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The Choice between Family CEO and Non-Family CEO: What Are the Determinants?

Yves Bozec[1], Kim Trottier[1] & Jackie Di Vito[1]

[1] HEC Montreal, Montreal, Quebec, Canada

Correspondence: Jackie Di Vito, HEC Montreal, 3000 chemin de la Côte-Sainte-Catherine, Montreal, Quebec, Canada, H3T 2A7. Canada. E-mail: jacqueline.divito@hec.ca

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Abstract

We examine the factors that influence family firms that are no longer run by the founder, to appoint a chief executive officer from the family rather than from outside the family. Based on agency and signaling theories, we hypothesize that the concentration of family ownership and the presence of the founder increase the likelihood of appointing a family CEO, whereas the gap between voting rights and cash-flow rights (excess voting rights) decreases it. Our regression analyses of Canadian S&P/TSX family firms over the 2002–2008 period confirm our theory that contextual governance factors are good predictors of the type of CEO chosen in family firms.

Keywords: family firms, family CEO, governance, ownership, excess voting rights, founder

1. Introduction

Claessens et al. (2000), Faccio & Lang (2002) and La Porta et al. (1999) demonstrate that most firms around the world, including large publicly traded firms, are controlled by founders and/or members of their family. Given their significant voting rights and influence on the board of directors, these family shareholders are particularly powerful (Bozec & Di Vito, 2019; Jaskiewicz et al., 2017). One of the key strategic decisions where these family shareholders can exert considerable influence is selecting the CEO of the company, including potentially choosing a family member (Lu et al., 2021). This is a critical decision, as appointing a family CEO is the most direct way to maintain control over the business and therefore make it easier for the family to implement its strategies, such as creating socio-emotional wealth (Gomez-Mejia et al., 2011; Nason et al., 2019).

The purpose of our study is to examine the factors that influence a family firm's decision to appoint a CEO from among family members (family CEO) rather than from outside the family (non-family CEO) when the founder is no longer the CEO. Recent studies show that firms with founder-CEOs are associated with higher financial performance (Anderson & Reeb, 2003; Block, 2012; Fahlenbrach, 2009; He, 2008; Villalonga & Amit, 2006), while family firms that are no longer run by the founders but by a member of their family, perform worse than family businesses with non-family CEOs (Bertrand & Schoar, 2006; Jaskiewicz et al., 2017; Kang & Kim, 2016; Miller et al., 2014; Perez-Gonzalès, 2006; Sharma et al., 2003; Wagner et al., 2015). It is thus worthwhile to explore factors that lead family firms to choose this solution. Although the literature on the economic consequences of recruiting a family CEO is well established, research on the driving force that makes family firms choose a family CEO rather than a non-family CEO is relatively scarce. The objective of this study is to fill this gap in the literature.

Family shareholders are often concerned about creating or preserving their social-emotional wealth (Gomez-Mejia et al., 2007; Nason et al., 2019) or integrating their children into the business (Eddleston & Kidwell, 2012; Schulze et al., 2002, 2003), but they must not neglect the interests of outside shareholders. The risk for investors is that the decisions taken by the company's management may be more focused on the socio-emotional wealth of the family rather than on the wealth of the shareholders, which feeds the conflicts of interest (Gomez-Mejia et al., 2007; Jaskiewicz et al., 2017). However, shareholders are important stakeholders for listed companies (Fernando et al., 2014) and therefore, family firms have a vested interest in sending a strong signal to investors that the company is well managed and that shareholders' interests are maximized (Certo, 2003).

We apply agency theory and signaling theory to explore how the governance structure of the family firm affects the potential conflicts of interest between the family and the rest of the shareholders, and how the choice of a CEO can mitigate it. In a context where the governance structure increases conflicts of interest, we argue that the decision to appoint a non-family CEO sends a strong signal to investors that the family will not pursue objectives that are contrary to the interests of shareholders. Conversely, when the governance structure reduces conflicts of interest, the family is able to appoint a family CEO.

Our governance structure variables are comprised of three fundamental characteristics of governance that are known to affect the extent of conflicts of interest between the family and the rest of the shareholders: family ownership (cash-flow rights), the gap between voting rights and cash-flow rights (excess voting rights), and the active presence of the founder (Bozec & Di Vito, 2019; Miller et al., 2011; Miller et al., 2007; Villalonga & Amit, 2006).

The concentration of cash-flow rights has the effect of aligning the family's economic interests with those of external shareholders (Jensen & Meckling, 1976). Similarly, when founders no longer hold the position of CEO but remain a principal shareholder and a member of the board of directors, they continue to positively influence decision-making and the value of the company (Gomez-Meji et al., 2003; Miller et al., 2011; Villalonga & Amit, 2006). Therefore, the concentration of cash-flow rights and the active presence of the founder are likely to reassure the external shareholders, which increases the likelihood that the firm is comfortable hiring a family member as CEO. On the other hand, when the family has excess voting rights, investors are concerned that a family CEO would pursue socio-emotional wealth to the detriment of firm value. In essence, the family could be motivated to pursue its own objectives while external shareholders bear a disproportionate portion of the financial consequences, thus exacerbating the conflicts of interest (Bebchuk et al., 2000; Bozec & Di Vito, 2019; Morck et al., 2005). In these situations, hiring a non-family CEO sends a signal that reduces shareholder concerns.

