Although large owners monitor managers effectively, they differ in important ways. Whereas founder owners focus on firm performance, family owners also pursue socio-emotional goals. We leverage this distinction to theorize that family owners offer hired CEOs more incentive pay—to attract nonfamily CEOs, signal good governance, and achieve better firm performance. Without socioemotional wealth distractions, founder owners do not need high incentives and overusing them is counterproductive. Bayesian regressions using a panel of 335 S&P 500 firms support our theory. A key implication is that founder and family owners approach governance differently and these differences affect firm performance.

Introduction

Most firms around the world are owned by their founders or by families, and they contribute significantly to economic growth, employment, and prosperity (La Porta, Lopez-de-Silanes, & Shleifer, 1999; Steier, 2007; Zahra, Hayton, & Salvato, 2004). The most successful founder- and family-owned firms often sell shares to the public as they grow in size and significance. Indeed, such firms represent about a third of all publicly listed firms in the United States (Anderson & Reeb, 2003). Although these firms are large, research has shown that founders and families continue to influence their strategies, governance, and performance (He, 2008; Miller, Le Breton-Miller, Lester, & Cannella, 2007).

Understanding how founders and families exert continued influence is important because prior research shows that these owners have very different goals. In particular, founder owners are focused almost exclusively on growth and financial performance.
(e.g., Miller, Le Breton-Miller, & Lester, 2011; Miller et al., 2007) whereas family owners also pursue socioemotional (i.e., affective) goals, such as dynastic control, family-member employment, and enhanced reputation (Astrachan & Jaskiewicz, 2008; Chrisman, Chua, Pearson, & Barnett, 2012; Deephouse & Jaskiewicz, 2013; Gómez-Mejía, Cruz, Berrone, & De Castro, 2011; Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007). These distinct goal foci are important because they have consequences for shareholders, employees, and other stakeholders (Gómez-Mejía et al., 2011; Miller et al., 2011). For example, founders’ focus on financial performance helps shareholders (Miller et al., 2007), while employees fare better, on average, in family firms where socioemotional issues matter (Block, 2010).

The most common way these large owners pursue their distinctive goals is by serving as CEOs (He, 2008; Naldi, Cennamo, Corbetta, & Gómez-Mejía, 2013), but this source of influence is often temporary in that founders and families at large public firms must eventually hire CEOs who might not fully embrace the founders’ or family’s goals (Boeker & Karichalil, 2002; Chua, Chrisman, & Bergiel, 2009). Whereas hiring a professional CEO reduces these owners’ overall control, prior research shows that large owners still can exercise considerable influence (Gómez-Mejía, Larraza-Kintana, & Makri, 2003; Miller et al., 2011). One key way they do this is by shaping hired CEOs’ compensation. Specifically, research shows that large owners, such as founders and families, reduce overall CEO compensation and tighten the link between CEO compensation and firm performance (Gómez-Mejía, Tosi, & Hinkin, 1987; McConaughy, 2000; Tosi, Werner, Katz, & Gómez-Mejía, 2000; Werner, Tosi, & Gómez-Mejía, 2005).

CEO compensation research, however, has tended to treat all large owners alike (e.g., Gómez-Mejía et al., 1987; Tosi & Gómez-Mejía, 1989). We challenge this implicit assumption based on research showing that founder and family owners possess distinct goal foci (Miller et al., 2007, 2011), and we build theory explaining why founder and family owners are (1) different in the way they influence their hired CEOs’ compensation and (2) in the way they link CEO incentives to firm performance. Given that founder and family owners’ distinct goals have important implications for shareholders, employees, and other stakeholders, and that a key way large owners pursue their goals is by exercising influence over their hired CEOs’ compensation, it seems worthwhile to learn whether founder and family owners are different in how they influence CEO compensation and its link to firm performance. Such knowledge is important because failure to distinguish among large owners might mislead researchers into assuming that they are similar in their CEO compensation and other governance practices.

Chrisman, Memili, and Misra (2014) and Chua et al. (2009) took important first steps by developing theory to explain differences between family and hired managers’ abilities, evaluations, likely compensation, and probable success. We build on these efforts and, more generally, on agency and signaling theories to develop and test theory about the influence of founder and family ownership on hired CEOs’ incentive compensation and the link between CEO incentives and firm performance. Our focus is on CEO incentives because they represent the lion’s share of CEO compensation in large public firms (e.g., Hayes, Lemmon, & Qiu, 2012), and because they focus hired CEOs’ attention on shareholder returns, which might weaken their focus on other goals such as family owners’ socioemotional wealth.

Although it might seem at first that offering incentives to hired CEOs and tying those incentives to firm performance would undermine family owners’ pursuit of

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1. Our theory applies to large public firms, so “large owners” usually hold between 5 and 40% of shares.
socioemotional wealth, our central theoretical contribution is to explain why family owners do exactly that. That is, based on agency and signaling theories, we suggest that firms with family owners offer greater CEO incentive compensation than do founder owners, both to entice high-quality CEOs to join the firm and to signal to other shareholders that the family shares their concerns about financial performance. Doing so might sacrifice some forms of socioemotional wealth (e.g., environmental investments—Berrone, Cruz, Gomez-Mejia, & Larraza-Kintani, 2010), but allows family owners to retain the support of other shareholders and thereby maintain their influence in key decisions, which is itself a foundational socioemotional wealth goal (Gómez-Mejía et al., 2011). Further, in an effort to offset lost socioemotional wealth from having a nonfamily CEO, family owners will bind higher CEO incentives tightly to firm performance—more so than their widely held (i.e., manager-controlled—Gómez-Mejía et al., 1987) counterparts. Founder owners, in contrast, do not need to offer high CEO incentives because they are well known to be effective at monitoring and they are focused almost exclusively on firm growth and performance. Indeed, high CEO incentives in the presence of founder ownership suggest that founder owners are not engaged in monitoring, and that firm performance might suffer.

Our empirical contribution is to find support for our theory using Bayesian regression analysis on a panel of 335 S&P 500 firms. Specifically, we (1) find different founder and family ownership effects on CEO incentive compensation and (2) different founder and family ownership effects on the CEO compensation–firm performance relationship. Our theory and results have important implications for understanding performance differences among firms. Specifically, founder owners outperform (e.g., Miller et al., 2007) because most founder owners continue to play an important monitoring role after stepping down as CEO; while many family owners underperform, those that hire external CEOs and tie incentives to performance do better.

Theory Development and Hypotheses

Ownership, CEO Compensation, and Firm Performance

The separation of ownership and control in large public firms with widely held ownership creates a principal–agent problem that has been long acknowledged and well researched (Berle & Means, 1932; Fama & Jensen, 1983; Jensen & Meckling, 1976). The essential problem is that managerial work is complex and largely hidden from principals’ (i.e., owners’) view, so it is difficult to know (through monitoring) whether agents are acting in principals’ best interests (Eisenhardt, 1989). Accordingly, agency theory predicts that boards of directors, as shareholder representatives, will institute strong CEO incentive compensation to align CEOs’ incentives with shareholders’ interests (Jensen & Murphy, 1990; Tosi et al., 2000). CEO compensation research shows that CEOs do indeed receive substantial incentive compensation and that incentives rise and fall with the severity of principals’ monitoring problems. CEOs are given more incentives, for instance, as job complexity, information processing demands, and discretion in decision-making increase (Carpenter & Sanders, 2004; Finkelstein & Boyd, 1998; Henderson & Fredrickson, 1996). Such job attributes mean that CEOs’ actions affect firm performance, but that it is difficult for shareholders to know in advance if CEOs are making the best decisions (Balkin, Markman, & Gómez-Mejía, 2000).

A partial solution to the principal–agent problem occurs when there is a large owner who has both the power and incentive to directly monitor managers. Consistent with agency theory, CEO compensation falls when active monitoring by a large owner reduces
the need for shareholders to rely largely on CEO incentives to protect their interests
(Barkema & Gómez-Mejía, 1998; Lippert & Moore, 1995; Rediker & Seth, 1995). Large
owners, on average, also make sure that CEO incentives are tightly linked to firm performance
(Gómez-Mejía et al., 1987; Tosi et al., 2000; Werner et al., 2005). However, large owners also create the potential for a second kind of agency problem, what Lubatkin
(2007, p. 61) calls the “principal–principal” problem, wherein large shareholders divert
resources toward self-interested goals that potentially harm firm performance (Jones,
Makri, & Gómez-Mejía, 2008; Villalonga & Amit, 2006).

Although prior CEO compensation research implicitly assumes that all owners are alike (e.g., Gómez-Mejía et al., 1987; Tosi et al., 2000; Werner et al., 2005), we challenge
this assumption based on research showing important goal differences between family-
and founder-owned firms; such differences imply that principal–principal problems are not the same for all large owners. In particular, research shows important goal differences between family- and founder-owned firms that create different agency problems (e.g., Miller et al., 2007, 2011). A founder-owned firm is defined by the presence of one or more founder owners with no family members involved as owners, managers, or board members. Family-owned firms, in contrast, are defined by the presence of at least one family member other than the founder involved as an owner, manager, or board member. By definition, founder- and family-owned firms are mutually exclusive (Miller et al., 2007).3 Because founder owners tend to focus on firm growth and performance goals, principal–principal agency problems are relatively low (Miller et al., 2007, 2011).4 Family owners, in contrast, might have broad socioemotional goals, such as preserving the family’s reputation for good deeds and employing family members (Carney, 2005; Chrisman et al., 2012; Deephouse & Jaskiewicz, 2013; Gómez-Mejía et al., 2011), and these can create principal–principal conflicts for nonfamily shareholders (Morck, Wolfenzon, & Yeung, 2005; Villalonga & Amit, 2006). Although prior theory describes different agency problems among founder- and family-owned firms, it is unknown whether these differences affect CEO incentive pay. Because CEO incentives are an important way that owners align the interests of owners and managers, there is merit in understanding how CEO incentive compensation and its tie to firm performance vary across firms with different large owners.

