. We think that narrow self-interest and monitoring (or lack thereof) will be less of a concern among

family business executives seeking outside directors. They already control large blocks of shares, are already wealthy, and are relatively sheltered from the market for corporate control. For these reasons, they can concentrate on strategic interests rather than narrow self-interests. The family business executive is probably less concerned about gaining personal benefits from outside director selection and more concerned about gaining valuable advice and support relevant to his or her unique situation.

It is also likely that some (perhaps much) of the knowledge shared and exchanged through family business interlocks will be tacit. This knowledge is difficult to transfer and requires that the parties to an exchange trust each other and have some level of shared experience (McFadyen & Cannella, 2004). Trust and shared experience are much more likely among individuals who reside near each other and are therefore more likely to spend time together. Many family business executives serve on civic and community boards, and invest family wealth (aside from the wealth invested in their corporations) in the local areas where the family resides (Palmer & Barber, 2001). These activities increase the likelihood of meeting and working with other family business executives in the local area, providing for shared experiences and the development of trust, and leading (we believe) to an important source of outside directors for family businesses.

In support of some of these notions, Mizruchi (1989) found localized patterns of corporate political donations, and Roe (1993) identified legislative lobbying coordination to be relatively localized. Both of these studies examine unified action by groups of influential individuals at a local and a regional level. We expect that this regional affiliation will extend to family business executives as well, and that regional ties are influential bases for the dissemination of information among family firms and thus are important bases for the exchange of tacit knowledge and social support among family business executives.

Finally, following work by Zeitlin (1974) we assume that family-controlled firms are situated in a multidimensional social network, one dimension of which we see as the geographic cluster of other family firm members. These clusters are likely to be important sources of resources for family businesses seeking to control family costs, as well as additional sources of opportunity. We do not necessarily expect that the clusters will be bound purely by location, as such factors as ethnicity, education, and club memberships will also be important. However, geographic proximity is clearly associated with better estimates of trust, understanding, and confidence, as well as with reduced cost of participation through convenience. For these reasons, we expect that family firms in close geographic proximity to one another will be more likely to have board interlocks.

Proposition 2: Family-controlled corporations will have a higher proportion of interlocks to other firms in the local area and nearby geographic areas than will nonfamily-controlled corporations.

Strategic Linkages

Because one of our central themes is that family firm interlocks will play an important role in organizational strategy, we contend that one way to avoid or mitigate possible family confrontations on strategic direction is to align with similar others (Tsui & O'Reilly, 1989). In this way, the family controlled firm is presented with exemplars or models that it can align with in order to resolve ambiguity and conflict among family members.

Board linkages are thought to be especially important conduits, because they are likely to provide information directly relevant to strategy and information that affects

behavior. Such information transmission might lead to imitation (DiMaggio & Powell, 1983) or learning (Levitt & March, 1988). There is a considerable body of work that suggests imitation flows through interorganizational ties (Ahuja, 2000; Davis & Greve, 1997; Galaskiewicz & Burt, 1991; Greve, 1996; Palmer, Jennings, & Zhou, 1993; Rao, Davis, & Ward, 2000; Westphal & Zajac, 1997).

There also appears to be some broad agreement in the literature that family firms tend to pursue strategies that are more risk averse than those of regular public companies. For example, some studies show that family firms shun debt in order to avoid the risk of bankruptcy or the risk that sizable debt will fall under the control of third parties, thus threatening the family's control (Gorriz & Fumas, 1996; Mishra & McConaughy, 1999; Schulze et al., 2003). Further, this risk aversion can limit the firm's ability to grow and innovate (Cho & Pucik, 2005). Family firms have also been found to pursue cautious investment policies that likewise tend to inhibit growth (Mustakallio, Autio, & Zahra, 2002). Finally, family business ownership has also been linked to slower economic growth when FCBs dominate the economic landscape. For example, La Porta et al. (1999) argue that "risk aversion [as a result of wealth concentration] limits the scope of activity of family firms . . . what may be optimal for the firm [in terms of minimizing risk bearing] can have the side effect of impeding overall economic growth" (p. 475). Similarly, Morck and Yeung (2003) suggest that family control of a large number of businesses can retard economic growth due to the inherent risk aversion of family firms. However, it is also important to recognize that outside directors individually bring varying experiences and trustworthiness to board discussions.

