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The relationship between corporate governance and corporate social performance of family firms in Korea

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The relationship between corporate governance and corporate social performance of family firms in Korea

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Abstract

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Agency theory from economics and stewardship theory based on psychology have emerged over the last decade to explain performance and conduct of family firms, and the two theories have found contradicting results and relationship between family firm and firm performance is still disputed. Therefore, unlike existing family firm researches that focused on financial performance of firms, this paper tests relationship and characteristics of corporate social performance and family firms. Family firm status, outside director ratio and institutional ownership are used as independent variables to test influences on corporate social performance, dependent variable of this paper. The samples are collected from KEJI Index from 2007 to 2009. The results indicate that family firms engage more in socially responsible activities and institutional ownership exerts positive influence on firm's corporate social performance. However, outside director ratio did not have significant influence on corporate social performance and institutional ownership also did not have moderating effects on family firm and corporate social performance relation.

Keyword: Family firm, corporate social responsibility, agency theory, stewardship theory, governance, KEJI index

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1. Introduction

Family-owned or family controlled firms consist the largest proportion of businesses worldwide (Porta & Lopez-De-Silanes, 1998; Shanker & Astrachan, 1996) and family firms are mostly small and midsized firms (Churchill & Hatten, 1987). Therefore, researchers in the past decades have put their effort to investigate the impact of family on firm's performance (Dyer, 2006). Previous researched have found that family is an important factor for business activities (Aldrich & Cliff, 2003), firm survival (Stafford, Bhargava, Danes, Haynes, & Brewton, 2010) and firm competitiveness (Cassia, De Massis, & Pizzurno, 2012) as well as local and regional development (Berghoff, 2006).

At the business level, how family affect firm performance has been getting much research attention. Previous studies have compared performance of family firm and non-family firms (Anderson & Reeb, 2003), sales growth of family firms (Chrisman, Chua, & Litz, 2004), job satisfaction (Beehr, Drexler, & Faulkner, 1997), and innovation (Tanewski, Prajogo, & Sohal, 2003).

However, relatively little is known of the impact of family on the corporate social performance. Morck and Yeung (2004) have found that family firms mostly care for their self-interest and therefore family firms are less inclined to do good to society where their firm belongs to. Other researchers, such as Godfrey (2005) have argued that family firms and non-family firms have incentives to be socially responsible in order to maintain a good image and reputation, therefore, having a positive relationship with family firm and CSP.

Baron (2001) explained motivations for firms to engage in CSR as increased long-term profit, altruism, and pressure from outside and found that firm’s strategic decision making, including motivations mentioned earlier play an important role in firm’s corporate social performance. Hart and Moore (2000) and Finkelstein (1992) found that corporate governance is one of the most important factor influencing firm’s strategic decision-making and previous researches about firm’s strategic decision-making on governance focused on R&D investment (Baysinger, Kosnik, & Turk, 1991), innovation (Kochhar & David, 1996), entrepreneurship (Zahra, 1996) and diversification (Eisenmann, 2002). As Aguilera, Rupp, & Williams (2007) found out, long-term strategic decision-making can be influenced by both economic or non-economic corporate governance, and recent researches started to investigate influence and relationship of corporate governance and CSP (Oh, Chang, & Martynov, 2011).

Previous researches on governance of family firms were focused on CEO characteristics, despite considerable impact family firms have on economy and society. Most of researches on family firms were about influence of family firm on economy (Claessens, Djankov, & Lang, 2000; Porta & Lopez-De-Silanes, 1998) and family owners, but there are mixed results on governance and family firms researches (Faccio & Lang, 2002). A number of researches focused on financial performance of family firms, however, investigating CSP from corporate governance perspective can give a better explanation of family firms (Wood, 1991). Therefore, this paper attempt to investigate influence of governance structure on family firm's CSP by taking outside director ratio and institutional ownership as dependent variables to study characteristics of family firms in Korea. This paper will investigate whether family firms engage more in CSP than non-family firms as well as influence of outside director and institutional ownership, in addition to testing moderating effects of institutional ownership on family firm's CSP.

The first chapter of this paper will review research background and question to explain how existing researchers have found contradicting arguments about characteristics of family firms from different perspectives and justifies a reason for using CSP as dependent variable of this paper. Second chapter reviews existing researches to build up hypothesis. In this chapter, concept of family firm and CSP, founding theories as well as relationship between CSP and family firm is reviewed. Third chapter build up from theoretical researches and introduces hypothesis on CSP of family firm, outside director ratio, and institutional ownership relation. Fourth chapter explains data and sample collection and fifth chapter discusses statistical results of the research. Lastly, sixth chapter provides discussion and contributions of this paper and suggests further research direction based on limitations of this research.

2. Literature review

2.1 Family firms

2.1.1 Definition of family firm

Family firms are an important subject of research (Aronoff & Ward, 1995) for the following reasons. Majority of independent businesses are family owned; family firms are likely to be managed differently from non-family firms; family firms would have different prioritization of objectives from non-family firms; and family firms contribute to creation of wealth, job and competitiveness (Westhead & Cowling, 1998). There has been numerous researches done on family firms, yet there's no single definition of family firms and the definition differs by countries and researchers (Zattoni, Gnan, & Huse, 2012). Most family firms are small and midsized firms (Churchill & Hatten, 1987) and among the small and midsized companies worldwide, family firms take up about 60-70% (Donckels & Frohlich, 1991). It is hard to settle on one definition of family firm that can be widely accepted, but academic researchers suggested many different ways to define the term (Astrachan, Klein, & Smyrnios, 2002; Astrachan & Shanker, 2003; Chrisman, Chua, & Steier, 2003; Handler, 1989).

Definition of family firm from previous researches includes family involvement of business perceived to be a family business, majority voting share ownership by family members, management of the business by at least one member from the family owning the business, or an inter-generational ownership transition (Handler, 1989; Westhead & Cowling, 1998). Westhead (1998) defines family firm with four criteria which are family ownership, family perception, family management and intergenerational ownership transition. Most commonly used definition of family firm in recent studies is by Ibrahim and Ellis (1994). Family firm is a firm or organization that has at least 51% of family ownership, more than one family member is involved with business management, and expected to have inter-generation ownership transition (Ibrahim & Ellis, 1994). This paper adopts definition from McGuire et al (2012) which defined family firms as those firms in which at least two family members own 5% or more of outstanding equity and family members being involved in management in the same year.

2.1.2 Agency theory and stewardship theory

Two distinct theories regarding the conduct and performance of family businesses have emerged over the last decade. According to agency theory, family owners and managers are driven by self-interest and tend to use their power and superior information to benefit the family (Bertrand & Schoar, 2006; Claessens, Djankov, Fan, & Lang, 2002; Gómez-Mejía, Takács Haynes, Núñez-Nickel, & Jacobson, 2007; Morck, Stangeland, & Yeung, 2000; Morck & Yeung, 2003; Wiseman & Gomez-Mejia, 1998). Although family businesses, like any other firms with concentrated ownership, may encounter less owner-agent agency costs, while family businesses are more likely to suffer from owner-owner agency costs where family owners exploit their asymmetric knowledge at the expense of other shareholders (Wasserman, 2006). Family owners tends to be risk averse because family fortune and wealth is tied to a single enterprise and have a lot to lose from failure (Beatty and Zajac, 1994; Tversky & Kahneman, 1986). And they also tend to be conservative in order to preserve the firm for their offspring (Bertrand & Schoar, 2006). Family owners and managers may also be generous to their offspring, assuring undeserved position in the company, compensation, and collateral benefits (Le Breton-Miller, Miller, & Lester, 2011; Lubatkin, Ling, & Schulze, 2007). Such agency cost may negatively influence family owners and managers' management participation or efficiency and could eventually hurt business integrity and transparency (Lubatkin et al., 2007).

Stewardship theory, on the other hand, explains that family owners and managers will act as stewards of their business and will be willing to sacrifice and make investment to make the firm healthy and durable as well as to enhance value for all stakeholders (Arregle, Hitt, Sirmon, & Very, 2007; James, 1999, 2006; Landes, 2008; Miller & Le Breton-Miller, 2005; Ward, 2004). Stewardship theory explains people's behavior in psychological perspective that people are motivated not only by self-interest but by service of others (Davis, James H. Schoorman David F. Donaldson, 1997). Stewardship is said to arise among people when relationships are stable, existence of strong interdependence and interaction, and when people have similarity in shared social network (Nahapiet, Janine. Ghoshal, 1998; Putnam, 2000). When family members identify with and are emotionally attached to the firm, these conditions of stewardship are likely to develop within family business and are willing to invest in long-term value for all stakeholders (Miller & Le Breton-Miller, 2005; Pierce, Kostova, & Dirks, 2001; Ward, 2004; Wasserman, 2006), behaving with committed effort to support the business and its shareholders (James, 2006; Lansberg, 1999; Ward, 2004). Family firm with stewardship appears in three aspects: tendency to invest in the future of the business, rich funding of the investment, and a willingness to sacrifice short-term gain for long-run values (James, 2006; Miller & Le Breton-Miller, 2005; Ward, 2004).

2.2 Firms' corporate social performance

2.2.1 Definition of corporation social performance

Wood (1991) proposed definition of corporate social performance as a business organization's configuration of principles of social responsibility processes of social responsiveness, and policies, programs and observable outcomes as they relate to the firm's societal relationships.

