



Handelshøyskolen BI

GRA 19703 Master Thesis

Thesis Master of Science 100% - W

Predefinert informasjon

Startdato:	16-01-2022 09:00	Termin:	202210
Sluttdato:	01-07-2022 12:00	Vurderingsform:	Norsk 6-trinns skala (A-F)
Eksamensform:	T		
Flowkode:	202210 10936 IN00 W T		
Intern sensor:	(Anonymisert)		

Deltaker

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Informasjon fra deltaker

Tittel *: The Determinants of ESG Ratings in Family Firms

Navn på veileder *: Charlotte Østergaard

Inneholder besvarelsen
konfidensielt
materiale?: Nei

Kan besvarelsen
offentliggjøres?: Ja

Gruppe

Gruppenavn: (Anonymisert)

Gruppenummer: 122

Andre medlemmer i gruppen:



The Determinants of ESG Ratings in Family Firms

Evidence from the Nordic Market

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This thesis is a part of the MSc programme at BI Norwegian Business School. The school takes no responsibility for the methods used, evidence found, or conclusions drawn.

Acknowledgements

We want to thank our supervisor, Charlotte Østergaard, for the guidance throughout this thesis writing process. We have significantly benefited from your wealth of knowledge and appreciate any advice, feedback, and support you have given us during this semester.

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Oslo, July 2022

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Abstract

By drawing on a sample of 528 public-traded corporations in the Nordic countries, this thesis explores the determinants of ESG ratings in family firms. We address three important research questions: (1) are family firms associated with lower ESG ratings than non-family firms; (2) do the unique characteristics of family firms materialize in a different prioritization of E, S, and G initiatives than their non-family counterparts; and (3) is the extent to which a family can control the firm's behavior decisive for their ESG rating. We find that family firms exhibit lower ESG ratings than non-family firms because they underperform on ESG initiatives that may threaten family control. Specifically, family firms tend to downgrade initiatives that affect internal stakeholders (managers, shareholders, and the workforce). However, they show the same level of ESG engagement as non-family firms on initiatives that concern external stakeholders and thus give reputational benefits. Furthermore, we demonstrate that family firms' ESG ratings are highly contingent upon the family's ability to shape the firm's behavior, goals, and strategies. We find that in firms with a family member as CEO or if the family controls the board of directors, the ESG ratings are even lower. On the contrary, family-founded firms have better ESG ratings than other family firms. Our theoretical contribution is based on the concept of SEW. We argue that retaining family control is the most critical factor in shaping family firms' ESG engagement.

Keywords – ESG performance, family firms, socioemotional wealth

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1 Introduction

In recent years, Environmental, Social, and Governance (ESG) investing has gained considerable traction among firms and their stakeholders. Firms are expected to take actions to minimize their negative impact and be transparent when disclosing their business practices. Firms' ability to perform well on ESG has consequently become essential to thrive in competitive markets (Schoenmaker & Schramade, 2019). The literature has responded to the momentum of ESG, and the question of what drives and hinders ESG performance is gaining prominence (Campbell, 2007; Rees & Rodionova, 2015). However, the determinants of ESG performance in family firms are under-explored in the literature (Izzo & Ciaburri, 2018). Family firms present unique perspectives that might affect their propensity to invest in ESG. In particular, they are often argued to prioritize family-centered goals in strategic-decision making (Gomez-Mejia et al., 2007; Rees & Rodionova, 2013). The interplay between family agendas and business objectives raises doubt about whether they show the same ESG engagement as their non-family counterparts.

In this master thesis, we aim to fill a gap in the literature by clarifying the determinants of ESG performance in family firms. The literature is relatively consistent in considering socioemotional wealth (SEW) as the main frame of reference for family firms (Berrone et al., 2010; Gomez-Mejia et al., 2007). Thus, SEW presents a lens for us to interpret family firms' ESG engagement. It captures the family-orientated goals family firms seek to achieve. Several scholars agree that two of the SEW dimensions are particularly important for family firms; (1) enhance the family's reputation and (2) retain family control (e.g., Cruz et al., 2014; Dick et al., 2021). Interestingly, these two dimensions provide contradictory proposals as to whether family firms are more selfish or altruistic in their behavior compared to non-family firms. On one hand, family firms may engage in strategies to enhance family control. If family owners can appropriate private benefits of control and neglect the interest of other stakeholders, they might exhibit lower ESG ratings (Dick et al., 2021). On the other hand, engaging in ESG activities can enhance the firm's reputation and legitimacy, which would spill over to the family's reputation (López-Perez et al.,

2018). In turn, they might exhibit higher ESG ratings than non-family firms.

