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The Effect of Large Controlling Shareholder's Presence and Board of Directors on Firm Value

Aymen JEBRI

Faculty of Economic Sciences and Management of Tunis, Tunisia

Tél: 216 – 22 974 891 *E-mail:* aymen.jbr@gmail.com

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Abstract

This study investigates the effect of large controlling shareholder's presence and board of directors on firm value.

The empirical results, based on a unique database of French firms, show a positive effect of cash-flow rights held by the largest controlling shareholders suggesting that an increase in cash-flow ownership makes the controlling shareholder's interest more closely aligned with other shareholders and incited to create value.

Our results also reveal that the wedge between voting and cash-flow rights of controlling shareholders have a negative effect on firm value.

Finally, our empirical evidence shows a positive but not significant effect of the board structure on firm value. In fact, efficient boards should have a majority of independent directors able to monitor and advice managers since the more directors are independent the more they are likely to provide a valuable contribution to firm valuation. However, if a board appoints busy directors, controlling and advisory capabilities on managers' decisions will be limited since there is no sufficient time. We should therefore expect to see resource diversion and decreased firm value.

Keywords: Ownership structure, Corporate Control, Corporate Value, French firms

Introduction

Prior studies have focused on ownership structure as a primary determinant of agency problems that may arise between atomistic shareholders and powerful controlling managers (e.g. Jensen & Meckling (1976): Demssetz (1983) and Demsetz & Villalonga (2001)). These conflicts are stemmed from managers' tendency to divert resources for their personal consumption. This is a focal point in the study of modern corporations when ownership is widely diffused such as in the US and the UK (Berle & Means (1932)).

An important question to ask is why do firms choose dispersed ownership if there are agency problems? One answer given by Bolton & Von Thadden (1998) is that dispersed ownership provides greater market liquidity and better risk diversification.

Since the controlling owner has the power and the incentive to discipline managers, he may interfere to put constraints on managerial initiative and hence protect himself (Burkart and al. (1997)). But, as he maintains the control of the firm, Claessens and al. (2002) document that another governance problem may arise between that controlling shareholder and minority shareholders. This is the type Il agency problem that dominates the continental Europe (Enriques & Volpin (2007)).

Studying 5232 firms in 13 Western European countries, Faccio & Lang (2002) find that 44, 29% of the samples are family controlled. More than two-third of these firms have family members in top management. Moreover, controlling shareholders seek a lot of control without owning higher stakes. La Porta and al. (2002) carry the same task for 27 wealthy economies. They contend that agency costs are extremely sharp in countries with weak legal investors' protection since controlling shareholder can easily extract private benefits that otherwise would have been shared with other shareholders.

Other complementary studies dealt with the effect of the controlling party on firm value. They consider two opposite effects, namely commitment and entrenchment. On the one hand, the desire to divert resources is decreasing with cash-flow ownership. Controlling shareholders owning greater cash-flow rights are more prone to better run their firms and generate presumably higher firm value.

The evidence highlights the positive incentive of cash flow ownership by controlling shareholders (La Porta and al. (2002)). On the other hand, when ownership exceeds a certain point, controlling shareholders win virtually the full control of the firm. Thus, they might use the firm to divert resources to themselves (Shleifer & Vishny (1997)). This is consistent with the findings of Stulz (1988) suggesting that the entrenchment effect begins to overcome the incentive effect as managerial ownership and control rights increase.

Firms tend to have a controlling shareholder - either an individual or a family-who exerts excess of control over the firm while holding only a small fraction of cash-flow rights. This is, exactly, the problem of separation between cash-flow and voting rights stressed in Claessens and al. (2002) and Faccio & Lang (2002). It may be ensured, mainly, through dual-class shares, pyramids and cross-holding structures (Bebchuk and al (2000)).

Controlling shareholders with excess control tend to monitor the management team and interfere in the project selection (Graziano & Luporini (2005)). The latter are also able to influence the board selection process (Yeh & Woidtke (2005)). The premise of this thesis is to test whether their actions ultimately influence firm value or strong boards could offset their effect if ever it exists.

Our study is close to that of Yeh & Woidtke (2005). They make insight into the influence of both ownership structure and board composition as firm-level governance variables on firm value. If the controlling shareholder would like to entrench himself, he will have the incentive to divert corporate resources from minority shareholders to himself for personal consumption.

Under concentrated ownership, busy outside directors have received less attention despite their significant effect on firm valuation (See; Ferris and al (2003)). In this study, we provide a theoretical and empirical framework for this effect. Since additional directorships decrease oversight of management (FIch & Shivdasani (2004)), we assume that a controlling shareholder tends to appoint busy outside directors to entrench himself.

Setting on the management board, he can reduce managerial discretion and prevent managers from firm-specific investments that can help to improve firm value (Burkart and al. (1997)). But, when the controlling shareholder sits in the supervisory board, he cannot interfere with managers' decisions. As a consequence, his ability to expropriate minority shareholders decreases.

