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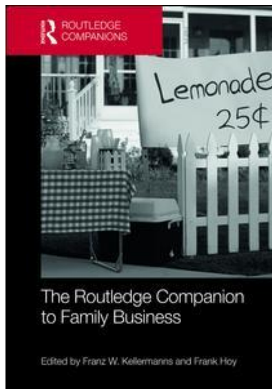

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Agency Theory in Family Firm Research

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3

AGENCY THEORY IN FAMILY FIRM RESEARCH

Accomplishments and Opportunities

Kristen Madison, Zonghui Li, and Daniel T. Holt

"Agency theory offers a rich and fruitful frame of reference by which the peculiar problems of family businesses might be studied."

—Chrisman, Chua, and Litz, 2004: 351

Introduction

Agency theory has received considerable research attention since its migration into the family firm literature (Le Breton-Miller and Miller 2009; Madison et al. 2016; Shukla et al. 2014). Knowledge can be gained by this migration, such as new insights regarding agency theory, or importantly, the uniqueness, behavior, performance, and competitive advantage of family firms. Accordingly, the first objective of this chapter is to provide an overview of agency theory and its general tenets. We then transition to reviewing and synthesizing agency theory's use in the family firm literature, with a focus on both the content and methods of the articles. While we acknowledge that agency theory has been extensively reviewed in the extant family firm literature (e.g., Chrisman et al. 2005; Madison et al. 2016), our review differs by its focus on empirical articles. Accordingly, not only are we able to document the empirical support that demonstrates how agency theory has been extended by the family firm context, but we are able to examine the methodology employed in these studies. We conclude the chapter with suggestions for future research opportunities that can further extend theory, reduce methodological limitations, and provide additional insights into the family firm.

Theory and Context

Every theory should contain three necessary elements; namely, the *what, how,* and *why* (Whetten 1989). The *what* seeks to describe the phenomenon and the associated factors in a comprehensive but parsimonious way, the *how* describes the relationship between the factors, and the *why* explains the rationale underlying the selected factors and their proposed relationships (Reay and Whetten 2011; Whetten 1989). Theories should also be generalizable, but instead often suffer from boundary conditions and limitations when context, like the *where* is taken into consideration (Lee and O'Neill 2003; Smith and Hitt 2005; Whetten 1989). Context refers to "situational opportunities and constraints that affect

the occurrence and meaning of organizational behavior as well as functional relationships between variables" (Johns 2006: 386).

We consider both theory and context in this chapter. We first provide an overview of agency theory organized by the theoretical elements of *what*, *how*, and *why*. We then transition to the element of *where* by reviewing agency theory specifically within family firm research to assess its strength and generalizability with contextual considerations. We refer to the family firm context as the unique opportunities, challenges, and resulting behavior and performance implications arising from residing at the intersection of the family system and the business system. Family control frees family firms from the formalized, short-term-oriented demands often imposed by capital markets. At the same time, however, family influence often leads to the pursuit of non-economic goals that the family values, sometimes at the expense of economic returns, leading to emotional and inflexible attachment to existing assets and strategies.

What

Agency theory is one of the most widely used theories in management (Daily et al. 2003; Wasserman 2006), and family firms in particular (Madison et al., 2016). Broadly, agency theory is about the relationship between two parties, the principal (owner) and the agent (manager; Eisenhardt 1989; Jensen and Meckling 1976; Ross 1973). More specifically, it examines this relationship from a behavioral and a structural perspective. Theory suggests that given the chance, agents will behave in a self-interested manner, behavior that may conflict with the principal's interest (Chrisman et al. 2004; Eisenhardt 1989; Jensen and Meckling 1976; Wiseman et al. 2012). As such, principals will enact structural mechanisms that monitor the agent in order to curb the opportunistic behavior and better align the parties' interests (Cruz et al. 2010; Eisenhardt 1989; Fama and Jensen 1983).

How

Firm performance by way of cost minimization and greater efficiencies is the desired outcome of the agency theory perspective (Corbetta and Salvato 2004; Fama 1980). Theory suggests that agency costs are incurred to alleviate the agency problems associated with the separation of the firm's ownership and management (Eisenhardt 1989; Jensen and Meckling 1976; Karra et al. 2006; Lee and O'Neill 2003; Wasserman 2006). Separation of ownership and management is a key component of agency theory; the principal delegates work to the agent, and the agent is expected to act in the best interest of the principal (Ross 1973; Wiseman et al. 2012). However, when the interest of the principal is not aligned with the interest of the agent, and when the principal lacks the information to assess the agent's behavior, an agency problem is created (Eisenhardt 1989; Karra et al. 2006; Lee and O'Neill 2003; Ross 1973). Agency problems are categorized as moral hazard or adverse selection (Chrisman et al. 2004; Eisenhardt 1989; Karra et al. 2006). A moral hazard agency problem is when the agent lacks effort in the scope of the employment relationship (Chrisman et al. 2004; Ross 1973). It is considered a form of opportunistic behavior that includes free-riding, shirking, and perk-consumption (Chrisman et al. 2004; Chua et al. 2009; Karra et al. 2006). An adverse selection agency problem is when the agent lacks the ability or skills to competently behave in the scope of the employment relationship (Eisenhardt 1989; Fama 1980; Schulze et al. 2001).

Agency problems can be reduced in two ways (Eisenhardt 1989). The first is to create a governance structure that enables the principal to monitor and assess the actual behavior of the agent (Anderson and Reeb 2004; Chrisman et al. 2007). This structure includes, for example,

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reporting procedures, additional management, or a board of directors (Donaldson and Davis 1991). The second is to create a governance structure where the employment contract is based on actual outcomes (Eisenhardt 1989). For example, compensation incentive plans, where the agent receives incentives for high firm performance, fall into this category (Chrisman et al. 2007). This shifts the risk to the agent, thereby creating alignment between the principal and agent's interests (Davis et al. 1997; Eisenhardt 1989). In sum, the principal can choose to establish a governance structure based on the agent's actual behavior or the outcomes of that behavior (Eisenhardt 1989). Either choice creates agency costs for the principal (Jensen and Meckling 1976).

