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Summary

In this paper, we build on the theoretical literature to develop a framework that yields predictions on the payout policy of private family firms. We argue that two forces primarily drive dividend policy in private family firms: (1) non-value-maximizing behavior as described by Chen et al. (2005) and (2) a private family firm variant of the managerial entrenchment hypothesis. Our empirical analysis supports the predictions. Based on a subsample of 1180 Belgian private family firms for which ownership data are available, we find a significant positive relation between the payout and controlling shareholder ownership above 50%. This finding illustrates that large controlling shareholders are extracting a relatively high amount of resources out of the firm in the form of dividends. We also find that the payout is negatively related to the CEO power balance in the board of directors, measured as the combined effect of CEO duality and the number of board directors. The latter finding is consistent with more powerful CEOs enjoying more discretion over the use of the assets remaining within the firm compared to less powerful CEOs.

Keywords: dividend policy, agency costs, family firms

1. Introduction

The question "how firms choose their dividend policies" has intrigued scholars for decades (La Porta et al., 2000). Contrary to the expectation of the irrelevance of dividend payout policy in a frictionless world (Miller and Modigliani, 1961) and the disadvantage of dividends vis-à-vis capital gains in a world with taxes, firms do pay out dividends in the real world. Several explanations for this dividend puzzle have been proposed, of which a substantial number are grounded in agency theory. In general, these agency models assert that the payout of dividends may mitigate the shareholder-management conflict when ownership is dispersed (Jensen, 1986; Easterbrook, 1984).

Starting from an agency framework, several empirical studies examine the relationship between ownership structure and dividend policy of publicly listed firms (e.g. La Porta et al., 2000; Faccio et al., 2001; Gugler, 2003; Chen et al., 2005; Khan, 2006). These studies differentiate between several types of ownership structure such as family controlled, state controlled, bank/insurance company controlled, control by individuals and foreign controlled ownership structure.

According to several studies (La Porta et al., 1999; Faccio et al., 2001), family-controlled firms seem to be the predominant ownership structure in the world. Family-controlled firms

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are often considered as firms in which major conflicts of interest or large information asymmetries are not present. Large family shareholders are expected to be either members of the management team or have enough incentive and ability for efficient direct monitoring (Gugler, 2003). Schulze et al. (2003) challenge the idea that family ownership can be considered as one homogeneous form of ownership structure. Drawing from a model of generational evolution in entrepreneurial family ventures (Gersick et al., 1997), Schulze et al. (2003) and Lubatkin et al. (2005) discuss agency problems in private family firms in three broad stages of ownership dispersion. Introducing the factor "parental altruism" in traditional agency models, Schulze et al. (2003) argue that the incentives of directors in private family firms are different from those of directors in public firms.

Building on agency theory, we examine the relationship between the ownership structure and dividend policy in private family firms. Since internal governance mechanisms could have an influence on payout policy (Farinha, 2003; Hu and Kumar, 2004), we also discuss and investigate the power balance between the CEO and the board of directors and its influence on dividend policy. Despite the fact that (private) family firms represent the majority of firms worldwide (IFERA, 2003), as far as we know, no study empirically investigates the determinants of the dividend policy in private family firms.

The organization of the paper is as follows. Section 2 discusses agency problems of ownership in private family firms, the role of dividends as an agency cost control mechanism and dividend policy in private family firms. Section 3 derives the main hypotheses. Section 4 describes the data set, the variables and the estimation method. The empirical results are presented and discussed in section 5. Section 6 concludes the paper.

2. Theoretical issues

2.1 Agency problems in private family firms

In their seminal work, Jensen and Meckling (1976) assume a rational model of wealth maximization and, combining arguments from agency theory with those from property rights theory, conclude that conflicts of interest and agency problems emerge, stemming from the separation of the rights of ownership from the rights of control. In the academic literature, divergent views exist about the impact of family ownership and control on agency costs stemming from the separation of ownership and control.

