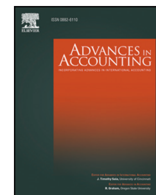
Advances in Accounting, incorporating Advances in International Accounting xxx (2016) xxx–xxx

Contents lists available at ScienceDirect

Advances in Accounting, incorporating Advances in International Accounting

journal homepage: www.elsevier.com/locate/adiac



The influence of family firm dynamics on voluntary disclosures☆

Joanna Golden [a], Mark J. Kohlbeck [b,*]

[a] University of Memphis, United States
[b] Florida Atlantic University, United States

ARTICLE INFO

Article history:
Received 2 September 2015
Received in revised form 21 November 2016
Accepted 22 November 2016
Available online xxxx

Keywords:
Family firms
Voluntary disclosure
Management forecasts
Stock-based incentives

ABSTRACT

We examine the voluntary disclosure practices of family firms. Family firms have longer investment horizons and lower agency conflicts between owners and managers. However, they also exhibit higher agency conflicts between controlling and non-controlling shareholders, and greater concerns about their own reputations. We therefore hypothesize that the previously documented association between stock-based incentives and voluntary disclosures is dampened for family firms. In comparison to non-family firms, we find that family firms are less likely to provide management earnings forecasts when their CEO's wealth (linked to the firm) is higher. We note this influence only in larger firms, which is consistent with the finding that larger firms have a significantly higher number of stock-based incentives than smaller firms. Additionally, the main result continues to hold when a family member serves as CEO or on the board of directors. We contribute to the literature by extending the research on stock-based incentives and voluntary disclosure, linking this research to family firms, and providing insight on the conflicting results found in prior family firm research.

© 2016 Elsevier Ltd. All rights reserved.

1. Introduction

Family firms play a critical role in the economy. A family firm is defined as any company where the founders or their descendants maintain positions in top management, as board members, or are among the company's largest stockholders (BusinessWeek, 2003). Family firms represent approximately 33 and 46% of the Standard and Poor's (S&P) 500 and 1500 index firms, respectively, and cover a broad range of industries. For example, two-thirds of S&P 1500 companies in the following sectors are family firms: high-tech industries (e.g., pharmaceuticals and electronic equipment), wholesale and retail, transportation, and printing and publishing. Family firms also account for over 30% of companies in capital-intensive industries (steel works, machinery, automobile, petroleum, and natural gas), regulated industries (banking and insurance companies), and the business supplies industry (Cheng, 2014). However, our understanding of family firms' influence on voluntary disclosure is limited. In this paper, we investigate the incremental family firm effect concerning the relationship between CEOs' stock-based incentives and voluntary disclosure (management forecasts).

Agency problems emerge when the principal owner of a firm delegates decision-making authority to the firm's managers. The owner can minimize such problems by providing incentives that encourage the managers to align their interests with those of the owner (Schulze, Lubatkin, Dino, & Buchholtz, 2001). One way to align managers' and investors' interests is through stock-based incentives. As a result, manager disclosures can mitigate agency problems, reduce contracting costs, and lower the risks associated with mis-valuation (Healy & Palepu, 2001). In addition, managers with stock-based incentives may voluntarily disclose information to increase the liquidity of the firm's stock, which results in a higher stock price. Nagar, Nanda, and Wysocki (2003) document that stock-based incentives encourage managers to provide private information to shareholders; however, the researchers do not address whether family firm dynamics influence this relationship.

When the owner manages a firm, the cost of decreasing information asymmetry between managers and shareholders, as well as the accompanying moral hazards, are the lowest (Jensen & Meckling, 1976). As a result, a family firm is one of the least costly forms of organizational governance (Daily & Dollinger, 1992; Kang, 2000). The principal source of agency costs for a firm is the separation of ownership and control (Jensen & Meckling, 1976). When the firm is managed by a single owner or group of owners (that is, a family group), these costs are eliminated or minimized. Owner management reduces the disclosure agency problem by naturally aligning the managers' and owners' interests (Schulze et al., 2001). As a result, stock-based incentives to encourage management to voluntarily disclose private information are not as important to family firms as they are to non-family firms.

☆ We appreciate helpful comments and suggestions on earlier versions from Jian Cao, Shirley Hsieh, Matthew Magilke, Maya Thevenot, and workshop participants at Florida Atlantic University.

* Corresponding author at: School of Accounting, Florida Atlantic University, 777 Glades Road, Boca Raton, FL 33431, United States.
E-mail address: mkohlbec@fau.edu (M. J. Kohlbeck).

http://dx.doi.org/10.1016/j.adiac.2016.11.003
0882-6110/© 2016 Elsevier Ltd. All rights reserved.

Most family firm agency problems exist between controlling and non-controlling shareholders. If a control position is maintained, the family members can use the companies to generate private benefits that are not shared by the other shareholders (Shleifer & Vishny, 1997). Therefore, when family firms engage in private rent-seeking activities, they may be reluctant to disclose their private information to the market for fear of increasing litigation risk.

Jensen and Meckling (1976) indicate that incentive-based compensation should not impact family agent performance because the family's personal wealth is already tied to the value of the firm. Consistent with this argument, family firms tend to build and protect their reputations. Family owners have longer investment horizons than other shareholders and generally consider their ownership to be an asset to pass on to future generations. As William Lauder, grandson of the founder of *Estee Lauder*, commented: “I am committed to the company. It's the vast majority of my personal wealth and my family's personal wealth—and we fully expect to be actively involved with this company going forward” (Byron & Lublin, 2007; Cheng, 2014). With a longer horizon, family owners may be more concerned about the firm's long-term value than their own short-term gain, and therefore may consider the disclosure of timely information to be less important (Salvato & Moores, 2010). Taking all these factors into account, we expect to find that the association between stock-based incentives and voluntary disclosures for family firms is dampened or eliminated.