Developing from this definition, Wood and Jones (1995) argued that stakeholder theory is key to understand structure and dimensions of the firm's societal relationships. They redefined the policies, programs, and outcomes as "internal stakeholder effects, external stakeholder effects, and external institutional effects" and suggested that stakeholders set norms for corporate behavior, experience the effects of corporate behavior, and evaluate corporate behavior. In this study, the term corporate social performance will be defined as ‘both conceptual social responsibilities of companies and the measurement of a company’s performance related to CSP’ (Manner, 2010).

Bowen’s publication of ‘Social Responsibilities of the Businessman (1953)’ is considered to be the very first study attempted to seek theoretical explanation between firm and social relationship. Bowen conceptualized firm’s CSR as social obligation for the firm, and argued that firm is obliged to pursue policies that fit social purpose and value, make decision and act upon (Bowen, 1953). McGuire (1963) recognized importance of economic obligations, but also combined a broader definitions of the firm’s social responsibilities. He suggested that “the idea of social responsibilities supposes that the corporation has not only economic and legal obligations, but also certain responsibilities to society which extend beyond these obligations” (McGuire, 1963).

Carroll (1979), drawing from various discussion on social responsibilities in the 60s and 70s, suggested a definition of social responsibility that fully addresses the entire range of obligations business has to society. Those include economic, legal, ethical, and discretionary categories of business performance. This categorization combines social responsibilities of business in a more broad term as well as combining existing views of social responsibilities.

Early studies of corporate social performance mostly focused on the outcomes, instead of determinants, of corporate social performance and this might be because this was a relatively young field of study (Borgatti, 2003) or because of prevailing criticism that firms rarely gain financial profit from engaging in corporate social performance. Therefore, antecedents of CSP remained relatively understudied compared with consequences of CSP (Orlitzky, Marc, Frank L. Schmidt, 2003).

More recent studies developed some arguments to explain motivation for firms to engage in CSP (Aguilera et al., 2007). One explanation is that firms engage in CSP to achieve greater profit with instrumental motives (Bansal & Clelland, 2004; McWilliams & Siegel, 2001). Second is moral motivation, which suggests that firms engage in CSP when firms' top decision makers are committed to moral and social values. Moral motivation argument is supported by stewardship theory (Davis, James H. Schoorman David F. Donaldson, 1997). Third arguments emphasizes the institutional motives and views CSP as firm's reaction to institutional forces (O'Shaughnessy, Gedajlovic, & Reinmoeller, 2007), such as regulatory structures, governmental agencies, laws, courts, professions, interest groups, and public opinions (Scott, 1987). Because these institutions exerts great deal of influence on firm's strategic decisions (Weber, 1978), this argument suggests that firm's strategic decisions on CSP may relate to firm's intensions and efforts to adopt to institutional pressures (Kagan, Thornton, & Gunningham, 2003). However, some scholars have criticized the institutional theory for overlooking firm's active internal mechanisms to response to institutional pressures and expectations (Ashforth & Gibbs, 1990).

2.2.2 Corporate social performance of family firms

Whetten and Mackey (2005) explain reasons for family firms to act more socially responsibly, because of desire to maintain a good reputation of family business and to create a positive image. Godfrey (2005) describes firms and family owners want to act in a socially responsible way because positive results and images created by social responsible activities can be used to protect their asset and firm when in need in the future.

Some other researchers have argued that family owners will behave in a selfish way that might hurt the firm and broader society. In the family firm context, it is suggested that family owners may not likely act in a socially responsible manner and emphasize self-interest because of amoral familism. Such selfish behavior of family firms could create disadvantage to company and other stakeholders and broader society (Schulze, William S.Lubatkin, Michael H.Dino, Richard N.Buchholtz, 2001). Morck and Yeung (2004) investigate family-controlled firms and found that family-controlled firms may be socially irresponsible actor and conclude that the family owners are more interested in protecting their own interest and asset than contributing to development of their countries' economy and society.

3. Hypothesis

Previous researches on family firms have found unique characteristics of family firms and the most distinctive characteristics is that family owners are highly likely to prefer non-financial utility than other stakeholders. Examples of non-financial utility that family owners purse include positive images of family and maintaining good reputation (Chrisman, Chua, & Sharma, 2005; Westhead P, Cowling M, 2001), social reputation and trust through socially responsible behavior (Schulze, Lubatkin, & Dino, 2003), prestige in local community and social support (Guido Corbetta & Carlo A Salvato, 2004; Lee & Rogoff, 1996), and accumulation of social capital (J.-L. Arregle, Hitt, Sirmon, & Very, 2007). Berrone et al (2010) and Gomez-Mejia et al (Gómez-Mejía et al., 2007) defined all of these as 'socio-emotional wealth' and emphasized importance of 'socio-emotional wealth' along with reputation and prestige. Berrone et al (2010)'s study also have found that family firms emit less environmental pollutant because cost generated in the process is compensated by socio-emotional wealth of the family. His study concluded family firms have stronger environmental performance than non-family firms. Many studies show that up to a certain point, reputation and prestige is one of the most important factors for most family firms.

Other researches also have argued that social performance is especially important to family firms as a means of generating potentially useful goodwill or resources which may be useful at a later time, acting as a form of insurance for family firms (Dyer & Whetten, 2006). Also families in family firms represent the firm and negative images of the firm created from their behaviors that are easily observed and evaluated may hurt reputation of family owners as well as the firm (Gersick, 1997; Westhead P, Cowling M, 2001). Lower social performance of a firm can create negative image of the firm as a whole and this can directly lead to loss of socio-emotional wealth of family.

In addition, firms need long-term vision and sustainable implementation in order to response to social demand (Aragón-Correa & Sharma, 2003; Hart, 1995). And it is expected that dealing with such social demand will be easier for family firms than non-family firms to fulfill, because family firms consider permanence of the business to be an important factor and implement generational investment that can create patient capital that can be passed on to next generations (Sirmon & Hitt, 2003). Also, top managements of family firms generally can hold their position longer (Cruz, Gómez-Mejia, & Becerra, 2010) and are less pressured from short-term financial performance and is more apt to making and executing long-term plan (Gomez-Mejia, Nunez-Nickel, Gutierrez, 2001; Ward, 2011). Therefore, the following hypothesis is presented.

Hypothesis 1: Family firms will have stronger social performance than non-family firms.

Existing researches about relationship between corporate governance and corporate social performance have focused on agency cost that can occur in family firms (Gomez-Mejia, Luis R. Nunez-Nickel, Manuel. Gutierrez, 2001; Schulze et al., 2003; Schulze, William S.Lubatkin, Michael H.Dino, Richard N.Buchholtz, 2001). These researches are focused on ways to remove agency cost in terms of incentives to non-family agency (Schulze, William S.Lubatkin, Michael H.Dino, Richard N.Buchholtz, 2001), altruism of family members (Schulze et al., 2003), and direct family CEO effect (Gomez-Mejia, Luis R. Nunez-Nickel, Manuel. Gutierrez, 2001). Schulze et al (2003) proposed that discrepancy between different ownership shares and family firm’s debt usage has U-shaped relationship. That is, family firm’s ownership structure can be either consisted of multiple investors who are involved with decision making or be different from that of firms that executive shareholder has small amount of share. And therefore, it can be inferred that family firm’s governance structure will play a crucial role in corporate social performance since corporate social performance depends on how family perceives social objectives and profit attainment.

Previous researches considered ownership type, such as institutional investor, top management team, outside director, as governance structure and investigated different social performance of firms in terms of ownership type and ownership ratio (Oh et al., 2011). However, since Korean family firms have distinct structure that the major shares are owned by one individual or affiliated person, it is highly likely that adopting empirical research results from researches focused on firms that have western governance structure would yield results that are different from reality (Chang & Choi, 1988; Chang & Hong, 2000, 2002).

Board of directors generally assists and audits decision making process of firms including long term strategy, investment and financial decisions (Beasley, 1996; Fama & Jensen, 1983). Because board members may be influenced from interaction with family owners (Miller, Le Breton-Miller, & Lester, 2011), it is possible that non-family board members represent interests of other stakeholders about decisions that are made in favor for family owners and may actively participate in decision making related to socially responsible activities.

When majority of board of directors are family members and family owners act as agent, then the board's influence may weaken and family will have superior influence on board's decision making. In other words, if board of director is dominated by family members, board may make decisions that may damage interest of small shareholders and other stakeholders instead of making fair decision taking account of shareholders' interest. Therefore, from the agency theory's perspective, it can be expected that as more family members participate in the board, motivation for socially responsible activities may be lowered.

Other researchers also argue that outside directors' participation in the board helps firms to be more stakeholder-oriented decisions. Because outside directors are expected to represent shareholders and other stakeholders, they must understand expectations and demands of stakeholders around the company (Wang & Dewhirst, 1992) and must put their efforts to improve firm's credibility and legitimacy. Therefore, as outside director's ratio increases, opinions of shareholders and stakeholders are reflected in the decision making process which will result firms to more active engage in socially responsible activities (Johnson, R.A., and Greening, 1999). If outside directors fulfill the same role in the family firm, family firms will better understand social expectation and demand and therefore make firm decision in a way that increases long term financial performance and interest of stakeholders, along with improving integrity and transparency of the firm. Outside directors' such role is expected to exert positive influence on family firm's corporate social performance, therefore the following hypothesis is proposed.

