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The mediating effect of ethical codes on the link between family firms and their social performance

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This article brings together research on social performance, codes of ethics and family firms. Using a panel dataset composed of 547 internationally listed companies for the period 2002–2010, we test empirically whether the use of formal ethical codes could be a reason to explain the differences between social performance in family and non-family firms. We empirically show that family firms tend to present a lower social performance than non-family firms, and the use of formal ethical codes mediate such relationship.

Introduction

Sustainability issues are beginning to play a renewed role in society, and social consciousness is gaining weight among citizens since it represents a way of integrating corporate business with social and environmental welfare. In this regard, social and environmental performance (i.e. corporate social performance) could be defined as a company's voluntary commitment to social development and environmental preservation, developed within the company's social sphere, as well as a responsible commitment to the people and social groups with whom the company interacts. It defines the company as a set of relationships, not just between owners and managers but also with parties or groups interested in the evolution of the company: employees, customers, suppliers, competitors, environment, and society (Adams, 2002).

Nonetheless, companies are profit-making entities, and very few would subscribe to the idea that they can be persuaded to commit to environmental and social policies that benefit the community at a cost to insiders. Because corporate aims, strategies, management forms, and governance systems differ considerably between family and non-family firms (Haalien and Huse, 2005), their social and environmental commitment may also differ.

In this respect, some previous studies (Déniz and Cabrera, 2005; Burak and Morante, 2007; López-Iturriaga and López-de-Foronda, 2011) agree, pointing out that family firms tend to have a lower social performance than non-family firms. Since family members have a relevant amount of investment in their own companies, they tend to be more committed to achieving the greatest possible financial return, relegating environmental and social commitment to the background.

However, little or nothing is known about the indirect determinants that may justify such behaviour. From a wide range of possibilities, this study focuses on the use of formal ethical codes in family firms because: (i) on the one hand, they are a common tool of social and environmental performance designed for the explicit details of sustainable commitment (Agatiello, 2008; Erwin, 2011); and (ii) on the other hand, the degree of formal mechanism varies according to family firms and non-family firms.

Concretely, this exploratory study proposes a mediating effect of formal ethical codes in the relationship between family ownership and social performance. This effect is tested on a sample of 547 international non-financial listed companies from different countries for the period 2002–2010. Our findings empirically confirm four statements: (i) family businesses tend to

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present a lower social performance than non-family firms; (ii) ethical codes play a key role in the effectiveness of achieving a good social performance; (iii) family firms are more likely to follow informal codes; and (iv) the lack of formal codes could be considered a reason for the lower social performance in family businesses. In other words, the lack of formal codes of ethics exerts an indirect impact on the family ownership–social performance relationship.

Therefore, this article is structured as follows: firstly, we describe the previous literature related to our study and subsequently develop arguments to propose our hypothesis; Section Method shows the methodological aspects, such as the sample, variables, and models for the empirical analysis (moreover, we include an annex providing an explanation of the measures of variables employed in our analyses); the results are presented and discussed in Section Results; and, finally, the contributions, implications, and limitations are summarized in Section Concluding remarks.

Theoretical background and hypothesis research

Considerable research has been conducted on the question of how family firms behave and, particularly, whether they behave differently from non-family firms. Significant differences have been identified in terms of corporate governance, leadership, performance, and succession (e.g. McConaughy et al., 2001; Klein et al., 2005; Brenes et al., 2011). However, the literature until now has overlooked other topics, such as corporate social responsibility (CSR) (Benavides-Velasco et al., 2013; Materne et al., 2013).

Although there is no universal definition of a family business, one of the most accepted definitions is the one proposed by Chen et al. (2008), who define a family firm as a business in which family founders continue in a top managerial position, are present on the board, or are able to act as blockholders. This means that they have great power and hold fundamental positions that affect the management and decision-making processes. Through their participation in management, family members seek to ensure the company's survival and vitality, as well as the transmission of its legacy (Singal, 2014) and goodwill (McVey and Draho, 2005) to their descendants.

One of the important management decisions nowadays is the level of commitment to social and environmental practices, which determines the level of corporate social performance. Traditionally, family firms have been characterized by non-financial aims, such as identity, reputation, longevity, and the preservation of a positive image in the public domain (Sharma et al., 1997; Anderson and Reeb, 2003; Berrone et al., 2010). In order to ensure the survival of the firm in the market, family firms can carry out actions approved by society, with the aim of satisfying stakeholders' demand, gaining a positive image, and legitimating the company.

However, these socially responsible actions pose a risk in relation to solid long-term financial performance. As Virakul et al. (2009) suggest, among the main motives for promoting socially responsible practices, it is necessary to note economically driven motivations. If family members run their business with a profit maximization aim, the conflict between social and economic goals may create a dilemma for the decision maker. For example, the risk of investing in expensive pollution prevention beyond compliance with regulations may not be compensated for by financial gains or the firm may never achieve a reliable cost–benefit estimate of such actions (Margolis and Walsh, 2003).

This is especially relevant to family businesses, since family members usually have large investments in their own firms, so they may be more interested in profitability and financial performance than in environmental issues (Burak and Morante, 2007). Most family businesses do not think that socially responsible practices generate competitive advantages, although some assume that they have the resources to carry them out; as such, they view these practices as a cost and not as an opportunity (Déniz and Cabrera, 2005). Therefore, we expect that family businesses tend to be less socially responsible than non-family firms, as Burak and Morante (2007) and López Iturriaga and López de Foronda (2011) find. However, until now, we have not identified any studies explaining the determinants of such behaviour.

In this respect, we expect that the existence of a formal ethical code may determine the social performance of a company. It should constitute “a distinct and formal document containing a set of prescriptions developed by and for a company to guide present and future behaviour on multiple issues of at least its managers and employees toward one another, the company, external stakeholders and/or society in general” (Kaptein and Schwartz, 2008, p. 113). Ethical codes transmit ethical values to the members of the organization (Wotruba et al., 2001), offering them moral guides or anchors when new and confusing situations are encountered in the workplace (Chua and Rahman, 2011) and in decision making (Urbany, 2005).

Codes of ethics are a common tool of social and environmental performance designed for the explicit details of sustainable commitment, affecting positively the promotion of such behaviour (Agatiello, 2008; Erwin, 2011). Therefore, the establishment of a formal code of ethics, as an effective guide (Mijatovic and Stokic, 2010), is related to a positive impact on the perceptions about the sustainable level within companies (Adams et al., 2001). Mijatovic and Stokic (2010) support a positive influence of transparent codes of conduct and corporate values on all types of sustainable issues and activities. Erwin (2011) shows a positive link between the quality of ethical codes and the probability of being included in the ranking of the most sustainable companies.

In the case of family businesses, they are likely to have a less formal mode of operating; thus, they tend to adopt fewer formal policies, systems, rules, etc. The organizational culture and climate tend to be informal in family businesses; we can even say that the business is the “lengthening shadow” of the founder family (Hollander and Elman, 1988). Thus, family firms appear not to rely primarily on formal codes of ethics since they are likely to operate with a lower degree of formalization (Adams et al., 1996), showing great trust in their values without needing formal rules or codes. It is therefore less likely that