We use regression analysis (PROBIT and LOGIT) to assess whether governance structure affects the likelihood of hiring a family CEO. Our sample is comprised of Canadian family firms with shares listed on the S&P/TSX Toronto Stock Exchange Index over the period 2002–2008 (315 firm/year observations). Our results confirm our hypotheses. The concentration of family cash-flow rights and the active presence of the founder increase the likelihood of finding a family CEO, whereas the likelihood decreases when families have excess voting rights. Our findings suggest that when the governance structure exacerbates conflicts of interest, the appointment of an external CEO is used as a strong signal to investors that the family firm is committed to primarily pursuing objectives of value creation for all shareholders.

Our study contributes to the literature on CEO succession decisions within family businesses in several ways. Previous studies by De Massis et al. (2016), Lu et al. (2021) and Shen & Su, (2017) show how the individual psychological dimensions of incumbent family CEOs or their family (religion, traditionalism, or emotional attachment) influence intentions to recruit a successor among family members. Our approach extends this area of literature by looking at the decision the family actually made rather than its intentions. Furthermore, we enrich these previous studies, which focus on private family firms, by exploring situations with greater conflicts of interest. The division between the family shareholder and the rest of the shareholders is practically non-existent in private family firms. Our study of large, publicly traded family firms provides a context where the nature and extent of conflicts of interest between the family and the rest of the shareholders are potentially more severe. Finally, previous studies have examined governance as a determinant of family choice of successor (Ansari et al., 2014; Kang & Kim, 2016). However, our approach is to examine the impact of different characteristics of family firm governance separately, which is important given the heterogeneous nature of family firms (Chua et al., 2012), By estimating the impact of founder involvement, family ownership, and excess voting rights separately, we avoid averaging out (and possibly cancelling out) the effect exerted by each of these factors, and thus, potentially neglecting significant moderating effects.

2. Theory Development and Hypotheses

2.1 The Choice of Type of CEO in Family Firms

When the time comes to appoint the CEO of the company, founders of family-controlled firms are often inclined to choose a family member rather than someone external to the family (Chrisman et al., 2014; Lu et al., 2021). There are at least two reasons for this behavior. First, appointing a family member to the position of CEO is the most direct way to maintain control over the business and therefore make it easier for the family to implement strategies that create socio-emotional wealth (Gomez-Mejia et al., 2011; Nason et al., 2019). Second, this preference could be the result of parental altruism (Eddleston & Kidwell, 2012; Schulze et al., 2002, 2003).

Parents are naturally generous to their children, caring for them, protecting them, favoring them, and prioritizing their welfare. Thus, family members have an advantage over non-family applicants for CEO positions even when they are not the most qualified (Bertrand & Schoar, 2006).

Despite this predisposition to choose a family member, we argue that the choice of the type of CEO depends on the severity of the conflicts of interest between the family and the rest of the shareholders. These conflicts of interest are perceived by investors as a risk factor if decisions made by the company's management are more focused on the socio-emotional wealth of the family than on the wealth of the shareholders (Gomez-Mejia et al., 2007; Jaskiewicz et al., 2017). When conflicts of interest are severe and therefore the perceived risk to investors is high, the family business has a vested interest in sending a strong signal to investors that its governance is sound and that the interests of shareholders are protected (Certo, 2003). The absence of such a signal would result in the devaluation of the family business (Zhang & Wiersema, 2009). Public companies, including family firms, are concerned about the value of their shares as they regularly use capital markets to finance their growth (Fernando et al., 2014; Guedhami & Mishra, 2010). Ultimately, the family's control of the company and the preservation of its social-emotional wealth are largely dependent on the ability of family shareholders to meet the expectations of the rest of the company's shareholders (Morck et al., 1988; Tsao et al., 2021). Thus, appointing an external CEO in a context of severe conflict of interest would send a strong signal that the family is restraining its pursuit of objectives that are contrary to the interests of shareholders (Naldi et al., 2013). This CEO appointment is a signal insofar as it responds to a need for information, is easily observable, and is costly to imitate by other signalers (Connelly et al., 2011; Sekercy et al., 2021). The cost in this case includes certain private benefits the family members might otherwise have enjoyed. Moreover, this signal is credible given that the external CEOs will likely be reluctant to implement the family's socio-emotional wealth strategies at the expense of the company's financial performance since this would negatively affect the CEOs' reputation and the value of their human capital on the labor market (Jaskiewicz et al., 2017; Fama, 1980). Thus, we postulate that the governance structure of family firms, as reflected by the conflict of interest between the family and external shareholders, will likely determine the type of CEO appointed.

2.2 Family Firms and Governance Challenges

In contrast to widely held public firms where agency problems manifest themselves in conflicts of interest between managers and shareholders (Jensen & Meckling, 1976), the concentration of shares in family businesses creates a conflict of interest between the family shareholders and the rest of the shareholders (La Porta et al., 1999). The governance of a family firm is impacted by its ownership structure, including the concentration of family cash-flow rights, their excess voting rights, and the active presence of the founder (Bozec & Di Vito, 2019; Miller et al., 2011; Miller et al., 2007; Villalonga & Amit, 2006; Wagner et al., 2015). In all cases, the key governance challenge is to align the interests of the decision-makers with those of shareholders.