To test these hypotheses, we use a sample of 346 French firms from NYSE EURONEXT in 2008. Similar to Yeh & Woidtke (2005), we find that the largest controlling shareholders have a significant effect on firm value. First, we find that Ln (Tobin Q) is positively related to ultimate cash-flow rights held by the largest controlling shareholders while it is negatively related to the wedge between their voting rights and cash-flow rights. In accordance with previous research, we find that French firms benefit from appointing independent directors but it is contingent upon their busyness.

Our thesis is the first that considers busyness hypothesis under concentrated ownership. The evidence suggests that busy outside directors make the controlling shareholder more likely to interfere with management team due to the lack of time. Finally, this thesis contains a large literature on CEO duality. It shows that firms profit from having the same person being the CEO and the Chairman of the board.

We attempt to analyse the conflicting evidence between controlling and minority shareholders and to understand the board of directors. Three axes define our subject namely ownership, control and management.

1. Control mechanisms

Usually managers enjoy significant control over the firm and particularly over how to allocate investors' funds (Shleifer & Vishny (1997)). It is quite easy for them to expropriate outside shareholders. This managerial expropriation may be through using lower dividends in order to keep resources for investing in negative net present value projects or overpaying

executives (Jensen (86)). La Porta and al. (1999b) explain that installing unqualified family members in management team are perfectly legal methods to expropriate outside shareholders.

Other forms of expropriation are absconding with money, transfer pricing, theft, shirking, perquisite consumption and empire building (Shleifer & Vishny (1997)).

Numerous studies such as Morck and al. (1988) and Stulz (88) investigate the relationship between this discretion and firm valuation as a function of ownership and voting rights held by management. Others (e.g. Sort & Keasey (1999) and Demsetz & Villalonga (2001)), continue in the same line of research and confirm that expropriation reduces corporate resources practices are arisen to constraint these opportunistic actions. Agrawal & Knoeber (1996) shed light on this framework and recognises that there are control mechanisms that help to align managers' interests and those of shareholders and are related to firm performance.

2. The effect of the largest controlling shareholder on firm value

2.1 Cash-flow ownership

Jensen & Mechling (1976) argue that the cost of deviation from value-maximization increases when managerial ownership is low. As the fraction of the equity held by the manager decreases, his fractional claim on the outcomes decreases. Thus, he tends to divert corporate resources for non-pecuniary consumption particularly in the form of perquisites. Minority shareholders find it too craved to spend more resources in monitoring his behaviour. In contrast, as his equity interests rises, the manager pays large share of the costs of deviation from value-maximization. In this situation, he is less likely to squander corporate resources (Morck and al. (1998)). This is typically what the convergence-of-interest hypothesis predicts.

Consistent with Morck and al. (1998), Gompers and al (2003) confirm that an increase in cash-flow ownership makes the controlling shareholder's interest more closely aligned with other shareholders. This leads to better decision-making. However, they argue that this positive incentive effect is less important at higher levels of cash-flow rights. They justify that as cash-flow rights increase, the CEOs become wealthier enough and thus their incentives to work hard and to look for riskier strategies decrease.

Shleifer & Wolfenzon (2002); La Porta and al. (2002) and Cronqvist & Nilsson (2003) provide strong evidence that firm value is positively associated with cash-flow rights of controlling shareholder. Gompers and al (2009) derive similar results. They find that when insiders are controlling about 60% cash-flow rights, the total effect of their ownership reaches a peak. At this level, firm value, as measured by Tobin Q, is 25% points higher than its median value. Based on the above reasoning, we derive the first hypothesis:

H1: Greater cash-flows ownership held by the largest controlling shareholder is associated with higher firm value.

2.2 The separation between cash-flow and control rights

When the fraction of voting rights held by the controlling shareholder is large, an increase in this fraction makes him more enriched. This substantial voting power makes it desirable for him to be less worried about his employment. Rather, he may engage in non-value-maximizing activities (Morck and al. (1988)). Thus, the deviation from on share-one vote may not be a socially optimal scheme (Harris & Raviv (1988) and Grossman & Hart (1988).

Claessens and al. (2002) show that the deviation between ultimate voting rights and cash-flow rights is associated with a value discount. Such discount is an increasing function of the magnitude of ownership-control discrepancy. For instance, Cronqvist & Nilsson (2003) identify empirically that estimated agency costs of controlling minority shareholders are between 6% and 25% of firm value for listed Swedish firms, particularly, family controlled firms that display the largest discount on firm value.