A good research opportunity exists to reconcile these discrepant arguments and enrich the current understanding of whether and why family firms perform differently on ESG than non-family firms. Therefore, we aim to explore (1) if family firms exhibit better or worse ESG ratings than non-family firms, (2) if the unique properties of family firms materialize in a different prioritization of E, S, and G initiatives, and (3) if the extent to which a family can enforce control over the firm's behavior is decisive for their ESG rating.

We apply data from 528 public-traded corporations in the Nordic market to answer these questions. We find that family firms typically have 4% lower ESG scores than non-family firms, caused by adverse performance on three ESG category scores. Family firms will, on average, exhibit a 5% lower workforce score, 9% lower management score, and 10% lower shareholder score. Hence, families' desire to retain family control seems to run counter to the interest of internal stakeholders. Specifically, family firms underperform on diversity and inclusion requirements by typically getting a 12% lower score than non-family firms. Nevertheless, family firms show the same level of ESG engagement as non-family firms on initiatives that concern external stakeholders. Next, we find that the extent to which a family can enforce control over the firm's behavior is highly decisive for their ESG score. If the firm has a family member as CEO or the family controls the board of directors, this will reinforce the adverse effect on their ESG score. On the contrary, if the firm is founded by a family member, the ESG score is expected to rise by 8%.

We argue that in shaping their ESG engagement, family firms might prioritize maintaining family control, at least until a high risk of damaging the family's reputation changes their frame of reference. Accordingly, family firms' desire to retain control over the firm's behavior gives rise to unique agency conflicts, which limit resources available to fund ESG activities.

The remainder of the paper proceeds as follows. First, we outline our hypotheses by reviewing theory and prior literature. Second, we explain our methodology. Third, we present our results and discuss our findings. Finally, we provide an overall conclusion.

2 Research Question

In this study, we examine if public-traded family firms in the Nordic market exhibit different ESG ratings than their non-family counterparts. Hence, we propose the following research question:

Do family firms exhibit better or worse ESG ratings than non-family firms in the Nordic market?

To shed further light on the relationship between family firms and ESG performance, we answer two additional questions:

1. Do the unique characteristics of family firms materialize in a different prioritization of E, S, and G initiatives compared to their non-family counterparts?

2. Is the extent to which the controlling family owners can control and influence the firm's behavior decisive for their ESG rating?

Limitations. We only examine the governance structure of the family firms in our sample, which makes us unable to compare it with the governance structure of non-family firms. The data on family firms' internal governance is hand-collected for each firm. Thus, we acknowledge that errors may occur. ¹

¹We have hand-collected data on families' ownership stake and voting power, the number of family members on the board of directors, and if a family member is a CEO, chairman of the board, or founder of the firm. We collected our data in January 2022, and do not take into account any changes in internal governance structures after this point in time.

3 Prior Research and Hypotheses Development

3.1 Family Ownership and ESG Ratings

Previous literature has long stressed the unique properties of family firms, which appear from their joint pursuance of both business- and family goals. They are often argued to display a strong preference for non-financial goals in strategic decision-making (Faller & Knyphausen-Aufseß, 2018; Villalonga, 2018). Unlike other equity owners, families often possess significant influence over the firms' decisions through their presence as shareholders, managers, employees, and board members. This ability to enforce control over the firms' behavior reinforces their power to pursue non-financial goals. Many scholars agree that these characteristics may materialize in the firms' behavior, which may be different from the one of non-family firms that do not strive for non-financial goals (Block, 2010; Chrisman et al., 2012; Chua et al., 2015; Dick et al., 2021; Le Breton-Miller & Miller, 2006). Ultimately, this motivates us to examine whether the emphasis on specific family-orientated goals determine family firms' ESG ratings.