Hypothesis 2: Outside director ratio is positively associated with social performance in family firms.

Many scholars have suggested that institutional owners exert significant influence on firm's decision making process. Especially, because institutional investors are often in form of corporation that owns significant percentage of the firm's share and cannot easily sell their shares (Pound, 1991a), they are more likely to influence firms to make sustainable long-term decisions (Holderness & Sheehan, 1988; Hoskisson, Johnson, & Moesel, 1994). Institutional investors tend to be risk averse and prefer long-term oriented decisions. Because institutional investors tend to avoid risks (Chaganti & Damanpour, 1991), they put pressure on managers to actively respond to social demand such as activities related to social responsibility which can reduce risky potentials that can damage firms' value (Graves & Waddock, 1994). Also, institutional investors are likely to make continued investment in the firm if they feel firm's vision and objectives are optimistic. Therefore, higher institutional investors' share ratio will lead to risk aversive decision making and improved social performance.

Institutional investors' trait coincides with family firm's pursuit of long-term survival. Unlike western companies which are centered around shareholders and have dispersed ownership, family firms continuously renew founder's vision and aims to remain as ongoing firm as long as possible (Miller et al., 2011). Because institutional investors own large share of stocks and it's not easy to withdraw their investment (Anderson & Reeb, 2003), institutional investors spend lots of effort and time to figure out target of investment, amount and appropriate timing and because of that their investment tend to last long. Because institutional investors prefer firms with increasing value in the long term instead of those firms with low credibility and short term profits, family firms which aim to survive in the long run are likely be on top of list for institutional investors for investment. Therefore, institutional investors holding part of ownership of family firm signal that the family firm has appropriate objectives and vision for long run and such strategic planning can positively influence firm's corporate social performance (Graves & Waddock, 1994; Yap Teoh & Y. Shiu, 1990). Building on prior works, the following hypothesis is presented.

Hypothesis 3: Institutional ownership is positively associated with social performance in family firms.

As strong corporate governance makes greater scrutiny possible, it may also weaken engagement in activities that are negative to social policies. As long as socially responsible actions help family firms to build stakeholder support and social capital, corporate governance will encourage socially responsible decisions. Therefore, strong corporate governance should encourage firms to engage in socially responsible activities that are in line with firm's strategic goals (Siegel, 2009). Schulze et al (2003, 2001) have suggested that corporate governance may play a key role in restraining family altruism and as a result, strong corporate governance may mitigate the family firm-social performance relationship. Building on prior works, this paper forwards the following hypothesis.

Hypothesis 4a: Institutional ownership moderates the positive relationship between family firm and social performance.

Hypothesis 4b: Institutional ownership moderates the positive relationship between outside director ratio and social performance.

4. Methods

4.1 Data and Sample

All the sample firms are large Korean firms listed on Korean Stock Exchanges. Korea Economic Justice Institute (KEJI), a leading Korean corporate social responsibility institution, accesses listed firms and announces ratings of their social activities every year, officially labeled as KEJI Index. This paper uses KEJI Index from year 2009 (18th) to 2011 (20th) which are based on fiscal years of 2007 to 2009. This implies that KEJI Index has 2 year of time lag since KEJI announces the results two years later. Also, because KEJI selects top 200 best corporate lists, firms appear on lists are different every year. Therefore, this paper selected 315 samples (105 firms X 3 years) that appeared on the list from year 2009 to 2011.

Firm-level data, including board and shareholder composition, were drawn from Data Analysis, Retrieval and Transfer system provided by Financial Supervisory Service. Control variables, including firm age, firm size, industry classification, financial performance and debt ratio, were collected from FnGuide and KISVALUE, a Korean electronic database.

4.2 Variables

4.2.1 Independent variables

(1) Family Firm

Existing researches typically define family firms as firms in which family members have ownership stakes and possess senior management positions (Dyer & Whetten, 2006). Adopting from McGuire et al (2012)'s study, this paper defines family firms as those firms in which at least two family members own 5% or more of outstanding equity and family members were involved in management in the sample years. This paper created a dummy variable that coded as 1 if it is family firm and 0 otherwise.

(2) Outside director ratio

Outside directors can contain and monitor top managers' arbitrary decision making (Fama & Jensen, 1983), and therefore it is expected that outside directors will also exert influences in family firms and represent external stakeholder's demand including corporate social performance (Miller & Le Breton-Miller, 2005). Outside director ratio is measured by dividing total number of board directors by number of outside directors and these data were obtained from business reports.

(3) Institutional investor share ratio

Share ratios of institutional investors are taken from FnGuide which details share ratio of institutional investors out of 100% of total share. There are varied types of institutional investors including public pension fund, insurance companies, security firms, investment company and more (Oh et al., 2011) but this paper didn't differentiate different types and studied all the institutional investors at the same time considering that each institutional investors will have influence on corporate social performance in the long term through majority ownership (Pound, 1991b).

4.2.2 Dependent variables

Corporate Social Performance (KEJI Index)

The Korea Economic Justice Institute Index (KEJI Index) is used as corporate social performance in this paper, which is collected and managed by Citizens' Coalition for Economic Justice Institute. KEJI Index rates firms with standardized values 60 sub evaluation indexes in 7 categories, including Corporate Integrity, Corporate Justice, Community, Customer Satisfaction, Environment, Employee Relations, and Long-term Orientation. Each evaluation indexes are weighted and have sub-categories. KEJI auditing committee performs a quality review of every company profile for quality assurance, and previous researches have used KEJI Index as a valid measure for corporate social performance (Chang, Oh, Jung, & Lee, 2012). The highest possible score of KEJI Index is 100; qualitative evaluation score of 75 and quantitative evaluation score of 25, but only qualitative evaluation is available. Therefore, this paper used qualitative evaluation score of 75 to evaluate firm’s corporate social performance.

4.2.3 Control variables

(1) Firm size

It has been found and supported by various researches that firm size have positive influence on corporate social performance (McWilliams & Siegel, 2000; Waddock & Graves, 1997), and previous studies on corporate social performance have controlled firm size (Oh et al., 2011). Because of firm’s large scale of business activities, larger firms are more likely to engage in social responsible practices more actively (Cowen, Ferreri, & Parker, 1987). Another study also found that because of large firms’ visibility, they are highly motivated to engage in social responsible practices (Udayasankar, 2008). Additional empirical studies also have found positive relationship between CSP and firm size because larger firms tend engage actively in socially responsible activities because of higher exposure to public attention (Fombrun, 1990; Johnson, R.A., and Greening, 1999; Muller & Kolk, 2010). Therefore, the larger firm size is, the higher corporate social performance it will have and this paper controlled firm size by taking logarithms of total sales.

(2) Firm age

Previous studies have found that firm age and corporate social performance have close association (Oh et al., 2011; Orlitzky, Siegel, & Waldman, 2011), and therefore controlled firm age by taking logarithms of firm age, calculated by subtracting firm's established year from the year of KEJI Index.

(3) Industry control

Industries classification followed 1 digit classification of Korea standard industrial code. In order to control for possible industry-specific influences, all the industries from manufacturing to education service industries were included regardless of frequency.

(4) Return on asset (ROA) and debt/sales ratio

Firms' strong commitment to corporate social performance might be because of slack resources firms have and expectations for social performance likely to increase as firms achieve higher financial performance (Waddock & Graves, 1997). Corporate social performance can increase as firms have more slack resources, and therefore this paper also controlled return on assets (net profit/total sales X 100) and debt ratio (debt/total asset) as proxy of slack resources.

4.3 Analysis methods

To test hypotheses, random effect model, one of the panel data analysis methods, was chosen and the sample was analyzed with statistics program STATA. This paper used random effect model instead of fixed effect model because of the panel data structure which has large number of firms and relatively small number of years in which case could lose degree of freedom with fixed effect model. Also, random effect model was preferred in order to measure dummy variables that do not change over time because such effect is ignored in fixed effect model. In order to ensure the decision, Hausman test was implemented and random effect model was chosen. Only the firms repeatedly included in the KEJI 200 list for the chosen period was selected as sample and balanced panel data analysis was used.

5. Results

The means, standard deviations and correlations for sample firms are presented in Table 1. Total of 315 samples were used for analysis by taking 105 firms over 3 years period (105 X 3 years). Average of CSP is 48.42 with standard deviation of 2.21. 30.5% of total sample are family firms. In average, outside directors participate in board meetings in 37% ratio, and institutional investors own 42.22% of total share in average. Variance inflation factor, which tells whether correlation coefficient among variables are eligible for regression analysis, are shown in the far right column and since all the measures are below cut-off threshold of 10 recommend by Belsley et al. (1980), these are free from multicollinearity issue.