Fortunately, researchers have begun to explore how large owners impact CEO incentive compensation. Two studies focused on family firms and investigate whether CEO compensation differs between family and manager-controlled firms (i.e., Combs, Penny, Crook, & Short, 2010; Gómez-Mejía et al., 2003). They discovered that, except for family firms where only one family member actively participates, family-member CEOs earn less incentive, fixed, and total compensation (Combs et al., 2010; Gómez-Mejía et al.).

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2. Agency-based theory that monitoring by large owners and CEO incentives are substitutes is well estab-
lished and consistent with several (cited) empirical studies. This does not, however, imply that substitution
is perfect and firms with large owners use zero CEO incentives. It means only that they do not rely wholly
on incentives. Indeed, any incentive scheme will require some monitoring and more complex incentive
schemes might even require relatively more monitoring in order to prevent abuse.

3. Our definition is the same as in Miller et al. (2007, 2011), but we do not use the term “lone founder”
because there can be multiple unrelated founders in founder firms. Also, we label founder-owned but
family-managed firms as family-owned firms because Miller et al. (2011) show that founder-owned firms
start acting like family-owned firms when a second family member becomes involved as owner, manager, or
board member.

4. Founder firms are not immune to principal–principal agency conflict because founders can pursue private
benefits of control (i.e., financial benefits from exerting organizational influence) to the detriment of minor-
ity shareholders (e.g., Demsetz & Lehn, 1985).
Two other studies showed that founder CEOs also receive less incentive and total compensation than their counterparts at manager-controlled firms (He, 2008; Wasserman, 2006). These four studies take valuable steps toward understanding how families and founders influence CEO compensation, but they also highlight two questions that are important to address in order to extend knowledge in this area.

First, whereas compensation for founder- and family-member CEOs differs from CEOs at other firms (e.g., Finkelstein & Hambrick, 1989; Gómez-Mejía et al., 2003; He, 2008; Wasserman, 2006), it is not known whether incentive compensation differs between hired CEOs in founder- and family-owned firms. This is important because goal differences between founder and family owners (Miller et al., 2007, 2011) may impact owners’ desire to incentivize hired CEOs. Chrisman et al. (2014), for example, theorize that despite the need to pay more to entice high-quality nonfamily managers, family firms might underpay hired CEOs in a misguided effort to protect socioemotional wealth (see also Chua et al., 2009). Although their theory suggests that hired managers in founder and family firms are compensated differently from one another, and from managers in other firms, empirical evidence is lacking.

Second, although a key goal of CEO incentive compensation in manager-controlled firms is to reduce agency conflicts by incentivizing CEOs to maximize firm performance (Werner & Tosi, 1995), the link between CEO incentive compensation and firm performance is weaker than agency theory anticipates (Jensen & Murphy, 1990; Tosi et al., 2000). In particular, CEOs at manager-controlled firms frequently increase their incentive compensation and limit the extent to which it is tied to firm performance (e.g., Gómez-Mejía et al., 1987; Werner & Tosi). What is not known is whether there are differences among large owners in their ability to tie CEO compensation to firm performance. Given different agency conflicts in founder- and family-owned firms, it appears important to know whether CEO incentive compensation is an effective tool for mitigating agency conflicts in firms with different large owners.

In answering these questions, it is important to separate founders’ and families’ influence as owners from other sources of influence (i.e., as CEOs or board members). Agency theory asserts that a central purpose of CEO incentives is to focus CEOs’ attention on shareholder wealth (Jensen & Murphy, 1990). When the CEO is a large owner as in the case of founder- and family-member CEOs, it is not surprising that such incentives are not needed (Gómez-Mejía et al., 2003; He, 2008; Wasserman, 2006) because there is little separation of ownership and control (i.e., the agent and key principal are the same person—Fama & Jensen, 1983). Knowing that founders and family member CEOs take less compensation, however, does not reveal whether founder and family owners are equipped to focus the interests of hired CEOs on firm performance. This is important because whereas recent theory suggests that founders and families impact firms differently in different roles—i.e., as top managers, board members, and owners (He; Miller et al., 2011; Villalonga & Amit, 2006)—the empirical practice of using indicator variables that combine these effects has resulted in an inability to empirically separate owners’ distinctive roles (e.g., Anderson & Reeb, 2003; Miller et al., 2007).

CEO Incentive Pay in Founder-Owned Firms

Relative to dispersed owners with small ownership stakes, agency theory anticipates that large owners have more incentive and ability to monitor managers’ decisions and influence their actions (Fama & Jensen, 1983; Jensen & Meckling, 1976). These owners often have representatives on the board, and managers will consult with them regarding
important decisions (Maury & Pajuste, 2005; Park & Shin, 2004). Thus, firms with large owners need not rely on incentives as the only way to ensure that managers take actions in shareholders’ best interests (Burkart, Gromb, & Panunzi, 1997; Eisenhardt, 1989). Indeed, there is strong evidence at the firm level that incentives decline as principals’ ability to perform direct monitoring improves (Aghion & Bolton, 1992; Gómez-Mejía et al., 1987; Maug, 1998; Rediker & Seth, 1995).5

Founder owners should be particularly well equipped to perform such monitoring. They are emotionally and financially attached to their firms (Arthurs & Busenitz, 2003; He, 2008). They identify profoundly with their firms and are emotionally committed to their success (Miller et al., 2011). Founders realize their financial and emotional ambitions by means of their firms’ long-term success (Langlois, 2007; Schumpeter, 1934). This is especially true of founders whose firms are already large and well established (Miller et al., 2007). According to Wasserman (2006), a founder will even sell ownership and relinquish control if it will provide means for further firm growth. Not surprisingly, founder-owned firms often pursue above average growth and performance goals. Because founder agendas align particularly well with other shareholders’ interests, agency problems are relatively low when founders also serve as CEOs or members of the board of directors (He; Langlois; Miller et al., 2007, 2011).

Even when founder owners are no longer CEOs or on the board of directors, they retain their deep and tacit knowledge about the firms they built. Because founder owners have been present since day one, they know major customers, suppliers, and key employees—especially top managers. Thus, founders have the expertise to effectively monitor hired CEOs, and their ownership power and emotional attachment give them incentive to do so (He, 2008; Jensen & Meckling, 1976). As a result, founder owners can evaluate CEO decisions and observe and monitor CEO actions to make sure that decisions and actions are geared toward maximizing firm performance. Such monitoring, according to agency theory, reduces the need to rely merely on incentives to align the interests of hired managers and shareholders (Fahlenbrach, 2009; Hall, 2003; Himmelberg & Hubbard, 2000; Murphy, 1999). Thus, the more ownership founders hold, the more power and financial incentive they have to effectively monitor hired CEOs and avoid the use of unnecessarily high CEO incentive pay. Accordingly, we expect that:

**Hypothesis 1:** Founder ownership has a negative effect on hired CEOs’ incentive compensation.

**CEO Incentive Pay in Family-Owned Firms**

Like founder owners, family owners have strong incentives to monitor their hired CEOs (Fama & Jensen, 1983; Gómez-Mejía et al., 1987, 2003). In addition to their financial wealth, the family’s history, status, and reputation are inextricably tied to the firm (Deephouse & Jaskiewicz, 2013; Gómez-Mejía et al., 2007; Miller et al., 2011). Unlike founder owners, however, family owners also pursue socioemotional wealth goals (Gómez-Mejía et al., 2011), and evidence suggests that socioemotional wealth goals

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5. Hoskisson, Castleton, and Withers (2009) observe that incentives and several sources of monitoring (e.g., board independence, ownership concentration) have increased jointly at the society level, and theorized that incentives and monitoring might have complementary ratcheting effects rather than the substitution effects observed at the firm level. We address this alternative theory in the Discussion section.
regularly detract from firm performance (Gómez-Mejía et al., 2007, 2011). Several recent studies suggest that the strength of family involvement in firm ownership, management, and on the board is positively related to the strength of socioemotional wealth goals in family firms (Chrisman et al., 2012; Deephouse & Jaskiewicz; Naldi et al., 2013).

Prior research on private family firms has also shown that family owners might sacrifice financial returns in exchange for socioemotional wealth—especially when a focus on financial returns might weaken the family’s control (e.g., Gómez-Mejía et al., 2007). Among publicly listed firms, however, a family’s control, and thus its power to protect socioemotional wealth, is contingent on high share prices and satisfied shareholders (Morck, Shleifer, & Vishny, 1989; Slovin & Sushka, 1993). This raises a conundrum for family owners in that they could either satisfy family members by hiring a family-member CEO, focusing on socioemotional goals, and underperforming as suggested by previous research (Bloom & van Reenen, 2007; Naldi et al., 2013; Pérez-González, 2006), or they can hire nonfamily CEOs, tie CEO incentive pay to firm performance, and achieve superior firm performance at the cost of some socioemotional wealth.6 The latter is in line with the idea that some families focus on firm performance by pursuing only those socioemotional wealth goals that can be aligned with firm performance (i.e., reputation—Deephouse & Jaskiewicz, 2013), but give up those socioemotional goals that are incompatible with firm performance (i.e., family management jobs as a birthright; Bloom & van Reenen). Chua et al. (2009) and Chrisman et al. (2014) propose that when family owners hire nonfamily CEOs, they might attempt to overcompensate for lost socioemotional wealth with a greater focus on financial returns. Although hiring a nonfamily CEO and giving them strong performance-based incentives might reduce the family’s ability to pursue socioemotional wealth goals that are inconsistent with performance maximization (e.g., environmental investments—Berrone et al., 2010), it can increase the family’s hold on the most essential socioemotional wealth goal, which is maintaining family control over the firm (Gómez-Mejía et al., 2007).