The Concept of Socioemotional Wealth. Socioemotional wealth (hereafter referred to as SEW) is often used to describe the non-financial value that families derive from their firms (Berrone et al., 2010; Gomez-Mejia et al., 2007; Zellweger et al., 2013). It encapsulates a variety of preferences that yield personal benefits to the controlling family. For instance, SEW includes the ability to retain family control, enhance family reputation, personal identification with the firm, prestige, autonomy, and accumulation of social capital (Block, 2010; Gomez-Mejia et al., 2007). An extension of the behavioral agency theory is often used to describe the importance of SEW for family firms (Gomez-Mejia et al., 2007). The theory implies that a firm's dominant principal will be motivated to make decisions that preserve the accumulated endowment in the firm (Berrone et al., 2012). For family firms, their primary reference point is to preserve SEW. Hence, the controlling family might even accept threats to the firm's financial health to protect their SEW in strategic decision-making (Dick et al., 2021).

SEW and ESG Engagement. Given family firms' desire to protect SEW, they

will be motivated to engage in ESG if the non-financial benefit they gain exceeds the potential cost incurred by allocating resources to ESG initiatives (Faller & Knyphausen-Aufseß, 2018). In other words, if ESG effort enables family firms to retain or even extend SEW, they might exhibit higher ESG ratings than their non-family counterparts. Several scholars agree that two SEW dimensions are particularly decisive for family firms' behavior; (1) enhance the family's reputation, and (2) retain family control and influence over the firm's behavior (e.g., Cruz et al., 2014; Dick et al., 2021). Hence, we will focus on these two dimensions to explore family firms' propensity to invest in ESG.

The most salient benefit of excessive ESG investing is to mitigate future risks and ensure wealth for future generations, as firm survival is essential for family firms (López-Perez et al., 2018). In addition, ESG investing enhances corporate reputation and creates a protection against damages to corporate brand value (Faller & Knyphausen-Aufseß, 2018). Failure of ESG effort could deter the firm's image, which would spill over to the family's image and thus compromise their SEW (Dick et al., 2021). For these reasons, family firms may tolerate the short-term costs incurred from ESG investing as they seek to achieve longevity for future generations.

However, the literature is ambiguous. It also exists arguments for why family firms may not find benefits from excessive ESG investing. Several scholars agree that families' desire to retain control is the key determinant of their behavior (Chrisman et al., 2012, Dick et al., 2021, Gomez-Mejia et al., 2007), most likely since control is prime to influence a firm's behavior and thus protect SEW. Therefore, families tend to pursue strategies to retain or enhance family control. Such strategies might enable family members to appropriate private benefit of control and thus often contradict to a high ESG rating (Dick et al., 2010). One example is limiting the number of independent board members to ensure control over the firm's resources (Anderson & Reeb, 2014), which would make them less willing to disclose their corporate governance practices (Ali et al., 2007). Other examples are using control-enhancing mechanisms to protect their voting share (Villalonga & Amit, 2006) or lack of diversity and inclusion initiatives by favoring family members in recruiting and compensation (Verbeke & Kano, 2012). Hence, families' desire to protect SEW may lead to

more selfish behavior by prioritizing family interests and thus neglecting the interest of other stakeholders (Gomez-Mejia et al., 2007).

Consistent with evidence from Rees & Rodionova (2015), we hypothesize that these arguments are predominant. In a study with similarities to ours,² they found that family firms show lower ESG ratings than non-family firms. Even if failure to initiate ESG efforts may damage firms' corporate reputations, prior research suggests that family firms have less reputational pressure to act responsibly. They are considered the most trusted form of business globally (Deephouse & Jaskiewicz, 2013; Villalonga, 2018). Hence, we argue that family firms' focus on retaining family control is more crucial than reputational deliberations. Family owners might prefer to avoid losing control over the firm's behavior until they face a high threat of damaging reputation that requires an effort to avoid loss of SEW (Dick et al., 2021). Consequently, at least a proportion of ESG activities may be perceived as value-destroying, especially since families' wealth is closely tied to the firm's financial health. Consistent with evidence from Barth et al. (2005), family firms will resist unappealing expenditures since they appreciate a stable cash flow to ensure personal wealth.

To summarize, we predict that family firms show lower ESG engagement than their non-family counterparts as they (1) have a strong desire to sustain family control, (2) can thus appropriate private benefits of control, and (3) tend to downgrade the reputational benefits of ESG engagement.

