

Comparison of Governance Cases in Owner-Managed SMEs

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ABSTRACT ¹

Small and medium-sized enterprises (SMEs) represent in Europe up to 99% of all businesses and provide two-thirds of the total employment in private sector. However, business literature as well as training programs often tend to use large companies and corporations as best practice examples for setting up management practices.

This research review existing literature on governance and management system development in context of small and medium enterprises and compare findings with three small-medium-sized companies from different European countries.

Companies analyzed demonstrate different ways of setting up management system and processes to achieve positive financial and market results. This leads to conclusion that it is essential to achieve fit of management system elements to business circumstances, rather implementing selected good practices. For small and medium enterprises, this is even more important, as they are characterized by limited resources and competences. This paper enlighten challenges SMEs are facing and some possible solutions that will contribute to improving their management and sustainability.

Keywords: Small and medium-sized enterprises. Governance. Management system. Management processes. Owner-manager.

1. INTRODUCTION

Small and medium-sized enterprises (SMEs) play a significant role in most economies. In Europe SMEs represent up to 99% of all businesses and provide two-thirds of the total employment in private sector [1]. Compared with larger organizations, SMEs have limited

internal resources and internal knowledge, and shall use external knowledge. However, business literature as well as training programs often tend to use large enterprises and corporations as best practice examples for setting up management practices, and often they are no appropriate for SMEs.

There is also a high diversity in the SME sector. These companies represent almost all business sectors, have different operational patterns, different cultures, different growth potentials, and no single recommendation could fit them all. Large proportion of small and medium sized enterprises is owned by individuals or by families and at the same time managed by their founders or owners. Managerial style of these entrepreneurs is influenced by a series of demographic and situational factors, personal values and views.

New situation, which is characterized with globalization, development of new technologies, increasing customer expectations, pressure on prices and other emerging issues is putting serious challenges on small and medium enterprises and their management to maintain future growth and sustainability of business.

Purpose of this article is to enlighten challenges SMEs are facing in development of their management practices and draw possible solutions that will contribute to improving SME management and sustainability.

Methods: Research is based on a literature review using the state-of-the-art method to understand previous research on governance and management system development in small and medium enterprises and owner-managed companies in particular. Then structured interviews with owners-managers of three small-medium sized companies are conducted to identify underlying factors and particularities on how management system is developed in these companies. Cases are compared in order to find possible similarities and differences across different companies and diverse business environments.

Findings/Results: This paper enlighten challenges that SMEs are facing in context of current business

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environment and contribute to discussion on possible solutions that improve the SMEs management and sustainability.

2. LITERATURE REVIEW

Literature review includes recent theoretical and empiric findings on governance and management system development with particular focus on small and medium businesses and owner-managed companies.

The concept of "governance" is not new, however, there is no universally accepted definition. According to Bevir, governance refers to all processes of governing, whether undertaken by a government, market, or network, whether over a family, tribe, formal or informal organization, or territory, and whether through laws, norms, power or language. Governance differs from government as it focuses less on the state and its institutions and more on social practices and activities [2].

Governance can be used in several contexts such as corporate governance, international governance, national governance and local governance. In 1992 the World Bank introduced "good governance" as part of its criteria for lending to developing countries [3]. Major donors and international financial institutions are increasingly basing their aid and loans on the condition that reforms that ensure "good governance" are undertaken. Good governance assures that corruption is minimized, the views of minorities are taken into account and that the voices of the most vulnerable in society are heard in decision-making. Simply put, "governance" means: the process of decision-making and the process by which decisions are implemented or not implemented [4].

OECD Principles of Corporate Governance, first published in 1999, has become an international benchmark and help policy makers evaluate and improve the legal, regulatory, and institutional framework for corporate governance, with a view to supporting economic efficiency, sustainable growth and financial stability [5].

Governance can be defined also as: "The system by which entities are directed and controlled. It is concerned with structure and processes for decision making, accountability, control and behavior at the top of an entity. Governance influences how an organization's objectives are set and achieved, how risk is monitored and addressed and how performance is optimized". Governance is a system and process, not a single activity and therefore successful implementation of a good governance strategy requires a systematic approach that incorporates strategic planning, risk management and performance management [6].

Meaning of governance is close to the meaning of management. There are also several interpretations in literature what is the management system.