Why

The underlying assumption of agency theory is based on the economic model of man (Davis et al. 1997; Eisenhardt 1989; Jensen and Meckling 1976). This model assumes that individuals seek to optimize their own utility. In the principal-agent relationship, an agent is hired to maximize the principal's utility (Ross 1973). However, agency theory assumes agents will instead behave opportunistically because they too are self-serving. Therefore, the principal enacts mechanisms to minimize losses to their own utility (Davis et al. 1997; Eisenhardt 1989; Jensen and Meckling 1976; Ross 1973).

Where

As described, agency theory contains the essential elements of theory. It has predictive and explanatory power as shown in the descriptions of the *what, how,* and *why.* However, the question remains as to whether agency theory is adequate and relevant when context is taken into consideration. In other words, are expansions necessary or boundary conditions or limitations apparent if the *where* is considered? To assess its strength and generalizability, the next section of this chapter examines agency theory within family firms, an important organizational context. Family firms represent a unique context for several reasons. Family-controlled firms differ from their nonfamily controlled counterparts along several important dimensions. On the one hand, families have little need to monitor management as their equity stakes overlap considerably with their own. On the other, large equity stakes give families considerable discretion to implement strategies that serve the family, providing them with incentives to monitor management more closely and the voting power to discipline them should they engage in unproductive, opportunistic activities.

Literature Review

Although family firms are deemed the most prevalent and oldest organizational type, scholarly investigations of these businesses pale in comparison (Goel et al. 2012). Scholars stress that family firm research "should describe why family businesses are distinct, how the uniqueness builds, and how and under what conditions this may lead to a competitive advantage" (Klein et al. 2005a: 333). Accordingly, family firm governance and its related performance implications have been a topic of interest due to the unique structures and dynamics brought about by residing at the intersection of the family system and the business system (Goel et al. 2012). Since agency theory addresses governance and firm performance, it is not surprising that it has become a prominent lens in family firm research (Chrisman et al. 2005; Goel et al. 2012; Le Breton-Miller and Miller 2009), and as such, is the focus of our review.

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Family firm agency theory articles were found through an electronic and manual search of the literature using combinations of keywords such as *family firm, family business, family enterprise* plus *agency theory* or *agency costs*. Family firm articles citing the seminal theoretical works (e.g., Jensen and Meckling 1976; Eisenhardt 1989) were also reviewed to determine appropriateness for inclusion. To be considered for inclusion, the theoretical underpinning for the empirical model had to be agency theory.

Characteristics of the Literature

This search process yielded 89 articles grounded in agency theory within the context of family firms. These articles appeared in 22 journals across several disciplines and were published between 2000 and 2014. The articles comprised 18 conceptual articles and 71 empirical articles. Four of the empirical articles were qualitative in nature, and 67 were quantitative. We focus specifically on the quantitative articles for this review because we are interested in the methodological approaches associated with these articles. Table 3.1 provides an alphabetical list and the characteristics of these 67 articles. The focus of our literature review is twofold; we first synthesize the content of agency theory articles, and second we analyze the methodology. We then present future research suggestions that can further extend theory while simultaneously addressing the methodical limitations in extant investigations.

Content of the Literature

Agency Problems. At the heart of agency theory is the separation of ownership and management and the problems that arise from this separation (Eisenhardt 1989). This owner-manager conflict is referred to as a Type I agency problem (Villalonga and Amit 2006). However, it was assumed that family firms are not susceptible to Type I agency problems due to a lack of separation among owners and managers (Chrisman et al. 2004; Goel et al. 2012; Jensen and Meckling 1976); and therefore, agency perspectives remained absent in this organizational context. However, the work of Schulze and his colleagues challenged this logic (Schulze et al. 2001; Schulze et al. 2003a, 2003b), and began an important stream of literature. This stream seeks to conceptually and empirically demonstrate that family firms are indeed susceptible to agency problems. Unique to the family firm, research supports nontraditional agency problems such as those created by asymmetric altruism (Moores 2009; Schulze et al. 2001; Schulze et al. 2003a, 2003b) and entrenched family ownership (Block 2012; Moores 2009; Nicholson 2008).

Altruism is often regarded as a selfless other-serving behavior but is presented in a different light by agency theorists (Eddleston et al. 2008). Agency theory perspectives refer to altruism as asymmetric, which describes behavior that is exploitable and not reciprocated (Chua et al. 2009; Wright and Kellermanns 2011). It can cause harm to the family firm by creating both moral hazard and adverse selection agency problems (Schulze et al. 2001; Schulze et al. 2003a). Moral hazard problems are created by asymmetric altruism when parents are overly generous to their children and their children take advantage of this act by shirking or free-riding in the employment relationship (Dawson 2011; Eddleston et al. 2008; Schulze et al. 2001, 2003a). This agency problem then becomes worse because family firm leaders don't often monitor the behavior of other family members in the firm (Chua et al. 2011; Eddleston et al. 2010). Adverse selection agency problems are created when family firms hire family members who may be less qualified and skilled than nonfamily members for the position (Karra et al. 2006; Schulze et al. 2001, 2003a), and may even pay them more generously (Chua et al. 2009). These agency problems created by asymmetric altruism are shown to decrease the performance of the family firm

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Table 3.1 Family Firm Agency Theory Research

