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European family firms and acquisition propensity: A comprehensive analysis of the legal system's role[☆]

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A B S T R A C T

This study focuses on family firms' acquisition propensity. Recognizing that family firms are per se reluctant to acquire, we investigate how the legal system in which such firms operate directly affects their reluctance to undertake acquisitions. Extending previous work on the role of the institutional environment in family firms' strategic decisions, we also analyze the legal system's moderating effect in the relationship between family involvement in the business and the probability of acquisitions. Our sample covers family firms from Western European countries with four different legal systems over a nine-year period (2007–2015). We find that family involvement makes family firms more reluctant to undertake acquisitions, and that family firms operating in legal systems with a higher level of shareholder protection are more prone to acquire other businesses. Additionally, our results show that the aversion towards acquisitions associated with family participation in the business is mitigated in countries where shareholders are better protected, thus supporting the view that the legal system moderates the negative impact that family involvement has on acquisition propensity.

1. Introduction

Previous studies have mostly posited that family firms are generally reluctant to undertake mergers and acquisitions (M&A) (e.g., Caprio, Croci, & Del Giudice, 2011; Miller, Le Breton-Miller, & Lester, 2010; Shim & Okamuro, 2011). A likely factor influencing family firms' low acquisition propensity seems to be the desire family members have to avoid strategic decisions that could eventually erode their socio-emotional wealth (SEW) (Gomez-Mejia, Patel, & Zellweger, 2015). SEW is defined as the "non-financial aspects of the firm that meet the family's affective needs" (Gomez-Mejia, Haynes, Nuñez-Nickel, Jacobson, & Moyano-Fuentes, 2007, p. 106), and includes elements such as the emotional engagement of family members, the desire to retain family control, and the preservation of the founder's legacy across generations (Berrone, Cruz, & Gomez-Mejia, 2012; Gomez-Mejia, Cruz, Berrone, & De Castro, 2011; Gomez-Mejia et al., 2007). M&A may involve potential losses of firm control due to the use of external resources (e.g., financial and human resources) (Gomez-Mejia, Makri, & Larraza-Quintana, 2010), which would represent a considerable threat to the owning family's socioemotional endowment. M&A decisions may also threaten firm reputation (with the subsequent impact on transgenerational succession) because they can have adverse consequences, such as lay-offs, inefficient resource redeployment, lower-than expected market power, and unsatisfactory cost reductions (Gomez-Mejia et al., 2015), all of which might reduce SEW. Additionally, and also prompting a low acquisition propensity, the performance after M&A sometimes does not live up to expectations due to the complexity and far-reaching changes they involve for the firm (Reus, Lamont, & Ellis, 2016).

The influence of family members' socioemotional priorities on firms' strategic choices is a cornerstone of family business research (e.g., Anglin, Reid, Short, Zachary, & Rutherford, 2017; Gomez-Mejia et al., 2011; Gu, Lu, & Chung, 2016). However, considering other determinants may help us to further our understanding of the different preferences among family firms, inasmuch as they form a heterogeneous group (e.g., Chrisman, Chua, Pearson, & Barnett, 2012; Chua, Chrisman, Steier, & Rau, 2012; Nordqvist, Sharma, & Chirico, 2014). There have been several recent calls encouraging family business scholars to provide new evidence on the impact institutional factors have on family firms' decision-making processes (e.g., Chen, Hou, Li, Wilson, & Wu, 2014; Lebedev, Peng, Xie, & Stevens, 2015; Luo & Chung, 2013; Miller, Le Breton-Miller, & Lester, 2013). In an effort to fill this gap and provide an analysis that combines different drivers of family heterogeneity in terms of acquisition propensity, we therefore assume the need to examine not only internal sources of family firm

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heterogeneity (i.e., family involvement), but also dimensions external to the firm (i.e., the institutional environment) (Peng, 2002; Peng & Jiang, 2010; Zhu, Ma, Sauerwald, & Peng, 2017; Peng, Sun, Vlas, Minichilli, & Corbetta, 2018). Considering both sources of heterogeneity enables us to integrate the SEW approach with institutional explanations, while providing a holistic view of family firms' likelihood of engaging in acquisitions. As recently pointed out, "the institution-based view and the socioemotional priorities of large family firms can be fruitfully integrated" (Peng et al., (2018) p. 27).

Specifically, the objective here is to explore whether institutions matter (Peng, 2002, 2003; Peng, Sun, Pinkham, & Chen, 2009; Peng et al., 2018), and how they may lead family firms to either reduce or increase their propensity to make strategic choices, such as acquiring other companies. To address this challenge, we first propose a direct effect of the legal system, and examine how family firms' acquisition propensity may vary across countries depending on that system (Vishny, 1997, 1998;), as a dimension of a country's formal institutions (Jiang & Peng, 2011; Peng & Jiang, 2010). We further hypothesize the moderating role the legal system plays, and investigate whether the relationship between family involvement and acquisition propensity is contingent on the legal structure of the country where the family firm operates (La Porta et al., 1997, 1998; Peng & Jiang, 2010). Thus, the legal system is regarded as an external governance mechanism that can either mitigate or intensify the expected negative impact family involvement has on acquisition propensity.