< Table 1 > Descriptive statistics and correlations

	Mean	S.D.	Min	Max	CSP	Firm age (lo	ROA	Debt ratio	Firm size (lo	Family Firm	Outside di	Institutiona	VIF
CSP	48.417	2.213	44.14	54.36	1								1.12
Firm age (logged)	3.657	0.477	2.197	4.489	-0.052	1							1.03
ROA	0.095	0.603	-0.192	10.737	-0.048	-0.008	1						1.01
Debt ratio	78.584	90.094	9.95	1022.33	-0.029	0.08	-0.001	1					1.26
Firm size (logged sales)	26.772	1.663	21.448	31.921	-0.071	0.048	-0.031	0.439	1				1.31
Family Firm	0.305	0.461	0	1	0.261	-0.112	-0.043	-0.04	0.071	1			1.44
Outside directors ratio	0.376	0.142	0.125	1	0.229	-0.014	-0.059	0.049	0.082	0.514	1		1.39
Institutional ownership	4.224	6.419	0	31.27	0.151	-0.122	-0.038	-0.02	-0.175	0.085	0.05	1	1.08

Table 2 shows results of regression analysis. Model 1 is baseline which only includes control variables. Model 2 tests effects of family firm, outside director ratio and institutional ownership on corporate social performance. Model 2 test results found that family firms have stronger corporate social performance than non-family firms and the hypothesis was

< Table 2 > Regression analysis results

	Model 1	Model 2	Model 3	Model 4	Model 5
ksic1==C	0.7316	0.3267	0.3406	0.6209	0.2948
	(0.72)	(0.33)	(0.34)	(0.62)	(0.30)
ksic1==D	1.3053	0.6160	0.7268	0.9667	0.5700
	(0.94)	(0.45)	(0.53)	(0.70)	(0.42)
ksic1==F	1.7436	1.1109	1.2390	1.4986	1.1565
	(1.32)	(0.86)	(0.96)	(1.15)	(0.89)
ksic1==G	0.8778	0.6064	0.6531	0.7871	0.6063
	(0.69)	(0.49)	(0.53)	(0.63)	(0.49)
ksic1==H	-1.9900	-1.8803	-1.7790	-1.9036	-1.9277
	(-0.91)	(-0.89)	(-0.84)	(-0.89)	(-0.91)
ksic1==J	3.2839*	2.8707*	2.9907*	3.0706*	2.9029*
	(2.21)	(2.00)	(2.07)	(2.11)	(2.01)
Firm age (logged)	-0.0568	0.1554	0.1703	0.0347	0.1619
	(-0.14)	(0.38)	(0.42)	(0.08)	(0.40)
ROA	-0.3043*	-0.2889*	-0.2921*	-0.2951*	-0.2898*
	(-2.09)	(-2.03)	(-2.05)	(-2.06)	(-2.03)
Debt ratio	0.0028^{+}	0.0029^{+}	0.0028^{+}	0.0028^{+}	0.0029^{+}
	(1.72)	(1.85)	(1.77)	(1.74)	(1.82)
Firm size (logged sales)	-0.2142^{+}	-0.1986^{+}	-0.1966	-0.1712	-0.1981
	(-1.76)	(-1.67)	(-1.64)	(-1.42)	(-1.64)
Family Firm		1.0078*	1.0506*		0.9111^{+}
		(2.29)	(2.30)		(1.83)
Outside directors ratio		1.0634		1.6017	0.9465
		(1.01)		(1.47)	(0.79)
Institutional ownership		0.0650**	0.0560*	0.0285	0.0423
		(3.15)	(2.16)	(0.48)	(0.66)
Faminst			0.0261		0.0190
			(0.60)		(0.34)
Outinst				0.1040	0.0412
				(0.72)	(0.22)
Constant	53.3385***	51.5508***	51.8099***	51.0823***	51.6141***
	(14.70)	(14.52)	(14.49)	(14.18)	(14.42)
Observations	315	315	315	315	315
Chi-squared	17.4996	39.1042	38.3217	33.8253	39.3221
Degree of freedem	10.0000	13.0000	13.0000	13.0000	15.0000

supported with regression coefficient 1.0078 ($P < 0.005$). However, hypothesis 2 about the effects of outside director ratio was not supported with regression coefficient 1.0634. Therefore, representation of outside director did not have significant effect on family firms' corporate social performance, and hypothesis 2 was rejected. Hypothesis testing relationship of institutional ownership and family firm's corporate social performance was also tested in the Model 2 and hypothesis 3 was supported with significant level at 0.01 with regression coefficient of 0.065.

Model 3 tests moderating effects of institutional ownership on family firm and corporate social performance relation and Model 4 test moderating effects of institutional ownership on outside director ratio and corporate social performance relation in interaction term. Regression coefficient was positive value for both Model 3 (0.6) and Model 4 (0.72), however both did not have significant relationship. Therefore, hypothesis 4a, b which tested moderating effect of institutional ownership was not supported.

The results shows outside director ratio did not have significant influence on family firm's corporate social performance and the results found no support for moderating effect of institutional ownership. However, the results found that family firms have stronger corporate social performance than non-family firms and institutional ownership exerts positive influence on family firm's corporate social performance.

6. Conclusion and limitation

6.1 Conclusion and discussion

Previous researches on family firms focused on agency cost problem from the agency and stewardship theory perspective, while this paper tried to analyze influence of corporate governance on social performance by taking outside director ratio and institutional investors share ratio as representative measures for corporate governance of family firms. First hypothesis which assumed family firms would have greater corporate social performance than non-family firm was supported.

Among the hypothesis 2 and 3 which looked into influence of corporate governance, in terms of outside director ratio and institutional ownership, on corporate social performance, only hypothesis 3 was supported. This may be because unlike western firms which have well developed governance structure, outside directors' role is not active enough to exert influence on corporate social performance in Korean family firms. Previous researches by Fama and Jensen (1983) and Walsh and Seward (1990) have found results supporting relationship between outside director and corporate social performance in western context. However, different results came out in the Korean family firm context and the reason for this may be attributed to how outside directors are appointed in Korean firms. Outside directors are often chosen from relatives of family owners or those who are in close relationship and this may deter outside directors from fulfilling their role because of their complex relationship or they maybe have less interest in improving transparency and engaging in socially responsible activities. In addition, some scholars argue that firms involuntarily appointed outside directors especially during the institutional transition period following the Asian Financial Crisis because of institutional pressures (Chizema & Kim, 2010). Researchers also have attributed such passive reaction may not be significant enough to influence board to engage more in corporate social performance since large Korean firms have appointed a minimal scale of outside directors.

This paper can make some contributions in the following aspects. Firstly, unlike existing researches which focused on financial performance of family firms in terms of agency or stewardship theory at the CEO level, this paper looked into relationship between corporate governance and social performance and investigated which governance structure exerts positive or negative influence on corporate social performance. Secondly, previous researches didn’t take into account of family firm specific traits and measured block shareholders’ stock or executive holders’ position without distinction. In order to supplement this point, this paper investigated corporate governance in terms of outside director ratio and institutional investors and studied its relationship with corporate social performance. Lastly, many researches on family firms have focused on family firms in the US or Europe in relation to their distinct governance structure, but his study investigated governance structure and social performance in Korean context.

6.2 Limitation

This paper investigated relationship between corporate governance structure and social performance. Despite some contributions mentioned above, this paper bears some limitations. Firstly, to define corporate governance, this paper used outside director ratio and institutional investors. Besides these two aspects, there can be other factors related to governance such as family members' share ratio, founder or descendent CEO, or different types of share owned by family members and implementing these factors can yield different results.

Secondly, this paper uses KEJI Index as measure for corporate social performance, however since KEJI Index only announce top 200 firms and it's likely that these are composed of firms that have relatively high corporate social performance which could create sample bias. Also, it should be noted that since difference among firms in KEJI Index are quite narrow that small difference can yield different results.

Lastly, for the analysis data was collected for 3 year period. Since 3 years is the minimum period required for panel data analysis, later research could use data for longer period to improve credibility and accuracy of the results.

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국문초록

기업의 지배구조와 한국 가족기업의 사회적 성과에 관한 연구

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기존 연구들은 경제학에 기반한 대리인 이론과 심리학에 기반한 청지기 이론에 따라 가족기업을 운영하는 가족에게 나타날 수 있는 특징들을 상반되게 설명하고 있어, 가족의 경영참여와 기업의 성과의 관계에 대해서는 논란이 있다. 이에 따라, 재무적 성과로 가족기업을 평가해왔던 가족기업에 대한 기존 연구와는 달리, 본 연구에서는 기업의 사회적 성과 (corporate social performance)를 통해 가족기업의 특성을 살펴보고자 하였다. 본 연구는 가족기업여부, 사외이사비율, 기관투자자비율을 독립변수로 하여 종속변수인 기업의 사회적 성과에 어떤 영향을 미치는지 연구하였으며, 기관투자자비율을 조절변수로 하였다. 기업의 사회적 성과는 2007년부터 2009년까지 한국경제정의연구소에서 발표된 경제정의지수(KEJI Index)를 이용하였다. 연구 결과, 가족기업은 비가족기업보다 높은 사회적 성과를 달성하는 것으로 나타났으며, 사외이사의 비율은 기업의 사회적 성과와 유의미한 관계가 없는 것으로 나타났다. 한편, 기관투자자 비율은 가족기업과 사회적 성과에 조절변수로서는 유의미한 결과가 나오지 않았지만, 기관투자자비율은 사회적 성과에 긍정적인 영향을 미친 것으로 나타났다.