Source	*Key Theoretical Findings*	*Sample*	*Location*	*Data Analysis*	*Response Rate*	*Random Sampling*	*Alternative Measures or Explanation*	*Correlation Matrix*	*Temporal Ordering*
Ali, Chen, and Radhakrishnan (2007)	Family firms have lower principal-manager agency costs but higher principal-principal agency costs than nonfamily firms. Disclosure practices are different between family and nonfamily firms due to these agency problems.	177 family firms & 323 nonfamily firms	US	Regression	NA	No	Yes	No	Longitudinal
Anderson, Duru, and Reeb (2009)	Transparency helps mitigate the principal-principal agency problem	2000 firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Anderson, Mansi, and Reeb (2003)	Family firms outperform nonfamily firms; family ownership structures reduce the shareholder-bondholder agency problem and are associated with lower cost of debt financing	252 firms	US	Regression	NA	No	Yes	No	Longitudinal
Anderson and Reeb (2003a)	Family firms outperform nonfamily firms; family ownership structures reduce agent behavior (opportunism)	141 family & 262 nonfamily firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Anderson and Reeb (2003b)	Family ownership reduces principal-principal agency problems; minority shareholders benefit from higher levels of family ownership.	319 firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Anderson and Reeb (2004)	Agency structures apply in family firms; family directors monitor business; independent directors monitor family	141 family & 262 nonfamily firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Andres (2008)	Family firms outperform nonfamily firms; families can successfully balance both Agency I and Agency II problems	103 family firms & 172 nonfamily firms	Germany	Regression	NA	No	Yes	Yes	Longitudinal

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Source	*Key Theoretical Findings*	*Sample*	*Location*	*Data Analysis*	*Response Rate*	*Random Sampling*	*Alternative Measures or Explanation*	*Correlation Matrix*	*Temporal Ordering*
Asaba (2013)	Family firms invest more than nonfamily firms because of their reduced agency costs; self-interested managers underinvest.	184 firms (approximately 1/3 family firms)	Japan	Regression	NA	No	Yes	Yes	Time-lagged longitudinal
Barth, Gulbrandsen, and Schøne (2005)	Family firms are less productive than nonfamily firms, unless managed by nonfamily. Findings support moral hazard agency problem	220 family firms & 218 nonfamily firms	Norway	Regression	NA	No	Yes	No	Cross-sectional
Bartholomeusz and Tanewski (2006)	Family and nonfamily firms have different governance structures that impact firm performance. To improve firm performance, family firms should adopt transparent structures and implement independent monitoring.	50 family firms & 50 nonfamily firms	Australia	Regression	NA	No	Yes	No	Cross-sectional
Ben-Amar and André (2006)	Principal-principal agency problems are reduced with increased family ownership and in countries with legal institutions that protect minority shareholders	327 acquisitions by 232 firms	Canada	Regression	NA	No	No	No	Cross-sectional
Block (2010)	Examines the agency relationship between family owners (agents) and society (principal). Family firms downsize less than nonfamily firms because of their reputational concerns	414 firms	US	Regression	NA	No	Yes	Yes	Time-lagged longitudinal
Block (2012)	Family ownership fosters agent behavior (moral hazard and information asymmetry)	154 family firms	US	Regression	NA	No	Yes	Yes	Longitudinal

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Braun and Sharma (2007)	CEO duality does not affect family firm performance; agency structures protect minority shareholders	84 family firms	US	Regression	NA	No	No	Yes	Cross-sectional
Cai, Luo, and Wan (2012)	Family CEOs reduce principal-agent costs that outweigh the principal-principal costs and enhance firm performance in China	351 firms	China	Regression	NA	No	No	Yes	Longitudinal
Chen, Chen, Cheng, and Shevlin (2010)	Family firms are less tax aggressive the principal-principal agency conflict impacts the level of the family firm's tax aggressiveness.	476 family firms & 527 nonfamily firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Chen, Gray, and Nowland (2013)	Nonfamily managers are used by controlling families to extend their influence within their firms, increasing agency costs to minority shareholders (i.e., nonfamily can be an agency concern to minority shareholders)	536 family firms	Taiwan	Regression	NA	No	Yes	Yes	Cross-sectional
Chen, Hsu, and Chang (2014)	Family ownership reduces agency costs; family ownership increases internationalization (i.e., make long-term investments in the business despite the risks)	217 firms	Taiwan	Regression	NA	No	Yes	Yes	Time-lagged longitudinal
Chirico and Bau (2014)	Inverted U-shaped relationship between % family on TMT and firm performance. Prevalence of stewardship and agency behaviors depends on the extent of family influence and market dynamism.	199 family firms	Switzerland	Regression	33.61%	No	No	Yes	Cross-sectional
Choi, Park, and Hong (2012)	In emerging economies, agency theory may not adequately explain the relationship between ownership and innovation performance.	301 firms	Korea	Regression	NA	No	No	Yes	Cross-sectional