Previous work has suggested that, outside, directors play an important role in corporate governance. For example, research has demonstrated associations between interlocks and executive compensation (O'Reilly, Main, & Crystal, 1988), changes in organizational structure (Palmer et al., 1993), likelihood of merger or acquisition (Haunschild, 1993), or adoption of poison pills (Davis, 1991). Interlocks not only serve as conduits through which information travels, but also as norms for corporate governance practices (Useem, 1984). As an example, it is likely that, in board discussions on diversification strategies, outside directors with experience in diversification will bring their experience to the forefront and be influential in board meetings. It is more likely then that outside directors with a familiarity to the structure and strategy of a firm will be more influential in guiding board discussions and will have a subsequent impact on strategy and firm direction.

In a community of family business executives, we believe that information obtained from one another is likely to be inexpensive, trustworthy, and credible (Haunschild & Beckman, 1998). Credibility is additionally established when the interlock partner has direct experience applicable to the focal firm. First-hand knowledge has been shown to be more reliable and influential than abstract retelling of another's story (Nisbett & Ross, 1980). We also expect that information received from peers, as in the case of one family firm executive to another, is more likely to be regarded as trustworthy. Further, when the source of the information is well positioned in the family business community, the information is more likely to be perceived as relevant and appropriate to the family business context.

We mentioned earlier that conflicts within the family are a very important cost of doing family business, though they have been largely ignored in scholarly research. Having trusted advisors on the board who are from other family businesses can help keep family conflicts from raging out of control. Trusted advisors can act as impartial third parties in resolving disputes among family members before the two sides become fixated. This would particularly be the case when the source of the dispute involves a disagreement about strategic direction.

Our previous discussion extends the development of community-level social capital through interlocking boards at family-controlled firms and subsequent linkages between their executives. We additionally argue that family firm outside directors on the board are chosen not only for their status as family firm executives, but also due to their ability to sympathize with issues relevant and peculiar to family run firms. Family firm strategies are often different than their nonfamily counterparts. Likewise, imitation of firm strategies is found to flow through interorganizational ties. When setting strategic direction, we suggest that one way to resolve ambiguity and conflict is to rely upon trusted confederates or impartial judges. Following the logic of Westphal and Fredrickson (2001) we expect outside directors from family firms to guide strategic direction toward the strategies that they are implementing in their own firms, and to seek alignment with, and be recruited by, firms of like preference, all else being equal. Therefore:

Proposition 3: Relative to nonfamily corporations, the interlocks of family business boards of directors are more likely to be with firms that share similar strategic orientations.

Centrality in the Family Business Community

The notions developed so far highlight the existence of a community of family firms sharing common interests and providing for an institutionalized pattern of business decision making. However, while this argument might seem to suggest broad similarity among family firms, we know already that the population of family firms in the United States is quite diverse.

A central notion in community-level social capital is the importance of strong, networking relationships. Thus, the network constitutes a valuable resource from which members are able to draw upon collectively owned capital. Bourdieu (1986) argued that much of this capital is embedded within networks of mutual acquaintances. However, the strength of network ties is also influential. Granovetter (1973) found that, through weak ties, network members can access influential others and thereby gain privileged information and opportunities. Additionally, social status and reputation are enhanced from membership in specific networks, particularly those in which membership is restricted (Burt, 1992; D'Aveni & Kesner, 1993).

There is also empirical support for the notion that preferred partners for interaction are those occupying slightly higher status (Galaskiewicz & Burt, 1991). Termed the "prestige effect" (Laumann, 1966), this theory implies that interaction with prestigious parties will enhance the prestige of the less advantaged actor. While preference in forming linkages may be quite different from the interactions that arise from linkages after formation, Laumann's (1966) principle does assist our understanding of why individuals tend to pursue association with others of similar, or slightly higher status. The reciprocal nature of the interaction likely serves the interests of both parties, as those who associate with prestigious individuals seek to gain prestige for themselves from that association (Lin, 2001a).

Typically the most prestigious members of a community are also the most visible, successful, and prominent. Just as executives from high-performing firms are more likely to accept invitations to join other firms' boards as outside directors (Brickley, Linck, & Coles, 1999; Lester & Cannella, 2005), it is just as likely that successful firms will form intercommunity linkages that serve their continued prosperity as well. Additionally, given the sense of community that we believe exists among family businesses, the most successful of these firms are those most apt to be sought after for their advice and council

(Johnson et al., 1996). A prominent way to acquire advice and council is through board interlocks (Pfeffer & Salancik, 1978). In this way, successful family firms are able to disseminate business practices; e.g., succession planning, family grievance procedures, diversification strategies, and the like, thereby promoting and preserving the community, and reducing a potential source of conflict within the family business.