At one extreme, agency models (e.g. Jensen and Meckling, 1976; Ang et al. 2000) assume that the effects of concentrated ownership and owner-management will lead to a minimized or even zero level of agency costs. In line with this view, no major conflicts of interest between management and the ultimate owners are expected to be present in family-controlled companies. Managers and large family shareholders are often the same persons, and therefore, the residual claimants bear (nearly) all of the costs and receive (nearly) all of the

benefits of their actions. Moreover, self-interest by family agents is assumed being tempered by kinship and parental altruism (= utility function in which the welfare of individuals is positively linked to the welfare of others) (Schulze et al., 2003). Altruistic behavior in family firms has several beneficial effects such as the creation of a self-reinforcing system of incentives encouraging family members to be considerate of one another (Schulze et al., 2003) and the enforcement of the incentives to communicate and cooperate (Van den Berghe and Carchon, 2003).

More recently, a growing literature (e.g. Gomez-Mejia et al., 1999; Schulze et al., 2001; Schulze et al., 2003, Van den Berghe and Carchon, 2003; Chrisman, et al., 2004; Lubatkin et al., 2005) on agency issues in private family firms contends this more traditional agency view. Schulze et al. (2001) develop an agency framework based on the behavioral economics assumption and conclude that private ownership, because it isolates firms from the discipline of external markets, and owner management expose firms to agency threats ignored by the model of Jensen and Meckling (1976). Lubatkin et al. (2005) argue that a combination of private ownership and owner-management in private firms threaten owner-managers with self-control problems. Private firms are more vulnerable to self-control problems than public firms because private firms' large-block-holding owner-managers enjoy almost unchallenged discretion over the use of their firm's assets. Since owner-managers do not have to justify their behaviour to an independent board of directors or outside shareholders, the likelihood increases that they use the resources of the firm in their own interest.

Discussing these ideas in the context of family firms, Schulze et al. (2003) argue that altruism may not only have a mitigating but also an exacerbating effect on agency problems in family firms. Altruism may leak from the household into the operations of the firm and exacerbate the agency problems of adverse selection, moral hazard and hold-up. Family agents face very high exit costs (e.g. illiquidity of shares, loss of privileges that generally come with being employed by the family) and as a consequence, are more vulnerable to being held up than agents in public and non-family private firms. Schulze et al. (2003) also argue that parents' altruism will lead them to be generous to their children even when these children free ride and lack the competence or intention to sustain the wealth creation potential of the firm.

Furthermore, Chrisman et al. (2004) argue that family firms are especially vulnerable to agency problems resulting from honest incompetence (Hendry, 2002) and deficits of expertise. Both an unfavourable self-selection process in the external labor market (Lubatkin et al., 2005) and a self-imposed preferential family treatment personnel selection criterion (Chrisman et al., 2004) will lead to lower-quality agents in private family firms. Moreover, the study of Gomez-Mejia et al. (2001) reports a positive relation between family contracting and agency costs as a result of executive entrenchment.

In addition, Lubatkin et al. (2005) discuss the influence of ownership stage on agency problems in family firms. They assert that agency problems are driven by the quality and nature of familial relationships within the firm. They reason that the nature of altruism and the type of agency problems are contingent upon the stage of ownership dispersion. Based on the model of Gersick et al. (1997) about generational evolution in entrepreneurial family ventures, Lubatkin et al. (2005) distinguish three types of family firms based on ownership forms: (1) the controlling-owner family firm, where the founder/owner/manager also exercises the rights of control (Jaffe and Lane, 2004), (2) a sibling partnership, where varying proportions of ownership are held by members of a single generation and (3) a cousin consortium/business dynasty where ownership is further fractionalised as it is passed on to include third and later generations.

2.2 Agency problems and dividend policy

Several theoretical explanations[2] for the dividend puzzle have been developed following the Modigliani-Miller irrelevance propositions. Agency models (e.g. Easterbrook, 1984; Jensen, 1986; Myers, 2000) assert that dividend payments address conflicts of interest between corporate insiders (such as managers and controlling shareholders) and outside (minority) shareholders. Corporate insiders can pursue company policies that benefit themselves at the expense of minority shareholders, for example through the diversion of corporate assets to themselves, excessive salaries, outright theft (La Porta et al., 2000) or investments in low-return projects (Jensen, 1986). These agency problems are particularly severe when a firm generates substantial amounts of free cash flow (Jensen, 1986). Dividend payments could mitigate these problems by removing corporate resources away from the control of corporate insiders.

La Porta et al. (2000) discuss two alternative agency models. Their first model posits that a better legal protection of the minority shareholders leads to more dividends being extracted from the firm. Their alternative model postulates that dividends are a substitute mechanism for legal protection. Dividends are then paid out when firms try to establish a reputation for good treatment of shareholders and signal that expropriation does not have to be a concern. Hence, dividend policy acts as a corporate monitoring mechanism.