For family firms, some of the decisions are more complex. The family also pursues other, non-financial objectives aimed at creating or preserving the family's socio-emotional wealth (Gomez-Mejia et al., 2007). These socio-emotional objectives include the reputation of the company and the family, the preservation of control of the company, and the satisfaction of the family's needs, whether in terms of careers within the company or job security (Jiang et al., 2018; Miller et al., 2014). Although these objectives are not always contrary to the interests of external shareholders, the family is often willing to sacrifice the profitability of the company in order to preserve its socio-emotional wealth (Gomez-Mejia et al., 2011).

2.2.1 Concentration of Family Cash-Flow Rights

Concentration of cash-flow rights is associated with the positive incentive effects discussed in Jensen and Meckling (1976). The greater the cash-flow rights held by the family, the closer the family's economic connection to the business becomes, potentially mitigating the conflicts of interest between the family and the external shareholders. Combining this strong alignment with the family's ability to control the firm attenuates problems usually caused by the separation of ownership and control. Although the family is free to make all the decisions, it nevertheless bears almost all the financial consequences. In this context, the appointment of a CEO from the family would not be perceived by external shareholders as an additional risk factor. Therefore, we formulate the following research hypothesis:

Hypothesis 1: Family concentration of cash-flow rights increases the likelihood that the CEO of the company is a family member.

However, cash-flow rights can be associated with power only when voting rights are attached. In these cases, the concentration of family ownership is not only accompanied by governance benefits, but also involves risks for external shareholders. It allows the family to become entrenched, to take root at the head of the business, and to

act as if the business were its personal fiefdom (Morck et al., 1988).

The concentration of cash-flow rights can culminate in a concentration of voting rights, which weakens the effectiveness of the main governance mechanisms. For example, the controlling family can block any hostile takeover attempt. It can also appoint a majority of the directors and thus control all decisions taken by the board of directors. Well-entrenched and in control, the family can impose its decisions even if they are not necessarily in the best interest of the outside shareholders (Bozec & Laurin, 2008; Holderness & Sheehan, 1988). In short, the concentration of ownership and the entrenchment that results from it, can give rise to all kinds of abuse, which represents a source of serious conflicts of interest between the family and the rest of the shareholders. This is particularly an issue when family owners are endowed with excess voting rights, which occurs when the family's control through voting rights is proportionately higher than its cash-flow rights (Morck et al., 2005).

2.2.2 Excess Voting Rights

Excess voting rights is common among family companies (Faccio & Lang, 2002; La Porta et al., 1999;). It is largely the result of a dual-class common share structure, where one category of shares confers more voting rights per share than the other. Take for example, Couche-Tard, a Canadian company that is one of the largest operators of convenience stores in North America. Couche-Tard issued Class A shares and Class B shares with voting rights that differ from cash-flow rights. Every share is equally entitled to dividends, therefore has the same cash-flow rights. However, Class A shareholders are entitled to 10 votes per share whereas Class B grants only one vote per share. The founders of the company own most of the multi-voting Class A shares, which allows them to control 65% of the voting rights with a 22% equity stake. A more extreme example is Magna International, a Canadian auto parts giant. Their multi-voting shares entitle shareholders to 300 votes per share, allowing the founder and family to control more than two thirds of the votes with only 1% of the cash-flow rights.

In terms of governance, the main advantage of multi-voting shares is that it enables long-term decision-making. By being protected from a hostile takeover bid, the family can deploy all its talent, energy, and expertise to the implementation of its strategic vision since it has a certain assurance of being able to benefit from the long-term gains. Nevertheless, excess voting rights can put external shareholders at risk (Baek et al., 2004; Bebchuck et al., 2000) if the voting power gives the family absolute control of the company despite having minimal equity at stake. The family makes all the decisions in the company while external shareholders bear almost all the risks and financial consequences. Excess voting rights is associated with an entrenchment problem and misalignment of the interests of the family with the rest of the shareholders. Unsurprisingly, empirical evidence shows the negative effects of excess voting rights on the performance and value of family firms (Bozec & Di Vito, 2019; Claessens et al., 2002; Gompers et al., 2010; Villalonga & Amit, 2006).

Excess voting rights exacerbates the usual conflicts of interest between the family and the rest of the shareholders, creating an additional perceived risk that the family's decisions will not be aligned with other shareholder interests. Appointing a family CEO in this situation could unduly increase the risk perceived by investors, so the family is more likely to select a non-family CEO as a risk-mitigating signal. Therefore, we formulate the following research hypothesis:

Hypothesis 2: Excess voting rights of the family decreases the likelihood that the CEO of the company is a family member.

2.2.3 The Active Presence of the Founder

Previous studies show that the severity of the conflict of interest between families and external shareholders varies depending on whether the founders or their heirs control and manage the company. Miller et al. (2007, 2011) find that firms where the founder is a major shareholder as well as the CEO outperform other firms, especially when no other family member is involved in the business either as a shareholder, a member of senior management or a board director. Similarly, Villalonga and Amit (2006) show that the value of family firms is positively associated with the active presence of founders, not only during their tenure as CEO, but also when they no longer hold the CEO position but continue to sit on the board of directors. However, when founders are no longer active, and have transferred the control and management of the company to their heirs, the performance becomes significantly lower (Claessens et al., 2002; Morck et al., 2005; Villalonga & Amit, 2006).

