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Does founding family control affect earnings management?

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Notes

[1] This is analogous to the literature on the board of directors. There is mixed evidence on the association between boards and firm performance. Thus, several studies focus on specific situations rather than on the overall firm performance. For examples, research has been conducted on the impact of boards on CEO turnover (Weisbach, 1988; Perry, 2000), on earnings management (Xie et al., 2002) and on executive compensation (Hallock, 1997; Core et al., 1999).

[2] To the extent that shareholders make poor decisions based on managed accounting numbers, earnings management can be classified as an agency cost (Davidson et al., 2004).

[3] This proportion of family-owned firms is remarkably consistent with Anderson and Reeb (2003a,b; 2004). They find that one-third of their sample is family owned.

[4] Anderson and Reeb (2003a,b, 2004) make their classification of family firms available to the public. More detailed discussions about the classification can be found in their studies.

[5] For instance, the Ablon family is perceived as controlling the Ogden Corporation as if they were majority owners but, in actuality, they hold merely 2% of the outstanding shares. (… to maintain control.

[6] We em … found to have ‘th … 995). In addition … odels appear t … ccruals.’ More … nodel are cons…

[7] This ap … 98a, b; Davidso…

[8] Other s … ffect of income-i … et al., 1995; Becker e…

[9] In a separate regression (data not shown), the raw DCA (not the absolute value) is used. The family firm dummy does not produce a significant coefficient.

[10] As in Anderson and Reeb (2003a,b, 2004), the magnitude of the reduction in earnings management is computed as the coefficient of the family dummy divided by the average | DCA | for the sample = 0.017/0.047 = 0.36.

[11] Although the R^2s appear to be low, this should not be particularly problematic for Lev (1989) finds that a majority of earnings studies exhibit low R^2s. The R^2s in this study are comparable to those in other earnings studies. We also make sure that multi-collinearity is not a problem. We examine the variance inflation factors (VIF) and find that none of them are higher than 2.

[12] The fixed-effect approach helps reduce the possibility that the documented relation is caused by unobservable omitted variables, i.e. the fact that the firm is family owned and the extent of earnings management may be driven by some unobservable variables that are not included in the model. The fixed-effects analysis has been found to resolve this potential problem.

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