Our view of community at the family firm level entails a network of firms which are linked together through board interlocks. However, not all family firms are equal. Additionally, success in the community of family firms connotes success in noneconomic areas as well, e.g., succession planning, compensation, and diversification strategies. Such noneconomic strategies are essential in maintaining and improving the likelihood of survival for a family-run firm. Our theory suggests that those firms with the most prestige and prominence in the community are apt to be those most sought after for outside-board appointments. Therefore, we expect that successful family firms will have a higher representation on the boards of other family firms than on the boards of their counterparts. Accordingly:

> **Proposition 4:** The most prestigious and successful family firms are the most likely to be located in the center of the intercorporate network of family-controlled companies.

Organizational Performance

Our theory of interorganizational familiness to this point has centered on the concept of a system of formal linkages among family firms with an emphasis upon promoting, maintaining, and preserving family control and influence over the organization. We have additionally alluded to the notion that this may not necessarily be in opposition to minority shareholder interests. However this view is not prominent in previous work. There is a substantial amount of empirical and theoretical evidence to suggest that minority shareholders are placed at a disadvantage in family-controlled firms or firms in which there is an individual with a controlling interest (Claessens, Djankov, Fan, & Lang, 2002; Demsetz, 1983; Fama & Jensen, 1983; Holderness & Sheehan, 1988; Jensen & Meckling, 1976; Shlefer & Vishny, 1997). However, more recent research has called this perspective into question (Anderson & Reeb, 2003; Anderson & Reeb, 2004; Miller et al., 2005; Villalonga & Amit, 2006).

Most studies that conclude the performance of family firms is worse than their nonfamily counterparts (e.g., Morck, Strangeland, & Yeung, 2000) suggest that the family's desire for capital preservation, stability, and risk aversion keep the firm from pursuing strategies that might otherwise improve performance, but would also threaten the family's continued control. Conversely, research suggesting that family firm performance is superior to others usually explains this result with the argument that families are better stewards of firm resources because of an overall aversion to managerial opportunism. Recent research seems to provide compelling evidence of superior family firm performance (Miller et al., 2005).

However, as suggested earlier, we expect that there will be important differences among family firms. In other words, not all family-controlled firms are alike and therefore not all family controlled firms will perform similarly. We expect that in the community of family firms, some are more likely than others to seize upon the opportunities and advantages that links to the community other family firms provide.

To this point we argue that family firms will find important resources in the community of other family firms. These resources include, but are certainly not limited to,

strategic alignment, intercorporate learning, reduction in family conflict, and reliance on a set of trusted advisors. In this way we see family firms which take advantage of such resources as gaining an important competitive advantage *vis-à-vis* rivals. Therefore we expect that board linkages between family-controlled firms will, in general, be a positive influence on firm performance.

Proposition 5: For family-controlled corporations, there is a positive relationship between the ratio of board interlocks to other family firms and overall firm performance.

Discussion

Our article began with a puzzle. How have family businesses thrived and prospered despite the fact that they face all the costs and obstacles of nonfamily firms, plus the added risks and costs of intra-family conflict? We have argued that family-controlled firms operate in a community of similar firms, and that community's aim is to foster and maintain the family control and persistence. Further, we framed our ideas around social capital as a community-level shared resource, and director interlocks as a key mechanism through which resource is fostered and maintained. Through this community-level social capital, families might reduce or mitigate intra-family conflict. Previous literature addressing family-controlled firms in large part focuses on firm and individual levels of analysis and suggests that family-controlled firms will fare differently than other types of firms. However, previous empirical work has found conflicting bases for this differentiation, viewing family-controlled firms as influenced by generational and governance factors (Villalonga & Amit, 2006), ownership stake (Anderson, Mansi, & Reeb, 2003), governance and control mechanisms (La Porta et al., 1999), and risk seeking behavior (Gomez-Mejia et al., 2003). While recent research has tended to show family firms in a more favorable light than previously, most research still seems to proceed from the assumption that families are inefficient stewards and that that family-controlled firms are more likely to appropriate wealth at the expense of minority shareholders.