주요어: 가족기업, 기업의 사회적 성과, 대리인 이론, 청지기 이론, 지배구조, 경제정의지수

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The relationship between corporate governance and corporate social performance of family firms in Korea

기업의 지배구조와 한국 가족기업의 사회적 성과에 관한 연구

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The relationship between corporate governance and corporate social performance of family firms in Korea

by

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Abstract

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Agency theory from economics and stewardship theory based on psychology have emerged over the last decade to explain performance and conduct of family firms, and the two theories have found contradicting results and relationship between family firm and firm performance is still disputed. Therefore, unlike existing family firm researches that focused on financial performance of firms, this paper tests relationship and characteristics of corporate social performance and family firms. Family firm status, outside director ratio and institutional ownership are used as independent variables to test influences on corporate social performance, dependent variable of this paper. The samples are collected from KEJI Index from 2007 to 2009. The results indicate that family firms engage more in socially responsible activities and institutional ownership exerts positive influence on firm's corporate social performance. However, outside director ratio did not have significant influence on corporate social performance and institutional ownership also did not have moderating effects on family firm and corporate social performance relation.

Keyword: Family firm, corporate social responsibility, agency theory, stewardship theory, governance, KEJI index

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1. Introduction

Family-owned or family controlled firms consist the largest proportion of businesses worldwide (Porta & Lopez-De-Silanes, 1998; Shanker & Astrachan, 1996) and family firms are mostly small and midsized firms (Churchill & Hatten, 1987). Therefore, researchers in the past decades have put their effort to investigate the impact of family on firm’s performance (Dyer, 2006). Previous researched have found that family is an important factor for business activities (Aldrich & Cliff, 2003), firm survival (Stafford, Bhargava, Danes, Haynes, & Brewton, 2010) and firm competitiveness (Cassia, De Massis, & Pizzurno, 2012) as well as local and regional development (Berghoff, 2006).

At the business level, how family affect firm performance has been getting much research attention. Previous studies have compared performance of family firm and non-family firms (Anderson & Reeb, 2003), sales growth of family firms (Chrisman, Chua, & Litz, 2004), job satisfaction (Beehr, Drexler, & Faulkner, 1997), and innovation (Tanewski, Prajogo, & Sohal, 2003).

However, relatively little is known of the impact of family on the corporate social performance. Morck and Yeung (2004) have found that family firms mostly care for their self-interest and therefore family firms are less inclined to do good to society where their firm belongs to. Other researchers, such as Godfrey (2005) have argued that family firms and non-family firms have incentives to be socially responsible in order to maintain a good image and reputation, therefore, having a positive relationship with family firm and CSP.

Baron (2001) explained motivations for firms to engage in CSR as increased long-term profit, altruism, and pressure from outside and found that firm's strategic decision making, including motivations mentioned earlier play an important role in firm's corporate social performance. Hart and Moore (2000) and Finkelstein (1992) found that corporate governance is one of the most important factor influencing firm's strategic decision-making and previous researches about firm's strategic decision-making on governance focused on R&D investment (Baysinger, Kosnik, & Turk, 1991), innovation (Kochhar & David, 1996), entrepreneurship (Zahra, 1996) and diversification (Eisenmann, 2002). As Aguilera, Rupp, & Williams (2007) found out, long-term strategic decision-making can be influenced by both economic or non-economic corporate governance, and recent researches started to investigate influence and relationship of corporate governance and CSP (Oh, Chang, & Martynov, 2011).

Previous researches on governance of family firms were focused on CEO characteristics, despite considerable impact family firms have on economy and society. Most of researches on family firms were about influence of family firm on economy (Claessens, Djankov, & Lang, 2000; Porta & Lopez-De-Silanes, 1998) and family owners, but there are mixed results on governance and family firms researches (Faccio & Lang, 2002). A number of researches focused on financial performance of family firms, however, investigating CSP from corporate governance perspective can give a better explanation of family firms (Wood, 1991). Therefore, this paper attempt to investigate influence of governance structure on family firm's CSP by taking outside director ratio and institutional ownership as dependent variables to study characteristics of family firms in Korea. This paper will investigate whether family firms engage more in CSP than non-family firms as well as influence of outside director and institutional ownership, in addition to testing moderating effects of institutional ownership on family firm's CSP.

The first chapter of this paper will review research background and question to explain how existing researchers have found contradicting arguments about characteristics of family firms from different perspectives and justifies a reason for using CSP as dependent variable of this paper. Second chapter reviews existing researches to build up hypothesis. In this chapter, concept of family firm and CSP, founding theories as well as relationship between CSP and family firm is reviewed. Third chapter build up from theoretical researches and introduces hypothesis on CSP of family firm, outside director ratio, and institutional ownership relation. Fourth chapter explains data and sample collection and fifth chapter discusses statistical results of the research. Lastly, sixth chapter provides discussion and contributions of this paper and suggests further research direction based on limitations of this research.

2. Literature review

2.1 Family firms

2.1.1 Definition of family firm

Family firms are an important subject of research (Aronoff & Ward, 1995) for the following reasons. Majority of independent businesses are family owned; family firms are likely to be managed differently from non-family firms; family firms would have different prioritization of objectives from non-family firms; and family firms contribute to creation of wealth, job and competitiveness (Westhead & Cowling, 1998). There has been numerous researches done on family firms, yet there’s no single definition of family firms and the definition differs by countries and researchers (Zattoni, Gnan, & Huse, 2012). Most family firms are small and midsized firms (Churchill & Hatten, 1987) and among the small and midsized companies worldwide, family firms take up about 60-70% (Donckels & Frohlich, 1991). It is hard to settle on one definition of family firm that can be widely accepted, but academic researchers suggested many different ways to define the term (Astrachan, Klein, & Smyrnios, 2002; Astrachan & Shanker, 2003; Chrisman, Chua, & Steier, 2003; Handler, 1989).

Definition of family firm from previous researches includes family involvement of business perceived to be a family business, majority voting share ownership by family members, management of the business by at least one member from the family owning the business, or an inter-generational ownership transition (Handler, 1989; Westhead & Cowling, 1998). Westhead (1998) defines family firm with four criteria which are family ownership, family perception, family management and intergenerational ownership transition. Most commonly used definition of family firm in recent studies is by Ibrahim and Ellis (1994). Family firm is a firm or organization that has at least 51% of family ownership, more than one family member is involved with business management, and expected to have inter-generation ownership transition (Ibrahim & Ellis, 1994). This paper adopts definition from McGuire et al (2012) which defined family firms as those firms in which at least two family members own 5% or more of outstanding equity and family members being involved in management in the same year.

2.1.2 Agency theory and stewardship theory

Two distinct theories regarding the conduct and performance of family businesses have emerged over the last decade. According to agency theory, family owners and managers are driven by self-interest and tend to use their power and superior information to benefit the family (Bertrand & Schoar, 2006; Claessens, Djankov, Fan, & Lang, 2002; Gómez-Mejía, Takács Haynes, Núñez-Nickel, & Jacobson, 2007; Morck, Stangeland, & Yeung, 2000; Morck & Yeung, 2003; Wiseman & Gomez-Mejia, 1998). Although family businesses, like any other firms with concentrated ownership, may encounter less owner-agent agency costs, while family businesses are more likely to suffer from owner-owner agency costs where family owners exploit their asymmetric knowledge at the expense of other shareholders (Wasserman, 2006). Family owners tends to be risk averse because family fortune and wealth is tied to a single enterprise and have a lot to lose from failure (Beatty and Zajac, 1994; Tversky & Kahneman, 1986). And they also tend to be conservative in order to preserve the firm for their offspring (Bertrand & Schoar, 2006). Family owners and managers may also be generous to their offspring, assuring undeserved position in the company, compensation, and collateral benefits (Le Breton-Miller, Miller, & Lester, 2011; Lubatkin, Ling, & Schulze, 2007). Such agency cost may negatively influence family owners and managers' management participation or efficiency and could eventually hurt business integrity and transparency (Lubatkin et al., 2007).

Stewardship theory, on the other hand, explains that family owners and managers will act as stewards of their business and will be willing to sacrifice and make investment to make the firm healthy and durable as well as to enhance value for all stakeholders (Arregle, Hitt, Sirmon, & Very, 2007; James, 1999, 2006; Landes, 2008; Miller & Le Breton-Miller, 2005; Ward, 2004). Stewardship theory explains people's behavior in psychological perspective that people are motivated not only by self-interest but by service of others (Davis, James H. Schoorman David F. Donaldson, 1997). Stewardship is said to arise among people when relationships are stable, existence of strong interdependence and interaction, and when people have similarity in shared social network (Nahapiet, Janine. Ghoshal, 1998; Putnam, 2000). When family members identify with and are emotionally attached to the firm, these conditions of stewardship are likely to develop within family business and are willing to invest in long-term value for all stakeholders (Miller & Le Breton-Miller, 2005; Pierce, Kostova, & Dirks, 2001; Ward, 2004; Wasserman, 2006), behaving with committed effort to support the business and its shareholders (James, 2006; Lansberg, 1999; Ward, 2004). Family firm with stewardship appears in three aspects: tendency to invest in the future of the business, rich funding of the investment, and a willingness to sacrifice short-term gain for long-run values (James, 2006; Miller & Le Breton-Miller, 2005; Ward, 2004).

2.2 Firms' corporate social performance

2.2.1 Definition of corporation social performance

Wood (1991) proposed definition of corporate social performance as a business organization's configuration of principles of social responsibility processes of social responsiveness, and policies, programs and observable outcomes as they relate to the firm's societal relationships.