The founders' beneficial contribution to the company is thought to transcend their entrepreneurial talent and economic ties towards an emotional connection that makes them want the firm to thrive. Having been involved in the company since its very beginning, founders have acquired a deep understanding and expertise on the company, and developed a network of relations with the partners of the company such as customers, suppliers,

creditors, etc. (He, 2008; Li & Srinivasan, 2011). But in addition, the creation of a business is thought to be the strongest way to identify with and develop a deep attachment to it (Wasserman, 2006). In this regard, founders are probably the most emotionally committed and successful members of the organization (Arthurs & Busenitz, 2003; Miller et al., 2011). Creating the company is often one of the greatest achievements in their life (Fahlenbrach, 2009), so they invest a lot of attention, time and energy into it (Le Breton-Miller et al., 2010). Finally, as documented in the literature, founders are known to stand out for their commitment to focus on the company's growth and performance objectives (Miller et al., 2011; Bozec and Di Vito, 2019). Thus, the active presence of the founder is likely to mitigate the conflicts of interest between the family and the rest of the shareholders (Jaskiewicz et al., 2017).

The active presence of the founder, focusing on the growth and financial performance of the company, is likely to reassure external shareholders. The literature confirms that conflicts of interest between the family and the rest of the shareholders are mitigated when the founder is present, either as an officer and/or director. In these situations, we argue that a family CEO can be appointed since this is not perceived by investors as an additional risk factor that the family's decisions run counter to the interests of minority shareholders. Therefore, we formulate the following research hypothesis:

Hypothesis 3: The active presence of the founder increases the likelihood that the CEO of the company is a family member.

3. Methodology

3.1 Sample

From the Canadian companies included in the S&P/TSX index on the Toronto Stock Exchange during the period 2002–2008, we select all family firms (n = 459 firms/years). Family firms are categorized as those for which the principal shareholder and other members of the principal shareholder's family hold at least 10% of the voting rights. Given our research question, we eliminate observations where the founder of the company holds the position of CEO. The final sample consists of family firms that are no longer run by the founder, such that the position of CEO is held either by a family member or by an individual external to the family. Our final sample is an unbalanced panel consisting of 79 family firms and 315 firm/year observations. We manually collect information on founders and family members from management proxy circulars, corporate websites, and Wikipedia. Family members are identified as individuals with the same surname as the founder.

3.2 Dependent Variable

Our dependent variable FAMILY CEO is a binary variable taking the value 1 if the CEO of the company is a member of the family, and zero otherwise.

3.3 Independent Variables

3.3.1 Ownership and Control

We manually collect the family's ownership variables. Using the management proxy circulars available on the SEDAR website, we follow the methodology of La Porta et al. (1999), Claessens et al. (2000) and Faccio and Lang (2002) to identify the company's ultimate shareholder, often referred to as the principal shareholder (hereafter). The principal shareholder is the shareholder who holds, directly or indirectly through another corporation, the greatest number of voting rights. When the principal shareholder and his/her family members hold at least 10% of the voting rights, the company is categorized as a family firm.

We create VOTING RIGHTS as the proportion of voting rights held by the principal shareholder and his/her family. We also create the CASH FLOW RIGHTS variable, which measures the proportion of the equity stake of the principal shareholder and family in the firm. Sometimes, the principal shareholder's voting rights differs from his/her cash flow rights. This stems from the existence of excess voting rights mechanisms present in certain corporate ownership structures. When there is no difference between the voting and cash flow rights, VOTING RIGHTS is equal to CASH FLOW rights. When there is a difference, we measure this difference by introducing the EXCESS variable.

For example, Bombardier Inc. has Class A common shares that grant its holders ten votes per share while Class B common shares grant only one vote per share. In 2008, Bombardier family members held approximately 80% of the Class A shares and less than 1% of the Class B shares, allowing them to control 57% of Bombardier's voting rights with a total equity stake of 15%. (Bozec & Di Vito, 2019). In this example, VOTING RIGHTS would be 80%, CASH FLOW RIGHTS would be 15%, and EXCESS would be 65%.

As an alternative measure of EXCESS, we also use a binary variable (SEPARATION) that takes the value of 1 if

the principal shareholder has excess voting rights, and zero otherwise.

Finally, we create an additional binary variable to identify the family firms where the founder is still active. This variable (ACTIVE FOUNDER) is coded as 1 if the founder is the principal shareholder of the company and continues to sit on the board of directors, and zero otherwise.

3.3.2 Control Variables

Our analysis controls for other factors that may influence the chosen type of CEO. First, we control for the effect of certain governance mechanisms that can mitigate conflicts of interest between the family and the rest of the shareholders and potentially affect the likelihood of appointing a family CEO (Ansari et al. 2014; Shen & Su 2017). We include a GOVERNANCE variable that measures the overall quality of governance using the Governance Index developed by the Report on Business (ROB) and published annually by the Canadian newspaper The Globe and Mail. The ROB score assesses the quality of several dimensions of governance such as the board of directors, executive compensation, shareholder protection and disclosure of financial information. Our DEBT variable, which is the ratio of debt to assets, controls for the supervisory role of the company's creditors. We also control for the effect of institutional investor oversight. Our INSTITUTIONAL variable represents the percentage of the company's shares held by institutional investors. In addition to the three previous variables, we control for the size of the company (SIZE), its performance (ROA) and the number of family members involved in the company (NUMFAMILY). The coefficient of SIZE (the logarithm of assets) is expected to be negative since larger firms tend to be more complex. In this context, firm size may reduce the pool of family candidates with the skills and knowledge to run a complex business (Chrisman et al., 2014), therefore reducing the likelihood of hiring a family CEO. The firm's performance is controlled using the return on assets (ROA) achieved during the previous year. When the performance is low, we expect the likelihood of appointing a family CEO to be lower. As suggested by previous studies (Gomez-Mejia et al., 2003; Lu et al., 2021), the family will tend to turn to an external CEO to redress the financial situation and bring a new direction to the company. Finally, the variable NUMFAMILY represents the number of family members involved in the business either as members of the board of directors and/or as members of the top management team. NUMFAMILY may have ambiguous effects. On the one hand, it can increase the likelihood of having a family CEO because a high number of family members may reflect a larger pool of competent family-based candidates (Lu et al., 2021). On the other hand, it can decrease the probability of having a family CEO if it reflects a higher risk of intra-family conflicts about founder succession or, more company resources dedicated to meeting the family's career and job security ambitions within the company (De Massis et al., 2016). Finally, our control variables also include a series of binary variables for years (YEAR) and industries (INDUSTRY). All variables are defined in Appendix A.