Management system, according to Kaplan and Norton, is the integrated set of processes and tools that a company uses to develop its strategy, translate into operational terms and monitor and improve effectiveness of both. Along with definition, they suggest a concept, called the Balanced Scorecard, which integrates Financial, Market, Process and Development dimensions of business and link various financial and non-financial aspects of business by defined cause and effect relationships [7].

More often term Management system is used in particular context like Quality management system, Environmental management system, marketing management system, and others. International Organization for Standardization (ISO) has developed series of recommendations for management systems. One of the first and most popular set of recommendations is for the quality management systems, named as ISO-9000 series [8]. ISO-9000 series defines fundamentals of quality management systems, while other series of standards defines principles for managing environmental (ISO-14000 series), risk management (ISO-31000 series), IT (ISO/IEC-20000 series), Food Safety (ISO-22000 series) and other aspects of business. In addition, a set of quality management principles are defined, covering seven areas - Customer focus, Leadership, Engagement of people, Process approach, Improvement, Evidence-based decision making, Relationship management [9].

Implementation of the management system itself can be described as a process. Garengo and Biazzo suggest the framework process for implementation of management systems in SME in an integrative way, called Integrated Management system (IMS). Their framework is based on changeover from the adoption of separate ISO quality standards to the implementation of an IMS [10].

In systems' engineering the Management system assumes set of dedicated IT tools and technologies for monitoring and controlling processes in enterprise or technological system. There are attempts also to clarify the concept of business models, its usages, and its roles in the Information Systems domain [11]. This is essential for companies, which employ technologies and Information system in sales, logistics, customer care or manufacturing processes.

For a SME with own limits in knowledge and resources, there are several challenges: to understand variety of terminology, handle specific language of recommendations and select appropriate principles for particular business and appropriate way for their implementation.

Changes in external environment puts other challenges on SMEs. Last decades show that consumers get increasing choices of products and services, and companies have to shift away from product-centric and company-centric approaches to customer and value-centric approaches. Value creation in company and selecting appropriate business model have become dominant themes for managers and described in series of publications by Porter [12] and Prahalad [13]. The process of value creation can be done independently, but it requires links to an external environment in order to be innovative [14]. Business modelling approach proposed by Osterwalder and Pigneur [15] suggest to link Value proposition to Customer segments through Relationship and Delivery Channels, and link it with Key suppliers through Key resources and processes.

Business model thinking intends to show value creation logic for company, and it is valuable approach, However, language and elements in a business modelling approach to some extent overlaps with language and elements in the Management system approach. While academics and business consultants can handle this complexity in own way, this can be confusing for SME management.

Organization structure or organization design is one aspect of the management system. According to Daft, challenges in today's environment are leading to changes in organization design and management practices - many managers are redesigning companies towards the learning organization, which is characterized by a horizontal structure, empowered employees, shared information, collaborative strategy and an adaptive culture [16].

Small and medium enterprises have limited internal resources and internal knowledge and shall use external knowledge; however, diversity in the SME sector is high. Chesbrough et.al identified several trends how open innovation develops. One of trends is that innovation goes from large companies to SMEs. Other trend is that industry is starting to professionalize the internal processes to manage open innovation more effectively and efficiently. Nevertheless, it is currently still more trial and error than a professionally managed process [17].

There are more and more controversial evidences of particular concepts having impact on organizations, their performance and processes. According to Yusr, the arguments on the relationship between Total Quality Management (TQM) and innovation have been classified into two groups: the first group supports the positive relationship between TQM and innovation, whereas the second group claims that TQM does not support innovation in firms [18].

Literature still more focuses upon large organizations, and many questions on how to develop management

system in small and medium enterprises remains unanswered.

Empirical large-scale survey of owner-managed small and medium sized enterprises (SMEs) conducted in the UK draw evidence and explored the association of small business managerial style and performance. Survey revealed that the managerial style of entrepreneurs is influenced by a series of demographic and situational factors, and owner-managed businesses characterized by delegation of authority appear to achieve higher growth in sales and operationalize in a more professional way [19].

For an owner-managed company, entrepreneurial behavior of owner-manager is affected by their personal values and views. Jaouen & Lasch suggested a new typology of owner-managers exploring the extent to which the views of owner-managers regarding growth and lifestyle issues, such as success, subsistence, hedonism and paternalism, affect their entrepreneurial behavior [20].

According to literature, owner and manager personality also influence the way how company is managed, and its performance. For an owner-manager this puts one more challenge - to deal with company issues and at the same time handle own personal development.

