

CONFLICTING SELVES: FAMILY OWNERS' MULTIPLE GOALS AND SELF-CONTROL AGENCY PROBLEMS IN PRIVATE FIRMS

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CONFLICTING SELVES: FAMILY OWNERS' MULTIPLE GOALS AND SELF-CONTROL AGENCY PROBLEMS IN PRIVATE FIRMS

This study examines the self-control agency problems associated with family ownership in private firms. Theorizing that family owners' inner conflicts between economic and non-economic goals lead to competing preferences in the allocation of financial resources, we predict that the relationship between financial slack and firm profitability is contingent on factors that increase the potential salience of either economic or non-economic goals for family owners. Accordingly, our findings suggest that self-control is a separate source of agency costs in private firms and that family ownership is not as crucial as owners' goals in predicting the impact of financial slack on firm profitability.

INTRODUCTION

Agency theory has been a major paradigm for understanding differences in profitability across firms. The agency theory perspective focuses on problems arising when more powerful and better-informed actors are able to extract value from the firm to the detriment of other stakeholders and firm profitability (Jensen & Meckling, 1976). Such perspective emphasizes conflicts of interest between owners and managers (i.e., principal-agent problems, see Jensen & Meckling, 1976) or between majority and minority shareholders (i.e., principal-principal problems, see Bruton Filatotchev, Chahine, & Wright, 2010). However, these agency conflicts are deemed rare in private firms where concentrated ownership and the overlap between ownership and management should naturally limit these conflicts (e.g., Durand & Vargas, 2003; George, 2005). This is expected to be particularly true for private family firms, given that owners and managers belonging to the same family are bound by altruism and should hence have lower incentives to appropriate firm resources (Chrisman, Chua, & Litz, 2004; Herrero, 2011). However, the agency consequences of family ownership in private firms are still much debated (e.g., Chrisman et al., 2004; Schulze, Lubatkin, & Dino, 2003b) and empirical evidence linking family ownership and firm profitability remains mixed (see Carney, Van Essen, Gedajlovic, & Heugens's (2015) meta-analysis).

Focusing on conflicts between different parties, agency theory scholars emphasize the differences between insiders and outsiders, treating family owners as a homogeneous category with

a well-defined set of goals and preferences (Dharwadkar, Goranova, Brandes, & Khan, 2008; Kim, Kim, & Lee, 2008). However, a growing body of research indicates that even single family owners can simultaneously pursue competing economic and non-economic goals, which may lead to inner conflict when facing decisions (Kotlar & De Massis, 2013; Zellweger, Kellermanns, Chrisman, & Chua, 2012a). According to Thaler and Shefrin (1981), conflicting goals can lead an individual to be both a farsighted planner and a myopic doer at any time, potentially leading to a “self-control” agency conflict with oneself that is similar to the classic conflict between owners and managers. Private firms are exposed to self-control problems as they are exempt from the disciplining effect of the market for corporate control (Jensen, 1994). Moreover, the family owner’s simultaneous pursuit of economic and non-economic goals suggests that these problems can be even more pronounced in family firms (Gedajlovic, Lubatkin, & Schulze, 2004; Schulze et al., 2001). Thus, resource allocation is likely to involve difficult tradeoffs for family owners torn between economic and non-economic goals, possibly leading to myopic decisions that hurt firm profitability and compromise their own financial welfare (Lubatkin, Schulze, Ling, & Dino, 2005; O’Donoghue & Rabin, 2000; Thaler & Shefrin, 1981). Unfortunately, despite the noted importance of self-control problems in private firms (e.g., Lubatkin et al., 2005; Schulze, Lubatkin, Dino, & Buchholtz, 2001), the concept remains poorly integrated in studies on the agency costs of private firms.

To gain a deeper understanding of self-control agency problems in private firms, we focus our attention on the resource allocation issues that are relatively understudied in agency theory literature (Cheng & Kesner, 1997; Kim et al., 2008). We argue that the coexistence of economic and non-economic goals that are important to a family owner could generate conflicting preferences for the allocation of firm resources. We study self-control problems by examining the performance consequences of financial slack allocation (Cheng & Kesner, 1997; Kim et al., 2008; Nohria & Gulati, 1996). Financial slack refers to uncommitted excess financial resources, or free cash flow, which can be allocated for numerous purposes (Bourgeois, 1981; George, 2005) and can be used to

seek, seize and pursue new market opportunities (Cyert & March, 1963). However, financial slack also provides firm owners with the opportunity to freely pursue their goals (Jensen, 1986; Schulze et al., 2003b), which can prompt complacency and the unprofitable use of resources (George, 2005; Leonard-Barton, 1992). Therefore, deeper understanding of self-control agency problems in private firms requires considering the availability of financial slack resources in the firm as well as the interests and goals that are most salient to family owners, which will drive their preferences for the allocation of financial slack and its implications on firm profitability.

Our study of 294 private firms in Italy adopts a lagged design combining survey and secondary data to show that family ownership alone is not sufficient to predict the effect of financial slack on the profitability of private firms, whereas factors that increase the potential salience of either economic or non-economic goals for family owners (namely, *overlap of family and firm name* and *overlap of family and firm wealth*) have a significant interactive effect with financial slack in predicting the profitability of private firms. Thus, this article makes three contributions: (1) providing evidence indicating self-control as a separate source of agency costs relevant in the allocation of financial slack in private firms; (2) extending the boundaries of agency theory by highlighting the importance of considering the sources of owner preferences and goals to understand agency problems arising from resource allocation in private firms; and (3) providing new theoretical insights on family firm heterogeneity explaining performance differences between firms with similar degrees of family ownership.

THEORY AND HYPOTHESES

The concept of self-control has its roots in psychology literature on temptation and visceral cues influencing individual choices, which shows that the human brain is formed of multiple systems responding variously to different goals and rewards (e.g., Gul & Pesendorfer, 2001; Rook, 1987). Similarly, neurophysiology suggests that different areas of the brain are associated with short-term impulsive behavior and long-term planned behavior (McClure, Laibson, Loewenstein, &

Cohen, 2004). Further, experimental and theoretical research points to self-control problems that challenge rational choice models by introducing the possibility of a dynamic inconsistency between goals referring to different points in time (e.g., Hoch & Loewenstein, 1991; Jain, 2009). Self-control problems have numerous applications in economic and social phenomena, including impulse buying, (over)eating, addiction and procrastination (O'Donoghue & Rabin, 2000), suggesting that individuals have biased preferences and that a decision that seems desirable in the distant future is often undesirable in the near future.

In applying the self-control concept to economic decisions, Thaler and Shefrin (1981) suggest that lack of self-control gives rise to issues that are fundamentally similar to traditional agency problems between people. However, differently from conventional agency problems, self-control agency problems are defined as inner conflicts with oneself arising when a single decision-maker's preferences are influenced by multiple and conflicting goals at the same point in time (O'Donoghue & Rabin, 2000; Thaler & Shefrin, 1981). Therefore, self-control agency problems concern the competing preferences for how firm resources should be allocated for different purposes (Cheng & Kesner, 1997). Consistent with the view that self-control problems can be particularly important in the context of resource allocation decisions, we focus our theory and hypotheses on the performance consequences of financial slack allocation. We first establish our baseline hypothesis on the importance of self-control agency problems in driving the relationship between financial slack resources and the profitability of private firms. Then, we turn our attention to a more explicit account of the sources of self-control agency problems associated with family ownership to identify factors that moderate this relationship.

