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From institutional duality to institutional trifecta: Implications for family firms' international subsidiaries

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From Institutional Duality to Institutional Trifecta: Implications for Family Firms' International Subsidiaries

Introduction

Family enterprises are playing increasingly important roles in contributing to the global economy through internationalization (De Massis *et al.*, 2018). In recent years, more family firms have adopted forms of internationalization involving higher levels of commitment and become multinational corporations with subsidiaries in many different countries (Cesinger *et al.*, 2016). Such activity introduces new challenges to family managers to do with cross-border management, adaptation to new institutions and transfer of capabilities. This results in the family firm being exposed simultaneously to at least two types of pressure: the family's desire to protect and preserve its decision rights over its subsidiaries against institutional pressures to conform to rules, regulations and standards different to its domestic market.

The extant literature established that subsidiaries are subject to institutional duality (Kostova and Roth, 2002). This duality results from external institutional pressure on the subsidiary to adapt to laws, regulations and normative rules intended to dictate legitimate behaviour, while the subsidiary is also subject to internal pressure from the corporate parent to adopt its own approved best practice. Externally, institutions in the host countries can differentially influence firms' internationalisation, both in terms of the processes of internationalisation and its results (Meyer *et al.*, 2009). First, institutions are seen as the rules of the game in the foreign country market, and will therefore have an effect on the behaviour of the firm. Moreover, firms directly investing in a foreign market with a new subsidiary typically must adjust their behaviours to the 'rules of the game' as defined by the host country's institutions. This adjustment occurs as a response to coercive and mimetic institutional isomorphism (DiMaggio and Powell, 1983) and can affect the subsidiary's performance in the foreign market (Mellahi *et al.*, 2013). Internally, the corporate parent places its own institutional pressure on the subsidiary to adopt established practices that render legitimacy in the eyes of the parent. This pressure competes with the subsidiary's efforts to adjust to external institutional pressure (Hughes *et al.*, 2017).

However, we argue that the family itself introduces an important institutional pressure unique to their subsidiaries. We theorize that family firms' international subsidiaries are subject to a third institutional force, creating an institutional *trifecta*, that fundamentally affect the prospects of the family subsidiary. Specifically, we predict that: (1) the desire of family owners and managers in the domestic parental family firm to retain family control and family influence create a new third institutional pressure acting simultaneously on the family subsidiary; (2) that materially affect the behaviour and outcome of the subsidiary; and (3) potentially its survival by preventing the subsidiary from adapting to essential external institutional pressures. Given these institutional pressures, we are led by the following research question: how does the institutional trifecta manifest in the family subsidiary? How do family subsidiaries manage these trifecta of institutional pressures? What are the consequences for the family subsidiary from this institutional trifecta?

We contribute to the family firm and international business literatures in two ways. First, we break new ground in the application of institutional theory in international business studies by conceptualizing a third institutional force acting the international subsidiaries of

multinational family businesses: the family institution. Second, we introduce the notion of institutional trifecta and propose how the subsidiary is shaped and affected by the synergy of these forces.

Preliminary Literature Review and Background

Family Firm Behaviour

The central theory setting predictions of the behaviours and features of family firms is socioemotional wealth (SEW) theory (Berrone, Cruz and Gomez-Mejia, 2012). SEW theory suggests that a unique motivation of family firms in shaping any business operation is to protect family control, influence, and perpetuate family independence, protecting the family firms' assets from appropriation from any parties other than the family members (Berrone *et al.*, 2010). SEW represents nonfinancial wealth and is considered to be more important to family firms than financial wealth (Gomez-Mejia, Neacsu and Martin, 2017). Therefore, family firms are prone to take higher risks to protect SEW (Chrisman and Patel, 2012).