3.4 Empirical Model

Our research hypotheses are tested using the following panel regression model:

$$FAMILY\ CEO_{it} = \beta_0 + \beta_1\ CASH\ FLOW\ RIGHTS_{it-1} + \beta_2\ EXCESS_{it-1} + \beta_3\ ACTIVE\ FOUNDER_{it-1} + \beta_4\ Control\ Variables_{it-1} + Year/Industry\ Effects + error\ term \quad (1)$$

To mitigate problems of endogeneity (due to reverse causality), our dependent variable FAMILY CEO is estimated against lagged independent variables. For the variables CASH FLOW RIGHTS, EXCESS and ACTIVE FOUNDER, the lag is just under a year since they are measured about 3 months after the beginning of the fiscal year. We exclude VOTING RIGHTS from the model since it is a linear combination of CASH FLOW RIGHTS and EXCESS therefore would introduce multicollinearity. We include SEPARATION in some of the analysis.

To deal with potential outliers, we winsorize all our control variables at the 99th percentile levels. Accordingly, all extreme values above (below) the 99th (1st) percentiles are set to the 99th (1st) percentile values.

Our binary dependent variable requires the use of a PROBIT or LOGIT model. In a cross-sectional time series sample such as ours, serial correlation of the error terms for observations from the same company can potentially lead to misspecification. We therefore use a random-effects PROBIT model which has the advantage of accounting for cross-sectional heteroscedasticity and serial correlations, thereby producing better estimates of model parameters (Clarkson et al. 2004). To be consistent with previous studies (Lu et al., 2021; Shen & Su, 2017) we also estimate the coefficients with a random-effects LOGIT model.

4. Results

4.1 Univariate Analysis

Descriptive statistics are presented in Table 1.

Table 1. Descriptive statistics

Variables	Mean	SD	Min	Max
FAMILY CEO	0.40	0.49	0.00	1.00
VOTING RIGHTS	0.51	0.24	0.10	0.94
CASH FLOW RIGHTS	0.21	0.18	0.01	0.73
EXCESS	0.30	0.27	0.00	0.87
SEPARATION	0.68	0.47	0.00	1.00
ACTIVE FOUNDER	0.33	0.47	0.00	1.00
GOVERNANCE	62.33	11.90	29.00	92.00
DEBT	0.25	0.16	0.02	0.70
INSTITUTIONAL	0.04	0.07	0.00	0.47
SIZE	14.80	1.39	8.45	17.60
ROA	0.03	0.07	-0.16	0.16
NUMFAMILY	2.16	1.34	1.00	7.00

Note. This table presents descriptive statistics of our sample composed of 79 family firms and 315 firm/year observations. See Appendix A for the definition of the variables.

We note that 40% of family firms that are no longer run by the founder are run by a family member (FAMILY CEO). Therefore 60% are led by a CEO who is external to the family (non-family CEO). We also note that on average, the family holds 51% of voting rights (VOTING RIGHTS), 21% of cash-flow rights (CASH FLOW RIGHTS), and 30% of excess voting rights (EXCESS). The founder remains the principal shareholder and sits on the board of directors (ACTIVE FOUNDER) in about one third of our sample. In addition, we note that on average, 2.16 family members are involved in the company, either as a director and/or a member of the top management team (NUMFAMILY).

Overall, these family shareholders are not only the largest shareholder of the company, but we find that they control a significant proportion of the votes. In addition, untabulated results reveal that the family frequently (nearly 60% of cases) holds majority control of the votes and are particularly active because they sit on the board of directors in more than 80% of cases. Therefore, family shareholders have a lot of influence in the decision-making process, including decisions concerning the choice of the CEO.

Table 2 presents Pearson correlation coefficients for all the variables. The statistics in Table 2 indicate that the choice of appointing a family member to the position of CEO (FAMILY CEO) is positively correlated with the concentration of family cash-flow rights (CASH FLOW RIGHTS) and the active presence of the founder (ACTIVE FOUNDER). These preliminary results are consistent with our research hypotheses H1 and H3.