The Relationship between Financial Slack and Firm Profitability in Private Firms

Financial slack resources are uncommitted excess financial assets including cash and receivables that accumulate as the firm performs well (Bourgeois, 1981). These are highly flexible and can thus be applied to a wide range of activities without putting firm survival at risk (Stevens,

Moray, Bruneel, & Clarysse, 2015). As these resources are easy to redeploy, financial slack resources can allow firms to engage in experimentation, risk-taking and innovation, and pursue long-term investments that will eventually increase firm profitability (Bourgeois, 1981; Cyert & March, 1963). However, financial slack resources are also a cost item for firms (e.g., Bourgeois, 1981) and closely resemble the concept of free cash flow (Jensen, 1986) typically seen by agency theorists as a source of inefficiency, unnecessary costs and waste. These issues are likely to become especially important when a firm has very high levels of financial slack, because the additional availability of resources enables powerful actors in the firm to perform a wide variety of tasks and pursue personal agendas (Jensen, 1986; Stevens et al., 2015). Beyond a certain structural level, financial slack resources may relax the attention of decision-makers to risk-taking and innovation (Kim et al., 2008; Nohria & Gulati, 1996) and increase the temptation to use firm resources for other ends, possibly at the expenses of firm profitability (Tan & Peng, 2003). For example, high financial slack could lead decision-makers to exploit existing competencies over exploring new competencies (Hu, Blettner, & Bettis, 2011) and pursue growth through non-profitable sales (Brush, Bromiley, & Hendrickx, 2000).

Based on these arguments, prior research suggests that low levels of financial slack will be positively associated with firm performance, whereas excessive financial slack will trigger agency costs that hurt firm profitability, thus suggesting a curvilinear (i.e., inverted U-shape) relationship between financial slack resources and firm profitability (see Daniel, Lohrke, Fornaciari, & Turner, (2004) for a review and meta-analysis). However, most of this research focuses on large and publicly traded firms and on traditional principal-agent or principal-principal agency issues, while theory and empirical evidence of this relationship in private firms is limited. One notable exception is George (2005), who argues that the negative agency consequences of high financial slack tend to disappear in private firms because “in private firms, principals and agents are more likely to be the same individuals” (2005: 662). Accordingly, George (2005) finds a positive relationship between

financial slack and firm profitability in a sample of US private firms. However, this conclusion contradicts other studies pointing to the existence of different types of agency issues in private firms, which arise when the disciplining effect of the market for corporate control is absent (Schulze et al., 2001).

Agency theory literature has paid limited attention to the possibility that individual owner-managers of private firms can have multiple goals driven by their links to numerous stakeholders who they must attempt to satisfy. Even a single owner-manager may thus be torn between multiple and competing goals, resulting in self-control agency problems (Thaler & Shefrin, 1981) that can lead to substantial performance heterogeneity among private firms. The two-self economic man modeled by Thaler and Shefrin (1981) suggests that the simultaneous existence of multiple goals can lead to an internal conflict similar to the principal-agent conflict between the owner and manager of a firm (Jensen & Meckling, 1976). Therefore, to provide a more complete account of the performance consequences of financial slack resources in private firms, extant research requires a theoretical extension to highlight the self-control agency issues potentially arising in the presence of high financial slack.

Self-control problems are likely to be lower when financial resources are limited, as in such cases firm owners have fewer opportunities to misallocate resources and a stronger incentive to tightly monitor resources to ensure they are not wasted. When the availability of financial slack resources increases, such incentives are likely to be relaxed and firm owners will have lower constraints in the allocation of financial slack resources. Therefore, when financial slack is very high, firm owners will have a greater ability to allocate such resources to projects and activities that fulfill their own goals even if such projects may have a negative impact on firm profitability. For example, firm owners may decide to invest in existing technologies rather than exploring new technologies simply because they are already familiar with these. Such a decision may lead to the deterioration of the firm's competitive advantage and ultimately harm firm profitability (Lubatkin et

al., 2005). Thus, contrary to the view that the allocation of slack resources in private firms is exempt from agency issues (George, 2005), we propose that financial slack will foster investments that favor future firm profitability up to a certain point. Thereafter, further financial slack will increase the likelihood of self-control agency problems that lead firm owners to allocate financial slack resources to actions that satisfy non-economic goals, even if leading to negative consequences for future firm profitability. Accordingly, we hypothesize that:

Hypothesis 1: In private firms, there is an inverted U-shaped relationship between financial slack and firm profitability.

Family Ownership and Self-Control Agency Problems in Financial Slack Allocation

In the debate on financial slack, there is increasing awareness that different types of owners have different preferences in allocating financial slack resources (Carney & Gedajlovic, 2002; Kim et al., 2008). Agency theory literature typically distinguishes between different classes of firm owners based on their ability to influence the management of the firm (David, Hitt, & Gimeno, 2001; Herrero, 2011; Hoskisson, Hitt, Johnson, & Grossman, 2002). Scholars have particularly highlighted the role of family owners (Durand & Vargas, 2003). Family ownership is very common (Faccio & Lang, 2002), especially in private firms (Astrachan & Shanker, 2003) where family owners typically have majority ownership and tend to select top managers based on family ties rather than professional expertise (Chrisman, Memili, & Misra, 2014; Fiegenger, 2010). As such, family owners have access to firm-specific information, dominate decision-making and are exempt from the internal bureaucratic constraints that limit the latitude of managerial actions in other firms (Carney, 2005; Gedajlovic et al., 2004; Schulze et al., 2001). Thus, family owners have greater freedom to unilaterally and idiosyncratically influence firm behavior, and are thus in a privileged position to allocate financial slack in ways that do not necessarily benefit the firm (Kim et al., 2008).

Empirical evidence on the influence of family ownership on firm performance is mixed (Carney et al., 2015). On one hand, some scholars emphasize the tendency of family owners to use their power to divert firm resources to pursue non-economic goals, even at the expense of firm profitability (Bertrand & Schoar, 2006; Gedajlovic et al., 2004; Schulze et al., 2001; Schulze, Lubatkin, & Dino, 2003a). Conversely, other scholars see family owners as highly committed investors with strong economic interest in increasing the firm's profits to preserve the firm's wealth-generating capabilities in the long run (Anderson & Reeb, 2003; Durand & Vargas, 2003; Le Breton-Miller & Miller, 2006). In view of these competing assumptions, we argue that considering family owners as a homogeneous block with a homogeneous set of preferences (Anderson & Reeb, 2003; Kim et al., 2008; Le Breton-Miller, Miller, & Lester, 2011) creates overly rigid assumptions on the goals that drive family owners' preferences. To improve our understanding of the influence of family owners on financial slack allocation, we contend that these assumptions must be revised to better specify the potential diversity of goals pursued by an individual family owner.

The degree of family ownership can indicate greater power and discretion to influence firm behavior, but such power and discretion, combined with slack availability and the simultaneous pursuit of multiple and conflicting goals, expose family owners to self-control problems that could have significant consequences on how they allocate firm resources. As family owners' individual values, desires and motives are arguably numerous and often competing, the existence of a self-control problem can cause the same level of family ownership to be associated with completely opposite firm behaviors. The growing recognition that economic and non-economic goals are intertwined in driving family owners' preferences and behaviors (Chrisman, Fang, Kotlar, & De Massis, 2015; Chua, Chrisman & De Massis, 2015, Zellweger et al., 2012a) suggests that the sources of family owners' preferences are key to understanding the increase in self-control problems and consequently predict whether they will use their influence to promote resource

allocations that result in superior or inferior firm profitability. Applying this logic to the case of slack resource allocation, we argue that the actual impact of financial slack on firm profitability should depend on the interests and goals that are most salient to family owners and drive their preferences for the allocation of financial slack. Thus, a more complete understanding of the agency consequences of family ownership requires a theory that explicitly considers both the family owners' ability to influence firm behavior and the sources of their preferences to use this ability to accomplish economic or non-economic goals (De Massis, Kotlar, Chua, & Chrisman, 2014).