Being inspired by these findings, Bennedsen and al. (2006) and Boubaker (2007) confirm that the presence of large controlling shareholders holding voting rights in excess of their cash-flow rights tends to decrease firm value. A similar analysis was undertaken by Masulis and al. (2009) for U.S. dual-class companies. They show that ownership control divergence allows insiders to pursue private benefits and to divert resources for themselves. Such diversion (or tunnelling) decreases firm value.

One major form of private benefits extraction is the ability to abuse corporate cash reserves. Although holding corporate cash mitigates the underinvestment problem when external financing is costly. Nevertheless, managers holding voting rights in excess of their cash-flow rights may misuse these reserves in shirking, perquisites, empire building and higher compensation (Masulis and al. (2009). These arguments allow us to draw the second hypothesis:

H2: Higher wedge between cash-flows and voting rights held by the largest controlling shareholder is associated with lowering the firm value.

3. Board of directors and firm value

3.1 Corporate board independence

Maassen (1999) gives three design strategies that help to improve board independence which protects minority shareholders from expropriation by the controlling shareholder with majority votes. Firstly, the independence may be enhanced through appointing non-executive (independent) directors who are not affiliated to controlling shareholder. Secondly, the separation of CEO and Chairman roles strengthens the control tasks of supervisory directors. This strongly highlights the independent decisions. Thirdly, the board independence may be accentuated by the distinction of decision management from decision control-through hierarchical layers.

Since controlling shareholder appoints and dismisses board members, he may exert pressure on directors to act in his favour (Dahya and al. (2009)). In such case, affiliated members are

less likely to reduce minority shareholders expropriation. They have usually family tiers of special relationships with controlling shareholder; Yeh & Woidtke (2005) find that the proportion of members affiliated to the largest shareholder is quite larger as that shareholder:

Has greater ownership-control discrepancy.

Is one among controlling family members.

Serves as chief executive and chairman at the same time (CEO duality).

Panasian and al. (2003) argue that appointing independent outside directors strengthens the monitoring role and discipline the management team. They are selected on the base of their knowledge in the firm industry and their affairs. By virtue of their objectivity, they may provide higher expertise and valuable experience on supervising, compensating and firing managers (Kim and al (2007)).

In such firms, agency problems between controlling shareholders and minority shareholders may decrease. This contributes to enhance firm performance. Yeh & Woidtke (2005) confirm the incentive of controlling shareholder with higher cash-flow rights to choose this structure. They tend to select professional members that are more likely to monitor and maximize shareholder wealth.

Numerous studies-Most forcefully (Patelli and Prencipe (2007) and Dahya, and al. (2008)) have examined the positive effect of independent board on firm valuation, in firms with controlling shareholders. More recently, Dahya and al (2009) claim that appointing directors who are unaffiliated to the controlling shareholders decrease the threat of resource diversion and the transfer of firm value from minority shareholders to controlling shareholders.

In additions, they show that fewer related-party transactions are associated with greater firm value in countries with larger fraction of independent directors. Our arguments give rise to the third hypothesis:

H3a: Appointing outside directors unaffiliated to controlling shareholders enhance firm value.

3.2 Appointments of busy outside directors

There is limited literature testing whether the appointment of an outside director holding three or more board seats harms firm performance. Using a U.S. sample of industrial firms between 1989 an 1995, Fich & Shivdasani (2004) document a negative and significant relationship between firm value and busy boards.

They suggest that serving on several boards makes outside directors so busy that they become ineffective monitors of managerial decision-making. Such directors may give CEOs excessive compensation packages (Core and al. (1999)) that reduce firm value, Ferris and al. (2003) explore the Busyness Hypothesis in greater detail. They confirm that accepting additional directorships may decrease oversight of management.

As a consequence, under supervised managers are more likely to misstate the firm and distort

its results. Thus, the exposure for securities fraud litigation is presumably high. Such litigation generates agency costs that decrease firm value. It may represent an opportunity for controlling shareholder to be empowered in the board and expropriate minority shareholders. Hence, we draw the hypothesis four:

H3b: Appointing busy outside directors makes the controlling shareholders more able to expropriate minority shareholders and thus harms firm value.

3.3 Board structure

In Continental European countries where the ownership is concentrated in the hand of large shareholders, some countries such as Germany, Austria and Belgium require the two-tier board structure. This structure contains a board of directors (the lower-level layer) and board of supervisors (the upper-level layer). But firms in other countries including France have the choice between both structures one-tier two-tier (Kil and al (2007)).

3.4 Board leadership

Joining the two posts, "there is never any question about who is boss or who is responsible". But, CEO duality may enable the board to do appropriately his functions since there will be a diffusion of management and monitoring functions.

The concentration of power may rather create agency conflicts. The idea being that as a chairperson, the CEO represents interests of stockholders-in particular shareholders. In such case, he cannot judge himself [See. Redcherche & Dalton(1991)]. Yeh & Woidtke (2005) show that when the controlling shareholder serves as both the CEO and the chairman of the board, he seems to select affiliated board members that are more likely to support him. In this case, he may capture greater benefits and expropriation than firm value maximization.