Table 2. Pearson Correlations

Variables	1	2	3	4	5	6	7	8	9	10
1. FAMILY CEO	1.00									
2. CASH FLOW RIGHTS	**0.27****	1.00								
3. EXCESS	0.07	**-0.42****	1,00							
4. SEPARATION	-0.05	**-0.28****	**0.77****	1,00						
5. ACTIVE FOUNDER	**0.16****	0.02	0.03	**-0.13***	1,00					
6. SIZE	0.11	**0.16****	**0.25****	**0.23****	**-0.16****	1,00				
7. DEBT	**0.21****	0.05	**0.24****	**0.34****	-0.10	**0.37****	1,00			
8. GOVERNANCE	-0.06	**0.12***	**-0.24****	**-0.15****	-0.11	**0.23****	0.01	1,00		
9. ROA	0.09	0.05	0.04	0.01	-0.09	0.10	**-0.21****	-0.04	1,00	
10. INSTITUTIONAL	-0.05	-0.03	**-0.31****	**-0.17****	-0.11	-0.08	-0.03	**0.26****	**-0.12***	1,00
11. NUMFAMILY	**0.36****	**0.39****	0.10	**0.19****	**0.21****	**0.23****	0.08	0.04	0.06	**-0.13***

Note. This table presents Pearson correlations. Our sample is composed of 79 family firms and 315 firm/year observations. *Two-tailed correlation significant at the 5% (*) and the 1% level (**). See Appendix A for the definition of the variables.

4.2 Multivariate Analysis

Table 3 presents the results from the PROBIT and LOGIT estimates of the coefficients associated with the likelihood of appointing a family CEO. Our empirical model contains all independent variables including our 3 main variables of interest: CASH FLOW RIGHTS, EXCESS and ACTIVE FOUNDER. We obtain Wald Chi^2 values between 77 and 85 which indicates the coefficients are significant at the 1% level.

Among the control variables, we note positive and statistically significant coefficients for governance (GOVERNANCE) and the number of family members involved in the firm (NUMFAMILY). In the LOGIT model, our results also show a significantly positive coefficient for performance (ROA). These results suggest that the likelihood of finding a family member in the position of CEO increases with the quality of governance of family firms, previous good performance and the number of family members already involved in the business. These results are consistent with the results observed by De Massis et al. (2016), Kang and Kim (2016), Shen and Su (2017) or Lu et al. (2021).

Hypothesis 1 predicts that the concentration of family cash-flow rights increases the likelihood that the CEO of the company is from the family. Our findings support this hypothesis. The coefficients for CASH FLOW RIGHTS are positive (β=13.93 and 21.88) and statistically significant at the 1% threshold. The results also support Hypothesis 2 which states that the likelihood of finding a family member in the CEO position decreases with the level of the family's excess voting rights. The coefficients for EXCESS are negative (β=-7.18 and -9.92) and statistically significant at the 5% threshold for the PROBIT model, and at the 10% threshold for the LOGIT model. Hypothesis 3, which predicts that the active presence of the founder (ACTIVE FOUNDER) increases the likelihood of observing a family CEO, is supported by results from the LOGIT model (β=4.04; $p < 0.10$) but not the PROBIT model.

Table 3. Random-Effects Panel Regressions: Determinants of the Choice to Appoint a Family-CEO

	Pred.	**Random-Effects PROBIT**		**Random-Effects LOGIT**	
	Sign	Coeff.	Z-Stat.	Coeff.	Z-Stat.
Intercept	?	**-13.95****	-2.23	**-31.06*****	-2.85
GOVERNANCE	+	**0.08***	1.90	**0.12***	1.65
DEBT	+	1.16	0.31	2.35	0.36
INSTITUTIONAL	+	-1.43	-0.17	11.33	0.82
SIZE	-	-0.48	-0.92	-0.45	-0.53
ROA	+	11.57	1.41	**29.99****	2.40
NUMFAMILY	?	**2.46*****	6.00	**4.95*****	5.71
CASH FLOW RIGHTS	+	**13.93*****	4.03	**21.88*****	3.75
EXCESS	-	**-7.18****	-2.45	**-9.92***	-1.93
ACTIVE FOUNDER	+	0.32	0.26	**4.04***	-1.92
Log Likelihood		-57.60		-59.00	
Wald Chi^2		77.23***		85.20***	
N obs.		315		315	

Note. This table presents the results for panel PROBIT regression and logistic regression (LOGIT) which estimate the likelihood of appointing a family CEO. Our sample is composed of 79 family firms and 315 firm/year observations. *, **, *** significant at the 10% level, 5% level and 1%, respectively. See Appendix A for the definition of the variables.

4.3 Robustness Analysis

Two additional analyses are conducted to test the robustness of our results. The results are presented in Table 4.

Table 4. Robustness Analyses

		Random-Effects PROBIT				Random-Effects LOGIT			
	Pred.	**(1a)**		**(2a)**		**(1b)**		**(2b)**	
	Sign	Coeff.	Z-Stat.	Coeff.	Z-Stat.	Coeff.	Z-Stat.	Coeff.	Z-Stat.
Intercept	?	-11.61	-1.03	-7.36	-1.63	-12.38	-1.14	-4.64	-0.41
GOVERNANCE	+	0.07	0.97	0.33	0.78	0.09	1.24	0.12	1.35
DEBT	+	0.33	0.07	-3.04	-0.89	-1.48	-0.18	-0.41	-0.06
INSTITUTIONAL	+	7.17	0.73	-1.85	-0.29	3.80	0.21	7.23	0.29
SIZE	-	-0.55	-0.85	**-0.52***	-1.64	-0.80	-0.98	**-2.25*****	-2.58
ROA	+	15.78	1.57	**11.39***	1.63	22.36	1.57	**33.31***	1.87
NUMFAMILY	?	**2.95*****	5.51	**2.11*****	4.86	**3.70*****	3.33	**4.19*****	4.47
CASH FLOW RIGHTS	+	**16.64*****	3.49	**13.87*****	3.28	**20.07*****	3.31	**22.97*****	0.01
EXCESS	-			**-7.79****	-2.21			-3.96	-0.66
ACTIVE FOUNDER	+	1.07	0.70	0.83	0.55	0.21	0.08	**8.67*****	2.56
ACTIVE FOUNDER x EXCESS	?			-4.66	-1.32			-11.04	-1.30
SEPARATION	-	**-6.17***	-1.88			**-9.31*****	-3.12		
Year dummies		yes		yes		yes		yes	
Log Likelihood		-58.17		-58.09		-58.20		-60.40	
Wald Chi²		53.34***		84.61***		42.03***		51.88***	
N obs.		315		315		315		315	