However, because it is well known that family owners often focus on socioemotional wealth goals that undermine firm performance, nonfamily shareholders in family-owned firms may be concerned that resources might be directed toward the family’s socioemotional wealth and away from financial performance—i.e., the principal–principal problem (Bertrand & Schoar, 2006; Villalonga & Amit, 2006). Accordingly, these shareholders need strong signals that their interests are central to management, and the need for such assurance rises with the level of family ownership and influence that fosters concerns that resources might be diverted toward socioemotional goals.

Family owners of publicly listed firms care about these shareholder concerns because families depend at least partly on nonfamily shareholders’ support to maintain significant control, which is itself a foundational socioemotional wealth goal (Gómez-Mejía et al., 2007). Thus, to avoid having their share prices discounted by wary shareholders, boards of directors need to send strong signals to shareholders that governance is sound and shareholders’ interests are protected (Certo, 2003; Miller & del Carmen Triana, 2009). Boards of family-owned firms need to send strong signals because the quality of top-management decision making and board monitoring is difficult and costly for shareholders to evaluate (Beatty & Zajac, 1994; Hendry, 2002). Strong signals are visible to

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6. Family firms are heterogeneous in their pursuit of socioemotional goals (Chrisman et al., 2012): Large, later generation and publicly listed family firms tend to focus less on socioemotional wealth than smaller, first generation, and privately held family firms (Jaskiewicz, Miller, Block, & Combs, 2014; Miller et al., 2011; Naldi et al., 2013; Schulze, Lubatkin, Dino, & Buchholtz, 2001).
Perhaps the most visible and easily interpreted signal that a family can send is to relinquish the family CEO position and hire a professional CEO (Naldi et al., 2013). This is a costly signal in that hired CEOs are unlikely to pursue socioemotional wealth goals that are detrimental to firm performance; hired CEOs must focus on shareholder interests in order to maintain their reputation and viability in the labor market (Cannella, Fraser, & Lee, 1995; Gómez-Mejía, Núñez-Nickel, & Gutiérrez, 2001). Indeed, top-notch candidates at family-owned firms might require a premium that compensates them for the personal risk that comes with working in a family firm (Chrisman et al., 2014); CEO job candidates might rightfully fear being asked to pursue socioemotional wealth goals that—although valued by family owners—reduce their own market value and reputation (Fiegener, 2005). As a result, nonfamily CEOs should demand larger pay packages. In particular, they might ask for more incentive pay so they can focus on firm performance rather than socioemotional wealth, and thus avoid underperforming on both counts (Chrisman et al.). Indeed, CEO incentive compensation above industry norms is likely to attract top-notch CEOs from competing firms, in part, because it signals to potential CEO candidates that they will be given the discretion that they need to maximize firm performance. An important part of that discretion might be the freedom to build their own high-caliber management team without being forced to include underperforming family members.

Once the family has signaled its willingness to sacrifice some socioemotional wealth by hiring a (nonfamily) CEO, signaling theory suggests that the family will also support their hired CEO’s demands for greater incentive pay because shareholders discount the value of firms when they receive inconsistent signals (Gao, Darroch, Mather, & MacGregor, 2008), and hiring a nonfamily CEO without supporting incentives might send mixed signals. Prior research shows that CEO compensation is an important signal for shareholders (Zajac & Westphal, 1995), so failing to support the hired CEO by not offering the incentives that shareholders expect might undermine much of the signaling value about family owners’ “true intentions” that is gained by hiring a professional CEO in the first place.

Overall, these arguments suggest that family owners will offer more CEO incentive pay than other firms. They offer more than founder-owned firms because whereas founders and families both have deep tacit knowledge about the firm to aid monitoring, shareholders rightfully fear that families but not founders will use this knowledge to direct hired managers toward socioemotional wealth goals that are not fully compatible with firm performance (Chrisman et al., 2012; Villalonga & Amit, 2006). To reassure shareholders and maintain control, families will hire nonfamily CEOs and offer high incentive pay. Family owners might even offer greater incentives than what is found at manager-controlled firms to attract talented CEOs who might otherwise avoid working for family owners (Chrisman et al., 2014). Thus, we predict that:

**Hypothesis 2:** Family ownership has a positive effect on hired CEOs’ incentive compensation.

**CEO Incentive Pay and Firm Performance**

Building on agency and signaling theories, we theorized that founder owners with hired CEOs offer fewer CEO incentives whereas family owners with hired CEOs offer
more. The higher use of CEO incentives in family-relative to founder-owned firms, however, raises questions about the incentives’ effectiveness relative to manager-controlled firms.

Among manager-controlled firms, powerful managers use their discretion to separate incentive compensation from actual firm performance (Gómez-Mejía et al., 1987; Tosi & Gómez-Mejía, 1989; Werner et al., 2005). They do this by encouraging boards to adopt low performance targets (Zajac & Westphal, 1995), reprice stock options (Callaghan, Saly, & Subramaniam, 2004; Pollock, Fischer, & Wade, 2002), or compare the CEO to weak peers (Gong, Li, & Shin, 2011). Because CEO incentives can be so easily separated from performance in manager-controlled firms, the link between incentive compensation and actual performance is weaker than at firms with large owners (e.g., Gómez-Mejía et al.; Werner et al.).

Among the large owners who might step in to tie CEO incentives to firm performance, in theory, founders confront the fewest agency problems (He, 2008; Miller et al., 2007). Their financial and emotional goals are strongly tied to the firm and its financial performance (Miller et al., 2007). As a result, founder owners do not need to offer CEOs high incentive compensation in order to signal good governance to shareholders (Miller et al., 2007, 2011), or to compensate them for large personal risks associated with being asked to pursue socioemotional wealth (Chrisman et al., 2014). Finally, founders have deep knowledge of their firm and relationships with stakeholders, including managers, which is why founder-controlled firms outperform among large public firms in the United States (Miller et al., 2007; Villalonga & Amit, 2006). Thus, even after founder owners are replaced with hired CEOs, they have strong incentives (as large owners) and the ability (because of deep knowledge and experience) to directly observe and monitor managers’ actions—thereby reducing the degree to which they must rely on CEO incentives to make sure CEOs are focused on shareholder actions (Baysinger & Hoskisson, 1990; Rediker & Seth, 1995). We therefore predicted that founder owners monitor their hired CEOs and rely less on CEO incentives (Hypothesis 1).

Accordingly, below average CEO incentives should be performance optimizing for firms with founder owners. Indeed, average or above average CEO incentives at such firms might indicate either that the founder is no longer actively engaged in monitoring, or that the board has lost confidence in the founder and has incentivized the hired CEO to act in shareholder interests regardless of founder input. Either way, the firm is not taking advantage of—or does not have access to—the monitoring abilities that founders typically bring, and is instead leaning more heavily on the incentives to focus the CEO’s efforts on shareholder interests. Because it is the founders’ expertise that enables strong monitoring, without it the firm is subject to the same challenges that manager-controlled firms confront (He, 2008). That is, CEOs are better equipped to use their informational advantages over the board to lobby for greater pay (Bebchuk & Fried, 2003; Bebchuk, Fried, & Walker, 2002; Dittmann & Maug, 2007) and reduce the extent to which pay is tied to firm performance (Gomez-Mejia et al., 1987; Tosi et al., 2000). Reduced focus on firm performance, in turn, should have negative consequences (Core, Holthausen, & Larcker, 1999). Thus, we anticipate that:

7. A complementary view is that some founder owners incur unnecessary cost by overpaying their CEOs. For instance, owners might overpay CEOs if they are worried about CEOs’ flight risk, or they might overpay CEOs by bending to pressure by institutional shareholders. Both instances are indicative of unnecessary costs and thus performance reducing waste.
Hypothesis 3: Higher CEO incentive compensation weakens the relationship between founder ownership and firm performance.

Family owners similarly have the ability and incentive to directly oversee and monitor hired CEOs. We predicted, however, that family owners will use more CEO incentives to attract and retain nonfamily talent and to signal good governance. Although family owners might offer relatively more CEO incentives, they only benefit financially when those CEO incentives are used properly. Indeed, there is no advantage to the family if CEO incentives play a largely symbolic role as they do in manager-controlled firms (Zajac & Westphal, 1995). This is so because family owners who are willing to give up the CEO position—and thereby weaken their ability to pursue socioemotional wealth (Naldi et al., 2013)—will want compensation for it (Chrisman et al., 2014). One way to do this is to offset lost socioemotional wealth with gains in financial performance (Chrisman et al.). Accordingly, once family owners give up socioemotional wealth by hiring professional CEOs, we theorize that family owners will not only offer greater CEO incentives but also make sure that hired CEOs are held accountable in that their incentives are tightly bound to firm performance.

Family owners, like founders, can further ensure accountability because they have considerable influence over the board. Family owners have deeply rooted social capital within their firms (Sirmon & Hitt, 2003) and extensive tacit knowledge about the firm (Carney, 2005), and, as large owners, they often sit on or have representatives on the board and their input is sought with respect to critical policy decisions such as CEO compensation (Anderson & Reeb, 2004; Voordeekers, Van Gils, & Van den Heuvel, 2007). Accordingly, it seems unlikely that family owners would allow boards to untie hired CEOs’ incentives from firm performance (e.g., by repricing options or adopting lower performance targets) as is common among manager-controlled firms (Gómez-Mejía et al., 1987; Werner & Tosi, 1995). Indeed, because they have already given up some socioemotional wealth, family owners should encourage increases in financial performance to help compensate for any lost socioemotional wealth from having a hired CEO who is focused on firm performance. In line with agency theory research (Chrisman et al., 2014), family owners’ effective use of higher CEO incentive pay is one step that they can take to offset lost socioemotional wealth from hiring a nonfamily CEO.