This highlights the entrenchment effect. For this reason, Maassen (1999) counsels to adopt independent board leadership to reduce agency problems between controlling and minority shareholders suggesting that "A move to a dual CEO top management structure is likely to be interpreted by investors as an adverse signal and may result in a fall of the share price of the corporation". Building on this research, we take disadvantage of holding CEO and chairman posts by the same individual.

H_4: *CEO duality has a negative effect on firm value.*

3.5 Board size

A focus on board size, which is also important to know, has a causal effect on firm performance under concentrated ownership. Lehnel and al. (2003) suggest that larger boards are advantageous in complexity environments. In fact, complex operating and financial structures need strong advising functions which are specially brought by more outside directors with valuable expertise. It may result in larger groups (Boone and al . (2007)) when the controlling shareholder becomes unable to select a large number of affiliated directors (See. Yeh & Woidtke (2005)).

Other papers tend to support the claim that small-sized boards are associated with fewer

conflicts between insiders and controlling shareholders. Since they are more cohesive and productive, they are more likely to monitor. CEOs are supervised by controlling shareholders.

They face dismissal for poor performance and their compensations exhibit greater sensitivity to performance (yermack (1996)). In contrast, Yeh & Woidtke (2005) contend that directors and supervisors tend to be affiliated to controlling shareholders in small boards. As the firm has higher information needs, the number of directors increases and control-affiliated members tend to decrease. This suggests the following hypothesis:

H5: Small-sized boards tend to be more dominated by controlling shareholders and are associated with a decrease in firm value.

Empirical Evidence

1. Data construction

Our sample consists of 346 French listed corporations present in the EURONEXT PARIS of NYSE EURONEXT database from different industries for 2008. These firms constitute the CAC ALL SHARES.

All information we need for cash-flow rights, voting rights and board structure are available in the firm's publications (annual reports). The majority of these are to be found in the AMF website while others are gathered from the "Boursorama" and corporate website. In accordance with Faccio &Lang (2002), we ascertain that France is one among other countries that have a disclosure rate about 100%. There are no difficulties to find board characteristics or information on capital structure and shareholders identities.

We consider, in our work, companies at December 31, 2008 (i.e. the end of the fiscal year). If the firm does not end its fiscal year at that date, we consider the annual report for which 2008 dominates the fiscal year.

2. Data specification

2.1 Dependent variables

Firm performance refers to individual and/or group productivity. It is measured to discern how efficient the use of corporate assets is. It evaluates the firm's ability to join instruments and board's effort to manage risks and to oversee the firm's activities on the whole. Famous performance proxies are classified in terms of different axes: Firm Value (Tobin Q), operating performance (Return on asset, Return on investment, Return on equity), Stock returns and profits…

2.2 Ownership and control variables

Ownership and control variables are given in Panel A of Table 1. We use the equity stakes owned by the largest controlling shareholder, LCF, to measure his incentive to expropriate minority shareholders. It is computed as the direct ownership stakes plus the product of all the indirect ownership stakes along the chain (Claessens and al. (2002)).

The difference between voting rights and cash-flow rights (Wedge) measures the wedge

between ownership and control held by the largest controlling shareholder. The fraction of voting rights held by the largest controlling shareholder is computed as the sum of direct voting rights and the weakest indirect voting rights in the chain of control rights (Claessens and al. (2002).

2.3 Board variables

The key explanatory variables are use to test the hypotheses about the board of directors (independence, Busyness). Independence is the number of independent outside directors divided by the total number of directors. Busyness is a dummy variable that assumes the value one if the number of busy directors is three or more in the board, and zero otherwise. To proxy for the board structure, we include the variable "structure".

This is a dummy variable that equals one when the firm adopts the one-tier board structure and zero when the firm adopts the two-tier board structure. We proxy for CEO status (Duality) using a dummy variable that equals one when the same person serves both a CEO and chairman and zero otherwise. Board (size) is the total number of directors. Panel B. Table 1 describes these board characteristics and gives their expected effect on firm value.

2.4 Other firm characteristics

We include controls for other firm characteristics to dodge any fallacious estimation (See Panel C of Table 1). We control for firm size with the natural logarithm of the book value of Total Assets (in (Total assets)). Using this variable, Maury & Pajuste (2005) expect a negative effect on Tobin Q indicating that larger firms tend to be in more mature stage of their life cycle. In such firms, largest controlling shareholders may increase their control through selection of affiliated supervisors (Yeh & Woidtke (2005)).

Other papers such as Demsetz & Villalonga (2001) and Maury (2006) find no significant effect of firm size on firm value (Tobin's Q). Firm age (Age) is the number of years since the foundation. Following Yeh & Woidtke (2005), we expect that firm value is negatively related to firm age. They suggest that controlling shareholders are more likely to exert control in older firms through appointing affiliated directors.