This article looks on governance and management system development in the small and medium-sized companies linking both system and process aspects with the role of the owner-manager in company.

3. METHODOLOGY

Research is based on a literature review using the state-of-the-art method to understand previous research on governance and management system development in small and medium enterprises and owner-managed companies in particular. Then structured in-depth interview with owners-managers of small-medium sized companies are conducted to identify underlying factors and particularities of how management system is developed in selected companies. Interview questions were formed to cover main elements and approaches for governance and management system development.

All three companies are small-medium sized enterprises and represent services, production and trade segments from three countries. Company A is a marketing services and training company from Netherlands. Company B produces design and promotional products using advanced technologies and is based in France. Company C is the B2B products supplies company from Latvia. All three companies are managed by their owners. All companies have positive financial situation, loyal customer base and no major operational problems.

In-depth interviews were conducted to identify background and ways how company owners-managers drive companies management system development. Interview results were compared among companies interviewed and with key findings from literature review.

4. RESULTS AND DISCUSSION

All three companies described in this article operates in comparable business areas, which includes providing professional services in B2B segments, have elements of production and some additional services. All three companies have positive financial and market results, and have no major operational malfunctions.

Company analysis through interviews show that there are differences how management practices are established and developed. These differences are mainly driven by

owners-founders and are not country or local business culture specific. Summary of company analysis derived through interviews is provided in Table 1.

There are differences among companies in organization and structure. Company A, in fact, is combination of three legal entities (enterprises), all with similar ownership structure, each with own brand name, where one enterprise is often involved as subcontractor for other enterprise in their customer's projects. Company B keeps smaller core team of permanent employees and use a larger network of freelance specialists who are involved in their customer projects in accordance to current needs and required competences. Company C has established own production capacity for particular product line, have own sales force, call center and delivery fleet, and each business unit has dedicated manager in charge.

Table 1: Comparison of governance practices in Company A, B and C

| Company A | Company B | Company C |
|---|---|---|
| Main business area | | |
| Marketing services and sales staff training for Business to business (B2B) customers. | Production of customized high-end technology-based products for B2B customers. | Business to Business (B2B) product supplies and production. |
| Organization model | | |
| Three interrelated enterprises working together and forming up one business. | One compact-sized professional company with a large freelancer network. | One company with fully equipped sales, production and delivery staff and resources |
| Defining strategy and policies | | |
| No written strategy. Market goals are set. Key principles are defined and reminded during project work. | Focus on short-medium tasks to develop business. Founders have vision and shared view on company development. | Strategy planning sessions were conducted with key team. Goals, plans and principles are written and followed-up. |
| Defined long term goal | | |
| Exit strategy - to sell business to larger market player in next few years. | Develop market and deploy further technologies. | Stabilization of business, increase of efficiency and profitability. |
| Culture and communication | | |
| Open communication with all employees, customers, partners. | Professionals at work and family-like outside the office. | Objectives and KPIs to be achieved with professional attitudes. |
| Process management | | |
| Formalizing best project practices to ensure best offer and service to customers. | Learning on the way. Understanding process and opportunities to select most appropriate way of work. | Key processes (sales, production, deliver) are defined and formalized in ISO-9000 certified system. |
| Motivation system | | |
| Salaries are defined in combination with project-based motivation approach. | Professional level salaries. Importance of informal family-like environment. Relevant fees for freelancers. | Combination of salary and performance-based bonus system. |
| Target market/ Target area | | |
| International (several locations in a few countries) | Country-wide, single country, limited to use of national language. | Country-wide in a few defined geographical service areas. |
| Role of Co-Owners/ Partners in company | | |
| Both co-owners are professionals in core business (marketing). | One is professional in core business area, other - in financial and administrative issues. | One is a founder and business developer; another is a business manager and administrator. |

Companies A and B both does not have formalized and written strategy. Founders of companies A and B have defined few essential principles which are shared and reminded to employees and also freelancers during regular work and customer projects. Company C has arranged series of workshops with key managers and specialists to formulate and write down key principles, objectives and implementation plans.

Company A uses extensive and open communication with staff, customers and business partners about business trends, customer needs, technology development. Company B tends to maintain professional relationships during projects and family-like environment outside working hours, arranging informal dinners and weekends for team members. Company C defines processes, sets targets and Key performance indicators (KPIs) for various business aspects, keeping informal relationships to a limited level.