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Source	*Key Theoretical Findings*	*Sample*	*Location*	*Data Analysis*	*Response Rate*	*Random Sampling*	*Alternative Measures or Explanation*	*Correlation Matrix*	*Temporal Ordering*
Chrisman, Chua, Kellermanns, and Chang (2007)	Family managers are agents; agency structures increase firm performance	208 family firms	US	Regression	18%	No	No	Yes	Cross-sectional
Chrisman, Chua, and Litz (2004)	Agency structures with family involvement decrease agency problems	901 family firms & 240 nonfamily firms	US	Regression	21.30%	No	No	Yes	Cross-sectional
Chua, Chrisman, and Sharma (2003)	Traditional agency problems operate in family businesses when they increase in size and employ nonfamily managers	272 family firms	Canada	Regression	28%	No	No	Yes	Cross-sectional
Cruz, Gómez-Mejía, and Becerra (2010)	CEO perceptions and trust impact agency contracts and implementation of agency structures	122 family firms	US	Regression	11%	No	Yes	Yes	Cross-sectional
Cucculelli, Mannarino, Pupo,and Ricotta (2014)	Family firms are less efficient than nonfamily firms due to unique agency costs (altruism and family entrenchment)	1835 family firms & 1085 nonfamily firms	Italy	Regression	NA	No	Yes	No	Cross-sectional
Dawson (2011)	Investors associate family and business negatively; prefer to invest in professional family firms	35 private equity firms	Italy	Regression	81.40%	No	No	No	Cross-sectional
De Maere, Jorissen, and Uhlaner (2014)	Agency and resource dependence theory are used to show that separation of ownership and management helps avoid bankruptcy (due to board monitoring) and increases a firm's resources (due to board capital)	116 bankrupt firms matched with 116 non-bankrupt firms	Belgium	Regression	NA	No	Yes	Yes	Cross-sectional

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De Massis, Kotlar, Campopiano, and Cassia (2013)	Nonlinear relationship: family ownership and management (alignment/lower information asymmetries) reduces agency costs to the point where the lack of external monitoring allows for opportunistic behavior to prevail	787 firms	Italy	Regression	NA	No	Yes	Yes	Cross-sectional
George, Wiklund, and Zahra (2005)	CEO and TMT ownership levels are negatively associated with the scale and scope of internationalization. This indicates agent behavior (opportunistic risk aversion)	889 firms	Sweden	Regression	36%	No	No	Yes	Cross-sectional
Gnan, Montemerlo, and Huse (2013)	Results indicate that family councils (relational stewardship perspective) partially substitute for corporate governance mechanisms (contractual agency perspective); agency and stewardship theory can complement one another.	243 family firms	Italy	MANOVA	3.20%	No	Yes	No	Cross-sectional
Gómez- Mejía, Larraza- Kintana, and Makri (2003)	Differing agency relationships affect pay structures. Family CEOs receive less pay than professional managers; family ties protect a CEO from bearing excessive personal risk but increase business risk.	253 family firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Gómez- Mejía, Núñez- Nickel, and Gutierrez (2001)	Executive entrenchment causes agency problems in family firms	276 firms	Spain	Regression	NA	No	Yes	Yes	Cross-sectional
González, Guzmán, Pombo, and Trujillo (2015)	Family involvement on the board reduces CEO turnover; serve as mediators in family conflicts (reducing agency problems within families) and effectively monitor performance of CEOs.	523 firms	Columbia	Regression	NA	No	Yes	No	Time-lagged longitudinal

(Continued)

Source	*Key Theoretical Findings*	*Sample*	*Location*	*Data Analysis*	*Response Rate*	*Random Sampling*	*Alternative Measures or Explanation*	*Correlation Matrix*	*Temporal Ordering*
Graves and Shan (2013)	Family firms outperform nonfamily firms; they have higher profit margins which can be attributed to having lower agency costs. Results can also be explained in that family leaders are altruistic stewards of the family wealth.	4217 firms	Australia	Regression	NA	No	Yes	Yes	Longitudinal
Herrero (2011)	Family firms outperform nonfamily firms; have reduced agency problems	58 family & 33 nonfamily firms	Spain	Regression	NA	No	Yes	No	Cross-sectional
Jaskiewicz and Klein (2007)	Both theories explain board composition: Agency = low goal alignment (need larger boards, more outside members); Stewardship = high goal alignment	351 family firms	Germany	Regression	6.09%	No	Yes	Yes	Cross-sectional
Kappes and Schmid (2013)	Family firms have longer time horizons than nonfamily firms; agency perspective explains differences (family firms are long-term oriented; nonfamily want short-term gains)	701 firms	Germany	Regression	NA	No	Yes	No	Longitudinal
Klein, Shapiro, and Young (2005b)	Agency: aligning principal-manager goals and reducing information asymmetry is important to investors. Stewardship: board of directors should be an advisor, not a monitor	263 family and nonfamily firms	Canada	Regression	NA	No	Yes	Yes	Cross-sectional
Kuo and Hung (2012)	Agency problem of free cash flow may lead to overinvestment, information asymmetry between firms and external capital markets may cause underinvestment; independent boards mitigate these effects of family control	1115 firms	Taiwan	Regression	NA	No	Yes	Yes	Longitudinal

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Liang, Li, Yang, Lin, and Zheng (2013)	Family involvement in boards strengthens the positive relationship between R&D investment and innovation; family involvement in management weakens it. Not all types of family involvement reduce agency problems.	102 family firms	China	Regression	NA	No	No	Yes	Longitudinal
Luo and Chung (2013)	Examines agency relationships in the institutional context. Family control creates varying levels of agency costs and performance depending on the pattern of family control and the strength of market institutions.	631 firms	Taiwan	Regression	NA	No	Yes	Yes	Longitudinal
Maseda, Iturralde, and Arosa (2014)	Proportion of outside members has a differing relationship with family firm performance across generations. No relationship by the third generation; results indicate boards serve as advisors rather than as monitors.	341 family firms	Spain	Regression	24.71%	No	Yes	Yes	Cross-sectional
Maury (2006)	Family controlled firms have reduced Agency I problems but suffer from Agency II problems. Increased transparency and policy is necessary to protect minority shareholders.	1672 firms	Western Europe	Regression	NA	No	Yes	No	Cross-sectional
McConaughy (2000)	Family CEOs receive less pay than nonfamily CEOs and their pay is less sensitive to performance. Nonfamily CEOs need pay incentives to align their interests.	82 family firms (45 family CEOs; 37 nonfamily CEOs)	US	Regression	NA	No	No	No	Cross-sectional
McConaughy, Matthews, and Fialko (2001)*	Firms controlled by the founding family have greater value, operate more efficiently, and carry less debt. This is because they have reduced agency costs.	219 family firms	US	Univariate analysis	NA	No	No	No	Cross-sectional