Data on Capital expenditure (Capex) and sales growth (Sales growth) are required to proxy for the importance of investment and growth opportunities. We define Capex as the ratio of total capital expenditure- changes in fixed asset plus depreciation- to the book value of Total Assets.

Sales growth is the ratio of changes in total sales over total sales in the previous year and is expected to have a positive effect on Tobin Q. The argument is that higher sales growth implies better future growth opportunities and presumably generates higher firm valuation (Claessens and al. (2002)).

3. Results

3.1 Summary statistics

Panel A. Table 2 shows the industry distribution of our sampled firms. Firms display 11

industries defined in Campbell's (1996) and span 53 different two-digit SIC codes. Among these industries, services and consumer durables are the most important ones. They represent respectively 26.59% and 18.50%/ Basic industry corresponds approximately to 11.56% while percentages of other industries are less than 10%. Petroleum firms represent only 1.73% of the 346 sampled firms.

Panel A in Table 3 presents ownership and control variables. We find that French firms feature concentrated ownership. Average cash-flow rights held by large controlling shareholder in the sample is 33.58% while average control rights is 42.09% which results in an average excess control of 8.51%. There is some divergence between different measures for control-ownership discrepancy. For example, at 75% (25%) percentile, ownership/control ratio (excess control) is 96.72% (0%). In parallel, ownership/control ratio (excess control) is 68.49% (13.44%) at 25% (75%) percentile.

Claessens and al. (2000) and Faccio & Lang (2002) consider that a 10% or a 20% cut-offs are sufficient to ensure control. Referring to these studies, Table 2 (Panel B) lists our firms with a controlling shareholder at 10% cut-off. We find that 88.44% of French listed firms have large controlling shareholders. This is consistent with Bolton & Von Thadden (1998) findings positing that France features concentrated ownership and excess control by large shareholders.

In more than ¾ of these controlled firms (257), we have single large controlling shareholders. Of all large controlling shareholders in our sample, 71.39% of firms were individuals or family controlled. Other types of large controlling shareholders are not important and range from 2.60% to 5.78% (See. Panel C. Table 2).

Panel B in Table 3 presents descriptive statistics for board composition. The average portion of independent directors is 0.38. The average and median French board has 7 members. Despite the fact that France offers firms the right to choose one or two-tier boards, we find that 74% of the sampled firms opt for on-tier board structure.

Similar results are obtained by Andres & Vallelado (2008) showing that 89% of French firms adopted the one-tier board system during the years from 1996 to 2005. The proportion of the sample exhibiting CEO duality is 57.23%.

Descriptive statistics for firm performance measures and other firm characteristics are given in Panel C (Table 3). Average level of Tobin Q is more than 0.5 while its median value is less than 0.35. The mean and median values of ROA are respectively 2.94 and 4.48.

The median value of debt ratio equals 0.21 suggesting that 50% of the sample's firms are leveraged at less than 21%. Average firm size and age for the sample are respectively €12.96 and 42.63 years. To check the existence of multicolinearity problem, we compute the Variance Inflation Factor (VIF).

Displayed in table 4 given below, our VIF values range from 1.07 to 2.69 (<10: the critical value) indicating the absence of a serious multicolinearity problem. Accurately, table 5 provides the correlation matrix according to Spearman and Pearson correlation tests. Results

and statistical significance of the two tests are roughly similar.

The Pearson coefficients are listed on the left of the "one" correlations (with Gray colour) while the Spearman coefficients are listed on the right (with violet colour). Board size is positively correlated with firm size at 1% level indicating that larger firms tend to have larger boards due to their various relationships.

The correlation between (CEO duality and Board structure is also relatively high (with correlation coefficient of 68.58%). This result suggests that firms adopting the one-tier board structure tend to have the same person as CEO and chairman. However, none of the other correlation coefficients exceed the usual threshold (r>0.5) for detecting multcollinearity problems (Pedersen & Thomsen (2003)).

3.2 Methodology

To evaluate the effect of both the presence of the largest controlling shareholders and boards characteristics on firm value, we conduct regression tests. Ln (Tobin Q) is the dependent variable. The correlation between Duality and Structure is previously computed and relatively high. Thus, these two board variables are estimated in separate regressions (1) and (2).