More recent studies concentrate on the managerial entrenchment hypothesis to explain dividend policy. Empire-building managers are expected to voluntarily pay out dividends as a protection against disciplinary sanctions by outsiders (Zwiebel, 1996). Managers who are more likely to take sub-optimal decisions choose higher payout levels. So do managers who can be disciplined by outsiders at relatively low costs (Hu and Kumar, 2004). Additionally, Farinha (2003) predicts that below a certain entrenchment level, insider ownership and dividend policies can be considered as substitute corporate governance devices. Starting from

[2] For an overview of these theoretical developments, see Allen and Michaely (2002).

a low level of inside ownership, an increase of this inside ownership may reduce agency costs (Jensen and Meckling, 1976), and hence, dividend policy may become less important as a monitoring vehicle. Therefore, a negative relationship is expected between insider ownership and dividend payments. Above the critical entrenchment level, dividend policy may play the role of a monitoring mechanism, mitigating entrenchment-related agency costs. Therefore, above the entrenchment level, a positive relation between dividend payout and insider ownership. Farinha (2003) finds evidence for this described U-shaped relationship between dividend policy and insider ownership.

Khan (2006) investigates the relationship between dividends and ownership concentration and composition. Khan finds a significant negative nonlinear relationship between dividends and ownership concentration. Examining the influence of ownership composition, Khan finds evidence that equity holdings in the hands of powerful shareholders are positively related to dividends.

2.3 Dividend policy in private family firms

Several empirical studies investigating the relationship between ownership structure and dividend policy also focus on family ownership (Faccio et al., 2001; Chen et al., 2005). Based on a sample of European and Asian listed companies, Faccio et al. (2001) conclude that in businesses controlled by a family, the salient agency problem is expropriation of outside shareholders by controlling shareholders. They find evidence that investors anticipate the expropriation in companies as higher dividends are paid out in this case.

Chen et al. (2005) find a positive relationship between dividend payouts and controlling family ownership between 10 and 35% for publicly listed, small market capitalization Hong Kong firms over 1995-1998. Two competing explanations are presented for this result. The first explanation postulates that dividends are beneficial because of the corporate monitoring effect. The alternative explanation postulates that higher payouts stand for extraction of company resources by the controlling family shareholders. The question whether this behavior of powerful shareholders is the result of improved corporate governance or non-value-maximizing behavior by powerful shareholders is an open one (Chen et al., 2005; Khan, 2006).

Although there is a general tendency of agency models to consider dividend policy as an agency conflict control mechanism, we believe that, in the context of private family firms, several facts indicate a higher likelihood in favor of the alternative non-value-maximizing explanation presented by Chen et al. (2005). First, the absence of the disciplining forces of the equity capital markets (e.g. absence of take-over threat) leaves the controlling family shareholders with little incentive to pay out dividends. Moreover, the signalling effect of dividend payouts (Jensen, 1986) has not much value in such a context as no consistency in dividend policy has no deteriorating effects on any stock price.

Second, and related to the first point, family firms are generally acknowledged to have both economic goals and non-economic (non-pecuniary) goals (Chrisman et al., 2004). Therefore, rational value-maximizing behaviour may not be the sole possible starting point in theoretical discussions. In light if this, evidence of non-value-maximizing behaviour is not necessarily evidence of sub-optimal behaviour. For example, if owners wish to divert resources to pursue non-pecuniary goals (e.g. wealth diversification objective) and managers conform to such wishes, there may be diminished economic performance but no sub-optimal behaviour (in light of the non-pecuniary goal).

3. Main hypotheses concerning dividend policy in private family firms

Dividend policy may change considerably over the three stages of ownership dispersion in private family firms as described by Schulze et al. (2003). Dividend policy is expected to evolve as family ownership disperses over several family members and family branches. Since there exist no liquid markets for shares of private companies, outside family owners (especially emerging in the cousin consortium stage) are likely to favor dividend consumption over value creation through additional investments (Schulze et al., 2003).