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Source	*Key Theoretical Findings*	*Sample*	*Location*	*Data Analysis*	*Response Rate*	*Random Sampling*	*Alternative Measures or Explanation*	*Correlation Matrix*	*Temporal Ordering*
Michiels, Voordeckers, Lybaert, and Steijvers (2012)	Family firms face agency costs; assumed because they use performance-based compensation. Agency costs appear to be lower in later generational stages.	529 family firms	US	Regression	NA	No	No	Yes	Cross-sectional
Miller, Le Breton-Miller, and Lester (2010)	Powerful owners prevent opportunistic acquisitions by managers: Family ownership is negatively related with acquisition volume and positively related with acquisition diversification.	898 family and nonfamily firms	US	Regression	NA	No	Yes	Yes	Longitudinal
Miller, Le Breton-Miller, Minichilli, Corbetta, and Pittino (2014)	Blends agency and behavioral agency theory governance structures. Nonfamily CEOs do best for a firm's performance when working alone and monitored by multiple major owners (agency); Family CEOs impact on performance doesn't vary much with regard to ownership and leadership structures (SEW).	893 family firms	Italy	Regression	NA	No	Yes	Yes	Longitudinal
Miller, Minichilli, and Corbetta (2013)	Supports both agency and stewardship theories; depends on the context of ownership and management; there must be an appropriate fit.	2522 family firms	Italy	Regression	NA	No	Yes	Yes	Longitudinal
Mustakallio, Autio, and Zahra (2002)	Blends social capital theory with agency theory to demonstrate that relational and contractual governance structures are important.	192 family firms	Finland	SEM	46%	No	No	Yes	Cross-sectional

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Naldi, Nordqvist, Sjöberg, and Wiklund (2007)	Family firms take less risk, and risk is negatively related to performance. Results indicate the need for formal agency structures to monitor the family and their business decisions.	265 family firms & 431 nonfamily firms	Sweden	Regression	28%	No	No	No	Cross-sectional
Peake and Watson (2014)	Family firms are less likely to use contracts among owners (a measure of formal control); family firms with economic goals, rather than family goals, are more likely to use contracts.	423 family and nonfamily firms	US	Regression	NA	No	Yes	Yes	Cross-sectional
Pieper, Klein, and Jaskiewicz (2008)	Both theories explain board presence: Agency = low goal alignment, have board; Stewardship = high goal alignment, no board	714 family firms	Germany	Discriminant analysis; regression	12.90%	No	Yes	No	Cross-sectional
Pindado, Requejo, and Torre (2012)	Family firms adopt higher dividend payments; used as a governance mechanism to overcome the agency conflict between the controlling family and minority investors.	482 family firms & 163 nonfamily firms	Eurozone	Regression	NA	No	Yes	Yes	Time-lagged longitudinal
Prencipe, Markarian, and Pozza (2008)	Both theories explain why family firms are less sensitive to short-term performance and stock fluctuations; agency and stewardship structures facilitate long-term orientations.	23 family & 21 nonfamily firms	Italy	Regression	NA	No	No	Yes	Longitudinal
Randøy and Goel (2003)	Agency structures (monitoring) are more relevant in nonfounder firms but are redundant in founding family-led firms.	68 firms	Norway	Regression	NA	No	Yes	Yes	Longitudinal
Schulze, Lubatkin, and Dino (2003a)	Proportion of family ownership influences board conduct.	1464 family firms	US	Regression	10.30%	No	Yes	Yes	Cross-sectional

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Source	*Key Theoretical Findings*	*Sample*	*Location*	*Data Analysis*	*Response Rate*	*Random Sampling*	*Alternative Measures or Explanation*	*Correlation Matrix*	*Temporal Ordering*
Schulze, Lubatkin, and Dino (2003b)	Family firms have unique agency problems; created by altruism	883 family firms	US	Regression	10.30%	No	No	Yes	Cross-sectional
Schulze, Lubatkin, Dino, and Buchholtz (2001)	Altruism creates agency problems; family firms must incur agency costs.	1376 family firms	US	Regression; Cluster analysis	10.30%	No	No	Yes	Cross-sectional
Sciascia and Mazzola (2008)	Family management decreases performance: infers family agent behavior (lack professional competencies and oriented toward nonfinancial goals). Stewardship effects do not outweigh agency costs.	620 firms	Italy	Regression	4.10%	Yes	No	Yes	Cross-sectional
Sciascia, Mazzola, Astrachan, and Pieper (2012)	Stewardship is advantageous for internationalization; agency structures should govern the business and the family.	1035 family firms	US	Regression	41%	No	No	Yes	Cross-sectional
Sieger, Zellweger, and Aquino (2013)	Psychological ownership can align interests of agents and principals, thus reducing agency costs of monitoring.	714 firms	Switzerland & Germany	Regression	9.50%	No	No	Yes	Cross-sectional
Songini and Gnan (2015)	Family involvement in governance had a negative relationship with agency cost control mechanisms; Family management had a positive relationship with agency cost control mechanisms; no relationship between cost controls and firm performance	146 family firms	Italy	SEM	15%	No	No	No	Cross-sectional

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Tsai, Hung, Kuo, and Kuo (2006)	Family firms need to refine governance systems; agency theory is not suitable for family firms.	63 family & 241 nonfamily firms	Taiwan	Regression	NA	No	Yes	Yes	Cross-sectional
Villalonga and Amit (2006)	Demonstrate that agency conflicts between shareholders are relevant in the US and affect firm performance. Firms can have Agency I and II problems.	508 firms	US	Regression	NA	No	Yes	No	Longitudinal
Westhead and Howorth (2006)	Management rather than ownership structure drives financial performance and pursuit of nonfinancial goals.	240 family firms	UK	Regression	48%	No	No	Yes	Cross-sectional
Zahra (2005)	Family ownership and management promote entrepreneurship, but long tenures of CEO founders do not. Agency theory research leads to contradictory conclusions.	209 family firms	US	Canonical analysis	24.85%	No	No	No	Cross-sectional

Note: * Does not use control variables in the model.