All the explanatory and control variables we defined previously are included in both multiple regressions. In what follows, we give the two equations:

(1) $\text{Ln(Tobin Q)} = \alpha_0^* + \alpha_1^*\text{LCF} + \alpha_2^* \text{ Wedge} + \alpha_3^* \text{ Independence} + \alpha_4^* \text{ Busyness}$

$+ \alpha_5^* \text{ Size} + \alpha_6^* \text{ Structure} + \alpha_7^* \text{ Ln(Total Assets)} + \alpha_8^* \text{ Age} + \alpha_9^* \text{ Sales growth}$

$+ \alpha_{10}^* \text{ Leverage} + \alpha_{11}^* \text{ Capex} + \varepsilon$

(2) $\text{Ln(Tobin Q)} = \alpha_0^* + \alpha_1^* \text{ LCF} + \alpha_2^* \text{ Wedge} + \alpha_3^* \text{ Independence} + \alpha_4^* \text{ Busyness}$

$+ \alpha_5^* \text{ Size} + \alpha_6^* \text{ Duality} + \alpha_7^* \text{ Ln(Total Assets)} + \alpha_8^* \text{ Age} + \alpha_9^* \text{ Sales growth}$

$+ \alpha_{10}^* \text{ Leverage} + \alpha_{11}^* \text{ Capex} + \varepsilon$

With: α_j (j=0,...,11) are coefficient estimates of the explanatory variables

ε is the error term.

4. Multiple regression results

4.1 Ownership structure of the largest controlling shareholder and firm value

We estimate regression including our various specifications of control and ownership rights held by the largest controlling shareholder. The key coefficients from our regression tests are displayed in Table 5. LCF is cash-flow rights. Previous researches (e.g., Shleifer & Wolfenzon (2002) and Cronqvist & Nilsson (2003)) show that firm value is positively related to cash-flow rights of controlling shareholders. Consistently, regressions (1) and (2) confirm that firms with higher cash-flow rights of large controlling shareholders experience higher firm value.

The average coefficient for LCF is 0.506 and indicates that for every unit increase in

cash-flow rights by the largest controlling shareholder, the natural logarithm of Tobin's Q is predicted to be 50.59% points higher. No support was found for H2 which hypothesizes that divergence between control and ownership rights of large controlling shareholders is associated with value loss (regression (1) and (2) of Table 5).

Our result differs from previous works such as Claessens and al. (2002)). It may be due to our sample quality since 11.56% firms have no controlling shareholders while 21.68% have no wedge between control and ownership. For this reason, we study the same relationship for different sub-sample afterward.

4.2 The effect of corporate board on firm value

The results are presented in regression (1) and (2) of Table 5. The coefficients on the fraction of independent directors are positive and statistically significant at 1% suggesting that independent directors are able to provide valuable contribution to firm valuation.

The result supports the Dahya and al. (2009) conclusion. We find that an increase in the percentage of independent directors is associated with an increase in Ln (Tobin Q). Efficient boards should have a majority of independent directors to monitor and advise managers.

We find that the proxy for Busyness exhibits the predicted negative sign, and is statistically significant at 1% level. We confirm the value discount generated by busy directors' presence established previously by Fich & Shivdasani (2004). Under diffused ownership, these authors show that busiest boards decrease the market-to-book ratio by about 4%. In our case, we find a decrease of Ln (Tobin Q) by 40.09%. If a board appoints busy directors, controlling and advisory capabilities on managers' decisions will be limited since there is no sufficient time. We should therefore expect to see resource diversion and decreased firm value.

The coefficient of board size was positive and significant at 1% indicating that larger boards are advantageous. On the one hand, controlling shareholders are less likely to influence board composition. On the other hand, the larger number of directors sitting on the board provides more experiences, and complementary skills. Thus, directors cooperate with themselves to fulfil their functions in efficient manner.

Our empirical evidence shows a positive but not significant effect of the board structure on firm value. We reach a totally different conclusion than the one presented by previous researches indicating a negative and significant effect. The regression 2 shows that CEO duality enhances firm value. Its coefficient is statically significant at 1% level. This justifies the increasing tendency to adopt CEO duality structure.

French firms want to see the CEO installed as chairman of their boards. Such combination of both titles lead to a single direction in board leadership (Rechner & Dalton (1991)). As a professional manager, the CEO may be endowed not only with knowledge but also with objectivity and abilities required to monitor and manage the board. In addition, CEO duality decreases costly and incomplete information transferred between a separate CEO and Chairman.

Except firm Age and Capex, all other control variables have significant effect on firm value.

The coefficient of Sales growth is positive and statistically significant at 1%. We confirm that firms benefit from better future growth opportunities. The coefficient of Leverage is, however, negative (and significant with a p-value=0.000) indicating that higher levels of debt decrease firm value. Firm size as measured by In (Total assets) is also negatively related to Firm value. Despite their various entrepreneurial knowledge and counselling they need more contracting relationships.

5. Conclusion

Our work draws on internal governance characteristics to advance the hypothesis that they are crucial to evaluate the firm. One segment of research analyzes the influence of ownership and control of the controlling shareholders, while another large body of literature addresses the issue of corporate board and its effort to monitor and rectify. To the best of our knowledge, our work combines the two lines.