Ownership rights in a private family firm can be exercised directly or through an (industrial or holding) company. When ownership rights are exercised through a company, a simple group structure often emerges consisting of a tightly affiliated company to a mother company. These simple family business groups are expected to be created especially in later ownership stages such as a sibling partnership or a cousin consortium, usually leading to a higher likelihood/amount of dividend payouts. Moreover, a holding firm could also be the result of a family management buyout in which the later generation buys out the founder/previous generation. The generated cash in the affiliated firm is then expected to be transferred to the mother company in order to pay back the loans in the buyout construction, increasing dividend rates. *On the basis of the above arguments, we predict a higher dividend payout in group-affiliated family firms as compared to non-group affiliated private family firms (Hypothesis 1).*

Dividends transfer wealth from the discretion of the controlling shareholder on a pro rata basis. The higher the ownership percentage of the major controlling shareholder is, the less this shareholder is hurt by the pro rata mechanism. Alternatively, the lower the percentage ownership of the controlling shareholder is, the greater the incentive he has to consume at his advantage instead of sharing pro-rata (and only getting a fraction of the amount). *On the basis of the resource extraction argument (Chen et al., 2005), we predict a positive relation between the dividend payout rate and the ownership percentage of the major controlling shareholder (Hypothesis 2).*

Managerial entrenchment models assume that (family) managers derive utility from empire building. The degree in which this could be considered as a problem depends on the managerial type (Hu and Kumar, 2004). Hu and Kumar state that strong manager types are less inclined to make payouts as a disciplining device, compared to weak manager types. We expect a similar relationship in private family firms based on different arguments. The management team in private family firms is often dominated by the (family) CEO (Feltham et al., 2005). From an empire building point of view, a powerful CEO will prefer to derive personal benefits from the control of assets and keep the cash in the company, even at the expense of minority (family) shareholders. Moreover, greater power makes the CEO less vulnerable to disciplining by outsiders (Hu and Kumar, 2004). The power of the CEO to determine payout policy is expected to be especially high when he has the ability to dominate the board of directors. This situation occurs when CEO duality is present, i.e. when the CEO is also chairman of the board. Jensen (1993) and Boyd (1994), for example, argue that CEO duality diminishes the independence and effectiveness of the board and increases CEO power.

Effective internal governance mechanisms could entail a moderating effect on CEO duality. In the founding owner stage, CEO duality usually is the basic case. When the family firm evolves over generations, the role of the board of directors as a monitoring mechanism is expected to increase. The role of outside directors in the monitoring of the management team is well documented in the literature (Brunarski et al., 2004; Hu and Kumar, 2004). However, we argue that even the inclusion of additional family directors on the board of directors may entail a moderating effect on the power of the CEO. These additional family directors then have the opportunity to defend their (minority) interest and dividend preferences directly in the board. Hence, we consider CEO power as a combined effect of the direct power of the CEO through CEO duality and the moderating effect of the number of directors in the board. *Because a more powerful CEO enjoys more discretion over the use of assets remaining within the firm compared to a less powerful CEO, we predict, ceteris paribus, a negative relation between dividend rates and the CEO power balance in the board of directors (Hypothesis 3).*

4. Methodology

4.1 Sample selection

Starting from a sample of 3968 Belgian family firms, we identify private family firms based on ex ante indicator criteria: (1) several directors have the same name and (2) directors have the same name as the company name. Although this criterion is rather straightforward and not in line with the definitional literature on family firms (Chua et al., 1999), other

studies in the Belgian context find that this ex ante criterion corresponds for more than 95% to an ex post definition based on ownership and management.

Firm level date, including dividends and ownership data, are drawn from unconsolidated balance sheets and income statements for the year 2004, available from Bureau Van Dijk. Firms are deleted when the data to calculate the payout ratio are missing (3), when they have an infinite (51) or negative payout ratio (15) or, when the payout ratio is above 200% (45). This leaves us with a sample of 3853 firms. For a subsample of 1180 firms, ownership percentages of the controlling owner are available.

4.2 Variables

Dependent variable

Our measure of dividend payout is regular cash dividends on common stock divided by net earnings after taxes. Table 1 reports descriptive statistics for payouts in our sample. The payout ratio averages 8,22%. 3359 firms (87% of the sample) do not pay a dividend in 2004. The average (median) payout of the 494 dividend paying firms is 63.98% (58.22%).