Our sample is based on the S&P 1500 firms from 1996 to 2000. Following Nagar et al. (2003), we investigate two forms of stock-based incentives: stock-based compensation and CEO ownership of the firm (CEO wealth). We find CEO wealth, but not stock-based compensation, to be associated with the existence and frequency of management forecasts, which are muted for family firms. The dampening effect is further limited to larger family firms, consistent with our prediction that proprietary cost incentive dominates the capital market incentive for family firms. Overall, our findings suggest that stock-based compensation is not as effective as CEO wealth in encouraging disclosure. Moreover, we determine that both are generally ineffective for family firms, and that larger family firms reduce their reliance on stock price-based incentives to encourage managers to disclose private information. In addition, our results pertaining to the likelihood of issuing management guidance and the frequency of management guidance generally hold when a family member serves as CEO or on the board of directors, but are weaker when the family members are the largest shareholder and the agency cost are greater.

Our study contributes to prior research in at least three ways. First, we extend the research on stock-based incentives and voluntary disclosure. The literature on corporate governance shows that managers, when not monitored by shareholders, make decisions that maximize their own wealth but may not be in the best interests of the shareholders (Hope & Thomas, 2008). Voluntary disclosure is one form of shareholder monitoring. Shareholders use stock-based incentives to align the managers' and investors' interests and to encourage management to disclose private information. However, the prior literature on voluntary disclosure tends to treat shareholders as a homogeneous group; research in this area may not be relevant to family firms, since the agency problem between managers and shareholders is less pronounced. Family firms and non-family firms also have different goals and incentives. We demonstrate that CEOs' stock-based incentives to encourage voluntary disclosure are weaker in family firms than in non-family firms.

Second, we establish a link between family firms and the overall research on voluntary disclosure. Shareholders generally prefer more voluntary disclosure and encourage managers to release timely information through equity incentives (e.g., Core, 2001). Prior research does not address the impact of family firms on this relationship. We contribute to this analysis by showing how the differences in agency problems across family firms and non-family firms affect their voluntary disclosure decisions when their CEOs have stock-based incentives. In addition, our study extends Chen, Chen, and Cheng (2008), which document that family firms disclose fewer earnings forecasts and hold fewer conference calls, but provide more earnings warnings than do non-family firms.

Third, we shed light on the conflicting results of prior studies on family firms and voluntary disclosure. Several studies find that family firms are less likely to voluntarily disclose information (e.g., Lakhal, 2005; Chen et al., 2008). These studies argue that the owners of family firms are actively involved in their firms' management, reducing the information asymmetry between themselves and their managers. Therefore, there is less demand from non-family owners for information disclosure (Salvato & Moores, 2010). In contrast, other researchers determine that family firms are more likely to provide voluntary disclosure (Ali, Chen, & Radhakprishnan, 2007; Hutton, 2007). They argue that the less severe agency problems within family firms result in less opportunistic behavior, particularly in terms of the withholding of bad news (Ali et al., 2007). Our study rationalizes the contradictory results of these prior studies and offers additional evidence that different levels and forms of stock-based incentives may impact the association between family firms and voluntary disclosure.

The remainder of this paper is organized as follows. Section 2 reviews the existing literature in this area and develops our hypothesis. Section 3 discusses our research approach and design. Our sample selection, descriptive statistics, and empirical results are presented in Sections 4 and 5. Finally, Section 6 includes our summary and concluding thoughts.

2. Prior research and hypothesis development

In this section, we first discuss prior research relevant to our study. Then, we develop and state our family firm and voluntary disclosure hypothesis.

2.1. Review of prior research

There is long-standing literature on corporate governance that managers, when not monitored by shareholders, will make decisions that maximize their own wealth but may not be in the best interest of shareholders (Hope & Thomas, 2008). From the agency perspective, managers avoid disclosing private information because such disclosure lessens their private control benefits (Nagar et al., 2003). The lack of information disclosure also limits the ability of capital and labor markets to efficiently monitor and regulate managers (Shleifer & Vishny, 1989). Managers only disclose their private information when compelled or it is advantageous.

Prior research illustrates the role that stock-based incentives play in mitigating this managerial agency problem. Healy and Palepu (2001) discuss that disclosures provide shareholders with an effective monitoring tool, and as a result reduce agency costs. Likewise, Bushman and Smith (2001) argue that monitoring manager behavior is one way to address this conflict, and one apparent monitoring system is through financial disclosures. Ball (2006) argues that managers act more in the interest of shareholders when there is increased transparency. Shareholders use stock-based incentives to encourage voluntary disclose, mitigate information asymmetry, and ultimately align the managers' and investors' interests (Nagar et al., 2003). In other words, managers are more likely to provide voluntary disclosure when their compensation is based on stock price or their wealth is tied to firm value.

Prior research addresses the relationship between family firms and voluntary disclosure. However, the empirical results are inconsistent. Ali et al. (2007) find that S&P 500 family firms report better earnings quality than S&P 500 non-family firms, and are more likely to provide quarterly forecasts. Similarly, Hutton (2007) documents that family firms in the S&P 500 provide better quality disclosure. On the other hand, Ajinkya, Bhojra, and Sengupta (2005) and Karamanou and Vafeas (2005) discover that firms with significant amounts of institutional

Download English Version:

https://daneshyari.com/en/article/7339771

Download Persian Version:

https://daneshyari.com/article/7339771

Daneshyari.com