The empirical evidence consists of multivariate estimations. First, we show a positive effect of cash-flow rights held by the largest controlling shareholder suggesting that an increase in cash-flow ownership makes the controlling shareholder's interest more closely aligned with other shareholders and incited to create value.

Second, we confirm the negative effect of the wedge between voting and cash-flow rights of controlling shareholders established by Claessens and al. (2002). In particular, these conclusions are reinforced when studying family firms. This strong association between firm value and both control and ownership of controlling shareholders addresses fruitfully the need for strong country's laws to enforce shareholder rights.

The empirical essay finds also significant ties between Ln (Tobin Q) and board characteristics.

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Appendix : Table 1: variables specification

Variables	Proxy	Description	Expected sigh	Authors
Dependent variables				
Tobin Q		It measures the firm value according to minority outside shareholder who does not receive any private benefits of control. It is proxied by the market capitalization divided by book value of total assets		Maury & pajuste (2005)
Explanatory variables: Panel A. ownership and control				
Voting rights held by the largest controlling shareholder	LCO	Fraction of voting rights held directly and indirectly by the largest controlling shareholder. It is computed as the sum of direct voting rights and the weakest indirect voting rights in the chain of control rights.		Claessens and al (2002)
Ultimate cash flow rights held by the largest controlling shareholder	LCF	Fraction of cash flow rights owned directly and indirectly by the largest controlling shareholder. It corresponds to the sum of the direct holdings and the product of all the indirect holding along the control chain.	+	Claessens and al (2002)
wedge	Wedge = LCO - LCF	The difference between ownership and control rights held by the largest controlling shareholder. It is a measure of ownership control discrepancy	-	Claessens and al (2002)
Panel B. Board composition				
The proportion of independent outside directors	independence	The numbers of independent outside directors divided by the total numbers of outside directors	+	Yeh & woidtke (2005)
The presence of	Busyness	A dummy variable that assumes the value one if the number of	-	Ferris et

busy directors		busy directors is three or more in the board, and zero otherwise.		al.(2003)
One-tier/two-tier	Structure	A dummy variable that equals one when the firm adopts the one-tier board structure and zero when the firm adopts the two-tier board structure.		Graziano & woidtke (2005)
CEO and chairman dummy	duality	A dummy variable that equals one when the same individual serves both as CEO and the chairman of the board and equals zero, otherwise.	-	Yeh & Woidtke (2005)
Board size	Size	The total number	+ -	Yeh & Woidtke (2005)

Panal C. control variable (firm characteristics)

Firm age	Age	Number of years since the foundation	-	Yeh & Woidtke
Firm size	In (total)	Natural logarithm of the book value of total assets	- +	Claessens et al.(2002) Yermack (1996) Mak, 2005# 17
Industry dummies	inddum	Control for possible industry effects on firm value		Claessens et al.(2002)
Capital expenditure	Capex	The ratio of total capital expenditure to the book value of total Assets. Capital expenditure is proxied by changes in fixed Assets plus depreciation.	-	Boubaker (2007)
Sales growth	Sales growth	One-year percentage change in sales(changes in total sales/total	+	Claessens et al.(2002)

		sales in the previous year)		
Leverage	leverage	Book value of non-equity liabilities/book value of total assest	+ -	Jensen (1986) Cronqvist & Nilsson (2003)

Table 2: Sample description

Panel A. Firms classified by industries using Campbell (1996) classification

SIC CODE	Industry description	Number of firms	%
13;29	Petroleum	6	1.73
25;30;36;37;39;50	Consumer durables	64	18.50
8;10;14;24;26;28;33	Basic industry	40	11.56
20;54	Food and tobacco	16	4.62
15;16;17;32;52	Construction	15	4.34
34;35;38	Capital goods	32	9.25
40;42;44;45;47	Transportation	13	3.76
48;49;94	Utilities	22	6.36
22;23;31;51;52;53;56;59	Textiles and trade	23	6.65
73;75;76;80;83;83;87;89	Services	92	26.59
27;58;70;78;79	Leisure	23	6.65
	Total	346	100

Panel B. sample description according to the presence of the controlling shareholders

	Number of firms	%
Firms with no controlling shareholder	40	11,56
Firms with large controlling shareholder at a 10% threshold	306	88,44
Firms with a single large controlling shareholder	257	74,28
Firms with multiple large controlling shareholders	49	14,16

Panel C. Identity of the largest controlling shareholder

	Number of firms	% total	% within controlled firms
Family	247	71,39	80,72
The State	16	4,62	5,23
Widely held firms	9	2,60	2,94
Widely held financial institution	20	5,78	6,54
Miscellaneous	14	4,05	4,57