The presence of community-level social capital is not a panacea for family firms. Community-level social capital can have a very important impact, but its effects on individual members can also be quite weak. Individual family firms can take or leave the community-level resource, and it seems likely that at least some family firms will avoid interactions with other family businesses. Future research could empirically test the role of family firm interlocks in intra-family conflict. Further, studying the role of interlocks on the difficult issue of succession in family firms would also seem likely to bear fruit. Finally, we also expect, though we did not offer a formal proposal, that in addition to board interlocks, family business executives will also share a range of other civic and social collaborations.

Studies of community-level social capital are far less prominent than those of individual or firm-level social capital, but they do exist, and our study adds to that body of knowledge. Inkeles (2000) argued that community-level social capital was particularly relevant in situations of family, where there exists a dominant culture, where modes of communication are important and there is a tendency for trust between parties to exist. We have drawn upon those ideas here. Additionally, Putman's (1993a) work in Italy convincingly demonstrates that cooperating for mutual gain has benefits for not only the individual, but also the community. Through norms of mutual trust and reciprocity, economic entities build upon their shared experiences, history, and mutual associations.

Implications and Future Research Potential

We hope that our work will spur additional theoretical and empirical studies. First, recent research studying family-controlled firms has generated a number of high-quality investigations, most often aimed at understanding performance differentials. We suspect that putting the family firm under a community lens will generate some interesting new perspectives. For example, while the notion of community-based trust implies a closed network, who actually gets into the family firm network is worthy of study. Are only direct family members considered as part of the inner elite, or are nonkin executive interlocks from family firms also influential in maintaining and preserving the family firm structure? Family firm community studies on succession also seem particularly relevant. We might expect that family firms with histories of successful succession planning and implementation would be highly sought after by other family firms facing this issue.

Second, beyond family firm research, the community-level social capital approach seems relevant to current strategic management scholars. Going beyond traditional strategic group or network research, scholars might use community-level social capital to examine issues such as compensation, board structure, contagion, succession, mergers, and acquisitions strategies, to name just a few. Defining the level of analysis through group social capital based on trust, shared respect, mutual learning, and reciprocity, will likely bring some new insights into our thinking. For example, it is conceivable that CEO compensation, while certainly a complex and thoroughly investigated process, might be even more complex than is currently perceived. Community-based social capital, enhanced through membership in a community of, e.g., founder-led firms, professional service organizations, or nonprofit entities, if linked to compensation practices and norms across those communities, might open up a multitude of new avenues for research.

Third, further empirical work in this area is needed to fulfill the promise of the concept. We suggest the family firm context is a community from which to begin. As organizations build routines and develop norms of behavior, we need to understand, from theoretical and practical bases, how such business practices are established, reinforced, and maintained.

Limitations

Our work is not without its limitations. While we argue that the interconnectedness of family firms is an important influence in family firm longevity and performance, other scenarios should be investigated as competing explanations. Scholars who take up the challenge to test our notions empirically should control for, and be alert to, alternatives. For example, while family firms are widely dispersed throughout the economy, there is some clustering and prominence in various industries (Villalonga & Amit, 2006). Additionally, as McConnell and Servaes (1990) discovered, there is a curvilinear relationship between ownership and performance. While we are arguing that the curve may be a bit flatter for family firms *vis-à-vis* others, investigating this relationship, specifically for family run firms, is likely informative.

We also alluded to the notion that part of the rationale for family firms using the community of other firms as a social capital resource is to counter some of the inherent and unique costs associated with family control. However, it is likely that certain family firms have different costs of organizing than others and may elect, or not, to interlock with other family firms. An investigation into family firms that do, and do not, utilize family firm interlocks may shed some light on the applicability of our theory.

Conclusion

We began our study by asking what mechanisms family-controlled firms might use to preserve and maintain the family firm as a distinct organizational entity. We additionally wanted to explore how family-controlled firms that face differential and additional agency costs than other firms are able to resolve those differences and/or minimize those costs. We attempt to answer this through a community-level social capital perspective examining board of director interlocks. We suggest our view provides some new reasoning for the diffusion of board practices, norms of behavior, and maintenance of the status quo in family-controlled firms. Our belief is that, by viewing family-controlled firms through the prism of a community of family controlled-firms, we are able to gain some new insights and understanding into how and why these types of firms seem to persist, and even thrive, under a variety of circumstances and contexts. Our theory of interorganizational familiness is therefore premised on the assumption that family firms will seek out one another and strive to foster, and even enhance, the community of family-controlled firms.

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