Indicator variable hold

We create an indicator variable 'hold' that equals one if the largest controlling shareholder of the family firm holds his ownership rights through an (industrial or holding) company. 'Hold' equals zero if the largest controlling shareholder is an individual. The indicator variable 'hold' equals one for 1180 firms in the sample. On the basis of a presumed positive relation between the presence of a family group structure and a later ownership stage (sibling or cousin consortium), a positive relation is predicted between dividend payout and the variable 'hold' (Hypothesis 1).

91.2% of the firms for which 'hold' equals zero pay no dividends; the corresponding percentage for firms for which 'hold' equals one is 78.1%. The average (median) payout for the firms for which 'hold' equals zero is 4.87% (0.00%); the average (median) payout for the firms for which 'hold' equals one is 15.80% (0.00%).

*** INSERT TABLE 1 HERE ***

Ownership percentage of largest controlling owner

For the subsample of 1180 family firms, we examine the relationship between dividend payout and the ownership percentage of the largest controlling shareholder. According to table 1, the largest controlling owner holds a substantial percentage in the firm: the average (median) percentage ownership is 75% (97%). As we argued above, we expect a positive relation between dividend payouts and the controlling shareholder ownership percentage (hypothesis 2).

87.9% of the firms with a controlling owner holding less than 50% pay no dividends; the corresponding percentage for firms with a controlling owner holding more than 50% is 73.7%. The average (median) payout for the low controlling ownership percentage group is 7.32% (0.00%); the average (median) payout for the high controlling ownership percentage group is 19.69% (0.00%).

Figure 1 reports the average payout ratio per class of controlling shareholder ownership percentage.

INSERT FIGURE 1 HERE

CEO power

As we argued above, we consider CEO power as a combined effect of CEO duality and the mitigating effect of the number of directors in the board. Our construct for CEO power is calculated as follows. If there is separation of CEO and chairman positions (CEO duality equals 0), CEO power takes the value of (1/number of board members). In this case, CEO power is assumed to be proportionate to the $(1/n)^{th}$ fraction of the board the CEO represents, where n is the number of members in the board. This reciprocal specification is used to indicate the non-linear relationship between the number of directors and dividend payout while taking into account a "satiety level" of the number of directors. If there is no separation of CEO and chairman positions (CEO duality equals 1), CEO power takes the value of (2/number of board members). It is thus assumed that, if the CEO cumulates two functions (CEO and chairman of the board), his power is twice as high than in the case where CEO and chairman functions are separated. We expect a negative relation between the dividend payout and CEO power (hypothesis 3).

90.3% of the firms have no separation of CEO and chairman positions. According to table 1, the average (median) number of board members is 3.35 (3.00).

Growth

Private family firms have no ready access to capital markets. Internal finance is crucial for private firms facing growth opportunities. A firm expecting rapid growth should pay out less in order to accumulate financial slack. This means that, other things equal, dividends should be negatively related to firm growth. Growth is measured as the increase in total assets between 2003 and 2004 divided by total assets in 2003. According to table 1, the mean (median) percentage of growth in total assets over 2003-2004 is 5.23% (1.91%).

Cash flow

The residual theory implies that, given investment opportunities, a firm with higher current cash flow will pay higher dividends. Similarly, the pecking order theory implies that,

given investment needs, a higher cash flow from existing assets will translate into higher dividends, as the need for slack is lower. Therefore, other things equal, dividends should be positively related to some measure of cash flow. The cash flow measure used is defined as net earnings adjusted for non-cash costs and revenues, divided by total assets. According to table 1, the mean (median) cash flow to total assets ratio is 9.23% (8.76%).

Leverage

We expect leverage to have a negative effect on payout, other things held constant, for three reasons. First, there may be a direct and restrictive impact of debt covenants on payouts. Second, there may be an indirect negative effect since debt-related payouts reduce firm liquidity and constrain (discretionary) payouts to shareholders. Third, debt and dividends are substitutes in controlling agency problems.

The leverage variable is defined as book value of total financial debt over book value of equity. According to table 1, the mean (median) leverage ratio is 1.1514 (0.4558).

Control variables

We control for firm size using the log of total assets. We use firm age as an additional control variable. According to table 1, the average (median) firm age is 25 (21) years. We hypothesize that the dividend payout is positively related to firm size and age.