Hypothesis 1: *Family firms will exhibit lower ESG ratings than their non-family counterparts.*

3.2 The Determinants of ESG Ratings in Family Firms

Even if we predict that family firms will show lower ESG ratings than non-family firms, we acknowledge that their unique attributes may materialize in a different prioritization of E, S, and G initiatives than their non-family counterparts. We briefly review the contradictory findings from prior research to give substance to this prediction.

²Rees & Rodionova (2015) focused on CSR engagement in family firms but used an ESG rating agency to extract data on CSR disclosure practices.

Environmental Performance (E). Many scholars agree that family firms comply with environmental concerns since failure to initiate eco-friendly behavior poses a high risk of damaging brand value and corporate reputation (Berrone et al., 2010; Garcés-Ayerbe et al., 2021; Giannarakis et al., 2014). For instance, Berrone et al. (2010) find that family firms pollute less than non-family firms. Also, Dyer & Whetten (2006) find that family firms are unwilling to damage their reputation through irresponsible actions since the family's reputation is closely linked to the firm's reputation. Other researchers suggest some moderating effects, e.g., that the effect is only prominent when the firm operates in the families' local area (Craig & Dibrell, 2006). Therefore, based on the evidence, we predict that family firms' environmental performance moderates the negative effect on the ESG ratings of family firms.

Social Performance (S). This dimension accentuates firms' treatment of both internal and external stakeholders. Concerning internal stakeholders, prior research makes ambiguous arguments for how family firms treat their workforce. While some argue that family firms are eager to invest in a talented and motivated workforce since employees reflect families' lifeblood (Neckebrouck et al., 2018), others argue that investing in family employees is of greater importance relative to non-family employees (Birdthistle, 2008; Jennings et al., 2017; Matlay, 2002). Concerning external stakeholders, prior research is more consistent in their arguments. Since family firms are concerned with creating long-term value and achieving longevity for future generations, Villalonga (2018) suggests that these preferences may manifest themselves in better and longer-lived relationships with customers, suppliers, and the community. In particular, several scholars agree that family firms go beyond ESG regulations to generate proper relationships with the local community (López-Perez et al., 2018; Tsai & Goshal, 1998). The preponderance of these arguments suggests that family firms will perform well on the social dimension of ESG, yet it lacks conviction on how family firms treat their internal stakeholders. We predict that family firms' social performance is not superior to that of the non-family firms, nor is it deficient.

Governance Performance (G). Several researchers criticize the current governance practices of family firms (Bertrand & Schoar, 2006; Carney, 2005;

Rees & Rodionova, 2015). Family firms' desire to enhance control over the firm's behavior may weaken the firm's internal governance, as good governance should serve the interest of various stakeholders (Aguilera et al., 2016; Spitzbeck, 2009). For instance, the agency conflict between minor non-family owners and large family owners is often argued to be major in family firms (Berzins et al., 2018). Family firms may neglect the interest of minor non-family shareholders, as the latter rarely care about non-financial goals but aim to create financial wealth (Chua et al., 2015). If this agency conflict is present in family firms, this suggests lower ESG ratings for family firms as it contradicts the requirements of equal treatment of shareholders. On the other hand, some scholars arrive at the opposite conclusion. A limited number of papers suggest that family firms respond more to institutional pressure than non-family firms and thus actively promote best-practice governance, for instance, by a larger proportion of independent directors on their boards (Ponomareva & Ahlberg, 2016). However, as the majority of evidence suggests that the internal governance in family firms tends to be weaker than that of non-family firms, we predict that family firms' governance performance is a preminent driver for lower ESG ratings in family firms.

To summarize, we agree with Cruz et al. (2014), who suggest that SEW can be a "double-edged sword". That is, family firms abstain from certain ESG initiatives that do not aid in protecting SEW. At the same time, they display a stronger preference for ESG initiatives that correspond well to their desire to protect SEW. Consequently, we postulate the following hypothesis:

Hypothesis 2: *Family firms will prioritize ESG initiatives differently than their non-family counterparts, which will be reflected in the ESG category scores.*

3.3 The Impact of Family Involvement

There is heterogeneity among family firms, which we must address to adopt a more nuanced view of their propensity to invest in ESG. There are differences in how family firms can enforce control and shape the firm's goals, strategies, and behaviors (Villalonga & Amit, 2006). Their power to enforce control depends on the families' ownership stake, voting power, management participation, and board presence. Consistent with evidence from Gomez-Mejia et al. (2007),

we propose that high family involvement in a firm will reinforce the firm's emphasis on preserving SEW. Hence, the firm's behavior is more likely to be guided by the personal benefits of the controlling family. The rationale behind the argument is that enhancing the family's welfare is of greater importance and defines the firm's identity to a greater extent when family members are highly involved in the firm's decision-making processes (Berman et al., 1999).