Developing from this definition, Wood and Jones (1995) argued that stakeholder theory is key to understand structure and dimensions of the firm's societal relationships. They redefined the policies, programs, and outcomes as "internal stakeholder effects, external stakeholder effects, and external institutional effects" and suggested that stakeholders set norms for corporate behavior, experience the effects of corporate behavior, and evaluate corporate behavior. In this study, the term corporate social performance will be defined as ‘both conceptual social responsibilities of companies and the measurement of a company’s performance related to CSP’ (Manner, 2010).

Bowen’s publication of ‘Social Responsibilities of the Businessman (1953)’ is considered to be the very first study attempted to seek theoretical explanation between firm and social relationship. Bowen conceptualized firm’s CSR as social obligation for the firm, and argued that firm is obliged to pursue policies that fit social purpose and value, make decision and act upon (Bowen, 1953). McGuire (1963) recognized importance of economic obligations, but also combined a broader definitions of the firm’s social responsibilities. He suggested that “the idea of social responsibilities supposes that the corporation has not only economic and legal obligations, but also certain responsibilities to society which extend beyond these obligations” (McGuire, 1963).

Carroll (1979), drawing from various discussion on social responsibilities in the 60s and 70s, suggested a definition of social responsibility that fully addresses the entire range of obligations business has to society. Those include economic, legal, ethical, and discretionary categories of business performance. This categorization combines social responsibilities of business in a more broad term as well as combining existing views of social responsibilities.

Early studies of corporate social performance mostly focused on the outcomes, instead of determinants, of corporate social performance and this might be because this was a relatively young field of study (Borgatti, 2003) or because of prevailing criticism that firms rarely gain financial profit from engaging in corporate social performance. Therefore, antecedents of CSP remained relatively understudied compared with consequences of CSP (Orlitzky, Marc, Frank L. Schmidt, 2003).

More recent studies developed some arguments to explain motivation for firms to engage in CSP (Aguilera et al., 2007). One explanation is that firms engage in CSP to achieve greater profit with instrumental motives (Bansal & Clelland, 2004; McWilliams & Siegel, 2001). Second is moral motivation, which suggests that firms engage in CSP when firms' top decision makers are committed to moral and social values. Moral motivation argument is supported by stewardship theory (Davis, James H. Schoorman David F. Donaldson, 1997). Third arguments emphasizes the institutional motives and views CSP as firm's reaction to institutional forces (O'Shaughnessy, Gedajlovic, & Reinmoeller, 2007), such as regulatory structures, governmental agencies, laws, courts, professions, interest groups, and public opinions (Scott, 1987). Because these institutions exerts great deal of influence on firm's strategic decisions (Weber, 1978), this argument suggests that firm's strategic decisions on CSP may relate to firm's intensions and efforts to adopt to institutional pressures (Kagan, Thornton, & Gunningham, 2003). However, some scholars have criticized the institutional theory for overlooking firm's active internal mechanisms to response to institutional pressures and expectations (Ashforth & Gibbs, 1990).

2.2.2 Corporate social performance of family firms

Whetten and Mackey (2005) explain reasons for family firms to act more socially responsibly, because of desire to maintain a good reputation of family business and to create a positive image. Godfrey (2005) describes firms and family owners want to act in a socially responsible way because positive results and images created by social responsible activities can be used to protect their asset and firm when in need in the future.

Some other researchers have argued that family owners will behave in a selfish way that might hurt the firm and broader society. In the family firm context, it is suggested that family owners may not likely act in a socially responsible manner and emphasize self-interest because of amoral familism. Such selfish behavior of family firms could create disadvantage to company and other stakeholders and broader society (Schulze, William S.Lubatkin, Michael H.Dino, Richard N.Buchholtz, 2001). Morck and Yeung (2004) investigate family-controlled firms and found that family-controlled firms may be socially irresponsible actor and conclude that the family owners are more interested in protecting their own interest and asset than contributing to development of their countries' economy and society.

3. Hypothesis

Previous researches on family firms have found unique characteristics of family firms and the most distinctive characteristics is that family owners are highly likely to prefer non-financial utility than other stakeholders. Examples of non-financial utility that family owners purse include positive images of family and maintaining good reputation (Chrisman, Chua, & Sharma, 2005; Westhead P, Cowling M, 2001), social reputation and trust through socially responsible behavior (Schulze, Lubatkin, & Dino, 2003), prestige in local community and social support (Guido Corbetta & Carlo A Salvato, 2004; Lee & Rogoff, 1996), and accumulation of social capital (J.-L. Arregle, Hitt, Sirmon, & Very, 2007). Berrone et al (2010) and Gomez-Mejia et al (Gómez-Mejía et al., 2007) defined all of these as 'socio-emotional wealth' and emphasized importance of 'socio-emotional wealth' along with reputation and prestige. Berrone et al (2010)'s study also have found that family firms emit less environmental pollutant because cost generated in the process is compensated by socio-emotional wealth of the family. His study concluded family firms have stronger environmental performance than non-family firms. Many studies show that up to a certain point, reputation and prestige is one of the most important factors for most family firms.

Other researches also have argued that social performance is especially important to family firms as a means of generating potentially useful goodwill or resources which may be useful at a later time, acting as a form of insurance for family firms (Dyer & Whetten, 2006). Also families in family firms represent the firm and negative images of the firm created from their behaviors that are easily observed and evaluated may hurt reputation of family owners as well as the firm (Gersick, 1997; Westhead P, Cowling M, 2001). Lower social performance of a firm can create negative image of the firm as a whole and this can directly lead to loss of socio-emotional wealth of family.

In addition, firms need long-term vision and sustainable implementation in order to response to social demand (Aragón-Correa & Sharma, 2003; Hart, 1995). And it is expected that dealing with such social demand will be easier for family firms than non-family firms to fulfill, because family firms consider permanence of the business to be an important factor and implement generational investment that can create patient capital that can be passed on to next generations (Sirmon & Hitt, 2003). Also, top managements of family firms generally can hold their position longer (Cruz, Gómez-Mejia, & Becerra, 2010) and are less pressured from short-term financial performance and is more apt to making and executing long-term plan (Gomez-Mejia, Nunez-Nickel, Gutierrez, 2001; Ward, 2011). Therefore, the following hypothesis is presented.

Hypothesis 1: Family firms will have stronger social performance than non-family firms.

Existing researches about relationship between corporate governance and corporate social performance have focused on agency cost that can occur in family firms (Gomez-Mejia, Luis R. Nunez-Nickel, Manuel. Gutierrez, 2001; Schulze et al., 2003; Schulze, William S.Lubatkin, Michael H.Dino, Richard N.Buchholtz, 2001). These researches are focused on ways to remove agency cost in terms of incentives to non-family agency (Schulze, William S.Lubatkin, Michael H.Dino, Richard N.Buchholtz, 2001), altruism of family members (Schulze et al., 2003), and direct family CEO effect (Gomez-Mejia, Luis R. Nunez-Nickel, Manuel. Gutierrez, 2001). Schulze et al (2003) proposed that discrepancy between different ownership shares and family firm’s debt usage has U-shaped relationship. That is, family firm’s ownership structure can be either consisted of multiple investors who are involved with decision making or be different from that of firms that executive shareholder has small amount of share. And therefore, it can be inferred that family firm’s governance structure will play a crucial role in corporate social performance since corporate social performance depends on how family perceives social objectives and profit attainment.

Previous researches considered ownership type, such as institutional investor, top management team, outside director, as governance structure and investigated different social performance of firms in terms of ownership type and ownership ratio (Oh et al., 2011). However, since Korean family firms have distinct structure that the major shares are owned by one individual or affiliated person, it is highly likely that adopting empirical research results from researches focused on firms that have western governance structure would yield results that are different from reality (Chang & Choi, 1988; Chang & Hong, 2000, 2002).

Board of directors generally assists and audits decision making process of firms including long term strategy, investment and financial decisions (Beasley, 1996; Fama & Jensen, 1983). Because board members may be influenced from interaction with family owners (Miller, Le Breton-Miller, & Lester, 2011), it is possible that non-family board members represent interests of other stakeholders about decisions that are made in favor for family owners and may actively participate in decision making related to socially responsible activities.

When majority of board of directors are family members and family owners act as agent, then the board's influence may weaken and family will have superior influence on board's decision making. In other words, if board of director is dominated by family members, board may make decisions that may damage interest of small shareholders and other stakeholders instead of making fair decision taking account of shareholders' interest. Therefore, from the agency theory's perspective, it can be expected that as more family members participate in the board, motivation for socially responsible activities may be lowered.

Other researchers also argue that outside directors' participation in the board helps firms to be more stakeholder-oriented decisions. Because outside directors are expected to represent shareholders and other stakeholders, they must understand expectations and demands of stakeholders around the company (Wang & Dewhirst, 1992) and must put their efforts to improve firm's credibility and legitimacy. Therefore, as outside director's ratio increases, opinions of shareholders and stakeholders are reflected in the decision making process which will result firms to more active engage in socially responsible activities (Johnson, R.A., and Greening, 1999). If outside directors fulfill the same role in the family firm, family firms will better understand social expectation and demand and therefore make firm decision in a way that increases long term financial performance and interest of stakeholders, along with improving integrity and transparency of the firm. Outside directors' such role is expected to exert positive influence on family firm's corporate social performance, therefore the following hypothesis is proposed.