Overall, whereas high CEO incentives are unnecessary for founder owners, family owners need CEO incentives to (1) attract high-caliber CEOs and (2) signal shareholders about management’s performance focus. Because family owners have both the incentive (as owners who want compensation for lost socioemotional wealth) and ability (because of deep knowledge and experience) to make sure the CEO is unable to separate incentives from performance, they will make sure that the incentives they offer are used to enhance firm performance. Therefore:

Hypothesis 4: Family ownership strengthens the relationship between CEO incentive compensation and firm performance.

Data and Method

Sample and Data Sources

Our sample frame consists of Standard & Poor’s 500 firms. We manually collected data on owners, board members, and top managers from corporate proxy statements for the years 1994 through 2002. Proxy statements are the most accurate sources of corporate ownership (Anderson & Lee, 1997; Dlugosz, Fahlenbrach, Gompers, & Metrick, 2006).
We read and recorded information from the text and footnotes because this is where corporations reveal family ties among owners, managers, and board members. We also employed various other data sources such as *Hoover’s Handbook of American Business* and company websites to fill in missing data or resolve ambiguous cases. We then merged our data set with the ExecuComp and Compustat databases. Finally, because our theory is about hired CEOs, we removed firms from our sample if the founder or a family member still served as CEO. Our final sample represents an unbalanced panel data set with 1,874 observations from 335 firms.

**Dependent Variables**

We ran two different analyses. In the Bayesian regression used to test Hypotheses 1 and 2, the dependent variable is *CEO incentive compensation* (He, 2008; Mehran, 1995), calculated as the sum of long-term incentive plans, the Black-Scholes stock-option-value estimate, and the value of restricted stock grants. In the Bayesian regressions used to test Hypotheses 3 and 4, the dependent variable is Tobin’s Q, which is calculated as the market value of equity plus the book value of debt divided by the book value of total assets (Chung & Pruitt, 1994). It represents the value of a firm as determined by the equity market, and thus resists earnings manipulations by CEOs (Villalonga & Amit, 2006). Tobin’s Q is together with return on assets (ROA) the most often used dependent variable in corporate governance research in general (McConnell & Servaes, 1990; Morck et al., 1998) and compensation research in particular (Chung & Pruitt, 1996; Mehran). Tobin’s Q is preferred over accounting performance measures (e.g., ROA) when the focus is on understanding how corporate governance affects shareholder wealth (Mehran). We logged both dependent variables due to their skewed distributions.

**Independent Variables**

To test our hypotheses, two predictor variables were constructed. The variable *founder ownership* is the percentage of stock owned by the founder or founder team where no relatives of the founder(s) are involved as shareholders, board members, or top managers. The variable *Family ownership* is the percentage of stock owned by the founding family where at least one family member other than the founder is involved as owner, manager, or board member.

**Control Variables**

Because many of the same factors potentially influence both dependent variables (*CEO incentive compensation* and *Tobin’s Q*), we used a largely overlapping set of control variables that have been used in prior studies on executive compensation and firm performance. We describe these variables in three groups: (1) other founder and family influences, (2) governance (including CEO compensation) and CEO characteristics, and (3) firm characteristics.

First, we control for nonownership forms of founder and family influence. Failure to separate ownership effects from other forms of influence (e.g., owners being board members) has been a critical concern in prior research (Chrisman et al., 2012; Villalonga & Amit, 2006), and doing so is especially important in our study because our theory is largely grounded in agency, which is concerned with how owners (principals) monitor and incentivize their hired agents (e.g., Eisenhardt, 1989). As described above, we
controlled for any influence that founder or family member CEOs might have by removing them from the sample. We then control for Founder board presence and Family board presence using indicator variables for each. We expect that both founder and family member board presence reduces CEO incentives because such board members will monitor CEOs directly, thus decreasing the need for heavy incentives (Eisenhardt). With regard to performance, founder board presence should enhance firm performance, but family board presence will not because of the potential for enhanced pursuit of socioemotional goals by family board members. Controlling for family board membership is also important because it is a potential indicator of a family’s socioemotional wealth (Deephouse & Jasikiewicz, 2013). Finally, we control for Family owner later generation. Gersick, Davis, Hampton, and Lansberg (1997) explain that first-generation owner-managers are usually followed by later-generation sibling partnerships and cousin consortia. Because the strength of family ties declines in later generations, later-generation family owners become more interested in financial performance relative to socioemotional wealth. As a result, later-generation family owners might be more inclined to use higher CEO incentive compensation and tie it more closely to firm performance.

The second group of controls holds constant other sources of governance—including CEO compensation—and CEO characteristics. CEO pay packages differ in their ratio of base and incentive pay, and these differences carry different implications for CEO motivation (Bloom & Milkovich, 1998). Thus, we control for CEO base pay, measured as the CEO’s annual fixed salary plus cash bonus. We also control for CEO other pay. Hoskisson et al., (2009) show that other forms of pay, such as golden parachutes and signing bonuses, have been growing over the last decades as compensation for various forms of employment risks. As such, higher levels of other pay can come at the cost of incentive pay because risk-averse CEOs want less risky pay contracts. However, other pay should nonetheless be associated with better firm performance because it compensates the CEO for employment-specific risks that might otherwise lead CEOs to choose suboptimal strategies aimed at mitigating risks rather than maximizing firm performance. Both CEO base pay and CEO other pay are log transformed. We control for Ownership by CEO measured as the percentage of equity that is owned by the CEO. CEO ownership reduces the need for incentives and strengthens the incentive to pursue firm performance goals (e.g., Brick, Palmon, & Wald, 2006). We also control for Ownership by institutional shareholders measured as the percentage of shares owned by institutional investors. Institutional shareholders foster the use of CEO incentive compensation and focus on firm performance (David, Kochhar, & Levitas, 1998). We then control for CEO duality using an indicator variable depicting whether the CEO also serves as chairperson, and for CEO tenure measured as the number of years the CEO has held this position. Both CEO tenure and CEO duality indicate higher discretion, which has been related to higher CEO compensation (e.g., Barkema & Gómez-Mejía, 1998). We also control for CEO compensation committee using an indicator variable depicting whether the CEO serves on the compensation committee (e.g., Gómez-Mejía et al., 2003). The CEO’s knowledge of the firm’s executives should enable the compensation committee to set more effective incentives for other top managers, which should have a positive effect on performance (Cyert, Kang, & Kumar, 2002). Finally, we accounted for the Number of board meetings per year. A higher number of board meetings indicates an organizational crisis that frequently leads to higher CEO compensation (Vafeas, 1999).

8. CEOs usually do not participate in committee meetings that determine their own compensation (Cyert et al., 2002).
A third group of controls includes firm characteristics that have been identified as important in prior compensation and/or governance studies (e.g., Carpenter & Sanders 2002; Combs et al., 2010; Gómez-Mejía et al., 2003). More established firms, as indicated by larger Firm size (measured as the logarithm of total assets) and higher Firm age (measured as the logarithm of years since the firm was founded) provide executives with better pay to compensate them for the increased complexity that comes with managing larger and more established firms (Beatty & Zajac, 1994; Cyert et al., 2002). CEO pay and firm performance can be further enhanced by firm risk. Higher risks are expressed in higher Firm leverage, which we measure as total debt divided by total equity, and in R&D intensity, which is defined as R&D expenditures divided by total assets (Balkin et al., 2000; Brick et al., 2006). Also, higher CEO compensation is common in firms that face higher Market risk—a firm’s Beta—because CEOs want to be compensated for risks they incur (Gómez-Mejía et al.; He, 2008). Higher risks should also translate into higher firm performance in the long run. Next, we account for ROA and Tobin’s Q in the CEO incentive compensation regression because better performing firms pay their CEOs more (Barkema & Gómez-Mejía, 1998). We also include ROA in the performance regression because it could drive higher Tobin’s Q. Moreover, we include the variable Dividend yield in both analyses because annual dividend payouts per share reduce available cashflows that could otherwise be used to pursue executives’ self-interested goals (Faccio, Lang, & Young, 2001). As such, higher dividend yields promote market confidence that may increase Tobin’s Q. Finally, we accounted for industry effects by controlling for Industry mean CEO incentive compensation (based on two-digit SIC codes) in the Bayesian regression on CEO incentive compensation and for Industry mean Tobin’s Q t0 based on two-digit SIC codes in the Bayesian regression on Tobin’s Q t1.

The large number of control variables is a first step toward reducing the threat of omitted variable bias (aka endogeneity). We take three additional steps. First, to ensure the direction of causality, all independent and control variables are lagged by 1 year. Second, to further control for the threat of reverse causality in the tests for Hypotheses 3 and 4, we include past performance (Tobin’s Q in t0) as a control in the regression predicting firm performance in the subsequent period (Tobin’s Q in t1) (e.g., Brick et al., 2006). Third, as described in more detail below, we use a two-stage instrumental approach when testing Hypotheses 3 and 4 to reduce endogeneity concerns.