Research on family firms' internationalisation processes shows that they tend to follow the establish chain (Johanson and Vahlne, 1977) of slowly accumulating knowledge of the foreign market to internationalize gradually in more controlled and measured ways to preserve family control over the business (Cesinger *et al.*, 2016). Family firms tend to avoid international entry modes that could threaten family control and SEW (Pisano, 2018). Therefore, when using high commitment entry modes, family firms will rarely involve outside agents, organisations and members (Pukall and Calabrò, 2014). Foreign direct investment (FDI) in which international subsidiaries are created places the family's wealth, financial and nonfinancial, at significant risk. Family firms with international subsidiaries face tremendous barriers that can interfere with their control and overseas management activities of the subsidiary (Buckley, 1989). The crucial areas of the family firm subsidiary that needs investigating include external institutional pressure to adopt domestic practices, parent firm pressure to accept the transfer of capabilities irrespective of the host market, and the family's governance of the subsidiary, and their collective and competing implications for the subsidiary.

Institutional Isomorphic Pressures to Adapt to the Host Market

Neo-institutional theory introduces institutional isomorphism as a mechanism to predict subsidiary behaviour in the host country (Kostova, Roth and Dacin, 2008). Isomorphism is a constraining process when pressures created by institutions in host country force the subsidiary to follow the behavioural or structural patterns of other organisations that face the same set of institutional conditions (DiMaggio and Powell, 1983). Institutions include formal and informal rules of the game that are confronted with subsidiaries in the markets where they operate, such as laws, regulations and cultures (Dacin, Goodstein and Scott, 2002). Coercive isomorphism predicts subsidiaries' actions under conformist pressures from formal and informal institutions which determine the access to critical resources the organisations depend on to survive and compete in the host country (DiMaggio and Powell, 1983). Mimetic isomorphism predicts that subsidiaries undergoing uncertainty over the business environment in the host country combined with unclear goals from the company, ill-defined performance measures and poorly

understood technologies, would alter their structures or behaviours to mimic other companies in the same organisational field (DiMaggio and Powell, 1983). Previous studies have indicated the tendency for subsidiaries under coercive and mimetic pressures to replicate constructs of other firms (Meyer and Rowan, 1977) including conversion to homogenous organisational form (D'Aunno, Succi and Alexander, 2000), adoption of a certain operating system, and firm strategy (Lee and Pennings, 2016).

Conformity to the institutional isomorphism by adopting particular templates of organising and operating in a locally accepted way can gain legitimacy domestically (Dacin, Goodstein and Scott, 2002). Subsidiaries require the endorsement of local social actors including government, business partners, customers, and the general public who are the important sources of support including social capital resources (Chan and Makino, 2007), material resources and technical information to survive and thrive in their social environments (Barney, 1991), and therefore have to conform to their prescriptions (Webb *et al.*, 2009). On the other hand, any forces preventing subsidiaries from adapting to the external institutions may lead to failure in being legitimate with any interests group, which could cause problems that threaten the survival of subsidiaries in the foreign market (Kostova and Zaheer, 1999).

Parental Pressure to Receive the Transfer of Capabilities

Institutionally, corporate parents exert their own institutional pressures on their subsidiaries to conform to practices deemed legitimate in the eyes of the parent (Kostova and Roth, 2002; Kostova, Roth and Dacin, 2008). In such instances, the pressure manifests as a desire for the subsidiary to accept and receive the transfer of best practices from the corporate parents – practices historically associated with competitive advantages (Mellahi *et al.*, 2013). Organizational practices are valued by corporate parents as critical firm resources capabilities that are the fundamental for subsidiaries to succeed (Helfat and Winter, 2011). Studies have found empirical evidence supporting that successful transfer of parent's best practice are positively related to subsidiary performance to some extent (Hughes *et al.*, 2017). According to Tsai and Ghoshal (1998), the relationship between the subsidiary and the parent matters. Specifically, subsidiaries recognising the value and trusting the efficiency of the practices transferred from the parent will enhance their adoption of the practices.

As the transferred practice is established as firm's capability over time, the more exactly a practice is duplicated by a subsidiary from its parent, the more legitimate the subsidiary might be internally (Chang, *et al.*, 2009), and the more support the subsidiary will gain from the parent (Kostova and Roth, 2002). However, these historically best practices transferred from the corporate parent may not be judged as legitimate in the host country, thus creating a competing institutional duality acting on the subsidiary. For example, consistent findings have shown certain HRM practices are taken by MNEs as tools of controlling and managing their subsidiaries with rare adaptation to the host environment (Lervik and Björkman, 2007). The danger to the subsidiary in loyally adopting parental practices for parental legitimacy is that it loses the opportunity to adjust to external institutional pressure to adopt competing host practices and fails in gaining legitimacy with external environment (Mellahi *et al.*, 2013).