Hypothesis 2: Outside director ratio is positively associated with social performance in family firms.

Many scholars have suggested that institutional owners exert significant influence on firm's decision making process. Especially, because institutional investors are often in form of corporation that owns significant percentage of the firm's share and cannot easily sell their shares (Pound, 1991a), they are more likely to influence firms to make sustainable long-term decisions (Holderness & Sheehan, 1988; Hoskisson, Johnson, & Moesel, 1994). Institutional investors tend to be risk averse and prefer long-term oriented decisions. Because institutional investors tend to avoid risks (Chaganti & Damanpour, 1991), they put pressure on managers to actively respond to social demand such as activities related to social responsibility which can reduce risky potentials that can damage firms' value (Graves & Waddock, 1994). Also, institutional investors are likely to make continued investment in the firm if they feel firm's vision and objectives are optimistic. Therefore, higher institutional investors' share ratio will lead to risk aversive decision making and improved social performance.

Institutional investors' trait coincides with family firm's pursuit of long-term survival. Unlike western companies which are centered around shareholders and have dispersed ownership, family firms continuously renew founder's vision and aims to remain as ongoing firm as long as possible (Miller et al., 2011). Because institutional investors own large share of stocks and it's not easy to withdraw their investment (Anderson & Reeb, 2003), institutional investors spend lots of effort and time to figure out target of investment, amount and appropriate timing and because of that their investment tend to last long. Because institutional investors prefer firms with increasing value in the long term instead of those firms with low credibility and short term profits, family firms which aim to survive in the long run are likely be on top of list for institutional investors for investment. Therefore, institutional investors holding part of ownership of family firm signal that the family firm has appropriate objectives and vision for long run and such strategic planning can positively influence firm's corporate social performance (Graves & Waddock, 1994; Yap Teoh & Y. Shiu, 1990). Building on prior works, the following hypothesis is presented.

Hypothesis 3: Institutional ownership is positively associated with social performance in family firms.

As strong corporate governance makes greater scrutiny possible, it may also weaken engagement in activities that are negative to social policies. As long as socially responsible actions help family firms to build stakeholder support and social capital, corporate governance will encourage socially responsible decisions. Therefore, strong corporate governance should encourage firms to engage in socially responsible activities that are in line with firm's strategic goals (Siegel, 2009). Schulze et al (2003, 2001) have suggested that corporate governance may play a key role in restraining family altruism and as a result, strong corporate governance may mitigate the family firm-social performance relationship. Building on prior works, this paper forwards the following hypothesis.

Hypothesis 4a: Institutional ownership moderates the positive relationship between family firm and social performance.

Hypothesis 4b: Institutional ownership moderates the positive relationship between outside director ratio and social performance.

4. Methods

4.1 Data and Sample

All the sample firms are large Korean firms listed on Korean Stock Exchanges. Korea Economic Justice Institute (KEJI), a leading Korean corporate social responsibility institution, accesses listed firms and announces ratings of their social activities every year, officially labeled as KEJI Index. This paper uses KEJI Index from year 2009 (18th) to 2011 (20th) which are based on fiscal years of 2007 to 2009. This implies that KEJI Index has 2 year of time lag since KEJI announces the results two years later. Also, because KEJI selects top 200 best corporate lists, firms appear on lists are different every year. Therefore, this paper selected 315 samples (105 firms X 3 years) that appeared on the list from year 2009 to 2011.

Firm-level data, including board and shareholder composition, were drawn from Data Analysis, Retrieval and Transfer system provided by Financial Supervisory Service. Control variables, including firm age, firm size, industry classification, financial performance and debt ratio, were collected from FnGuide and KISVALUE, a Korean electronic database.

4.2 Variables

4.2.1 Independent variables

(1) Family Firm

Existing researches typically define family firms as firms in which family members have ownership stakes and possess senior management positions (Dyer & Whetten, 2006). Adopting from McGuire et al (2012)'s study, this paper defines family firms as those firms in which at least two family members own 5% or more of outstanding equity and family members were involved in management in the sample years. This paper created a dummy variable that coded as 1 if it is family firm and 0 otherwise.

(2) Outside director ratio

Outside directors can contain and monitor top managers' arbitrary decision making (Fama & Jensen, 1983), and therefore it is expected that outside directors will also exert influences in family firms and represent external stakeholder's demand including corporate social performance (Miller & Le Breton-Miller, 2005). Outside director ratio is measured by dividing total number of board directors by number of outside directors and these data were obtained from business reports.

(3) Institutional investor share ratio

Share ratios of institutional investors are taken from FnGuide which details share ratio of institutional investors out of 100% of total share. There are varied types of institutional investors including public pension fund, insurance companies, security firms, investment company and more (Oh et al., 2011) but this paper didn't differentiate different types and studied all the institutional investors at the same time considering that each institutional investors will have influence on corporate social performance in the long term through majority ownership (Pound, 1991b).

4.2.2 Dependent variables

Corporate Social Performance (KEJI Index)

The Korea Economic Justice Institute Index (KEJI Index) is used as corporate social performance in this paper, which is collected and managed by Citizens' Coalition for Economic Justice Institute. KEJI Index rates firms with standardized values 60 sub evaluation indexes in 7 categories, including Corporate Integrity, Corporate Justice, Community, Customer Satisfaction, Environment, Employee Relations, and Long-term Orientation. Each evaluation indexes are weighted and have sub-categories. KEJI auditing committee performs a quality review of every company profile for quality assurance, and previous researches have used KEJI Index as a valid measure for corporate social performance (Chang, Oh, Jung, & Lee, 2012). The highest possible score of KEJI Index is 100; qualitative evaluation score of 75 and quantitative evaluation score of 25, but only qualitative evaluation is available. Therefore, this paper used qualitative evaluation score of 75 to evaluate firm's corporate social performance.

4.2.3 Control variables

(1) Firm size

It has been found and supported by various researches that firm size have positive influence on corporate social performance (McWilliams & Siegel, 2000; Waddock & Graves, 1997), and previous studies on corporate social performance have controlled firm size (Oh et al., 2011). Because of firm's large scale of business activities, larger firms are more likely to engage in social responsible practices more actively (Cowen, Ferreri, & Parker, 1987). Another study also found that because of large firms' visibility, they are highly motivated to engage in social responsible practices (Udayasankar, 2008). Additional empirical studies also have found positive relationship between CSP and firm size because larger firms tend engage actively in socially responsible activities because of higher exposure to public attention (Fombrun, 1990; Johnson, R.A., and Greening, 1999; Muller & Kolk, 2010). Therefore, the larger firm size is, the higher corporate social performance it will have and this paper controlled firm size by taking logarithms of total sales.

(2) Firm age

Previous studies have found that firm age and corporate social performance have close association (Oh et al., 2011; Orlitzky, Siegel, & Waldman, 2011), and therefore controlled firm age by taking logarithms of firm age, calculated by subtracting firm's established year from the year of KEJI Index.

(3) Industry control

Industries classification followed 1 digit classification of Korea standard industrial code. In order to control for possible industry-specific influences, all the industries from manufacturing to education service industries were included regardless of frequency.

(4) Return on asset (ROA) and debt/sales ratio

Firms' strong commitment to corporate social performance might be because of slack resources firms have and expectations for social performance likely to increase as firms achieve higher financial performance (Waddock & Graves, 1997). Corporate social performance can increase as firms have more slack resources, and therefore this paper also controlled return on assets (net profit/total sales X 100) and debt ratio (debt/total asset) as proxy of slack resources.

4.3 Analysis methods

To test hypotheses, random effect model, one of the panel data analysis methods, was chosen and the sample was analyzed with statistics program STATA. This paper used random effect model instead of fixed effect model because of the panel data structure which has large number of firms and relatively small number of years in which case could lose degree of freedom with fixed effect model. Also, random effect model was preferred in order to measure dummy variables that do not change over time because such effect is ignored in fixed effect model. In order to ensure the decision, Hausman test was implemented and random effect model was chosen. Only the firms repeatedly included in the KEJI 200 list for the chosen period was selected as sample and balanced panel data analysis was used.

5. Results

The means, standard deviations and correlations for sample firms are presented in Table 1. Total of 315 samples were used for analysis by taking 105 firms over 3 years period (105 X 3 years). Average of CSP is 48.42 with standard deviation of 2.21. 30.5% of total sample are family firms. In average, outside directors participate in board meetings in 37% ratio, and institutional investors own 42.22% of total share in average. Variance inflation factor, which tells whether correlation coefficient among variables are eligible for regression analysis, are shown in the far right column and since all the measures are below cut-off threshold of 10 recommend by Belsley et al. (1980), these are free from multicollinearity issue.