**Data Analysis**

We test our hypotheses using Bayesian panel fixed-effects regressions on the firm level. Such fixed-effects models have the advantage that they control for unobserved firm-specific factors, thus reducing endogeneity threats from firm-specific omitted variables. We use Bayesian analysis because it has strong small sample properties and is robust to including large numbers of correlated control variables (Hahn & Doh, 2006; Kruschke, Aguinis, & Joo, 2012). Bayesian regression is also robust to unbalanced panels such as ours where not all firms are represented in each year. Indeed, it is for these reasons that Bayesian analysis is becoming popular in many hard (e.g., Beaumont & Rannala, 2004) and social (e.g., Allenby, Bakken, & Rossi, 2004) sciences, including marketing and finance.

With respect to Bayesian’s small sample properties, although our overall sample is not small, only about 4% of sampled firms have founder ownership and hired CEOs and only about 9% have family ownership and hired CEOs, which results in a small number of data points for each subgroup. Unlike traditional regression analysis, Bayesian analysis has the power to detect effects within small subgroups and credibility intervals are not a
strict function of sample size (Kruschke et al., 2012). With respect to Bayesian’s robust-
ness to large sets of moderately correlated controls, this is important because while the
average management study has 6.6 control variables (not counting time and year indica-
tors) (Carlson & Wu, 2012) ours has 20. Including such a large set of control variables—
including common proxies for socioemotional wealth (i.e., having a family member on
the board) (Deephouse & Jaskiewicz, 2013)—reduces the danger of omitted variables
bias. Also, adding Tobin’s Q in \( t_0 \) as a control to the performance regression predicting
Tobin’s Q in \( t_1 \) does not pose a multicollinearity problem for a Bayesian regression.
Finally, family and founder ownership are correlated with board presence, so we needed
an estimation technique capable of separating these effects (without being influenced by
the order in which variables are entered). Not only is this critical to test our agency-based
theory about large owners but it is an important step forward in that prior research strug-
gled to disentangle the correlated effects that founders and families have in their different
roles as owners, CEOs, and board members (Chrisman et al., 2012; Villalonga & Amit,
2006).

The first step of Bayesian analysis is to formulate \textit{a priori} beliefs about relationships
between variables, called prior distributions. Bayesian analysis then uses a likelihood
function derived from our fixed-effects model and data to update the prior distributions.
The result is a posterior distribution that describes updated beliefs about relationships in
the model. The choice of a prior distribution is important. For the distribution of effects
for each independent variable on the dependent variable, we assumed a normal distribu-
tion (mean is 0 and standard deviation is 1). This assumption is conservative because it
does not assume any direction of effect; it ensures that any evidence regarding observed
effects is independent from the specification of the prior distribution. As a robustness
check, we varied the means of the prior distributions from \(-0.5\) to \(0.5\); this did not materi-
ally change our results.

The outcome of Bayesian analyses is a distribution of estimated coefficients (Hansen,
Perry, & Reese, 2004). The distribution of estimated coefficients, however, is a \textit{joint} post-
terior distribution, so we used a Gibbs sampling algorithm (Lancaster, 2004) to describe
the posterior distributions for each individual coefficient. The Gibbs sampling algorithm
takes 21,000 draws from the joint posterior distribution. After discarding the first 1,000
draws due to potential bias, the remaining 20,000 are used to describe the distribution of
the \textit{individual} regression coefficients.

The output of Bayesian analyses is a distribution function for each coefficient (Hahn
& Doh, 2006; Hansen et al., 2004), which is different from single point estimates or confi-
dence intervals found in traditional, null-hypothesis testing regressions (Schwab,
Abrahamson, Starbuck, & Fidler, 2011). Bayesian researchers do not rely on tests of sta-
tistical significance, but instead use the posterior distribution of estimated coefficients to
describe the probability that effects on the dependent variable are positive or negative.
Our tables for the Bayesian regression results report the mean and the probability that an
overall effect is positive. Probabilities near 100% indicate very probable positive effects;
those near 0% indicate very probable negative effects. Although Bayesian researchers
avoid cutoffs to determine significance, we follow the conservative custom of reporting
effects as “meaningful” when the probability of an effect approaches 90% (positive) or
10% (negative). However, the 90% cutoff in Bayesian cannot be compared to \(p\)-values in
traditional “frequentist” analysis. The former is based on the distribution of all possible
parameters around the mean and provides a probability for the direction of each variable’s
effect and its strength whereas the latter is a statement about the probability that a partic-
ular parameter or effect would re-occur in repeated samples (Cohen, 1994; Kruschke et al.,
2012).
While Bayesian regression can handle a much larger set of control variables, endogeneity threats remain the same. A particularly difficult problem confronting research in strategic management and entrepreneurship (where performance is the dependent variable) is that firms take (or select) certain actions (setting CEO incentives in our case) in the hopes of increasing performance, and if any of the reasons for selecting the action are omitted from the regression, selection bias occurs (Hamilton & Nickerson, 2003; Shaver, 1998). To reduce the threat of endogeneity from selection bias, we performed a two-stage procedure wherein, using Bayesian analysis, CEO incentive pay was regressed on the control variables and six instruments, all depicting different aspects of industry-level incentive pay. The predicted values were used in a second-stage Bayesian regression to test Hypotheses 3 and 4. Proper instruments must be reasonably strongly correlated with the endogeneous (selection) variable (CEO incentives) and not correlated with the error term of the structural equation. As for Hanlon, Rajgopal, and Shevlin (2003), the only acceptable instruments we could find involved industry-level incentive pay.

We did not perform a two-stage procedure when CEO incentives is the dependent variable because (1) CEO incentives are not (clear) outcomes from other selection choices (i.e., selection bias is theoretically not an issue), (2) reverse causality (another key source of endogeneity that is partially controlled using a lagged dependent variable in the performance regression) is logically unlikely (i.e., hired CEOs’ incentives should not materially change founders’ or families’ ownership), (3) we reduce the potential for omitted variable bias by including every control we could identify that was used in prior research, and (4) we could not find an instrument that satisfied the necessary validity criteria, and a weak or invalid instrument can create more bias than not having an instrument (Larcker & Rusticus, 2010; Roberts & Whited, 2012; Stock & Yogo, 2005). We do, however, perform a robustness test that estimates how much an omitted variable would need to be correlated with the endogeneous variable in order to affect the results (Larcker & Rusticus). Our results indicate that the threat of a bias due to a yet untheorized omitted predictor variable is very low.

9. The hypotheses can be regarded as a moderated-mediation model in which founder and family owners influence CEO incentive compensation AND moderate the effect of CEO incentive compensation on firm performance. Although we do not explicitly hypothesize and test such a model, our two-stage instrumental variable reduces the possibility that a moderated mediation relationship is behind our results.

10. The following six instruments were used: (1) mean industry incentive pay based on GICS codes (ExecuComp data item: INDDESC), (2) median industry incentive pay based on GICS codes (Global Industry Classification Standards) codes (ExecuComp data item: INDDESC), (3) mean industry incentive pay based on SIC codes (ExecuComp data item: SICDESC), (4) median industry incentive pay based on SIC code (ExecuComp data item: SICDESC), (5) mean industry incentive pay based on NAICS code (ExecuComp data item: NAICSDES), and (6) median industry incentive pay based on NAICS code (ExecuComp data item: NAICSDES).

11. We found a number of meaningful (i.e., they were correlated with the endogenous variable) but not valid instruments (i.e., they were correlated with the error term) instruments. An overview of tested instruments is available upon request from the second author.

12. We identified the most highly correlated variable with (1) founder ownership (i.e., founder board presence; correlation of 0.28) and (2) family ownership (i.e., family owner later generation; correlation of 0.72). After adding founder board presence and family owner later generation to the regression of the log of CEO incentive compensation, the regression coefficients of founder ownership and family ownership are not weakened but even strengthened, suggesting that omitted variables that are even moderately or highly correlated with the endogenous variable are unlikely to affect our results (see Larcker & Rusticus, 2010, for more information on this procedure).
Table 1 presents means, standard deviations, and correlations for all variables (including industry incentive pay on which the instruments are based).

Table 2 shows the results of the Bayesian regression on CEO incentive pay. It reports mean coefficients and, based on the posterior distribution, the probability that each effect is positive. Bayesian regression analyses do not have a way to directly assess multicollinearity, so we ran traditional fixed-effects regressions and assessed variance inflation factors. They showed moderate multicollinearity ranging up to 6.18 (4.04) for founder (family) ownership in the performance regression (Model 2).

Results for control variables were consistent with prior research. Founder and family board presence reduce hired CEOs’ incentives, as do later family generation owners. The latter can be explained because weaker kinship ties among later generation family members mean a greater focus on financial returns and less need to signal such focus (Gómez-Mejía et al., 2011). Also, CEO base pay is positively related to CEO incentive compensation (Bloom & Milkovich, 1998). Finally, long-tenured CEOs take less incentive pay (e.g., Cyert et al., 2002). With respect to firm characteristics, older and larger firms offer more CEO incentive pay. CEOs receive less incentive pay when market risks are high, presumably to shield their compensation from risks that are out of their control (Zajac & Westphal, 1994). Although ROA is negatively related to CEO incentive pay, Tobin’s Q is strongly positively related; shareholders’ perceptions of future growth prospects far outweigh short-term accounting performance in the design of incentive plans (Core et al., 1999; Jensen & Murphy, 1990). Finally, incentives are higher for CEOs in industries where other CEOs receive high incentives.

Hypothesis 1 predicts that founder ownership has a negative effect on CEO incentive pay. The hypothesis is supported with a 6.38% probability of a positive effect ($\beta = -3.72$). Hypothesis 2 predicts that family ownership has a positive effect on CEO incentive pay. Supporting Hypothesis 2, family ownership has a 99.96% probability of a positive effect on CEO incentive compensation ($\beta = 6.06$).