Family Owner Goals and Self-Control Agency Problems

Family owners' economic goals primarily concern obtaining financial wealth for themselves and their relatives, while non-economic goals include several utilities that the family can derive from being in control of the firm (Chrisman, Chua, J, Pearson, & Barnett, 2012; Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007; Kotlar & De Massis, 2013). Both economic and non-economic goals concur in determining the ultimate influence of family owners on their firms (Chrisman & Patel, 2012; Gagné, Sharma, De Massis, 2014; Gómez-Mejía et al., 2007; Kotlar, Fang, De Massis, & Frattini, 2014; Zellweger et al., 2013). Family owners may decide to prioritize economic goals by allocating great portions of financial slack to investments in capital assets, R&D or other projects, initiatives and activities that could increase firm profitability in the long term (e.g., Chrisman et al., 2004; Le Breton-Miller & Miller, 2006). At the same time, family owners may prioritize non-economic goals by allocating financial slack to unnecessary investments that are instrumental to family reputation (Miller, Le Breton-Miller, & Scholnick, 2008) or to accumulate excessive reserves to lower risk and accommodate the family's need for stability (Gómez-Mejía et al., 2007). These allocations will provide benefits for the family, but would inevitably limit the resources available for innovation and growth, thereby hurting firm profitability in the long term. These goal tradeoffs and competing preferences for financial slack

allocation suggest that such slack resources can exacerbate self-control agency problems and the preferences of family owners therefore need to be more explicitly considered.

Here, we address the heterogeneity of family owners' willingness in relation to different interests and goals by focusing on the sources of potentially diverse preferences associated with the same level of family ownership: (1) the overlap between family and firm name, which captures the identity link between the family and the firm and indicates the potential salience of non-economic goals for family owners; (2) the overlap between family and firm wealth, which indicates the financial commitment of the family to the firm and captures the potential salience of economic goals for family owners. Examining how these two factors moderate the relationship between financial slack and firm profitability, we now turn to refining our understanding of family owners' influence on self-control agency problems and formulate more fine-grained hypotheses on their impact on the allocation of financial slack resources in private firms.

Overlap between family and firm name. Family owners' non-economic goals include fulfilling their identification needs (Gómez-Mejía et al., 2007), preserving the family dynasty (Casson, 1999), perpetuating family values (Handler, 1990) as well as family name recognition, respect, status and goodwill in the community (Deephouse & Jaskiewicz, 2013; Kotlar & De Massis, 2013). Family business literature suggests that these non-economic goals create socioemotional rather than financial wealth for family owners (Gómez-Mejía et al., 2007), causing tradeoffs that, we argue, can exacerbate the self-control agency problem associated with family ownership in private firms.

Family business scholars have particularly drawn on organizational identity theory to provide important insights into the drivers of non-financially motivated behaviors of family owners (Berrone, Cruz, Gómez-Mejía, & Larrazza-Kintana, 2010; Deephouse & Jaskiewicz, 2013; Zellweger et al., 2012a, 2013). Family owners are strongly embedded in their firms in many tangible and intangible ways (Aldrich & Cliff, 2003). The names of private family firms frequently include or derive from the surname of the family itself, and this overlap between family and firm

name underlines a strong identity link between family owners and their firms (Deepphouse & Jaskiewicz, 2013; Lange, Boivie, & Westphal, 2015). The firm's name is indeed the most direct response to fundamental identity questions such as "who are we?" and "what is most important to us?" (Albert & Whetten, 1985) and is therefore considered an important component of the firm's identity (Glynn & Abzug, 2002). When the firm takes the family owners' name, the family is not a faceless owner but rather mirrors the face of the firm (Berrone et al., 2010). From this standpoint, we could expect that when the family name is tied to a firm, a family owner will be more sensitive to the family's standing in the community and more careful of the family's reputation (Ketzer De Vries, 1993; Lange et al., 2015). This leads to the potentially greater salience of non-economic goals for family owners when their name is included in the firm's name: owners will become more exposed to the temptation to pursue investment strategies and other actions aimed at maintaining and increasing their family name recognition, social status and goodwill within their community.

In this regard, the business press is replete with well-known companies whose names and reputations are closely linked to that of their controlling families. Prior research indicates that family owners are inclined to nurture a positive image of their firm to increase the reputation of their family's name (Deepphouse & Jaskiewicz, 2013; Dyer & Whetten, 2006). These initiatives can provide a family owner with the opportunity to fulfill non-economic goals, but are not necessarily beneficial to firm profitability, presenting a situation that is consistent with Thaler and Shefrin's (1981) definition of self-control agency problem: faced with competing goals, family owners may be myopic and accommodate their priority of nurturing the family name through financial slack allocations that promote a positive image of the family and the firm, even if this clashes with their economic goal to sustain the firm's financial performance in the long term. Accordingly, including the family name in the firm name can increase the potential salience of non-economic goals for family owners and may thereby aggravate self-control agency problems and hurt firm profitability. For example, family owners may favor using the firm's money in excess to pursue a positive image

of the family name by investing in pollution-reducing activities beyond environmental standards (Berrone et al., 2010) or making charitable and philanthropic donations to the community (Campopiano & De Massis, 2015; Campopiano, De Massis & Chirico, 2014). In doing so, family owners can obtain reputational benefits for themselves and their family (Johnson & Greening, 1999), albeit reducing the financial resources available for firm growth and innovation, thus potentially jeopardizing future profits.

In summary, when there is an overlap between family and firm name, we expect that the identity-based connections between the family and the firm become stronger and the salience of non-economic goals for family owners is therefore likely to increase. Consequently, the overlap between family name and firm name exacerbates self-control agency problems, increasing the potential for a family owner to use financial slack resources to achieve non-economic goals and reducing the likelihood of using financial slack to pursue economic goals and improve firm profitability. In line with this view, we argue that the overlap between family and firm name will increase the potential of financial slack resources being used in ways that hamper firm profitability:

Hypothesis 2: The overlap between family and firm name negatively moderates the inverted U-shaped relationship between financial slack and the profitability of private firms.

Overlap between family and firm wealth. A second dimension that could potentially differentiate family owners' influence relates to the salience of their economic interests in the firm. Although agency theory and family business literature commonly imply that family owners' economic and non-economic goals are always in conflict, some scholars have recently emphasized that in some situations these goals can be compatible (Chrisman & Patel, 2012; Zellweger & Nason, 2008). Accordingly, we argue that there could be situations where the tradeoffs between economic and non-economic goals are less severe and the self-control agency problems associated with family ownership in private firms are thereby ameliorated. To identify the factors that could assist the alignment of economic and non-economic goals, we draw on corporate governance research,

particularly the notion that firm owners can differ in their behavior and incentives depending on whether they are dedicated or diversified owners (Connelly, Tihanyi, Certo, & Hitt, 2010; Porter, 1992). According to Porter (1992), dedicated owners maintain large equity shares in one or a very small number of firms, whereas diversified owners hold stakes in many different firms and frequently trade in and out of these firms. While diversified owners have short time horizons, dedicated owners are primarily interested in the long-run profitability of the firm (Koh, 2007). Moreover, dedicated owners can more effectively monitor the behavior of their firms (Chen, Harford, & Li, 2007) and benefit more from investments with long-term payoffs compared to diversified owners (David, O'Brien, Yoshikawa, & Delios, 2010; Schnatterly, Shaw, & Jennings, 2008).