*** INSERT TABLE 2 HERE ***

Table 2 presents correlation coefficients between the variables defined above. Taking a look at the correlation between the main explanatory variables, ownership percentage of controlling shareholder and CEO power, and other variables, the most noteworthy results are the following. The percentage ownership of the controlling owner is negatively correlated (10% level) with the number of board members and positively correlated (5% level) with our construct for CEO power. The number of board members is negatively related (1% level) to CEO duality and positively related (1% level) to firm size and age. Our construct of CEO power is negatively related (1% level) to firm age, supporting our presumption that CEO power evolves (lessens) with the age (generational stage) of the firm.

5. Empirical analysis

We estimate a one-sided tobit-model (censored at zero) that relates payout ratios to the explanatory variables. Results are presented in table 3.

In model (1) (first column), the total sample is used and the variables hold and CEO power are included as main explanatory variables, next to asset growth, cash flow to total

assets, leverage, firm size and age. According to table 3, first column, the indicator variable 'hold', available cash flow, leverage and size are all significantly related to the payout ratio and have the predicted sign. The highly significant, positive coefficient of 'hold' confirms our prediction of a higher payout in group-affiliated family firms as compared to non-group affiliated firms. Payout appears to be negatively related to CEO power, the coefficient, however, is insignificant.

*** INSERT TABLE 3 HERE ***

In model (2), the ownership percentage of the largest controlling shareholder and CEO power are included as main explanatory variables, next to asset growth, cash flow to total assets, leverage, firm size and age. According to table 3, second column, the ownership percentage of the largest controlling owner, the cash flow measure, leverage and firm size are highly significant (1% level) in explaining the payout ratio. The positive coefficient of the ownership percentage of the largest controlling shareholder is consistent with the conjecture that, ceteris paribus, larger payouts are associated with higher ownership of the controlling shareholder, who thus receives a relatively high amount of dividend income. The coefficient on CEO power is negative and significant at the 10% level, confirming the prediction that, ceteris paribus, stronger CEOs tend to keep more resources under their control, i.e. within the firm.

In model (3), we allow for non-linearity in the relationship between corporate payout and ownership percentage of the controlling shareholder. The following two variables are defined (assuming that the actual ownership percentage of the largest controlling shareholder is m):

Ownership percentage [0,0.50) = m (if m<= 0.50), 0.50 (if m>0.50)

Ownership percentage [0.50, 1.00) = 0 (if m<= 0.50), m-0.50 (if m>0.50)

According to table 3, third column, the results show no significant relationship between dividend payout and controlling shareholder ownership up tot 50% of the company's stock and a significantly positive relationship (1% level) for controlling shareholder ownership between 50 and 100%[3]. As in model (2), the coefficient on CEO power is negative and significant at the 10% level.

[3] For the variables CEO power, growth, cash flow, leverage and for the control variables, parametric (non-parametric) tests were conducted for differences in mean (location shift in the distribution) between the low controlling ownership percentage group (<=50%) and the high controlling percentage group (>50%). None of the tests indicates that means (distributions) are significantly different.

6. Discussion of results and conclusion

In this paper, we build on the theoretical literature to develop a framework that yields predictions on the payout policy of private family firms. We argue that two forces primarily drive dividend policy in private family firms: (1) non-value-maximizing behavior as described by Chen et al. (2005) and (2) the CEO power balance in the board of directors, which is presumed to evolve with the generational stage of the family firm. Our empirical analysis supports the predictions.

We find that large controlling shareholders (ownership percentage above 50%) succeed in extracting relatively large resources from the company through dividend payments, ceteris paribus. This is in line with the resource extraction argument. There is no significant relation between the payout and controlling shareholder ownership below 50%. These findings are in the line with those documented by Chen et al. (2005) who find a negative relation between dividend yield and family ownership up to 10% of the company's stock and a positive relationship for ownership in the 10 to 35% range for a sample of publicly listed, small market capitalization firms. They are also in line with the finding of Farinha (2003) that, above a critical entrenchment level estimated in the region of 30%, the coefficient of ownership by management changes from negative to positive. The question whether the finding in this paper is the result of non-optimal behavior of the controlling shareholder (in light of the value-maximization objective) or private family firms pursuing non-pecuniary goals is an open one[4].