It mirrors a common opinion in the literature, which often cites that shareholders will exercise their influence on a firm's decisions more effectively if the CEO or board members share similar objectives (Boyd, 1995; Conyon & Peck, 1998). It is a consequence of the verity that the manager-owner agency conflict diminishes (Berzins et al., 2008). In general, the manager-owner agency conflict is minor in family firms. Large family owners have incentives to monitor the firm's behavior even when family members are unrepresented in the management or board of directors. In turn, it ensures that the interests of managers and owners are aligned. Indeed, several scholars agree that family firms actively monitor to retain control over the firms' resources and thus might appropriate private benefits of control (Arregle et al., 2007; Dick et al., 2021). In addition, several scholars find that family firms tend to use other control-enhancing mechanisms, for example, recruiting and promoting employees whose values are closely aligned with their own (Chrisman et al., 2012).

To summarize, if family members are highly involved in the firms' decision-making processes, the emphasis on preserving SEW becomes even more dominant. In turn, it might be easier to neglect the interest of other stakeholders. Consistent with our arguments, we predict that high family involvement will reinforce the predicted negative ESG ratings for family firms.

Hypothesis 3: *A high degree of family involvement will reinforce the negative impact on ESG ratings for family firms.*

4 Research Methodology

4.1 The Sample

We have chosen to study the Nordic countries because they are often regarded as leaders when it comes to sustainability. All five Nordic countries are top-ranked both in the SDG (sustainability development goals) rankings and throughout major ESG charts (Scanlon, 2021). Thus, we can analyze a top-performing sample with homogeneous ESG legislation and requirements (Zoëga, 2011).

Our sample includes public-traded corporations in the Nordic countries, on the condition that they have an ESG score for 2021 available in the Thomson Reuters Refinitiv Eikon database. The Nordic countries consist of Norway, Sweden, Denmark, Finland, and Iceland. Unfortunately, we are excluding Iceland from our study because of the lack of firms with available ESG ratings. Finally, after excluding 70 corporations with missing financial data, our sample includes 528 firms. Of the total firms, 126 are family firms and 402 are non-family firms. Table 4.1 reports the distribution of firms within each industry and states the corresponding prevalence of family firms.³

Table 4.1: Overview of the Sample

	Total Firms	Family Owned
Consumer Staples	25	44%
Industrials	145	33%
Real Estate	29	31%
Energy	17	29%
Materials	35	23%
Communication Services	27	19%
Consumer Discretionary	53	17%
Health Care	75	17%
Information Technology	73	16%
Financials	44	14%
Utilitites	5	0%

In addition, 79 (25%) firms operate in Norway, 307 (24%) firms operate in Sweden, 65 (27%) firms operate in Denmark, and 77 (15%) firms operate in Finland. The percentages stated in parentheses represent the prevalence of family firms within each country.

³The industries are classified after the Global Industry Classification Standard (GICS).

4.2 Identifying Family Firms

We analyze the ownership structure in each of the 528 firms in our dataset to identify whether they are family-owned or not.⁴ Prior researchers are inconsistent in their guidance on how to ascertain if a firm is family-owned or not. However, by a similar approach as Maury (2005) and Faccio & Long (2002), we define a firm as family-owned if the largest owner holds 25% of the votes and is family. In the same way as Villalonga & Amit (2006), we are not limited to the individual largest owner but add all large owners representing families together. The limit of 25% ownership rights is relatively high compared to previous studies. However, most similar studies are conducted in the U.S., where ownership is rather small and dispersed. The concentration of ownership is relatively higher in the Nordic countries. Thus, the choice reflects the heterogeneity in ownership structures worldwide. Even if 25% of the votes do not match the majority, it constitutes a large enough proportion that the family holds a lot of real power in the company by virtue of being the largest owner. All votes are unlikely to be represented at general meetings, which implies that large shareholders possess a larger influence over the firm's behavior than their voting share reflects (Leech, 2002).