Research typically describes family owners as highly undiversified investors (e.g., Anderson & Reeb, 2003), but scholars have recently noted that in reality many of these investors are more diversified and spread family wealth across many firms, keeping a smaller portion of their family wealth invested in each firm (e.g., Zellweger, Nason, & Nordqvist, 2012b). For the former, it would be reasonable to expect that the long-term profitability of the firm is likely to be a major concern as this has direct consequences on their family wealth, whereas the latter are more transient, focusing on short-term returns and trading in and out of firms in a portfolio investment logic. Family owners whose family wealth is highly concentrated in one firm are more likely to view this firm as an extension of their own wellbeing (Gómez-Mejía, Larraza-Kintana, Makri, 2003) and develop concerns for, and commitment to, preserving the wealth generating capabilities of firm assets for future family generations (Zellweger et al., 2012a). For example, Shleifer and Vishny (1986) observe that family owners' concern for the undiversified nature of their portfolios can lead to very cautious assessments of investment risks. Conversely, Faccio, Marchica, and Mura (2011) find that undiversified family owners tend to invest in any projects with potentially positive returns, regardless of their riskiness. Therefore, to the extent that family wealth overlaps with firm wealth,

we expect the greater potential salience of economic goals as well as the greater alignment between economic and non-economic goals for family owners.

Incorporating these insights into Thaler and Shefrin's (1981) theory of self-control, we expect that high overlap between family and firm wealth will lead to incentives and rules that can mitigate self-control agency conflicts. When the family's wealth is closely linked to the firm, family owners will have stronger incentives to use firm resources in ways that will not harm the profitability of the firm. Moreover, high wealth overlap is likely to motivate all family members to monitor the behavior of the firm, thereby setting informal rules that restrict the family owner's opportunities to engage in actions that are in conflict with the family's wealth.

In summary, we expect that dedicated family owners who have a high wealth overlap with the firm will have lower incentives to fulfill the non-economic goals of the firm at the expense of firm profitability. They will more likely view economic and non-economic goals as compatible and mutually reinforcing, and will be less subject to myopic temptations to pursue actions that accommodate non-economic goals and are thereby more likely to act as farsighted planners. Accordingly, when wealth overlap is high, we expect family owners to be more likely to allocate greater portions of financial slack to investments in capital assets and innovation or other projects and activities that could increase firm profitability in the long run. Under these conditions, the non-economic interests of the family are aligned with the profitability-oriented goals of the firm, minimizing self-control agency conflicts and promoting allocation decisions that turn financial slack resources into superior firm performance:

Hypothesis 3: The overlap between family and firm wealth positively moderates the inverted U-shaped relationship between financial slack and the profitability of private firms.

METHODS

Data collection

Our hypotheses are tested on a dataset constructed in a research program on firm strategy and performance (Mazzola, Sciascia, & Kellermeanns, 2013; Sciascia, Mazzola, & Kellermanns, 2014). We adopt a temporally lagged design with data collected in two waves: a first wave in 2000 to collect primary data relating to firm governance and non-financial aspects, and subsequently a second wave collecting secondary data on financial variables. In the first wave, 15,517 firms were randomly extracted from the entire population of independent, incorporated Italian firms and a questionnaire was sent to their CEOs. 620 firms returned the questionnaire. In the second wave, we collected archival data from the Italian chapter of the Bureau Van Dijk database to measure the dependent variable (i.e., firm profitability from 2001 to 2004) and other financial variables for these 620 firms. Financial data was available for 294 firms and we thus test our hypotheses on this final sample of 294 firms.

We consider this sample sufficiently large to avoid sampling errors and adequate to test our hypotheses through multiple regression analysis. Indeed, the sample size is larger than 58% of studies examining the relationship between financial slack and profitability reported in Daniel et al.'s (2004) meta-analysis. Published research has reported significant relationships between financial slack and firm performance even in studies with substantially smaller sample sizes (Combs & Ketchen, 1999; Hambrick, Cho, & Chen, 1996; Zahra, 1996). Moreover, to the best of our knowledge, our sample is larger than any published research using variables that are similar to the family name and family wealth overlap variables used in this study (Craig, Dibrell, & Davis, 2008; Deephouse & Jaskiewicz, 2013; Gallucci, Santulli, & Calabrò, 2015; Micelotta & Raynard, 2011; Sciascia, Nordqvist, Mazzola, & De Massis, 2015).

The response rate of the survey conducted in the first wave of data collection (4%) is relatively low compared to typically reported response rates for surveys mailed to top executives, which range between 10% and 15% (e.g., Bartholomew & Smith, 2006; Patel, Messersmith, & Lepak, 2013). This is unsurprising as prior research indicates that response rates are generally lower in privately

held firms (e.g., Messersmith & Guthrie, 2010) and particularly in Italy (e.g., Mazzola, Sciascia, & Kellermanns, 2013). Although the sample size relative to the population rarely affects the accuracy of the sample (Bryman & Cramer, 2001), the relatively low response rate warrants running additional analyses to ensure that response bias is not an issue and that the final sample is sufficiently representative of the population from which it was extracted (e.g., Eddleston, Otondo, & Kellermanns, 2008). To mitigate concerns pertaining to non-response bias, we compare the firm size and economic activity (manufacturing vs. service industries) of respondents versus non-respondents. The lack of significant differences indicates a low risk of non-response bias. Moreover, we assess the representativeness of our sample by comparing the firm size and economic activity of our sample with the 2001 Census of Industry and Services conducted by ISTAT (Italian National Institute of Statistics). The ISTAT dataset is constituted of 53.83% manufacturing vs. 46.17% non-manufacturing firms, and 96.28% small vs. 3.72% large firms (based on a threshold level of 250 employees). Similarly, our dataset is constituted of 48.62% manufacturing vs. 51.38% non-manufacturing firms, and 91.03% small vs. 8.97% large firms. Thus, the distribution of firms in our sample is very similar to the ISTAT database, meaning that the firms included in our study are sufficiently representative of Italian firms. Overall, these analyses support the adequacy of our sample size.

We test our hypotheses with OLS regressions. Below, we provide details on the variables used to test our hypotheses and those included to control for alternative explanations. All these variables derive from our data collection efforts in 2000, except for the dependent variable (i.e., profitability) that is lagged (average gross profit margin achieved in the subsequent 4 years). A discussion on this aspect is presented at the end of this section along with the other procedures adopted to address potential endogeneity issues.

Dependent Variable

The gross profit margin, namely, the difference between sales and the cost of goods sold scaled by sales, was chosen as the preferred measure of our dependent variable (i.e., *profitability*). This measure is consistent with our theoretical focus on self-control agency problems and the ensuing consequences associated with resource allocation, which are thought to be particularly important in the context of private firms (e.g., Coff, 1999). We also deemed gross profit margin to be the most suitable indicator of profitability in this study due to a dual rationale related to its nominator (the difference between sales and the cost of goods) and its denominator (sales). On the one hand, gross profit margin is more suitable than other indicators using net income as nominator (e.g., return on equity) not only because “possible variability in the tax treatment of income in private firms might undermine the reliability of estimates of performance” (George, 2005: 667), but also because gross profit margin does not include interest earned from financial investments, thus better capturing the impact of financial slack resources on business profitability. On the other hand, gross profit margin is more suitable in this specific study than so-called “asset-based profitability measures” such as total assets (e.g., return on assets, ROA) or capital employed (e.g., return on investments, ROI) as denominator. Indeed, the use of ROA would introduce two problems: first, it would generate biased estimations because its denominator (i.e., total assets) includes the nominator (i.e., quick assets) of our independent variable (i.e., financial slack resources). Second, it would introduce a measurement distortion that could lead to an incorrect interpretation of the effect of the behavior studied. In the case of financial slack resource extraction through dividends, ROA would be positively affected (because its denominator decreases) while, more correctly, gross profit margin would not show any improvement. Similarly, in the case of financial slack allocation to particularistic uses, gross profit margin would correctly register a decrease, while the effects on ROA would likely be mixed due to the concurrent reduction of the denominator (i.e., total assets). Conversely, if financial slack resources were invested in the firm for its future benefit, gross profit margin would show an increase, while the effects on ROA would likely be mixed, especially in the short run, because of an

increase of its denominator. The use of ROI (i.e., the difference between sales and the cost of goods sold scaled by capital employed) would partly avoid the first problem (i.e., the risk of endogeneity) given that capital employed excludes cash, but would not overcome the second problem (i.e., the risk of measurement distortion).