To test our hypotheses empirically, we use a broad sample of 4387 European publicly traded firms (27,861 firm-year observations) that have been operating in different legal systems over a nine-year period (2007–2015). Western European countries, which are homogeneous as regards the prevalence of family firms, but heterogeneous in terms of legal systems, provide a unique framework for the analysis of cross-country differences in terms of strategic decisions (Defrancq, Huyghebaert, & Luypaert, 2016; van Essen, Strike, Carney, & Sapp, 2015).

This paper contributes to existing literature in at least two ways. First, we provide new evidence on family firm heterogeneity arising from country-level variations (e.g., Peng, 2002; Peng & Jiang, 2010). We are thus in line with recent research indicating that exploring the heterogeneous nature of family firms is an interesting topic that deserves careful consideration (Chua et al., 2012; Jaskiewicz & Dyer, 2017). Not all family firms are the same, and differences may therefore be observed in their decision-making processes (e.g., Arregle, Naldi, Nordqvist, & Hitt, 2012; Boellis, Mariotti, Minichilli, & Piscitello, 2016; Strike, Berrone, Sapp, & Congiu, 2015). Specifically, by accounting for variations across institutional environments our work explores how the acquisition decision, which is usually viewed as a threat to family firms (Gomez-Mejia et al., 2015; Miller et al., 2010), may depend on the legal system (e.g., more shareholder-oriented). Our results show that family firms' acquisition propensity is higher in countries with stronger legal protection systems.

Second, we explore how family owners may pursue their objectives and react differently when making strategic choices (e.g., acquisitions) based on the formal institutions that inform their operating environment. Among family firms, the emphasis on SEW considerations (as proxied by family involvement), as opposed to economic-driven objectives, varies across countries depending on the level of legal support. In this sense, the institutional perspective (e.g., Peng & Jiang, 2010; Peng et al., 2009) may help to fully understand why some family firms are guided more closely by family-related goals (SEW) than others (Berrone et al., 2012). We are thus in line with recent research that addresses the question on "how institutional conditions shape SEW-oriented attitudes of controlling families" (Peng et al., 2018, p. 26). The empirical evidence obtained shows that shareholders' legal protection increases family firms' acquisition propensity by mitigating the negative relationship between family involvement in the business and the likelihood of acquiring.

The remainder of the article is organized as follows. The second section develops the testable hypotheses. The third section describes the data and methodology used in the empirical analyses. The fourth section presents the descriptive and regression results, and provides several robustness tests (e.g., subsample analysis, alternative specifications, and multilevel regressions). Finally, we conclude by discussing the implications and possible future strands of research that can be derived from our work.

2. Theoretical background and hypotheses development

2.1. Family involvement in the business and SEW concerns

Prior research suggests that family firms tackle strategic problems by anticipating the likely gains and losses in the family's affective endowment, besides considering the consequences for the firm's bottom line (Gomez-Mejia et al., 2011, 2015). Nonetheless, the influence of SEW considerations is unlikely to remain constant, and could vary across situations (Berrone et al., 2012; Souder, Zaheer, Sapienza, & Ranucci, 2016). For instance, the preservation of SEW has greater priority in family firms with higher family involvement in ownership and when family members are present in the boardroom (Gomez-Mejia et al., 2010; Le Breton-Miller, Miller, & Lester, 2011).

Family ownership and the presence of family members on the board are two of the main ways in which owner families exercise substantial control over the firm (Berrone et al., 2012). Family involvement in the business may strengthen the family's ability to influence a firm's strategic decisions, and thus its power to pursue family goals. In this setting, keeping control of the company becomes a priority, and family members will be more averse to decisions that could threaten to weaken their control (Basco & Calabrò, 2017; Feldman, Amit, & Villalonga, 2016; Jones, Makri, & Gomez-Mejia, 2008; Le Breton-Miller et al., 2011; Minichilli, Nordqvist, Corbetta, & Amore, 2014).

Over and above the desire to retain control of the business, other SEW dimensions, such as family identification with the firm or emotional attachment to it (Berrone et al., 2012), may also become more prominent if the family participates in the company. With family involvement, family values and needs are more strongly rooted in the firm, and family-centered goals will prevail in the decision-making process (Gomez-Mejia et al., 2011, 2010; Le Breton-Miller & Miller, 2016). Thus, concerns about meeting the family's affective needs, such as family harmony or the employment of family members regardless of their contribution, are likely to increase (e.g., Berrone et al., 2012; Debicki, Kellermanns, Chrisman, Pearson, & Spencer, 2016).

In sum, family involvement in the business exacerbates the importance given to the preservation of SEW over financial objectives among family firms (Gomez-Mejia et al., 2011; Minichilli et al., 2014).

2.2. The link between SEW concerns and acquisitions

Past research on family firms argues that acquisitions can be a potentially harmful growth option for these firms in terms of SEW (Gomez-Mejia et al., 2015). Following this rationale, we discuss various possible reasons that explain why family firms generally tend to restrict their involvement in acquisitions.

Acquisitions are a costly activity that requires major funding allocations and, as a result, external financial resources are frequently needed, in addition to internal funds. However, the wish to preserve high equity participation, and therefore keep ownership and control in the hands of family members, reduces the options for raising external funding. Both capital increases and debt financing will lead family owners to depend on other players (e.g., new shareholders or banks) that may undermine their autonomy and control, and thus damage their SEW (Gomez-Mejia et al., 2011, 2010). External funding (e.g., via debt or stock issues) may also imply high financial risk, which family firms will try to avoid (De Massis, Kotlar, Frattini, Chrisman, & Nordqvist,