To qualify as a family firm, we also require that the controlling owners are individuals who are tied together by marriage or blood up to the second degree of kinship. The definition is not limited to ownership by several individual family members but also includes ownership by foundations and companies owned by a family, given that the family has majority control (>50% of votes).

4.3 Family Involvement

To recognize the substantial heterogeneity among family firms, we have gathered additional data on the internal governance structures of the family firms in our sample.⁵ We have chosen the following variables, which reflect family members' ability to control the firm's behavior and strategic choices:

⁴We identify family firms by analyzing ownership information in the Thomson Reuters Eikon database, Orbis database, each company's website, and by using proff.no, proff.se, proff.dk, proff.fi, respectively.

⁵Data on internal governance structures in family firms is gathered by manually analyzing Investor Relations and Corporate History on each company's website.

- (i) CEO is a family member.
- (ii) Family presence on the board of directors.⁶
- (iii) Chairman of the board is a family member.

We also argue that two more variables should be included in our analysis:

- (iv) Firm is founded by a family member of the controlling family.
- (v) The family's name is represented in the firm's name.

The two latter variables address the concern that family involvement does not address goal differences among families (Chrisman et al., 2012; Gomez-Mejia et al., 2007; Zellweger et al., 2011). Hence, the motivation for our choices is that variable (iv) reinforces family members' identification with the firm and thus their motivation to pursue SEW (Deephouse & Jaskiewicz, 2013). In addition, variable (v) has a symbolic effect that increases families' incentive to enhance corporate reputation (Dyer & Whetten, 2006; Zellweger et al., 2011).

The five governance variables are often highly correlated with the percentage of ownership held by a family (Berrone et al., 2010). Indeed, since we employ a higher requirement to qualify as a family firm than the benchmark in prior studies, only 9.5 % of the firms in our dataset hold equity ownership without any family control. Table 4.2 reports the frequency of the governance variables in our dataset.

Table 4.2: Frequency of Governance Variables

	Yes	No
Family CEO	14	112
Family Chairman of the Board	53	73
Family Presence on Board	109	17
Family Founder	41	85
The Family's Name in the Firm's Name	25	101
Average Family Presence on the Board	20.1%	
Average Family Ownership Stake	53.3%	

⁶The proportion of family members on the board expressed as a percentage of total board size.

4.4 Dependent Variables

We use the total ESG score for 2021 as our dependent variable in our regression models, as well as the ten category scores that makes up the total ESG score. We obtain all scores from the Thomson Reuters Refinitiv Eikon database. The scores range between 0 and 100, reflecting each company’s ESG commitment, effectiveness, and performance. The category scores are divided between the three ESG pillars in the following way (Refinitiv, 2022):

Table 4.3: ESG Category Scores

Environmental	Social	Governance
Emissions score	Community score	CSR strategy score
Innovation score	Human rights score	Management score
Resource Use score	Product responsibility score	Shareholder score
	Workforce score	

A detailed description of each category score is available in Appendix A1 (Table A1.1).

4.5 Control Variables

We include five control variables in our regression models to control for firm and industry-specific effects. They represent common predictors of ESG performance confirmed by prior research. In this way, we are able to strengthen the validity of our results by avoiding biased estimates.

We control for firm size, financial performance, debt in capital structure, and market-based performance. We measure these effects by the natural logarithm of the book value of assets, ROA, leverage, and price-to-book ratio, respectively. In addition, we control for board size, as prior research suggests that it is necessary for ESG studies like ours to measure board governance (Giannarakis, 2014; Said et al., 2009).

We run a t-test to check whether the financial characteristics of family firms are significantly different from those of non-family firms (Table 4.4). The result suggests that family firms typically have fewer assets and higher leverage. This corresponds well to evidence found by prior scholars. Family firms tend to be smaller and tend to finance projects with debt since they are unwilling to issue

equity that brings their ownership stake down (Berzins et al., 2018). Hence, we conclude that the firms included in our study reflect the characteristics of the actual population of family firms and non-family firms in the Nordic market.

Table 4.4: T-test for Control Variables

Total Assets	ROA	Leverage	Board Size	P/B
0.069	0.171	0.094	0.491	0.343

4.6 Analytical Procedure

Hypothesis 1. For hypothesis 1, we perform an ordinary least squares regression (OLS) analysis with the total ESG score of 2021 as the dependent variable. We control for firm-specific and industry-wide effects.