We also find that the power balance of the CEO in the board of directors has explanatory power with respect to the level of payouts. Greater CEO power leads to less dividends being paid out and thus more resources under the control of the CEO, ceteris paribus. This finding is in line with earlier documented results for publicly listed firms. Hu and Kumar (2004), for example, find that for a sample of publicly listed US firms, the likelihood of making a dividend payment increases significantly with the proportion of outside directors on the board. Chen et al. (2005) also find a significant positive relationship between a dummy variable indicating that the majority of board members are independent non-executive directors and the dividend yield.

As far as we know, this is the first paper studying dividend policy in private family firms. Overall, we can conclude that the relations between dividend payouts and ownership and control structures in the context of private family firms, as documented in this paper, are similar to those derived in the context of publicly listed (family or non-family) firms. Underlying forces may, however, be different, because of the different nature of agency costs

[4] The negative relation between payout and controlling shareholder ownership above 50% could, for example, be the result of a managerial desire to diversify wealth by increasing liquidity when the shareholdings in the firm are large (wealth diversification objective).

in private family firms (evolving with generational stage) and/or because of the broader goals these firms often pursue.

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Table 1: Sample distribution of payout ratio, ownership and control variables, and other firm characteristics

				Percentile				
Variable	N	Mean	Standard deviation	Min	25th	50th	75th	Max
Payout	3853	0.0822	0.2631	0.0000	0.0000	0.0000	0.0000	1.9895
Ownership percentage largest controlling owner (%)	1180	0.7508	0.3101	0.0002	0.4900	0.9714	0.9980	1.0000
Number of board members	3853	3.3522	1.0867	2	3	3	4	11
CEO duality	3853	0.9029	0.2961	0	1	1	1	1
CEO power	3853	0.6207	0.2029	0.0909	0.5000	0.6667	0.6667	1
Asset Growth (%)	3853	0.0523	0.2828	-0.9449	-0.0603	0.0191	0.1239	4.1485
Cash flow to total assets	3784	0.0923	0.2126	-9.5598	0.0435	0.0876	0.1498	1.3749
Leverage	3853	1.1514	2.4539	-4.9038	0.0430	0.4558	1.3529	15.8888
Log of assets	3853	7.5125	1.1912	0.6931	6.7523	7.4230	8.2131	12.7891
Firm age (years)	3853	25	14	6	16	21	31	112

Table 2: Correlation of payout and explanatory variables.

	Percentage controlling owner	Number of board members	CEO duality	CEO power	Asset growth	Cash flow to assets	Firm leverage	Log of assets	Firm age
Payout ratio	0.1737 <0.0001 1180	0.0556 0.0006 3853	-0.0427 0.0080 3853	-0.06411 <0.0001 3853	-0.0007 0.9642 3853	0.0983 <0.0001 3784	-0.0844 <0.0001 3853	0.1392 <0.0001 3853	0.0370 0.0218 3853
Percentage controlling owner		-0.0567 0.0515 1180	-0.0097 0.7406 1180	0.0685 0.0186 1180	0.0319 0.2739 1180	0.0677 0.0211 1161	-0.0453 0.1203 1180	-0.0138 0.6362 1180	-0.0380 0.1923 1180
Number of board members			-0.1632 <0.0001 3853	-0.8057 <0.0001 3853	-0.0013 0.9352 3853	0.0137 0.4012 3853	-0.0130 0.4205 3853	0.3142 <0.0001 3853	0.1190 <0.0001 3853
CEO duality				0.5381 <0.0001 3853	-0.0148 0.3576 3853	-0.0186 0.2522 3784	-0.0041 0.8002 3853	-0.0772 <0.0001 3853	-0.0213 0.1865 3853
CEO power					-0.0136 0.3999 3853	-0.0287 0.0781 3784	0.0136 0.3985 3853	-0.2501 <0.0001 3853	-0.1010 <0.0001 3853
Asset growth						0.1461 <0.0001 3784	0.0626 0.0001 3853	0.1571 <0.0001 3853	-0.0305 0.0583 3853
Cash flow to total assets							-0.0551 0.0006 3853	0.0585 0.0003 3784	-0.0475 0.0035 3784
Firm leverage								0.0425 0.0083 3853	-0.0837 <0.0001 3853
Log of assets									0.2217 <0.0001 3853