Companies A and C use certain IT platforms to support their daily processes, and main operating procedures are aligned with IT processes. Company C has undergone their management system and processes certification according to international ISO-9000 series recommendations. Company B maintains flexibility to follow established processes or maintain certain standards, depending on customer project. Company B, as it employs relatively new technology, is gradually gathering best practices and currently has no defined plans to define standardized processes and approaches.

All three companies have similarities in ownership structure, as companies have two partners as co-owners. However, there are different roles of co-owners. Co-owners also have different long-term intentions. Both partners-founders of Company A are professionals in their field, and have common intent to sell their company to some larger market player in few years. Therefore, current intents are to ensure stability and growth of business and establish professional management that will allow both founders to exit business at some point of time. Founder of Company C invited his partner to join his company at later point of time as a professional manager and granted this partner certain number of company shares. Founder of Company C want that company bring him stable financial benefit in a long term and will enable him to invest his time and resources in other business projects. Company B has two founders – one has strong professional background in the core business, other keeps focus on financial and administrative issues. Company B keeps primary focus on business development and technology deployment and have no defined exit criteria for business at current stage of development.

During interviews every owner-manager was able to recognize and name some management practices or management system elements, which were ultimately

eliminated as inappropriate or ineffective for their particular company or situation. It shall be noted that practices such as ‘Delegation of authority’, ‘Weekly staff meeting’, ‘Formalized procedures’ were named among eliminated practices by some of companies interviewed, while similar practices are found to be effective in other companies.

Companies described in this research have some similarities in ownership structure and business areas. All companies have two owners-partners. All companies provide services in B2B segment and have value proposition including professional services, production of definite product range and product delivery to customers.

Although companies represent different countries and different markets, owners-managers have expressed several similar challenges in respect to their managerial and leadership abilities: communication to staff and customers, management of personal time and prioritization of own work, stress management, personal appearance. Also, the balance between private and professional life and personal values were named among factors that influence their managerial role in their companies.

All three companies have positive financial and market results and no major operational problems. However, there are more differences than similarities in way how management system and key principles are set up. Every company is setting up their system in their own way, based very much on owner’s own preferences, company circumstances and own learning process.

For these three companies there is no one single element that leads to positive result, but the combination of elements that well fits company situation and business circumstances.

5. RESEARCH LIMITATIONS/ IMPLICATIONS

This paper focuses on a governance and a management system as a general set of tools and processes in a company, and not specifically on management IT solutions what enterprises use for resource planning, performance management or other management processes.

Conclusions from this research are relevant to those particular medium-sized companies analyzed, and shall not be generalized without additional research and validation.

This particular research does not cover topics of management during global crisis as interviews were conducted before wide COVID-19 pandemic restrictions took place.

6. CONCLUSIONS

This research enlightens some challenges that SMEs are facing in context of current business environment, at least:

- Compared with larger organizations, SMEs have limited internal resources and internal knowledge, and shall use external knowledge.
- Academic and business literature, training programs and business consultants often use large companies as an example, use wide and difficult to understand terminology, specific language, formal recommendations, which create difficulties to select the most appropriate approaches and appropriate way for their implementation in SMEs.
- There is a high diversity in the SME sector as these companies represents almost all business sectors, have different operational patterns, different cultures, different growth potentials, and there are controversial experiences on how one or another approach impacts company, its performance and results.
- Success of company depends both on implementation of management practices and handling multiple personality factors of owners, managers and staff.

Three companies analyzed in this research demonstrate that they achieve positive financial and market results by applying different and sometimes controversial principles, and implementing governance practices in different ways. Valid conclusion for these three companies is that there is no one single element that leads to positive result. Combination of several elements that well fits company situation and business circumstances is essential for success. Selection of governance approach and implementation of management system is driven by personal preferences and abilities of owner-manager.

It is essential to achieve fit of management system elements to business circumstances rather than implementing particular governance practices. For small and medium enterprises, this is even more important, as they are characterized by limited resources and competences. This also drives need to provide simple and easy way to use concepts, avoid misunderstandings and overlaps in management system, business model, strategy and other recognized management concepts.

Authors expect that this research will contribute to discussion on possible solutions that improve the SMEs management and sustainability. Conclusions from this research are relevant to those particular companies analyzed in this research, and shall not be generalized without additional research and validation. Other enterprises can use outcomes of this research to analyze their governance and management practices. Further analysis of the internal and external factors affecting SME management system and performance should be considered.

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