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(Eddleston et al. 2010; Wright and Kellermanns 2011) and to create the need family firms are burdened with to incur agency costs by implementing governance mechanisms to monitor and assess behavior (Chua et al. 2009; Lubatkin et al. 2007).

Entrenched family ownership can also create unique family firm agency problems. Entrenchment is defined as "the relational contract between owners and managers that enable both to occupy key positions in the firm for a significant duration" (Moores 2009: 172). Family ownership is often described as effective because it reduces Type I agency problems associated with the separation of owners and managers (Anderson and Reeb 2003b; Chirico et al. 2011; Jensen and Meckling 1976; Tsai et al. 2006). However, some research suggests that family ownership is not effective because family dynamics and conflicts are difficult to monitor. With ineffective monitoring, moral hazard agency problems may increase, inhibiting productivity (Block 2012). Furthermore, the emotional attachment the owning family has on the firm may inhibit sound business decisions, decreasing firm performance further (Nicholson 2008).

Additionally, family ownership can create agency problems specific to family firms, referred to as Type II agency problems (Ali et al. 2007; Goel et al. 2012; Villalonga and Amit 2006). Instead of the Type I owner-manager conflict, the Type II represents the conflict between majority and minority shareholders (i.e., family and nonfamily shareholders; Villalonga and Amit 2006). An example of a Type II agency problem manifests itself in the misalignment of shareholder goals; family firms often pursue noneconomic goals at the expense of financial gain (Gómez-Mejía et al. 2007). Diverting resources to pursue the family's noneconomic agendas may negatively impact firm performance (Chrisman et al. 2004), thus creating conflicts between family and nonfamily shareholders.

In conclusion, the literature provides support that agency problems are indeed prevalent in the family firm context and is important for two reasons. First, this literature challenged the original agency theory research that argued agency problems did not exist in organizations typified by the convergence of ownership and management (i.e., Eisenhardt 1989; Fama and Jensen 1983; Jensen and Meckling 1976). In doing so, a host of nontraditional agency problems specific to family firms (i.e., asymmetric altruism, family entrenchment, Type II agency problems) was brought to light, thus expanding agency theory into the realm of the family firm. Second, this realization allows for continued agency research within a family firm context, but with a different focus. It allows scholars to research whether other tenets of agency theory are applicable to family firms. Accordingly, the next section shifts the focus away from agency problems and instead focuses on the governance mechanisms agency theorists call for to mitigate agency problems.

Agency Governance. Research supports agency theory's applicability within family firms by examining the firm-level governance mechanisms and their relationship with firm performance. For example, research investigates boards of directors (Anderson and Reeb 2004; Braun and Sharma 2007; Gersick and Feliu 2014; Goel et al. 2014), incentive compensation (Chrisman et al. 2007), and monitoring activities (Chrisman et al. 2007) as agency mechanisms used to mitigate agency problems and subsequently increase performance. Anderson and Reeb (2004) examine board independence and family influence to support their contention that an agency lens is applicable to family firms. They conclude that monitoring mechanisms such as a board of directors are necessary; outside board members monitor the family, and family board members monitor the business (Anderson and Reeb 2004). Likewise, Chrisman and his colleagues (2007) explore the motivations and control of family firm managers to determine if they are agents or stewards. They conclude that family managers are agents because family firms using governance mechanisms prescribed by agency theory (i.e., monitoring, incentive compensation) have higher levels of performance (Chrisman et al. 2007). Braun and Sharma (2007) explore CEO duality

and demonstrate that the separation of positions is a beneficial governance structure for family firm performance.

Instead of a focus on performance, others have focused on perceptions. Cruz and her colleagues (2010) examine how agency contracts are affected by the CEO's perceptions of the top management team. In line with agency theory, they suggest that monitoring and incentive mechanisms are implemented based on the CEO's trust perceptions of top managers. In the family firm context, they suggest that the presence of top managers who are related to the CEO and the level of family ownership in the firm affect these perceptions. Dawson (2011) examines the perceptions of private equity firms as they assess the attractiveness of family firms. She finds that investors prefer professionalized family firms, described as businesses that have agency prescriptions in place such as formal human resource management practices and the presence of nonfamily managers (Dawson, 2011).

In conclusion, this group of family firm articles focuses on the remedies prescribed by agency theory that are theorized to positively impact firm performance. Importantly, this research provides support that agency governance mechanisms, such as the presence of a board of directors, incentive compensation plans, and monitoring activities serve their theorized purpose within family firms. Similar to agency problem research, this research expands the boundary conditions of agency theory by supporting its governance mechanisms and related outcomes within a new organizational context.

Methods of the Literature

As suggested, the cornerstone of much of the agency theory research is that family involvement in the firm creates or causes unique agency conditions that influence the subsequent performance of the firm. Given the importance of research methods in establishing and validating these causal inferences, we examine the extent to which agency theory research includes research designs that effectively guard against key threats to causality and confounded results. Causal relationships can be inferred when three conditions are met. First, the cause and effect variables covary (Van de Ven 2007). Second, the cause precedes the effect in time (Van de Ven 2007). Third, alternative explanations for the covariance between cause and effect variables are eliminated (Cook and Campbell 1979). While exhaustively meeting these criteria is impossible, researchers can more confidently infer causal relationships as these conditions are addressed more thoroughly with a line of solid evidence being preferred over several lines of evidence of questionable quality.