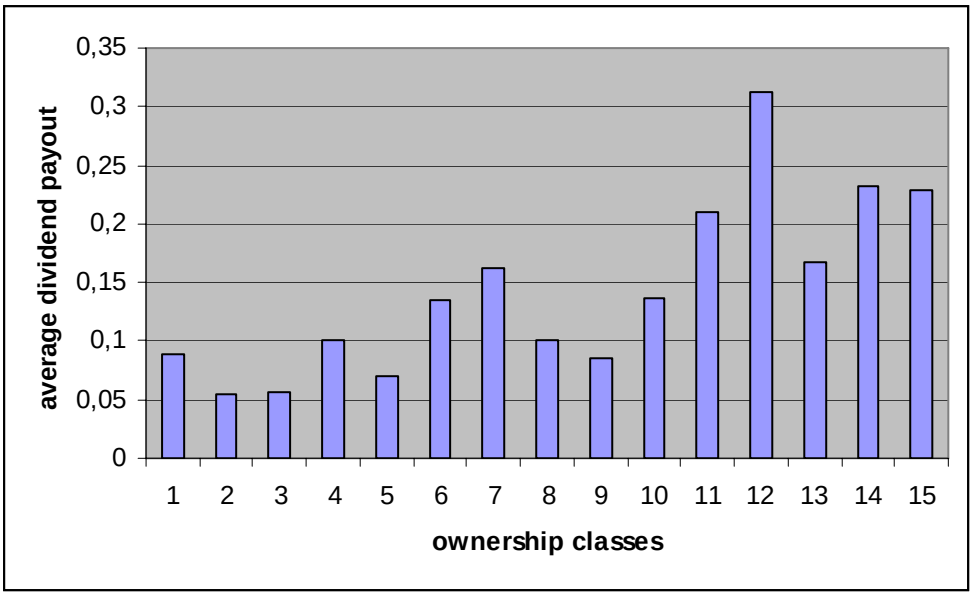
The first entry is the estimated correlation coefficient. The second entry is the p-value indicating statistical significance. The third entry indicates the number of observations.

Table 3: Tobit estimates of the determinants of payouts

Independent Variables	Model (1)	Model (2)	Model (3)
Hold	0.4989***		
	<0.0001		
Ownership percentage of controlling owner		0.8253***	
		<0.0001	
Ownership percentage [0,0.50)			0.5705
			0.2791
Ownership percentage [0.50,1.00)			0.9273***
			0.0003
CEO power	-0.1694	-0.3764*	-0.3730*
	0.2362	0.0608	0.0633
Asset growth	0.0076	-0.0515	-0.0528
	0.9584	0.7360	0.7298
Cash flow to total assets	4.1869***	3.8102***	3.7894***
	<0.0001	<0.0001	<0.0001
Firm leverage	-0.1519***	-0.0568***	-0.0566***
	<0.0001	0.0013	0.0014
Log of assets	0.2702***	0.1904***	0.1893***
	<0.0001	<0.0001	<0.0001
Firm age (years)	0.0010	0.0004	0.0004
	0.6458	0.9006	0.8897
Number of observations	3784	1161	1161
Log likelihood	-1461.0	-678.67	-678.55

The sample consists of family firms with firm-level data over 2004. The first entry in the table is the estimated coefficient. The second entry is the p-value indicating statistical significance.
*** Statistically significant at 1% level.
** Statistically significant at 5% level.
* Statistically significant at 10% level.

Figure 1: Average dividend payout per ownership class



Note: Ownership classes are defined by ownership percentage of largest controlling shareholder
Class 1: controlling owner holds between 0 and 10% (N=40)
Class 2: controlling owner holds between 10 and 20% (N=48)
Class 3: controlling owner holds between 20 and 30% (N=60)
Class 4: controlling owner holds between 30 and 40% (N=67)
Class 5: controlling owner holds between 40 and 50% (N=156)
Class 6: controlling owner holds between 50 and 60% (N=25)
Class 7: controlling owner holds between 60 and 70% (N=30)
Class 8: controlling owner holds between 70 and 80% (N=50)
Class 9: controlling owner holds between 80 and 90% (N=48)
Class 10: controlling owner holds between 90 and 95% (N=38)
Class 11: controlling owner holds between 95 and 97% (N=28)
Class 12: controlling owner holds between 97 and 98% (N=36)
Class 13: controlling owner holds between 98 and 99% (N=118)
Class 14: controlling owner holds between 99 and 99.5% (N=57)
Class 15: controlling owner holds between 99.5% and 100% (N=379)