Independent Variables and Moderators

Slack resources can exist in many forms, including organizational capabilities and intangible assets, but these are difficult to capture, especially in a sample of private firms. Therefore, based on the well-established argument that managers extensively use financial ratios in making strategic decisions (Bourgeois, 1981), we rely on financial ratios to measure our independent variable *financial slack resources*. Consistent with prior research, we focus on the “unabsorbed” financial resources, those that are uncommitted, highly flexible and applicable to a wide range of activities, providing managers with the greatest degree of freedom in allocating these to alternative uses (Sharfman, Wolf, Chase, Tansik, 1988; George, 2005). In particular, we measure financial slack as the ratio of quick assets to liabilities (e.g., Greve, 2003; Kim et al., 2008), namely, the most widely used measure in prior studies according to Daniel et al.’s (2004) meta-analysis.

The two moderators used to test Hypotheses 2 and 3 are name overlap and wealth overlap respectively. *Name overlap* is measured with a dummy variable set to 1 when the firm name is the same as the family name, consistent with prior studies and the view that the overlap between family and firm name is a strong indication of the link between family and firm identity (e.g., Deephouse & Jaskiewicz, 2013; Lange et al., 2015). The *wealth overlap* variable captures the extent to which family owners are dedicated to the firm, as opposed to diversified. Consistent with Porter’s (1992) definition of dedicated firm owners and the operationalization in accounting research (e.g., Bushee, 1998), we focus on the diversification of firm owner investment portfolios. However, existing measures have been developed in the context of institutional shareholders of publicly traded firms for which public information is available, whereas for owners of private firms, this constitutes

highly sensitive information. As such, we traded measurement accuracy for the possibility of accessing such information, opting for a 4-point scale capturing the degree to which the wealth of family owners and their family members is invested in the firm: less than 25%, between 26% and 50%, between 51% and 75%, over 75% (e.g., Sciascia et al., 2015). The ordinal scale adopted is able to capture the extent to which the wealth of the entire family overlaps with firm wealth (lightly, moderately, significantly or heavily) without excessively worrying respondents.

Control Variables

We adopt several control variables to assess whether our proposed effects drive our results versus alternative explanations: firm size, industry, sales internationalization, past profitability, potential slack resources, board presence, family council presence, family ownership dispersion and family ownership. We control for firm *size* as larger firms may have developed more sophisticated planning and control systems that can affect profitability (Kellermanns, Eddleston, Sarathy, & Murphy, 2012). We use number of full-time employees (at the start of 2000): the average number of employees is 100, with a standard deviation of around 319. For kurtosis considerations, we transform this measure into its logarithm. We also control for potential *industry* effects using the following dummy variables: agriculture, manufacturing, services, construction, extraction and mining, transport, retail, commerce and other. This choice was driven by the fact that these industries are characterized by different average levels of both financial slack resources and profitability (George, 2005). We additionally control for *sales internationalization*, i.e., percentage of sales abroad, given that this is considered a correlate of profitability (Lu & Beamish, 2001). Moreover, we control for *past profitability*, measured with the gross profit margin achieved in 2000, since good performance in subsequent years can derive from past good performance (Brush et al., 2000). We control for *potential slack* resources to clearly distinguish the effects of this type of slack from financial slack resources (or “unabsorbed slack”). Potential slack is measured as the ratio of debt to equity in 2000 (Greve, 2003).

Consistent with our argument that the self-control agency problem is an additional type of agency problem associated with family ownership in private firms, we include control variables accounting for traditional principal-agent and principal-principal agency issues. First, we include two dichotomous variables indicating the *presence of a board of directors* and the *presence of a family council* to control for type I (principal-agent) agency costs (Chrisman et al., 2004; Schulze et al., 2001). Second, we control for *family ownership dispersion* as a proxy of type II principal-principal agency conflicts (De Massis, Kotlar, Campopiano, & Cassia, 2013; Schulze et al., 2003b). To this end, we use the number of family owners, since it is not possible to adopt better measures such as the Herfindahl index. However, prior research shows that the two measures can be alternatively used without affecting the results (De Massis et al., 2013). Last, we control for *family ownership* with a continuous variable, ranging from 0 to 100, obtained by asking CEOs to report the percentage of firm ownership held by their family (e.g., Chrisman et al., 2012; Zellweger et al., 2012a).

Addressing Endogeneity Issues

Testing our hypotheses also requires rooting out the alternative explanation that the relationships between financial slack, family ownership and firm profitability are the result of endogeneity (Semadeni, Withers, & Certo, 2014). In particular, two different issues could potentially introduce endogeneity in our OLS regression models: reverse causality and omitted variables.

In the first case, if profits are an important source of cash flow, and cash flow is a major component of financial slack, the dependent variable may influence the independent variable in non-trivial and dynamic ways. As a consequence, the results of the regression models would be biased and inconsistent. An appropriate specification of time is crucial to address this issue (Mitchell & James, 2001). Hence, we use a lagged dependent variable by measuring financial slack in 2000 and firm profitability in the subsequent years. As prior research suggests that slack

resources take time to convert into performance-enhancing or performance-reducing activities (Daniel et al., 2004), we consider the average gross profit margin values from 2001 to 2004 to generate our final lagged value. This 4-year window is consistent with prior research on the relationship between financial slack resources and performance in private firms (Daniel et al., 2004; George, 2005). The results reported below are robust to alternative specifications of the dependent variable, measured as the punctual gross profit margin values in 2001 and 2004.

In the second case, if family owners have some risk preferences for the level of financial slack largely unobserved in the regressions, the exogeneity condition for OLS regressions would be violated and endogeneity would be present. The key to addressing this problem is to rely on an instrument to model the endogenous variable (i.e., family ownership). The instrument must fulfill two conditions: relevance and exogeneity (Kennedy, 2008). The duration of control could increase the perceived value of owning a firm and the attractiveness of continued family ownership (Zellweger et al., 2012a), but not firm profitability. We measure the duration of control with an open-ended question on the age of the firm, since in all cases in the sample, the founding families are still in control of the firms. For kurtosis considerations, we transform this measure into its logarithm. In a first stage, we regress family ownership against the control variables. In a second stage, we add the instrumental variable, which is significant ($\beta = .20$; $p < .01$). The adjusted R-square increases from .27 to .29 and the F-statistic increases from 6.55 to 9.95. As both the relevance and exogeneity conditions are fulfilled (Semadeni et al., 2014), we use the predicted values of family ownership in our OLS regressions. The results reported below are qualitatively the same when using the real values of family ownership, suggesting that endogeneity is not a problem in our sample.

RESULTS

In Table 1, we present the correlations among the variables. Multicollinearity is not a concern because the highest correlation coefficient is .46 (i.e., between past profitability and profitability)

and in the OLS regression analyses supporting our hypotheses, the variance inflation factors and condition indexes remain under the usual thresholds (Hair, Black, Babin, & Anderson, 2010). We also highlight that family ownership and financial slack resources are not correlated (correlation coefficient equal to $-.05$, n.s.), thus overcoming any remaining doubts of model endogeneity.