Table 3 presents the results of the two-stage Bayesian regressions on firm performance. Given that we control for the prior year’s Tobin’s Q, the coefficients depict the effect of the variable on the change in Tobin’s Q.

Coefficients for founder and family control variables are again consistent with theory. Both founder ownership and founder board presence enhance firm performance while family board presence lacks such a positive effect and family ownership reduces firm performance (Miller et al., 2007; Villalonga & Amit, 2006). With respect to governance and CEO controls, better paid CEOs—in terms of both base and other pay—deliver better firm performance. Moreover, institutional owners invest in firms with growing Tobin’s Q, and CEO ownership spurs better firm performance. Also, the positive relationship between CEO presence on the compensation committee and firm performance is consistent with prior research showing that CEOs help to incentivize other top managers (Cyert et al., 2002). Finally, in line with research showing that firms in crisis have many

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13. One small (and statistically not meaningful) exception is that the main effect of CEO incentive compensation on firm performance in Table 3 appears negative ($\beta = 0.01$, probability of a positive effect is 21.01). Given all of the controls, this effect probably reflects evidence that incentive compensation is subject to diminishing returns. At some point, people are fully incentivized and the effect of additional incentives is negative due to (1) waste (i.e., the added incentives are not needed, Frey & Osterloh, 2002), (2) “choking” (i.e., extreme incentives make people nervous and prone to errors, Hambrick, Finkelstein, & Mooney, 2005), and (3) excessive risk taking (i.e., managers “swing for the fences” in hopes of attaining an excessive reward; Carpenter, 2000).
### Table 1

Correlations, Means, and Standard Deviations

| Mean | SD  | 1    | 2    | 3    | 4    | 5    | 6    | 7    | 8    | 9    | 10   | 11   | 12   | 13   | 14   | 15   | 16   | 17   | 18   | 19   | 20   | 21   |
|------|-----|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| 1    | 7.29| 2.62 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 2    | 0.32| 0.78 | 0.04 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 3    | 0.01| 0.03 | 0.08 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 4    | 0.03| 0.10 | 0.15 | 0.04 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 5    | 0.13| 0.33 | 0.28 | 0.08 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 6    | 0.16| 0.37 | 0.00 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 7    | 0.09| 0.28 | 0.13 | 0.05 | 0.72 | 0.05 | 0.55 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 8    | 7.31| 0.75 | 0.22 | 0.13 | 0.05 | 0.01 | 0.12 | 0.05 | 0.02 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 9    | 2.17| 2.48 | 0.09 | 0.11 | 0.03 | 0.06 | 0.11 | 0.06 | 0.04 | 0.21 |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 10   | 0.01| 0.01 | 0.19 | 0.14 | 0.14 | 0.15 | 0.13 | 0.06 | 0.10 | 0.09 | 0.06 |      |      |      |      |      |      |      |      |      |      |      |      |
| 11   | 0.14| 0.12 | 0.01 | 0.03 | 0.01 | 0.19 | 0.00 | 0.12 | 0.19 | 0.05 | 0.02 | 0.07 |      |      |      |      |      |      |      |      |      |      |      |
| 12   | 0.76| 0.42 | 0.06 | 0.20 | 0.09 | 0.18 | 0.31 | 0.20 | 0.13 | 0.05 | 0.03 | 0.02 |      |      |      |      |      |      |      |      |      |      |
| 13   | 0.02| 0.05 | 0.06 | 0.01 | 0.13 | 0.06 | 0.04 | 0.04 | 0.03 | 0.01 | 0.03 | 0.07 |      |      |      |      |      |      |      |      |      |      |
| 14   | 0.13| 0.20 | 0.05 | 0.06 | 0.01 | 0.13 | 0.06 | 0.04 | 0.04 | 0.03 | 0.01 | 0.03 | 0.07 |      |      |      |      |      |      |      |      |      |
| 15   | 0.34| 0.08 | 0.06 | 0.03 | 0.09 | 0.00 | 0.09 | 0.06 | 0.09 | 0.13 | 0.09 | 0.05 | 0.14 | 0.02 |      |      |      |      |      |      |      |      |
| 16   | 0.05| 0.10 | 0.03 | 0.18 | 0.00 | 0.04 | 0.12 | 0.02 | 0.02 | 0.43 | 0.19 | 0.17 | 0.18 | 0.09 | 0.00 | 0.05 | 0.17 |      |      |      |      |
| 17   | 0.89| 0.10 | 0.50 | 0.00 | 0.04 | 0.12 | 0.02 | 0.02 | 0.43 | 0.19 | 0.17 | 0.18 | 0.09 | 0.00 | 0.05 | 0.17 |      |      |      |      |      |      |
| 18   | 0.62| 0.08 | 0.07 | 0.15 | 0.02 | 0.06 | 0.06 | 0.07 | 0.21 | 0.07 | 0.08 | 0.02 | 0.00 | 0.03 | 0.03 | 0.04 | 0.36 | 0.11 |      |      |      |      |
| 19   | 0.03| 0.05 | 0.04 | 0.39 | 0.02 | 0.02 | 0.16 | 0.09 | 0.02 | 0.18 | 0.11 | 0.01 | 0.02 | 0.07 | 0.10 | 0.03 | 0.37 | 0.37 | 0.13 |      |      |      |
| 20   | 0.30| 0.03 | 0.20 | 0.15 | 0.01 | 0.24 | 0.07 | 0.03 | 0.10 | 0.11 | 0.11 | 0.02 | 0.13 | 0.02 | 0.04 | 0.02 | 0.12 | 0.36 | 0.08 | 0.42 |      |      |      |
| 21   | 0.60| 0.76 | 0.05 | 0.44 | 0.03 | 0.10 | 0.03 | 0.04 | 0.10 | 0.04 | 0.06 | 0.10 | 0.06 | 0.07 | 0.01 | 0.08 | 0.10 | 0.25 | 0.01 | 0.16 | 0.01 | 0.10 |      |
| 22   | 0.33| 0.79 | 0.00 | 0.89 | 0.09 | 0.14 | 0.23 | 0.00 | 0.12 | 0.12 | 0.11 | 0.15 | 0.06 | 0.21 | 0.04 | 0.06 | 0.06 | 0.48 | 0.33 | 0.16 | 0.39 | 0.24 | 0.48 |
| 23   | 1.58| 1.60 | 0.00 | 0.34 | 0.08 | 0.07 | 0.25 | 0.00 | 0.01 | 0.04 | 0.10 | 0.15 | 0.06 | 0.14 | 0.05 | 0.01 | 0.18 | 0.23 | 0.41 | 0.07 | 0.29 | 0.40 | 0.07 |
| 24   | 6.51| 7.45 | 0.19 | 0.06 | 0.06 | 0.07 | 0.07 | 0.04 | 0.03 | 0.00 | 0.02 | 0.06 | 0.08 | 0.03 | 0.10 | 0.16 | 0.02 | 0.13 | 0.23 | 0.04 |      |      |      |
| 25   | 2.05| 1.30 | 0.05 | 0.56 | 0.06 | 0.06 | 0.12 | 0.03 | 0.03 | 0.08 | 0.12 | 0.06 | 0.02 | 0.06 | 0.02 | 0.01 | 0.02 | 0.38 | 0.26 | 0.09 | 0.43 | 0.19 | 0.23 |

Notes: comp., compensation; incent., incentive; correlations > 0.034 | | are significant at p < 0.05.

| 22   | −0.37 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 23   | 0.14  | 0.20 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 24   | 0.51  | 0.27 | 0.14 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
board meetings, the number of board meetings relates negatively to firm performance (Vafeas, 1999). With respect to firm characteristics, large firms’ Tobin’s Q grows at a slower rate while older firms have higher values. Given that markets discount uncertainty, it is not surprising that firms confronting high market risks have smaller Tobin’s Q values. Finally, industry competitors’ performance co-varies positively.

Hypothesis 3 predicts that CEO incentive compensation weakens the relationship between founder ownership and firm performance. The interaction between CEO incentive compensation and founder ownership is strong and negative ($\beta = -0.15$, probability of a positive effect is 7.49%), supporting Hypothesis 3. The effect of the interaction between CEO incentive compensation and family ownership on performance, in contrast, is strong and positive ($\beta = 0.20$, probability of a positive effect is 99.89%). As a result, we find support for Hypothesis 4, which states that family ownership strengthens the relationship between CEO incentive compensation and firm performance.