< Table 1 > Descriptive statistics and correlations

	Mean	S.D.	Min	Max	CSP	Firm age (lo	ROA	Debt ratio	Firm size (lo	Family Firm	Outside di	Institutiona	VIF
CSP	48.417	2.213	44.14	54.36	1								1.12
Firm age (logged)	3.657	0.477	2.197	4.489	-0.052	1							1.03
ROA	0.095	0.603	-0.192	10.737	-0.048	-0.008	1						1.01
Debt ratio	78.584	90.094	9.95	1022.33	-0.029	0.08	-0.001	1					1.26
Firm size (logged sales)	26.772	1.663	21.448	31.921	-0.071	0.048	-0.031	0.439	1				1.31
Family Firm	0.305	0.461	0	1	0.261	-0.112	-0.043	-0.04	0.071	1			1.44
Outside directors ratio	0.376	0.142	0.125	1	0.229	-0.014	-0.059	0.049	0.082	0.514	1		1.39
Institutional ownership	4.224	6.419	0	31.27	0.151	-0.122	-0.038	-0.02	-0.175	0.085	0.05	1	1.08

Table 2 shows results of regression analysis. Model 1 is baseline which only includes control variables. Model 2 tests effects of family firm, outside director ratio and institutional ownership on corporate social performance. Model 2 test results found that family firms have stronger corporate social performance than non-family firms and the hypothesis was

< Table 2 > Regression analysis results

	Model 1	Model 2	Model 3	Model 4	Model 5
ksic1==C	0.7316	0.3267	0.3406	0.6209	0.2948
	(0.72)	(0.33)	(0.34)	(0.62)	(0.30)
ksic1==D	1.3053	0.6160	0.7268	0.9667	0.5700
	(0.94)	(0.45)	(0.53)	(0.70)	(0.42)
ksic1==F	1.7436	1.1109	1.2390	1.4986	1.1565
	(1.32)	(0.86)	(0.96)	(1.15)	(0.89)
ksic1==G	0.8778	0.6064	0.6531	0.7871	0.6063
	(0.69)	(0.49)	(0.53)	(0.63)	(0.49)
ksic1==H	-1.9900	-1.8803	-1.7790	-1.9036	-1.9277
	(-0.91)	(-0.89)	(-0.84)	(-0.89)	(-0.91)
ksic1==J	3.2839*	2.8707*	2.9907*	3.0706*	2.9029*
	(2.21)	(2.00)	(2.07)	(2.11)	(2.01)
Firm age (logged)	-0.0568	0.1554	0.1703	0.0347	0.1619
	(-0.14)	(0.38)	(0.42)	(0.08)	(0.40)
ROA	-0.3043*	-0.2889*	-0.2921*	-0.2951*	-0.2898*
	(-2.09)	(-2.03)	(-2.05)	(-2.06)	(-2.03)
Debt ratio	0.0028^{+}	0.0029^{+}	0.0028^{+}	0.0028^{+}	0.0029^{+}
	(1.72)	(1.85)	(1.77)	(1.74)	(1.82)
Firm size (logged sales)	-0.2142^{+}	-0.1986^{+}	-0.1966	-0.1712	-0.1981
	(-1.76)	(-1.67)	(-1.64)	(-1.42)	(-1.64)
Family Firm		1.0078*	1.0506*		0.9111^{+}
		(2.29)	(2.30)		(1.83)
Outside directors ratio		1.0634		1.6017	0.9465
		(1.01)		(1.47)	(0.79)
Institutional ownership		0.0650**	0.0560*	0.0285	0.0423
		(3.15)	(2.16)	(0.48)	(0.66)
Faminst			0.0261		0.0190
			(0.60)		(0.34)
Outinst				0.1040	0.0412
				(0.72)	(0.22)
Constant	53.3385***	51.5508***	51.8099***	51.0823***	51.6141***
	(14.70)	(14.52)	(14.49)	(14.18)	(14.42)
Observations	315	315	315	315	315
Chi-squared	17.4996	39.1042	38.3217	33.8253	39.3221
Degree of freedem	10.0000	13.0000	13.0000	13.0000	15.0000

supported with regression coefficient 1.0078 ($P < 0.005$). However, hypothesis 2 about the effects of outside director ratio was not supported with regression coefficient 1.0634. Therefore, representation of outside director did not have significant effect on family firms' corporate social performance, and hypothesis 2 was rejected. Hypothesis testing relationship of institutional ownership and family firm's corporate social performance was also tested in the Model 2 and hypothesis 3 was supported with significant level at 0.01 with regression coefficient of 0.065.

Model 3 tests moderating effects of institutional ownership on family firm and corporate social performance relation and Model 4 test moderating effects of institutional ownership on outside director ratio and corporate social performance relation in interaction term. Regression coefficient was positive value for both Model 3 (0.6) and Model 4 (0.72), however both did not have significant relationship. Therefore, hypothesis 4a, b which tested moderating effect of institutional ownership was not supported.

The results shows outside director ratio did not have significant influence on family firm's corporate social performance and the results found no support for moderating effect of institutional ownership. However, the results found that family firms have stronger corporate social performance than non-family firms and institutional ownership exerts positive influence on family firm's corporate social performance.

6. Conclusion and limitation

6.1 Conclusion and discussion

Previous researches on family firms focused on agency cost problem from the agency and stewardship theory perspective, while this paper tried to analyze influence of corporate governance on social performance by taking outside director ratio and institutional investors share ratio as representative measures for corporate governance of family firms. First hypothesis which assumed family firms would have greater corporate social performance than non-family firm was supported.

Among the hypothesis 2 and 3 which looked into influence of corporate governance, in terms of outside director ratio and institutional ownership, on corporate social performance, only hypothesis 3 was supported. This may be because unlike western firms which have well developed governance structure, outside directors' role is not active enough to exert influence on corporate social performance in Korean family firms. Previous researches by Fama and Jensen (1983) and Walsh and Seward (1990) have found results supporting relationship between outside director and corporate social performance in western context. However, different results came out in the Korean family firm context and the reason for this may be attributed to how outside directors are appointed in Korean firms. Outside directors are often chosen from relatives of family owners or those who are in close relationship and this may deter outside directors from fulfilling their role because of their complex relationship or they maybe have less interest in improving transparency and engaging in socially responsible activities. In addition, some scholars argue that firms involuntarily appointed outside directors especially during the institutional transition period following the Asian Financial Crisis because of institutional pressures (Chizema & Kim, 2010). Researchers also have attributed such passive reaction may not be significant enough to influence board to engage more in corporate social performance since large Korean firms have appointed a minimal scale of outside directors.

This paper can make some contributions in the following aspects. Firstly, unlike existing researches which focused on financial performance of family firms in terms of agency or stewardship theory at the CEO level, this paper looked into relationship between corporate governance and social performance and investigated which governance structure exerts positive or negative influence on corporate social performance. Secondly, previous researches didn’t take into account of family firm specific traits and measured block shareholders’ stock or executive holders’ position without distinction. In order to supplement this point, this paper investigated corporate governance in terms of outside director ratio and institutional investors and studied its relationship with corporate social performance. Lastly, many researches on family firms have focused on family firms in the US or Europe in relation to their distinct governance structure, but his study investigated governance structure and social performance in Korean context.

6.2 Limitation

This paper investigated relationship between corporate governance structure and social performance. Despite some contributions mentioned above, this paper bears some limitations. Firstly, to define corporate governance, this paper used outside director ratio and institutional investors. Besides these two aspects, there can be other factors related to governance such as family members' share ratio, founder or descendent CEO, or different types of share owned by family members and implementing these factors can yield different results.

Secondly, this paper uses KEJI Index as measure for corporate social performance, however since KEJI Index only announce top 200 firms and it's likely that these are composed of firms that have relatively high corporate social performance which could create sample bias. Also, it should be noted that since difference among firms in KEJI Index are quite narrow that small difference can yield different results.

Lastly, for the analysis data was collected for 3 year period. Since 3 years is the minimum period required for panel data analysis, later research could use data for longer period to improve credibility and accuracy of the results.

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국문초록

기업의 지배구조와 한국 가족기업의 사회적 성과에 관한 연구

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기존 연구들은 경제학에 기반한 대리인 이론과 심리학에 기반한 청지기 이론에 따라 가족기업을 운영하는 가족에게 나타날 수 있는 특징들을 상반되게 설명하고 있어, 가족의 경영참여와 기업의 성과의 관계에 대해서는 논란이 있다. 이에 따라, 재무적 성과로 가족기업을 평가해왔던 가족기업에 대한 기존 연구와는 달리, 본 연구에서는 기업의 사회적 성과 (corporate social performance)를 통해 가족기업의 특성을 살펴보고자 하였다. 본 연구는 가족기업여부, 사외이사비율, 기관투자자비율을 독립변수로 하여 종속변수인 기업의 사회적 성과에 어떤 영향을 미치는지 연구하였으며, 기관투자자비율을 조절변수로 하였다. 기업의 사회적 성과는 2007년부터 2009년까지 한국경제정의연구소에서 발표된 경제정의지수(KEJI Index)를 이용하였다. 연구 결과, 가족기업은 비가족기업보다 높은 사회적 성과를 달성하는 것으로 나타났으며, 사외이사의 비율은 기업의 사회적 성과와 유의미한 관계가 없는 것으로 나타났다. 한편, 기관투자자 비율은 가족기업과 사회적 성과에 조절변수로서는 유의미한 결과가 나오지 않았지만, 기관투자자비율은 사회적 성과에 긍정적인 영향을 미친 것으로 나타났다.

주요어: 가족기업, 기업의 사회적 성과, 대리인 이론, 청지기 이론, 지배구조, 경제정의지수

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