Table 3: Descriptive statistics

Variable	Min	Q1	Median	Mean	Q3	Max
Panel A. Ownership and control variables (%)						
LCF	0	15.23	32.12	33.58	50.54	84.66
LCO	0	22.62	42.35	42.09	63	97.24
LCO-LCF	-24.5	0.00	7.69	8.51	13.44	70.18
LCF/LCO	0.18	68.49	80.64	78.57	96.72	1.59

Panel B.Corporate board (%)						
Independence	0	0.20	0.38	0.38	0.50	1
Size	3	5	7	7.88	10	21
Structure	Number of firms having one-tier system : 256; % Total: 73.99					
Duality	Number of firms adopting CEO duality: 198; % Total: 57.23					
Panel C. Firm characteristics (%)						
Tobin Q	0.02	0.21	0.34	0.56	0.70	5.51
ROA	-63.95	1.87	4.48	2.94	7.26	38.18
Total Assets (millions of euros)	4.11	76.09	278.36	5489.36	1642.22	197000
Total Debt (millions of euros)	0	9.41	59.83	1608.33	536.12	44000
Leverage	0	0.10	0.21	0.25	0.36	2.33
Capex	0	1.67	3.52	5.05	6.05	48.72
Sales growth	-100	-2.20	4.54	7.85	14.51	294.69
Age	3.19	18.66	31.15	42.63	70.04	95.31

Table 4: VIF values

The table presents the Variance Inflation Factor values for our independent variables: firm size (log of total assets in millions of Euros); Size the total number of directors; Structure, a dummy variable that equals one when the firm adopts the one-tier board structure and zero when the same person serves both as CEO and the chairman of the board and equals zero, otherwise; Age, the number of years since the foundation of the firm: Busyness, a dummy variable that equals one if the number of busy directors is three or more in the board and zero otherwise; Leverage, Total debt/total assets; independence, the percentage of independent outside directors: Capex, Capital expenditures/total assets: Sales growth (1 year); LCF, the

fraction of ultimate cash-flow rights held by the largest controlling shareholder and Wedge, equals the difference between voting rights and cash-flow rights of the largest controlling shareholder. A VIF in excess 10 is generally seen as indicative of severe multicolinearity.

Variables	VIF
Ln (Total Assets)	2.69
Size	2.37
Structure	2.14
Duality	2.04
Age	1.48
Busyness	1.35
Leverage	1.28
Independence	1.21
Capex	1.16
Sales growth	1.11
LCF	1.11
Wedge	1.07
	Mean VIF: 1.58

Table 5: Ownership structure, corporate board and firm value

This table reports the coefficients and p-values for large controlling shareholders and board of directors' effect on firm performance for 346 French firms. The dependent variable is Ln (Tobin Q) in both columns 1 and 2. Tobin Q is the market capitalization divided by book value of Total Assets and is normalized (Ln (Tobin Q)) to mitigate the influence of outliers.

The independent variables are: Wedge which equals the difference between voting rights and cash-flow rights of controlling shareholders: LCF, the fraction of ultimate cash-flow rights

held by controlling shareholders; independence, the percentage of independent outside directors; Busyness, a dummy variable that equals one if the number of busy directors is three or more in the board and zero otherwise: Size, the total number of directors: Duality, a dummy variable that equals one when the same person serves both as CEO and the chairman of the board and equals zero, otherwise; Structure, a dummy variable that equals one when the firm adopts the one-tier board structure and zero when the firm adopts the two-tier board structure; firm size (log of total assets in millions of Euros); Age, the number of years since the foundation of the firm; Sales growth (1 year); Total debt/total assets; Capex, Capital expenditures/total assets.

Dummy variables for industry effect following Campbell's (1996) classification are included in regressions but not reported. We recall that CEO duality and Board structure are strongly correlated. Board structure is included in regression 1 and CEO duality is included in regression 2. For each estimated coefficient, the p-value is given between parentheses. We use the Eicker-Whit's robust standard errors to correct the heteroscedasticity problems.

	Ln (Tobin Q)	
	Regression 1	Regression 2
LCF	5244 (0.008)***	4874 (0.013)**
Wedge	-7238 (0.134)	-7164 (0.135)
Independence	5595 (0.000)***	5409 (0.000)***
Busyness	-3876 (0.000)***	-4142 (0.000)***
Size	0462 (0.008)***	0496 (0.004)***
Structure	2171 (0.140)	
Duality		4721 (0.002)***
LN (Total Assets)	-0668 (0.028)**	-0680 (0.024)**
Age	0015 (0.188)	0013 (0.242)

Sales growth	0053 (0.002)***	0046 (0.006)***
Leverage	-9815 (0.000)***	-9108 (0.000)***
Capex	0064 (0.423)	0061 (0.442)
Industry Dummy	Yes	Yes
Intercept	-5883 (0.115)	-5726 (0.114)
Adjusted R-squared	0.2244	0.2364
F-Statistic	5.75***	6.09***

***, ** and* represent significance at 1% and 10% level, respectively.