The first criterion, covariation between cause and effect variables, suggests that a change in one variable is accompanied by a change in another (Van de Ven 2007). Presenting a correlation matrix that includes all the study variables provides a rather straightforward means to demonstrate covariance. Given the importance of covariation to causality (Van de Ven 2007), these matrices would be expected to be ubiquitous; however, reviews of the entrepreneurship literature have indicated that not all studies report these matrices (e.g., Crook et al. 2010). Indeed, we find this to be the case in our review of the family firm agency theory literature, finding that only 48 studies (71.6 percent) reported a covariation matrix.

Second, it is critical to establish that the cause precedes the effect, suggesting that the change in the cause variable occurs before the change in the effect variable (i.e., the agency conditions cause changes in outcomes; Van de Ven 2007). The ability to test whether an effect is actually caused by the hypothesized variable is limited when researchers rely on cross-sectional data where the cause and effect variables are collected at the same point in time. Hence, from a temporal perspective, causal influences can be inferred more confidently with longitudinal data

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or, at the very least, cross-sectional data using time-lagged variables. In our review, most of the investigations are cross-sectional in nature (59.7 percent), whereas some are time-lagged (7.5 percent) or longitudinal (32.8 percent articles).

The final criterion, the elimination of alternative explanations, suggests that if the influences of external forces are not eliminated it is impossible to assess the extent to which the external forces may be causing the effect (Van de Ven 2007). The ability to eliminate alternative explanations can be influenced by sampling design (Cook and Campbell 1979). Specifically, because of sampling bias, relationships reflected in the data may not accurately reflect the relationships in the population when small, nonrandom samples are used. Examining the sampling methods of the studies in our review, the majority (56.7 percent) examine differences between family and nonfamily firms. As such, the samples included both types of firms (391 family firms and 381 nonfamily firms, on average). The remainder of articles assesses family firm heterogeneity by examining agency theory within a sample of family firms only (498 family firms on average). Investigations use secondary data (64.2 percent) or primary data (35.8 percent). Of those using primary data, the average response rate is 23.80 percent. Samples of firms in North America (US and Canada) and Europe are equally represented (28 and 27 of the articles, respectively); firm samples from Asia (9 articles), Australia (2 articles), and South America (1 article) are also represented. Unfortunately, only one article used a random sample; in this study, the authors drew a random sample of 15,517 firms from the Italian population of nearly 5 million firms (Sciascia and Mazzola 2008).

Ruling out alternative explanations can also be accomplished by incorporating statistical control variables into the research design (Atinc et al. 2012; Becker 2005). By including theoretically meaningful control variables, variance in the dependent variable that is attributable to the alternative explanation is accounted for *a priori*, enabling researchers to assess the extent to which the remaining variance in the effect is explained by the hypothesized cause (Atinc et al. 2012). Given that regression is the data analysis approach in the overwhelming majority of investigations (60 of 67 articles; other approaches included structural equation modeling, cluster analysis, and canonical analysis), we expected a large percentage of articles in our data set to use control variables. Indeed, among the agency theory articles examined, all but one made use of control variables. In addition, authors often provided the proper rationale, theoretical reasoning, or citations to explain why a particular control variable was included. Schulze et al. (2003a, 2003b), for instance, argued that covariates were to reduce variance that was extraneous to the research question and could potentially confound the interpretation of the findings. In each article, the authors controlled for firm age, justifying this variable as it might be linked to the performance outcome studied due to a selection bias where older firms were in the sample just because they had survived and were successful.

Finally, by not accounting for endogeneity, scholars are not able to eliminate several alternative explanations, leading to incorrect generalizations. The problem of endogeneity arises when the cause that is hypothesized to have a particular effect is influenced directly by that effect. While a number of statistical techniques exist to test for such problems, these methods are just beginning to appear in the family business research (e.g., Patel and Cooper 2014). In fact, these methods were used in only 21 (31.3 percent) of the articles examined. This is particularly important in family firms where the involvement of the family clearly may influence the performance of the firm but the performance of the firm may also influence the family's involvement, especially the family's involvement in the day-to-day operations.

In summary, our review of the methodology employed in family firm agency theory studies reveals that our ability to effectively infer causality may be inhibited. Although roughly two-thirds of the studies include correlation matrices, only one-third are time-lagged or longitudinal, and only one-third rule out alternative explanations by accounting for endogeneity concerns.

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Furthermore, the samples are not random and often are relatively small with low response rates, which gives rise to generalizability concerns. Given the importance of research methods in establishing and validating causal inferences, we incorporate methodological remedies as we present our future research opportunities.

Future Research Opportunities

In this section, we present three future research opportunities that can further extend theory while simultaneously addressing the methodical limitations revealed from extant investigations. The first opportunity for future agency theory research specifically relates to causality, within the theory and the methods. The theorized outcome of agency theory is firm performance, which is often supported in the family firm literature (e.g., Anderson and Reeb 2004; Chrisman et al. 2007; Braun and Sharma 2007; Gersick and Feliu 2014; Goel et al. 2014). However, studies tend to ignore the reasons why there is a link between agency governance and firm performance. Agency theory prescribes governance mechanisms to curb opportunistic behavior thus resulting in increased performance (Eisenhardt 1989; Jensen and Meckling 1976). However, just because governance mechanisms are in place and performance levels are high, does not necessarily mean opportunistic behavior was thwarted; there could be other factors contributing to high levels of performance even in the presence of opportunistic behavior. To account for this possibility, governance, behavior, and performance must be considered. Extant studies neglect to consider behavior as the linking pin between structure and performance; therefore, it should be examined in future studies. For example, research could examine productive work behavior as the missing link; it is an appropriate proxy for capturing a lack of opportunistic behavior (i.e., shirking, free-riding), and has been conceptually and empirically linked to increased firm performance (Gerhart and Milkovich 1992; Huselid 1995).