Insert Table 1 about here

In a preliminary regression analysis, we explore the influence of family ownership on the relationship between financial slack and profitability. Consistent with our assumption that the degree of family ownership is not sufficient to predict whether financial slack will be allocated for pro-family or pro-business purposes, our results indicate that family ownership does not significantly moderate the relationship between financial slack and family ownership. More specifically, the regression coefficients of the product between financial slack resources and family ownership is negative but not significant, and the significance level of the product between financial slack resources squared and family ownership is positive and only marginally significant ($p < .10$). Table 2 shows the results of the regression analysis. We first introduce control variables and moderators in model 1 and then enter financial slack and its squared term in model 2 to test H1. In model 2, we find a positive significant coefficient for financial slack resources and a negative significant coefficient for financial slack resources squared (F change = 27.052 ; $p < .001$). This result provides support for H1, i.e., an inverted U-shaped relationship between financial slack resources and profitability.

Insert Table 2 about here

In model 3, we test and obtain support for the predicted negative interaction effect between financial slack resources and name overlap on gross profit margin as the regression coefficient of the product between financial slack resources squared and name overlap is negative and significant

($\beta = -.54$; $p < .001$). This means that the inverted U-shaped relationship between financial slack resources and gross profit margin is affected by name overlap (F change = 12.164; $p < .001$). To better interpret this result, we plot the identified relationships between financial slack resources and gross profit margin in firms with and without name overlap (Aiken & West, 1991; Cohen, Cohen, West, & Aiken, 2003). Based on the regression coefficients in model 3, we obtain the curves shown in Figure 1. The optimal financial slack resources level when there is no name overlap is .22 (i.e., quick assets equal to 22% of liabilities) and decreases to .11 (i.e., quick assets equal to 11% of liabilities) when there is name overlap. Moreover, profitability is always higher when there is no name overlap rather than when there is name overlap, especially at higher levels of financial slack. Therefore, we can conclude that H2 is empirically supported: the overlap between family and firm name likely creates incentives to divert a higher portion of slack resources away from profitable projects and activities.

Insert Figure 1 about here

In model 4, we find support for the predicted positive interaction effect between financial slack resources and wealth overlap on gross profit margin as the regression coefficients of the product between financial slack resources squared and wealth overlap is positive and significant ($\beta = .56$; $p < .001$). This means that the inverted U-shaped relationship between financial slack resources and gross profit margin is affected by wealth overlap (F change = 8.526; $p < .001$). Also in this case, we plot the identified relationships in Figure 2 based on the regression coefficients obtained in model 4. More specifically, following Aiken & West (1991), we plot the relationship between financial slack resources and gross profit margin at low and high levels of wealth overlap. By low levels of wealth overlap we mean wealth overlap below 25% and by high levels of wealth overlap we mean wealth overlap above 75%. As shown in Figure 2, at high levels of wealth overlap there is no inflection point: the curve assumes a J shape. An inflection point is present only if wealth overlap is below

25% and at .54 (i.e., quick assets equal to 54% of liabilities). Moreover, profitability is always higher when wealth overlap is higher rather than when wealth overlap is lower, especially at higher levels of financial slack resources. Therefore, we can conclude that H3 is also empirically supported: for higher levels of wealth overlap, family owners allocate a higher portion of slack resources to projects and activities that increase profitability.

Insert Figure 2 about here

Last, as an additional robustness test, we estimate a full model where all the interaction terms are entered simultaneously. The model has a lower quality (i.e., a lower F value and a lower significance of the F change value) and the linear interaction terms become non-significant. However, the sign, size and significance level of the relevant coefficients (i.e., financial slack resources, financial slack resources squared, the product between financial slack resources squared and name overlap and the product between financial slack resources squared and wealth overlap) do not significantly change.

DISCUSSION

Drawing on agency theory and family business literature, we examine and show that in the presence of financial slack resources, family ownership can both exacerbate and improve agency problems in private firms. Even after controlling for traditional sources of agency costs, we find an inverted U-shaped relationship: financial slack is initially beneficial but very high slack hurts the profitability of private firms. Thus, our findings indicate that private firms are not exempt from agency costs, but the coexistence of multiple goals combined with bounded rationality and the absent disciplining effect of capital markets can leave a firm owner torn between multiple preferences for the allocation of firm resources, some of which may hurt firm profitability and compromise their own financial welfare (Lubatkin et al., 2005; O'Donoghue & Rabin, 2000; Thaler & Shefrin, 1981). In contrast to the dominant view in agency theory (Bertrand & Schoar, 2006;

Kim et al., 2008), we also find that categorizing family owners as a single category may lead scholars to overlook how and why self-control agency problems can lead some private firms to allocate slack resources to the benefit or detriment of firm profitability. Thus, if used alone, family ownership entails theoretical limitations and empirical indeterminacy (De Massis et al., 2014). When taking into account the factors that increase the potential salience of economic or non-economic goals for family owners, we obtain a better understanding of how ownership structure shapes agency conflicts in private firms and more precise predictions of the relationship between financial slack and firm profitability.

These findings contribute to literature on financial slack by providing evidence on how financial slack relates to firm performance in private firms. This relationship has been scantily examined in prior research with the notable exception of George (2005) who finds a curvilinear yet monotonic positive relationship between financial slack and firm performance in a sample of US private firms. In contrast, we find an inverted U-shaped relationship, where high levels of financial slack have a negative effect on the profitability of private firms. Our study was conducted in Italy, a Catholic country where the significance of the family institution and family values is higher compared to Anglo-Saxon countries (Greenwood, Díaz, Li, & Lorente, 2010; James, 2006). Thus, it is possible that the salience of non-economic goals for firm owners is generally higher in our sample compared to George's (2005). We argue that the negative consequences of financial slack on firm profitability relate to self-control problems, a separate source of agency costs arising when firm owners are torn between economic and non-economic goals that imply different allocations of firm resources.

Our findings consequently extend prior literature by showing that private firms are not exempt from agency costs (George, 2005; Herrero, 2011) and point to the importance of self-control agency problems that can play a prominent role in the allocation of financial slack resources. While concentrated ownership and the overlap of ownership and management can minimize traditional

agency conflicts between people, the absent disciplining effect of the market for corporate control can exacerbate the self-control problems arising when an owner pursues conflicting goals, which create conflicts of interest with oneself. As such, this study enhances our understanding of the performance consequences of slack resources in private firms, showing that corporate governance and agency problems interact with resource-based issues in determining firm profitability (e.g., Makadok, 2003). Moreover, our focus on private firms in a developed country responds to prior calls to conduct careful inquiries comparing and contrasting agency costs encountered in different types of firms and across different contexts (Bruton et al., 2010; Dharwadkar, George, & Brandes, 2000; Garg, 2013; Kim et al., 2008; Tan, 2002).

Additionally, our findings extend previous approaches in corporate governance research (e.g., David, Yoshikawa, Chari, & Rasheed, 2006; Hoskisson et al., 2002; Kim et al., 2008) by suggesting that even a single owner can have multiple goals at a single point in time. In particular, our findings highlight that owners differ in terms of their ability - their power and discretion to dispose of firm resources - and their willingness - their interests and goals in using such power and discretion for a specific purpose. Both these dimensions are needed to understand the complexity of agency relationships in private firms. We use family ownership as a case in point, given that family owners are reported to have particularly high discretion in influencing firm behavior (Carney, 2005) and are characterized by multiple and competing selves that involve both economic and non-economic motives (Chrisman & Patel, 2012; Kotlar & De Massis, 2013). While the case of family ownership is particularly evident and intuitive, the theory developed in this article can be generalized across many types of owners.