**Robustness and Additional Tests**

We conducted numerous additional tests to ensure the robustness of our findings. First, we ran traditional fixed-effects regression analyses. Although Bayesian analysis has more power to detect effects among correlated variables in small subsamples, the

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### Table 2

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Mean effect</th>
<th>Prob. of effect $&gt; 0$ (%)</th>
</tr>
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<td>Founder ownership</td>
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<td>6.38</td>
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<tr>
<td>Family ownership</td>
<td>6.06</td>
<td>99.96</td>
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<th>Founder and family control variables</th>
<th>Mean effect</th>
<th>Prob. of effect $&gt; 0$ (%)</th>
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<td>Founder board presence</td>
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<td>Family board presence</td>
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<td>12.01</td>
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<tr>
<td>Family owner later generation</td>
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<td>0.00</td>
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<table>
<thead>
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<th>Governance control variables</th>
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<td>CEO other pay (log)</td>
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<tr>
<td>Ownership by CEO</td>
<td>-21.46</td>
<td>0.00</td>
</tr>
<tr>
<td>Ownership by inst. investors</td>
<td>-0.50</td>
<td>15.93</td>
</tr>
<tr>
<td>CEO duality</td>
<td>-0.03</td>
<td>40.61</td>
</tr>
<tr>
<td>CEO tenure</td>
<td>-0.07</td>
<td>0.00</td>
</tr>
<tr>
<td>CEO compensation committee</td>
<td>0.56</td>
<td>98.05</td>
</tr>
<tr>
<td>Number of board meetings</td>
<td>0.05</td>
<td>61.12</td>
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<table>
<thead>
<tr>
<th>Firm control variables</th>
<th>Mean effect</th>
<th>Prob. of effect $&gt; 0$ (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firm size</td>
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<tr>
<td>Firm age</td>
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<tr>
<td>Firm leverage</td>
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<tr>
<td>R&amp;D intensity</td>
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<td>28.05</td>
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<tr>
<td>Market risk</td>
<td>-0.55</td>
<td>0.00</td>
</tr>
<tr>
<td>ROA</td>
<td>-0.02</td>
<td>0.27</td>
</tr>
<tr>
<td>Tobin’s Q (log)</td>
<td>0.71</td>
<td>100</td>
</tr>
<tr>
<td>Dividend yield</td>
<td>0.06</td>
<td>84.00</td>
</tr>
<tr>
<td>Industry mean CEO incentive compensation</td>
<td>0.05</td>
<td>100</td>
</tr>
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</table>

N obs. (firms) 1,874 (335)
Obs. per firm: min., mean, max. 1, 5.6, 9
coefficient sizes should be comparable. Accordingly, we found very similar coefficient sizes for all main variables in Bayesian and traditional regression analyses on CEO incentive compensation and firm performance. Indeed, with one exception, all were identical or different by a magnitude of less than 0.1. Second, we accounted for potential nonlinear ownership effects by including squared terms for family and founder ownership. These additional tests did not condition our original findings. Third, we employed dummy variables for board presence, later generation, compensation committee, and number of board meetings.

The exception refers to the coefficient of founder ownership in the regression of CEO incentive compensation. While the coefficient is 6.6 in the Bayesian regression analysis, it is slightly lower in the traditional regression analysis (6.1).

### Table 3

Bayesian Fixed-Effects Instrumental Variables Regressions on Log of Tobin’s Q $t_1$

<table>
<thead>
<tr>
<th></th>
<th>Model 1</th>
<th></th>
<th>Model 2</th>
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<tr>
<td></td>
<td>Mean effect</td>
<td>Prob. of effect &gt; 0 (%)</td>
<td>Mean effect</td>
<td>Prob. of effect &gt; 0 (%)</td>
</tr>
<tr>
<td>Independent variables</td>
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<tr>
<td>Founder ownership</td>
<td>0.40</td>
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<td>95.37</td>
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<tr>
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<td>−0.20</td>
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<td>−0.74</td>
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<td>CEO incent. comp.</td>
<td>−0.01</td>
<td>21.01</td>
<td>−0.01</td>
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<td>CEO incent. comp. × founder ownership</td>
<td>−0.15</td>
<td>7.49</td>
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<td>CEO incent. comp. × family ownership</td>
<td>0.20</td>
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<tr>
<td>Founder and family control variables</td>
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<td></td>
<td></td>
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<tr>
<td>Founder board presence</td>
<td>0.23</td>
<td>100</td>
<td>0.24</td>
<td>100</td>
</tr>
<tr>
<td>Family board presence</td>
<td>−0.03</td>
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<td>−0.03</td>
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<tr>
<td>Family owner later generation</td>
<td>0.08</td>
<td>90.26</td>
<td>−0.02</td>
<td>39.53</td>
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<tr>
<td>Governance and CEO control variables</td>
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<td></td>
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<tr>
<td>CEO base pay (log)</td>
<td>0.06</td>
<td>100</td>
<td>0.05</td>
<td>100</td>
</tr>
<tr>
<td>CEO other pay (log)</td>
<td>0.01</td>
<td>95.42</td>
<td>0.01</td>
<td>93.84</td>
</tr>
<tr>
<td>Ownership by CEO</td>
<td>1.49</td>
<td>98.91</td>
<td>1.87</td>
<td>99.73</td>
</tr>
<tr>
<td>Ownership by inst. investors</td>
<td>0.09</td>
<td>90.82</td>
<td>0.07</td>
<td>87.21</td>
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<tr>
<td>CEO duality</td>
<td>−0.00</td>
<td>44.57</td>
<td>−0.00</td>
<td>43.09</td>
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<tr>
<td>CEO tenure</td>
<td>0.00</td>
<td>57.52</td>
<td>0.00</td>
<td>59.64</td>
</tr>
<tr>
<td>CEO compensation committee</td>
<td>0.06</td>
<td>96.12</td>
<td>0.08</td>
<td>98.91</td>
</tr>
<tr>
<td>Number of board meetings</td>
<td>−0.02</td>
<td>14.20</td>
<td>−0.03</td>
<td>7.96</td>
</tr>
<tr>
<td>Firm control variables</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Firm size</td>
<td>−0.20</td>
<td>0.00</td>
<td>−0.20</td>
<td>0.00</td>
</tr>
<tr>
<td>Firm age</td>
<td>0.21</td>
<td>100</td>
<td>0.22</td>
<td>100</td>
</tr>
<tr>
<td>Firm leverage</td>
<td>0.00</td>
<td>55.69</td>
<td>0.00</td>
<td>58.99</td>
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<tr>
<td>R&amp;D intensity</td>
<td>0.08</td>
<td>60.39</td>
<td>0.07</td>
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<tr>
<td>Market risk</td>
<td>−0.05</td>
<td>0.60</td>
<td>−0.05</td>
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<td>ROA</td>
<td>0.00</td>
<td>92.14</td>
<td>0.00</td>
<td>93.99</td>
</tr>
<tr>
<td>Tobin’s Q (in $t_0$) (log)</td>
<td>0.25</td>
<td>100</td>
<td>0.24</td>
<td>100</td>
</tr>
<tr>
<td>Dividend yield</td>
<td>−0.01</td>
<td>12.68</td>
<td>−0.01</td>
<td>12.45</td>
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<tr>
<td>Industry mean Tobin’s Q (in $t_0$)</td>
<td>0.15</td>
<td>100</td>
<td>0.15</td>
<td>100</td>
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</tbody>
</table>

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variables for founder and family firms because a large number of prior studies had used this approach (e.g., Miller et al., 2007). In line with theory stating that different sources of family and founder influence have different effects (e.g., Chrisman et al., 2012; Villalonga & Amit, 2006), we found that the use of dummy variables provides weaker results. Fourth, we split our measure of CEO incentive compensation into two new variables: CEO stock options and CEO restricted stock, and used them as alternative dependent variables. Results show that the differences we found are due to stock options and not restricted stock grants. Fifth, our dataset spans the Internet bubble (i.e., 1996–2000) (Bhattacharya, Galpin, Ray, & Yu, 2009), our relationships of interest could have changed. However, when we compare the correlations between CEO incentive compensation and firm performance before (1994–1995; mean: −0.07), during (1996–2000; mean: −0.04) and after the Internet bubble (2001–2002; mean: −0.04), we see that differences were rather low, suggesting that the CEO compensation–firm performance link did not change substantially. Similarly, we checked whether the average relationship between founder and family owners on the one hand and CEO incentive compensation on the other hand could have changed during or after the Internet bubble. However, the average correlations appear to be very similar for the time periods before (1994–1995), during (1996–2000), and after the Internet bubble (2001–2002) (−0.17 vs. −0.14 vs. −0.15). Moreover, we checked whether the share of family and founder firms might have substantially changed during or after the Internet bubble—for instance, as a result of founder or family firm sell-offs. However, a comparison of samples of large U.S. firms before and after the Internet bubble (e.g., Anderson & Reeb, 2003; Anderson, Duru, & Reeb, 2009; Anderson, Reeb, Upadhyay, & Zhao, 2011; Miller et al.; Villalonga & Amit, 2006) suggests that the overall proportion of these firms remained relatively constant; we also only observed a very small reduction in the share of these firms from roughly 19 to 18% in the S&P 500 from 1996 to 2002.

**Discussion**

The most successful founder- and family-owned firms often go public and grow in size and significance. Although these firms are no longer small, research shows that founder and family owners continue to influence their firms’ strategies, corporate governance, and performance (He, 2008; Miller et al., 2007, 2011). Understanding how founder and families owners influence their firms is important because prior research shows that these owners have very different goals that carry different consequences for shareholders, employees, and other stakeholders (Gómez-Mejía et al., 2011; Miller et al., 2011).

Founder- and family-owners often influence their firms by serving as CEOs, but these CEOs must eventually step down and most are replaced with hired professionals. At this point, achieving their goals requires that these owners use their status to influence board and management decisions. One decision that large owners are known to influence is CEO incentive compensation, perhaps because of its ripple effect on other decisions affecting firm performance (e.g., Werner & Tosi, 1995). Although professionally managed founder- and family-owned firms are common, theory has not yet been developed explaining how these large owners and their different goal foci affect (1) hired CEOs’ compensation and (2) its link to firm performance. Our purpose was to develop and test theory to help explain these relationships.