Additionally, effective research designs and statistical techniques can further support causality. For example, a longitudinal approach that captures variables at several intervals to determine the change in behavior and performance over time as a result of governance mechanisms implemented is warranted. Longitudinal studies can also capture the potential dynamic nature of governance and how that may change over time or generations (Madison et al., 2016). More effective statistical techniques, such as including a correlation matrix or control variables such as past performance, would assist in ruling out alternative explanations and increase our ability to infer causality. The more thoroughly these conditions are addressed, the more confidence researchers have that a causal relationship exists.

The second opportunity for future research is at the intersection of agency theory problems (i.e., opportunistic behavior) and sampling techniques. Current agency theory research assumes that managers are a homogeneous group. Agency theorists subscribe to the idea that self-serving behavior is curbed by the use of governance mechanisms (Eisenhardt 1989; Jensen and Meckling 1976). However, in a family firm context, it is likely that managers are both family and nonfamily members. As such, different behaviors may result between the two groups (Chua et al. 2009; Davis et al. 2010). For example, agency problems are created by asymmetric altruism, but this line of research focuses solely on family members (i.e., parent-child) (e.g., Schulze et al. 2001; Schulze et al. 2003a). There is a need for research to address the relationship between family and nonfamily members. Agency mechanisms may curb the assumed opportunistic behavior of family members, but do they have the same effect on nonfamily members? If not, what are the resulting performance implications for the family firm? Accordingly, future research is needed that addresses agency problems and outcomes with considerations of kinship status.

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From a methodological perspective, this infers that more research is needed that addresses the heterogeneity among family firms. As evidenced in our review, most research, particularly early family firm research, addresses the differences between family and nonfamily firms (Chrisman et al. 2005). More research is necessary to examine differences within and between family firms to provide additional insights. It has been suggested that there is more variation within family firms than in comparison with nonfamily firms (Chrisman and Patel 2012), and these variations can help explain performance differentials. Furthermore, when family firm research can look inside the firms, examinations between family and nonfamily employees can be made. Some studies have shown that family and nonfamily employees behave differently, thus impacting performance (e.g., Madison and Kellermanns 2013). This also implies that respondents are a key concern in family firm research. Results may be misleading if studies continue to mix survey responses from family and nonfamily employees or only have family members represented in the sample.

The third opportunity resides at the intersection of agency governance mechanisms and sampling techniques. Governance mechanisms can be categorized as formal (i.e., monitoring activities, human resource policies) or social (i.e., informal meetings, get-togethers; Mustakallio et al. 2002). Family firm literature is heavily focused on formal governance mechanisms like boards of directors (e.g., Anderson and Reeb 2004; Braun and Sharma 2007), incentive compensation plans (e.g., Chrisman et al. 2007; Schulze et al. 2001), strategic planning (e.g., Chrisman et al. 2004), or human resources practices (Dawson 2011). Importantly, agency research is "concerned with describing the governance mechanisms that solve the agency problem" (Eisenhardt 1989: 59); however, research neglects to consider the impact of social governance mechanisms, and thus should be a consideration for future research.

From a methodological perspective, scholars could explore this opportunity cross-culturally. As shown in our review, the majority of family firm agency theory research is from North America and Europe. As such, results may not be generalizable to other geographic contexts and cultures, such as those in South America. Collective-oriented cultures, such as South America, tend to focus on family harmony and relationships (Strike 2012). It may be plausible that in these cultures, social governance mechanisms are of more importance to family firms and their performance than formal governance. As such, cross-culture samples would provide valuable insight into the heterogeneity of family firms and strengthen the generalizability of findings.

Conclusion

Like others (e.g., Le Breton-Miller and Miller 2009; Madison et al. 2016; Shukla et al. 2014), our review suggests that agency theory is indeed applicable in a family firm context. The literature supports that agency problems are prevalent and uniquely created in family firms. Accordingly, agency costs must be incurred to mitigate these problems. Meaning, agency governance mechanisms, such as boards of directors, compensation incentive plans, and monitoring activities, are deemed necessary in family firms to curb opportunistic self-interested agent behavior and thus reap firm level performance benefits. Other governance structures, however, could be considered in future research to determine their applicability in altering the unique agent behavior problems found in family firms. Gersick and Feliu (2014), for instance, offered an atheoretical, description of unique governance practices in family firms to include formal (e.g., blockholding, dual class stock systems, and shareholder agreements) and informal, family specific (e.g., family offices and family assemblies) practices. Our review suggests that agency theory offers the theoretical lens to hypothesize and explore how each may influence specific agency problems (i.e., principal-principal problems) and the subsequent performance of the family firm.

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Assessing actual agent behavior is also warranted; in doing so, the behavior of family and non-family employees could be assessed to determine if the prescriptions of agency theory hold equivocally across employee types. Furthermore, supporting and validating causal inferences through the methodological approaches in future research is of utmost importance. Our review, unlike others who have reviewed agency theory and governance in family firms (cf. Gersick and Feliu 2014; Goel et al. 2014; Shukla et al. 2014), examined the strength of our causal inferences regarding agency relationships in family firms. While several findings were encouraging (i.e., the prevalent use of control variables), endogeneity testing has been limited. These tests are critical as family involvement may have a causal influence several on variables such as performance as well as an outcome which is dependent on the same variable. In conclusion, agency theory is an applicable theoretical perspective for family firm governance and performance research; however, more research is necessary to fully comprehend the impact of agency governance on the behaviors within and among family firms.

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