Note. This table presents the results for panel PROBIT regression and logistic regression (LOGIT) which estimate the likelihood of appointing a family CEO. Our sample is composed of 79 family firms and 315 firm/year observations. *, **, *** significant at the 10% level, 5% level and 1%, respectively. See Appendix A for the definition of the variables.

First, we replace the continuous variable EXCESS with a binary variable taking the value 1 if the family has excess voting rights and zero otherwise (SEPARATION). The results estimated with PROBIT (1a) and LOGIT (1b) are similar to those presented in Table 3, with coefficients for SEPARATION that are negative and statistically significant (β=-6.17; $p < 0.10$ and β=-9.31; $p < 0.01$).

The second analysis adds the interaction of the ACTIVE FOUNDER and EXCESS variables to test whether the negative impact of excess voting rights on the likelihood of recruiting a family CEO is moderated by the active presence of the founder. Models 2a et 2b include, in addition to our independent variables, the interactive variable obtained by multiplying ACTIVE FOUNDER by EXCESS. Some of our results in these models are slightly different depending on whether PROBIT or LOGIT is used. It is worthwhile to note that, while these two models often produce similar coefficients and significance levels, they can differ when estimated on data sets with observations in extreme values. This is because the logit function has "fatter tails" so is better able to estimate coefficients when outliers are present, whereas the probit function performs better when the data has fewer extreme values.

The results of model 2 complement those of Table 3. The coefficient of the ACTIVE FOUNDER x EXCESS interaction variable is not statistically significant in either model. This suggests that the negative impact of EXCESS and the positive impact of ACTIVE FOUNDER offset each other on average, which speaks to the importance of analyzing them separately. In the PROBIT model (2a) we note that the negative effect of excess voting rights (EXCESS) is not significantly different depending on whether the founder is still active or not, and the LOGIT model (2b) suggests that the positive effect associated with the active presence of the founder (ACTIVE FOUNDER) is not mitigated where the family enjoys excess voting rights. Overall, the results of models 2a and 2b rather seem to suggest that the positive effect of the founder is felt especially when there are no excess voting rights while the negative effect of excess voting rights is felt especially when the founder is no longer involved in the company, but control of the firm is now in the hands of the family heirs.

5. Discussion and Conclusion

This study examines the factors that influence family firms which are no longer run by the founder, in their decision to appoint a CEO from the family (family CEO) or from outside the family (non-family CEO). Founders and/or their family may be inclined to choose a family CEO due to parental altruism or a desire to preserve socio-emotional wealth. However, this could exacerbate agency issues that are particular to family firms in terms of the conflicts of interest between the family and the rest of the shareholders. We identify three contextual governance factors that capture this duality and use agency and signaling theories to explain how each

might affect the choice of CEO. We hypothesize that a concentration of cash-flow rights and/or the presence of the founder increases the likelihood of appointing a family CEO whereas in situations where the family has excess voting rights (where their voting rights exceed their cash-flow rights) they are more likely to appoint a non-family CEO.

Results from our regression analyses of Canadian S&P/TSX family firms over the 2002–2008 period support our theory that governance structure is a good predictor of the type of CEO chosen. As expected, we find that the concentration of family cash-flow rights increases the likelihood that the CEO is a family member. This is because when cash-flow rights are concentrated in the hands of the family, the family's economic interests are better aligned with those of the rest of the shareholders. There is less risk that the family CEO will pursue objectives of socio-emotional wealth to the detriment of the company's value and therefore no need to reassure investors by appointing a non-family CEO. Conversely, the risk that the family's behavior runs contrary to the interests of external shareholders seem higher when the family enjoys excess voting rights. Not only does the family have more control over the company's decision-making process, but its economic interests are poorly aligned with those of the rest of the shareholders, fueling conflicts of interest. In such a context, we find, as expected, that the likelihood of appointing a family CEO decrease. Finally, since founders are known for their beneficial contribution to the company, their mere presence in the company as the principal shareholder and board member is likely to reassure investors that the main focus continues to be value creation and preservation. This, in turn, increases the likelihood of appointing a family CEO rather than an external CEO.

Results on the trade-offs of these impacts suggest that when the family has excess voting rights, the mere presence of the founder does not seem to be a sufficiently reassuring signal for investors. Our results are consistent with previous studies on the founder's impact on the performance of family firms (Bozec & Di Vito, 2019; Miller et al., 2007; Miller et al., 2011). When founders are not the only ones involved in the company but rather accompanied by other members of their family, their focus on the performance and growth of the company is somewhat diverted towards the pursuit of socio-emotional wealth objectives. The impact of the founder on the firm's performance appears to be mixed (Miller et al., 2011) and even more so when he has excess voting rights (Bozec & Di Vito, 2019).