First, prior research demonstrated that CEO incentive compensation differs between manager-controlled firms and those with large owners (e.g., Finkelstein & Hambrick, 1989; Gómez-Mejía et al., 2003; He, 2008; Wasserman, 2006), but it was unknown
whether known goal differences among large owners translated into differences in the way they compensated their hired CEOs. Although prior theory suggests that founder and family owners both have reasons to minimize CEO incentive compensation—founders because of their focus on firm performance and their monitoring abilities and families because CEO incentives might make it harder to achieve some socioemotional wealth goals (e.g., a reputation for being environmentally friendly; Berrone et al., 2010)—our theory and findings contradict the assumption that all large owners are the same. Specifically, we drew upon agency theory to predict that founder owners’ active monitoring puts downward pressure on hired CEO incentives, and we drew upon signaling theory and theory about professional CEOs in family firms (Chrisman et al., 2014; Chua et al., 2009) to predict that both family owners and their hired CEOs push for above-average incentive compensation. Results are consistent with our theory in that founder owners put downward pressure on CEO incentives. A one standard deviation (3%) increase in founder ownership relates to an average 11.16% drop of $681,876 in CEOs’ mean $6.11 million in annual incentive compensation. As family ownership grows by one standard deviation (10%), hired CEOs’ incentive pay grows to $9.81 million, which is about 60.6% above CEOs’ mean incentive pay. Accordingly, it is misleading to treat founder and family owners the same.

Second, our theory helps explain why founder and family owners differ according to how CEO incentives affect firm performance. Knowing this is important because explaining CEO compensation is more valuable when its connection with firm performance is understood (Tosi et al., 2000; Werner & Tosi, 1995). We theorized that founder owners will rely less on CEO incentives, and that failure to do so implies that the founder is unavailable to furnish expert monitoring and that firm performance will decline. Results are supportive in that high CEO incentives weakened the positive effect that founder owners otherwise have on firm performance. Regarding family owners, we found that while they use more CEO incentives, they effectively tie them to firm performance. Our findings thus test and extend theory developed by Chua et al. (2009) and Chrisman et al. (2014) that family owners use incentive compensation effectively to compensate for lost socioemotional wealth from hiring nonfamily CEOs. Prior studies called for research into whether and how the principal–principal agency problem can be mitigated in family-owned firms (e.g., Villalonga & Amit, 2006). Our theory and results suggest that some family-owned firms use CEO incentive pay to improve shareholder value (Aghion & Bolton, 1992). Increasing shareholder returns bolsters the family’s influence with management and the board and thus strengthens their control over the firm, which is a foundational socioemotional wealth goal (Gómez-Mejía et al., 2007).

Implications for Research on Founder-Owned Firms

Focusing on ownership allowed us to construct an agency-based explanation for how ownership allows founders to mitigate agency problems using direct observation in lieu of CEO incentives. Although the prediction that monitoring can substitute for incentives is fundamental to agency theory (e.g., Eisenhardt, 1989) and well-grounded empirically (e.g., Lippert & Moore, 1995; Rediker & Seth, 1995; Zajac & Westphal, 1994), Hoskisson et al. (2009) observed that several forms of monitoring (including ownership concentration) are rising in intensity concomitantly with increases in CEO compensation, suggesting a complementary ratcheting effect wherein increases in monitoring create pressure for increased compensation (often in the form of incentives). Although it is an empirical question for future research, our results suggest one possible resolution in that the type of
monitoring differentiates between when monitoring and incentives are complements versus substitutes. For example, independent board members (Baysinger & Hoskisson, 1990) and many institutional owners (Ryan & Schneider, 2002) confront significant information asymmetries that make them more dependent on incentives. Founders (and families), in contrast, have deep tacit knowledge that reduces such asymmetries and makes them less dependent. More generally, future inquiry into firm-level factors that differentiate between when monitoring and incentives are complements versus substitutes appears warranted.

Our results are consistent with, and help explain, prior work showing that founder-owned firms are among the best performing public firms (Miller et al., 2007). Prior research shows that founder CEOs enhance performance (Wasserman, 2003). Our Bayesian regression isolates founders’ influence as board members and owners and finds that founders positively impact firms in both of these roles (see main effects in Table 3). The firm thus benefits from founder ownership and from having active founders who use their ownership power to monitor managers. However, when founders fail to monitor a hired CEO effectively and boards use CEO incentives instead, firm performance suffers. When juxtaposed with prior research showing that founders can become obsolete over time (Boeker & Karichalil, 2002; Wasserman, 2003; Willard, Krueger, & Feeser, 1992), one implication is that it is important to develop theory to explain when founders’ influence reaches the point of diminishing returns.

Implications for Research on Family-Owned Firms

Recent research shows that family firms tend to conform to common industry standards; doing so confers legitimacy that family owners need to overcome shareholders’ concerns that families will pursue socioemotional over financial goals (Gómez-Mejía et al., 2011; Miller, Le Breton-Miller, & Lester, 2013). By mirroring manager-controlled firms in their use of CEO incentives, it seems that family owners use heavy CEO incentive pay as a signal to garner legitimacy (Miller et al.). We theorized that such incentives are important not only because they signal to shareholders that their interests are protected, but also because they signal to potential CEO candidates that they won’t be subjected to pressure to capitulate to family demands for more focus on socioemotional wealth issues. If this theory is correct, the implication is that high incentives are needed to attract top-notch CEO candidates. As such, future inquiry might benefit by investigating whether the high incentives we see here actually do increase the reputation and caliber of CEOs family firms are able to attract.

Prior research on private firms shows that family owners sacrifice financial returns in exchange for socioemotional wealth, especially when focusing on financial returns might weaken the family’s control (e.g., Gómez-Mejía et al., 2007). Among publicly listed firms, however, a family’s control, and thus its power to protect socioemotional wealth, is contingent on high share prices and hence satisfied shareholders. This raises a conundrum for family owners in that they could either satisfy family members if they use a family-member CEO, focus on socioemotional goals, and underperform as suggested by previous research (Bloom & van Reenen, 2007; Naldi et al., 2013; Pérez-González, 2006), or they can hire nonfamily CEOs, tie CEO incentive pay to firm performance, and achieve superior firm performance at the cost of some socioemotional wealth. The former is consistent with evidence that, on average, large public family firms do not outperform (Miller et al., 2007). The latter is in line with Chua et al.’s (2009) and Chrisman et al.’s (2014) proposition that family owners who hire nonfamily CEOs might overcompensate losses in socioemotional wealth by focusing on financial returns. It is also consistent with the idea that
The most important socioemotional wealth goal is maintaining family control (Gómez-Mejia et al.). These alternatives are reflective of our finding that, while some family owners hire CEOs and offer strong incentives that are tied to performance, the mere presence of family ownership reduces firm performance (i.e., see main effects in Table 3). One implication is that there are benefits to further describing the characteristics of family firms that are focused on firm performance and maintaining control versus pursuing other socioemotional wealth goals. More generally, future research should not only look at direct effects of family owners on firm performance but also analyze family owners’ contingent effect upon the relationship between governance mechanisms (e.g., CEO compensation) and firm performance.

Our results also have implications for theory about how families affect firm performance, much of which uses dummy variables depicting “family” to draw the conclusion that family firms underperform. Despite numerous appeals to account for heterogeneity among family-owned firms (e.g., Chrisman et al., 2012; Deephous & Jaskiewicz, 2013; Villalonga & Amit, 2006), disentangling family influences and testing their different effects on organizational outcomes remain scarce. Our analysis enabled us to isolate the impact of ownership from other ways family members impact firms (i.e., as managers or board members), and to investigate how ownership operates in family firms with hired CEOs. Results reinforce the need to account for heterogeneity among family firms. Whereas family ownership has a negative effect on performance when isolated using Bayesian regression (see main effect in Table 3), these effects dissipate and turn positive when coupled with high CEO incentives. Because Bayesian regression allows researchers to isolate different ways that families (and founders) impact firms, perhaps it would be worth revisiting prior research that did not make this distinction to investigate whether ownership effects on key outcomes differ from other sources of family influence (i.e., as managers or board members).

**Practical Implications**

Our study’s practical implications pertain mostly to shareholders. Prior research could be interpreted to imply that founder control means that a firm is a potentially strong investment (e.g., Miller et al., 2007). Our results concur except that founders no longer appear beneficial in firms with hired CEOs who receive the same kind of incentives found at manager-controlled firms. Such incentives indicate that the board is relying on incentives to focus the CEO’s attention and is not benefiting from a founder’s expert monitoring. CEOs without such founder monitoring can separate pay from firm performance (Gómez-Mejía et al., 1987). In contrast, caution regarding investments in family firms is less once families hire external CEOs and tie their compensation to firm performance. At that point, family ownership appears to be an asset.

**Conclusion**

We began this article with the observation that some of the most successful founder and family firms have grown large and represent about a third of the publicly listed firms in the United States. While prior research shows that large owners offer fewer CEO incentives and tie those incentives more closely to firm performance than do manager-controlled firms (e.g., Gómez-Mejía et al., 1987; Werner & Tosi, 1995), treating all large owners alike ignores important goal differences between large founder and family
owners—goal differences that imply that these firms’ shareholders confront different principal–principal agency problems. Our theory explains how these owners’ different goal foci translate into differences in the way they compensate hired CEOs and tie CEO incentive pay to firm performance. Consistent with predictions from agency and signaling theories, founder owners rely less on CEO incentives and their firms perform better when doing so. Family owners, in contrast, employ more CEO incentive compensation and tie it closely to firm performance. Our theory and results provide further evidence that not all large owners are alike and, we hope, inspire others to further examine ways that these owners influence their firms.

REFERENCES


Peter Jaskiewicz is an associate professor and the CIBC Distinguished Professor in Entrepreneurship and Family Business at the John Molson School of Business, Concordia University, Montreal, QC, Canada.

Joern H. Block is a Full Professor at the Universität Trier and Erasmus University Rotterdam, Universitäetsring 15, 54296 Trier, Germany.

James G. (Jim) Combs is the Dr. Phillips Chair of American Private Enterprise in the College of Business at the University of Central Florida, Orlando, FL 32816, USA.

Danny Miller is the director, Family Business Research Center, HEC Montreal and chair in family enterprise and strategy, University of Alberta.

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