Family Pressure to Protect Ownership and Influence

A commonly used definition of family business was proposed by Chua, Chrisman and Sharma, (1999) that “the family business is a business governed and/or managed with the intention to shape and pursue the vision of the business held by a dominant coalition controlled by members of the same family or a small number of families in a manner that is potentially sustainable across generations of the family or families”. The way family business is defined reveals that a basic feature of the family firm is its unique composition of the management team- team members are also family members. The defining feature of the family managerial configuration can differentially influence the internationalisation of the family business (Cerrato and Piva, 2012; Calabrò *et al.*, 2013). Studies have found that family members in the top management team are motivated by coherent family goals, aspiring to higher level of business commitment and lower agency cost (Anderson and Reeb, 2016). Family firms can take advantage of the potential for lower agency costs (Jensen and Meckling, 1976) and elicit attitudes of stewardship (Miller and Le Breton-Miller, 2006) if the managers expatriated to the overseas subsidiary belongs to the family of business owners.

Expatriate assignment is normally used as a strategy by MNCs to transfer organisational capabilities across borders by sending experienced executives with extensive knowledge in the host market, for the purpose of enhancing success and minimising failure of business (Kawai and Chung, 2018). However, to protect the family ownership and control, family firms will expatriate family members to take over international subsidiary albeit their experience or expertise in the foreign market where the subsidiary operates does not suffice. The subsidiary would suffer problems of such sub-optimal appointment of executives who play a crucial part in deciding the subsidiary’s strategy and activities (Hambrick and Mason, 1984), which is a hidden danger to the survival of family firm subsidiary as well as the prospect to the family business. Therefore we argue that family owners of the business can introduce an unique pressure to family firms subsidiaries through expatriating family members as executives of the international subsidiary to maintain family control.

Conceptual Framework

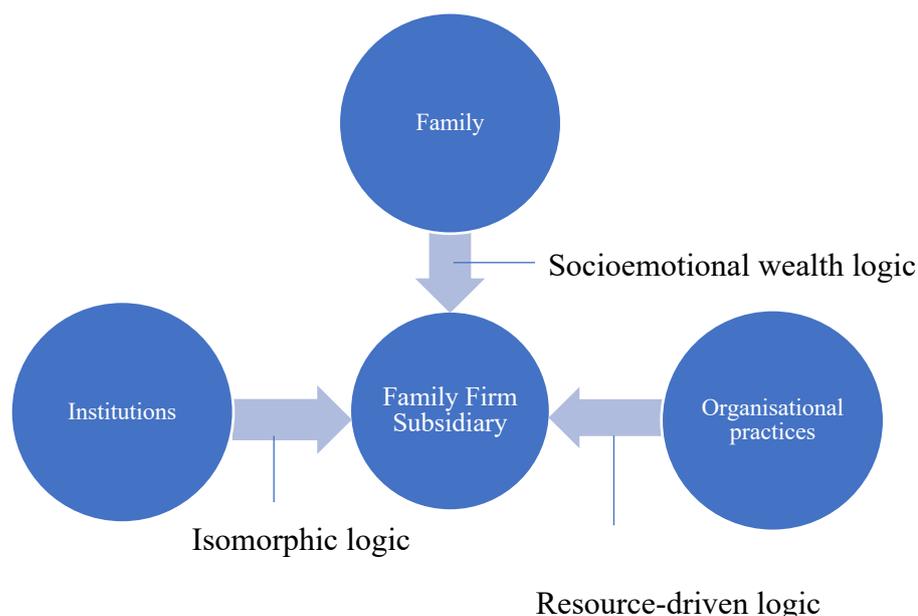


Figure 1 Institutional Trifecta Acting on Family Firms’ International Subsidiary

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