Altogether, our findings suggest that where the governance structure potentially exacerbates the conflicts of interest inherent in family firms, the likelihood of appointing a non-family CEO increases. CEO appointment appears, in this context, to be a strong signal that the firm is committed to pursuing objectives of value creation for all shareholders rather than for the benefit of the family. On the other hand, when the governance structure reduces potentially severe conflicts, family shareholders prefer to appoint a family member as CEO rather than one who is external to the family.

Our findings inform the literature on the performance of family firms. Previous studies on the performance of family-owned companies show that governance structures that create conflicts are associated with lower stock market value (Bozec & Laurin, 2008; Claessens et al., 2002; Miller et al., 2007; Villalonga & Amit, 2006; Wagner et al., 2015). In addition, studies focusing on the implications of family CEO appointments tend to show that family CEOs underperform non-family CEOs (Jaskiewicz et al., 2017; Kang & Kim, 2016; Miller et al., 2014; Perez-Gonzalès, 2006). Building on our results, it would be worthwhile to examine whether family businesses with high-conflict governance structures perform better when they are run by a non-family CEO, and whether the family CEO outperforms in low-conflict governance situation, or if the appointment of the CEO is merely a signal.

Our study also contributes to the literature on succession decision in family firms. Previous studies by De Massis et al. (2016), Lu et al. (2021) and Shen & Su, (2017), show how the individual psychological dimensions of the incumbent family CEO (religion, traditionalism or emotional attachment) influence intentions to recruit a successor among family members. Our study looks at the decision the family actually made rather than its intentions and shows, theoretically and empirically, that the factors associated with the governance context are good predictors of successor choice. Furthermore, our study context allows us to enrich these previous studies, which focused on private family firms. The division between the family shareholder and the rest of the shareholders is practically non-existent in the family businesses not listed. Our study explores a context where the nature and extent of conflicts of interest between the family and the rest of the shareholders are potentially more severe than in private family businesses. Our study also complements studies by Ansari et al. (2014) or Kang and Kim (2016) who examine the family's choice of a successor. In contrast to their studies, our approach has been to simultaneously examine the impact of the different characteristics of family firm governance on the decision to recruit a CEO from the family. This is important because, given the heterogeneous nature of family firms, the extant literature can be improved by distinguishing idiosyncratic characteristics such as founder

presence, family ownership and excess voting rights.

This study has practical implications. Given the importance of CEO choice for the performance and sustainability of the company, it is essential to understand how this choice is influenced by certain contextual factors. From the point of view of external shareholders, as well as that of family shareholders, if a family firm makes the right decision in choosing between a family CEO and a non-family CEO, it could be beneficial for its long-term profitability and value creation. Knowledge of these factors is also important for the current and future directors of the family business since they will be called upon to participate in the choice of the CEO of the company. The context in which these decisions are taken is quite different from that which prevails, in particular in companies whose capital is widely dispersed and/or there is no controlling shareholder.

Our study is subject to certain limitations. First, the family ties between shareholders, officers and directors are identified based on the family name and information found in management proxies, on the company's website, or in Wikipedia. Despite all the efforts made at the data collection level, it may be that the classification of family firms (number of family members involved, family CEO versus non-family CEO) contains some errors. It is more likely that we coded a family member as being non-family rather than the other way around, therefore if a bias was introduced through coding error, it would have reduced the power of our tests and prevented us from finding family-based results. Consequently, there is no concern emanating from this limitation. Second, the family firms selected in our study are among the largest publicly traded companies on the Toronto Stock Exchange. Therefore, our results cannot necessarily be generalized to private companies or to small listed small companies. In these smaller companies, the concentration of ownership is likely more pronounced and the operations simpler, which may alter the nature and extent of conflicts of interest between the family and the rest of the shareholders. Finally, the decision to recruit a family CEO, in addition to the signal it sends to investors, also depends on both the ability and the desire of family members to hold such a position. Our analyses control for the presence of family members among the company's senior executives and directors (NUMFAMILY). While this may, to some extent, be a proxy for family members' ability to serve as CEOs, it does not mean they have the desire to do so. For all these reasons, the limitations of our study require some caution in interpreting our results, but they open the door to new avenues of research.

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Appendix A. Variables Definition

FAMILY CEO	1 if the CEO is a family member, 0 otherwise
VOTING RIGHTS	% of voting rights held directly and indirectly by the family
CASH FLOW RIGHTS	% of cash-flow rights held directly and indirectly by the family
EXCESS	VOTING RIGHTS—CASH FLOW RIGHTS
SEPARATION	1 if VOTING RIGHTS> CASH FLOW RIGHTS, 0 otherwise
ACTIVE FOUNDER	1 if the founder is the principal shareholder and a member of the board of directors, 0 otherwise
GOVERNANCE	Annual ROB governance score from 1 to 100 provided by *The Globe & Mail*
DEBT	(Long-term Debt)/(Total assets)
INSTITUTIONAL	% of voting rights held collectively by institutional investors
SIZE	Log (Total assets)
ROA	Net Income/Total assets
NUMFAMILY	Number of family members involved in the top management team and/or board of directors.

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