Other scholars have emphasized the importance of self-control agency problems associated with private family ownership (Gedajlovic et al., 2004; Schulze et al., 2001). The notion that economic and non-economic goals coexist is present in several theories in family business research, including agency theory (e.g., Chrisman, Chua, & Sharma, 2005), the behavioral agency model

(e.g., Chrisman & Patel, 2012; Gómez-Mejía et al., 2007) and stewardship theory (e.g., Corbetta & Salvato, 2004). However, our study extends the too-rigid assumptions of these theories on goals pursued by family owners and specifies in more detail the mechanisms of self-control agency problems that increase the potential salience of some goals compared to others in the context of financial slack allocation. This article thus contributes important insights on the role of owners in allocating firm resources and the ensuing self-control agency costs, but also offers additional insights on the tradeoff between economic and non-economic goals that we hope can inform other theoretical frameworks. In particular, our study makes a step forward in the difficult task of identifying proxies that could capture the potential salience of economic or non-economic goals for family owners, namely, the overlap between family and firm name and between family and firm wealth. As such, our findings advance a theoretical link between wealth and name overlap, firm owner goals and the policies adopted in allocating firm resources. A better understanding of the mechanisms through which these two sources of economic and non-economic sets of preferences shape firm behavior would be a fruitful area for future research aimed at disclosing the nature of owners' goals as well as their organizational consequences.

Finally, our findings contribute to family business literature by adding new evidence to the debate on the effect of family ownership on firm performance (e.g., Carney et al., 2015; De Massis, Kotlar, Campopiano, & Cassia, 2015; Mazzola et al., 2013; Miller et al., 2008; Villalonga & Amit, 2006) and reconciles prior controversial findings by introducing the role played by family owners' multiple goals and preferences and the associated self-control agency problems that arise in private firms. Specifically, our study suggests that when traditional principal-agent and principal-principal agency conflicts are minimized, as in the case of private family firms, the overall agency costs incurred depend primarily on the multiple preferences of firm owners and the ensuing self-control problems that involve conflicts of interest with oneself as opposed to conflicts of interest with others. This theoretical extension allows more precise predictions on the profitability of private

firms. As such, our study also adds to our understanding of the heterogeneity of family firms by theoretically examining and empirically showing that family ownership does not univocally result in decisions that either benefit or detract from firm performance, but that such decisions depend primarily on the relative importance of economic and non-economic goals to family owners (e.g., Chrisman et al., 2012; Chua, Chrisman, Steier, & Rau, 2012).

Implications and Limitations

Our findings suggest that despite that traditional agency conflicts between principals and agents and between multiple principals are generally lower in private firms, these firms are exposed to other agency costs that entail a family owner's inner conflicts of interest with her/himself as opposed to with others. However, empirical evidence is still divided as to whether private family-owned firms need to implement the costly mechanisms, such as a board of directors and strategic planning, commonly used to mitigate agency conflicts in listed companies (e.g., Chrisman et al., 2004; Schulze et al., 2001). As we argue and our results suggest, it is likely that family owners have at least two conflicting identities and interests, hence exposing themselves to self-control agency problems that could lead them to inadvertently make use of firm resources in ways that accommodate their non-economic goals but potentially jeopardize firm performance. According to Thaler and Shefrin (1981), the external scrutiny provided by governance bodies (e.g., board of directors) and the decision-making rules imposed by strategic planning could prove useful in addressing self-control agency issues. Therefore, our evidence indicates that private family-owned firms may need such agency control mechanisms despite their advantages in terms of traditional agency costs incurred. However, the extent to which these mechanisms are needed ultimately depends on the set of goals and preferences that are most salient to the family owner.

The empirical study presented in this paper has several strengths, such as the innovative measurement of proxies that capture the potential salience of economic and non-economic goals for family owners (respectively, through the overlap between family and firm wealth and the overlap

between family and firm name) and the thorough consideration of endogeneity issues (Semadeni et al., 2014). Nonetheless, our study has some limitations that need to be acknowledged and also provide further opportunities for future research. First, a panel design would have been preferable. However, the use of lagged averaged profitability data, difficult to obtain for private firms, alleviates this concern. Further studies could test the robustness of our findings via a panel design, controlling for the stability of the independent variables. Second, data were collected exclusively in Italy. Although Italy is an interesting context due to the dominant role of family owners in private firms (Caselli & Di Giuli, 2010) and the great importance of the family unit in the Italian culture, our results may be culturally constrained. Future research could consequently test if our results hold in other geographic settings or if the cultural context is able to influence the relationships between financial slack resources, family ownership and profitability. Third, our proxies of family owners' interests and goals are of an indirect nature. A direct measure of goal salience is difficult to develop (Kotlar & De Massis, 2013) but would alleviate our concerns. The overlap between family and firm wealth and the overlap between family and firm name were respectively measured as an ordinal and dummy variable: future research could use interval variables to increase the accuracy of the results. Most importantly, our theoretical development focuses on self-control agency problems that have a psychological foundation, occur at the individual level and materialize as inner conflicts of interest with oneself. However, our empirical study and the measures employed could not directly assess this type of agency conflict. This represents an important area for future research to investigate the nature and sources of self-control problems in greater depth. Future research drawing on the insights from this study and examining the individual-level aspects of self-control problems could help address interesting and unexplored questions that are relevant to developing knowledge on the influence of ownership structure on firm behavior and organizational outcomes.

Our study examines the consequences of self-control agency problems on firm profitability. Self-control problems can also affect other organizational outcomes and our theoretical approach

could hence be used to examine the impact of ownership structure on other firm behaviors. For example, traditional agency conflicts of interest have been shown to be particularly relevant to understanding diversification (Tihanyi, Johnson, Hoskisson, & Hitt, 2003), innovation strategy (Hoskisson et al., 2002; Kim et al., 2008) or accounting practices (Young, Peng, Ahlstrom, Bruton, & Jiang, 2008). In light of our results, it would be interesting to extend the literature by examining how the ability (i.e., power) and willingness (i.e., goals) of owners concur in affecting organizational outcomes. In addition, ability and willingness can play a dissimilar role in different types of ownership. Future research should explore the differential role of owner power and goals in shaping self-control agency conflicts in different types of ownership contexts and their consequences on different types of organizational outcomes. Moreover, it would be interesting for future studies to examine the effect of the heterogeneity of owner power and goals on self-control agency problems in different types of firms, such as cooperative ventures, widely held corporations, venture capital-backed firms and state-owned firms. Ideally, this would be undertaken through comparative studies across different types of firms and would further advance our theorizing on the role of ability and willingness as key drivers of the heterogeneity of family firms. Seeking the answers to these questions indicates the next phase of clarifying the unique mechanisms through which the ownership structure of a firm shapes firm behavior and key organizational outcomes.

CONCLUSIONS

In assuming that private firms are exempt from agency costs and treating family owners as a homogeneous group of firm owners with consistent goals, prior studies have neglected self-control agency problems and provide an incomplete account of agency costs associated with family ownership. In the context of private firms in Italy, we show that family ownership has a mixed effect on the relationship between financial slack and profitability. When explicitly considering factors that increase the potential salience of either economic or non-economic goals for family owners, we are able to better predict the agency issues and performance consequences of financial

slack. Our study suggests that goals are crucial in predicting firm behavior and performance, offering important opportunities to advance understanding of agency costs in private firms.

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Table 1
Descriptive Statistics and Correlations

Variables	Mean	SD	1	2	3	4	5	6	7	8	9
1. Size	1.50	.61									
2. Agriculture	.02	.15	-.08								
3. Manufacturing	.41	.49	.32**	-.13*							
4. Services	.14	.35	.02	-.06	-.34**						
5. Construction	.05	.23	-.07	-.04	-.20**	-.10					
6. Extraction and mining	.00	.06	.08	-.01	-.05	-.02	-.01				
7. Transport	.04	.19	.05	-.03	-.16**	-.08	-.05	-.01			
8. Retail	.18	.38	-.31**	-.07	-.38**	-.19**	-.11	-.03	-.09		
9. Commerce	.07	.26	-.12*	-.04	-.24**	-.12*	-.07	-.02	-.06	-.13*	
10. Other	.07	.26	-.01	-.04	-.24**	-.12*	-.07	-.02	-.06	-.13*	-.08
11. Sales internationalization	.18	.26	.22**	-.04	.38**	-.19**	.02	.06	-.06	-.20**	-.17**
12. Past profitability	4.63	5.07	.02	-.04	.10	-.04	.07	-.17**	-.11	.01	-.12*
13. Potential slack	3.21	63.72	.02	.01	-.13*	.08	.01	.00	.02	.04	.02
14. Board of dir. presence	.68	.47	.23**	.06	.04	.01	-.09	.04	-.02	.01	-.08
15. Fam. council presence	.31	.46	-.03	-.06	.00	-.08	.00	-.04	.04	.04	.01
16. Fam. ownership dispersion	2.66	2.37	.18**	-.01	.05	-.05	.13*	-.04	-.07	.00	.00
17. Family ownership	77.75	35.92	-.03	-.03	.06	-.10	-.01	-.04	-.05	.02	.11
18. Financial slack	.10	.15	-.06	.00	-.05	.12*	-.03	-.02	.02	-.00	-.03
19. Wealth overlap	2.58	1.06	.31**	.09	.14*	-.21**	.03	-.04	.01	-.00	-.04
20. Name overlap	.36	.48	.03	.02	.09	-.15*	-.06	.08	-.04	.04	.05
21. Profitability	3.88	4.44	-.03	-.07	.10	.13*	.04	-.05	-.09	-.03	-.14*
	10	11	12	13	14	15	16	17	18	19	20
11. Sales internationalization	.04										
12. Past profitability	.04	.11									
13. Potential slack	.04	-.05	-.02								
14. Board of dir. presence	.00	-.00	.01	.11							
15. Fam. council presence	.06	-.00	-.01	.06	.03						
16. Fam. ownership dispersion	-.06	.06	.06	-.04	.09	.19**					
17. Family ownership	-.02	.10	.09	-.03	-.18**	.31**	.43**				
18. Financial slack	-.02	.11	.24**	.02	.02	.06	.02	-.05			
19. Wealth overlap	-.02	.18*	.16*	.02	.08	.10	.11	-.01	.10		
20. Identity overlap	-.03	.07	-.03	-.06	.08	.13*	.24**	-.00	.28**	.01	
21. Profitability	-.08	.07	.46**	.05	.03	-.00	.12*	.04	.11	.05	-.07

N=294; * = p<.05; ** = p<.01; *** = p<.001

Table 2
Regression Analysis

	Model 1	Model 2	Model 3	Model 4
Size	-0.141	-0.135	-0.111	-0.112
Agriculture	-0.057	-0.055	-0.049	-0.054
Services	0.061	0.069	0.081	0.057
Construction	-0.085	-0.075	-0.056	-0.054
Extraction and mining	0.052	0.057	0.056	0.032
Transport	-0.112	-0.102	-0.097	-0.112
Retail	-0.148**	-0.117	-0.112	-0.099
Commerce	-0.11	-0.1	-0.089	-0.114
Other	-0.022	-0.056	-0.049	-0.042
Sales internationalization	-0.012	-0.018	-0.074	-0.023
Past profitability	0.498***	0.568***	0.586***	0.468***
Potential slack	0.013	-0.001	-0.001	-0.008
Board of directors presence	-0.059	0.012	0.022	0.03
Family council presence	0.011	0.008	-0.041	-0.03
Family ownership dispersion	0.203	0.126	0.085	0.095
Family ownership ^a	-0.116	-0.07	-0.043	-0.019
Name overlap	-0.081	-0.055	-0.062	-0.053
Wealth overlap	0.021	0.02	0.029	0.072
<i>Hypothesis 1</i>				
Financial slack		0.667***	0.664***	0.719***
FS squared		-0.957***	-0.857***	-1.008***
<i>Hypothesis 2</i>				
Name overlap x Financial slack			0.298*	
Name overlap x Financial slack squared			-0.542***	
<i>Hypothesis 3</i>				
Wealth overlap x Financial slack				-0.401**
Wealth overlap x Financial slack squared				0.563***
R2	0.303	0.480	0.549	0.531
Adj. R2	0.225	0.414	0.486	0.465
Delta R2		0.177***	0.069***	0.051***
F	3.880***	7.327***	8.702***	8.067***
F change		27.052***	12.164***	8.526***

N=294; Standardized regression coefficients; * p<.05; ** p<.01; *** p<.001;

^a Re-estimated variable using duration of family control as an instrumental variable

Figure 1

Financial Slack Resources, Name Overlap and Gross Profit Margin

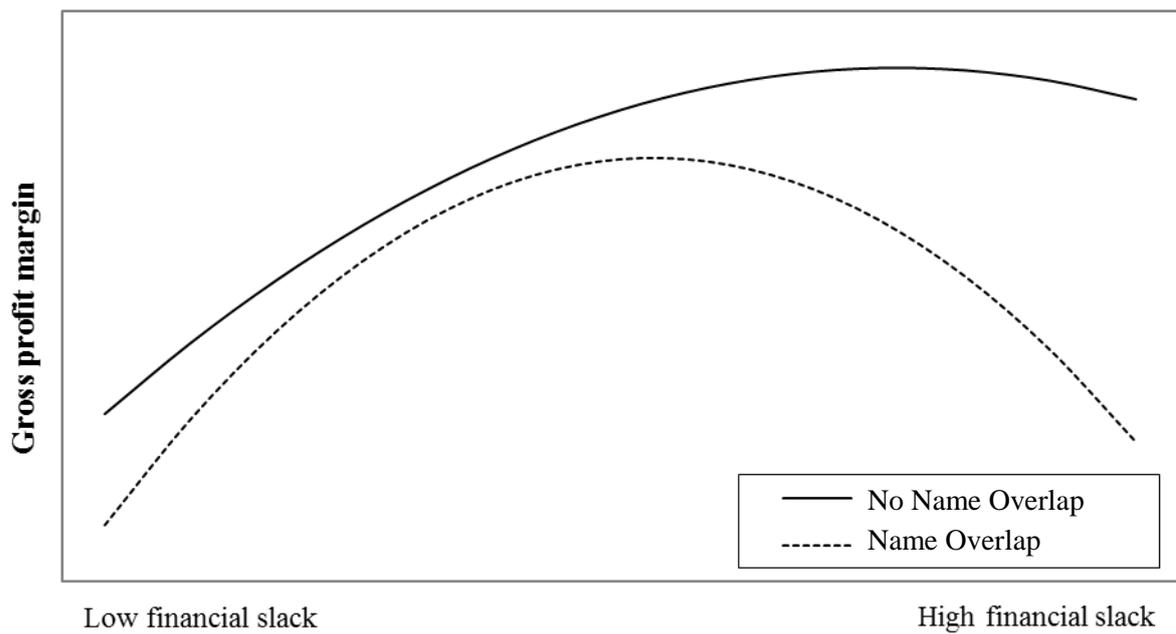


Figure 2

Financial Slack Resources, Wealth Overlap and Gross Profit Margin