Hypothesis 2. For hypothesis 2, we replace the dependent variable with the ten different category scores. Otherwise, the regressions are equal to the one used to test hypothesis 1. We write out the regression models used to test hypotheses 1 and 2 like this:

$$\text{ESG scores}_i = \beta_0 + \beta_1 \text{FamilyFirm}_i + \beta_2 (\text{ControlVariables}_i) + \beta_3 (\text{IndustryDummies}) + \epsilon_i$$

Hypothesis 3. For hypothesis 3, we perform OLS dummy regressions using the subset of family firms. We first use the total ESG score as the dependent variable, then we replace it with the ten different category scores. We use the governance variables as our independent variables. Hence, we write out the regression model like this:

$$\text{ESG scores}_i = \beta_0 + \beta_1 \text{FamilyOwnershipStake}_i + \beta_2 \text{FamilyCEO}_i + \beta_3 \text{FamilyPresenceOnBoard}_i + \beta_4 \text{FamilyChairman}_i + \beta_5 \text{FamilyFounder}_i + \beta_6 \text{FamilyFirmName}_i + \epsilon_i$$

Regression Diagnostics. We have checked all five conditions underlying the OLS to ensure the appropriateness of our models. First, the variance inflation factor (VIF) confirms that all estimations are free of multicollinearity bias.

Second, the Breusch-Godfrey test finds no signs of autocorrelation. Third, the Breusch-Pagan test for heteroscedasticity finds no evidence for heteroscedasticity in regressions used to test hypotheses 1 and 3. However, we find signs of heteroscedasticity in some of the regressions used to test hypothesis 2. We use White's heteroscedasticity consistent standard errors to address this concern. Further, by inspecting plots, we find no signs of patterns in the estimated residuals. Hence, the linearity assumption is satisfied. Finally, the normality assumption is also satisfied by inspecting the plots. We report all tests in Appendix A2 (Tables A2.1, A2.2 and A2.3).

The highest threat for severe multivariable problems is present in the regression used to test hypothesis 3, as the six governance variables may be highly correlated (Berrone et al., 2010). Even if the VIF values disprove this concern, we investigate further by reporting the correlation coefficients between the independent variables used in the respective model (Appendix A3, Table A3.1). The highest bivariate correlation is between the two predictors family founder and family firm name, with a correlation coefficient of 0.668. The second highest bivariate correlation is between family presence on the board and family chairman of the board, with a correlation coefficient of 0.558. None of the other variable pairs correlate high enough to suspect (severe) multicollinearity. Scholars often argue that the critical value for the correlation coefficient is 0.8 (e.g., Gujarati, 2009). Even if the correlation coefficients satisfy this criterion, we address the concern by performing the regressions several times. We omit a predictor highly correlated with another predictor each time. We find evidence to disprove the concern of multivariate problems. The results remain stable and thus will not interfere with our interpretation.

5 Results and Discussion

5.1 Descriptive Statistics

Table 5.1 shows the mean and median values for the ESG score, broken down by family and non-family firms. Family firms have an average ESG score of 42.9, while non-family firms have an average ESG score of 47.2. The median ESG scores points in the same direction, with a median score of 44.3 and 47.9, respectively. Hence, family firms typically exhibit lower ESG scores than their non-family counterparts. A t-test finds that the difference is significant with a p-value of 0.09. Additionally, Table 5.1 shows the differences in ESG scores between family and non-family firms within each industry. To check whether these differences are significant, we have used a Mann-Whitney U-test.⁷ The result suggests that the most prominent difference in ESG scores between family and non-family firms is in the financials, materials, and real estate industries. Family firms have, on average, 16.8 points lower ESG scores in the financial industry, 12.7 points lower ESG scores in the materials industry, and 10.4 points lower ESG scores in the real estate industry.

Note that the order of the industries is not random but reflects their overall performance on ESG in descending order, confirmed by checking all firms' mean and median values within each industry. The Tuckey letter display on the right side of the table shows which industries perform significantly differently from each other on ESG, revealed by running an ANOVA test. The industries not carrying the same letter are significantly different from each other.

⁷Mann Whitney U-test is used since the variables (ESG scores for family firms and ESG scores for non-family firms) are not normally distributed. All other conditions required to use the test are also satisfied.

Table 5.1: ESG Scores for Firms within each Industry

	Family Firms		Non-family Firms		p-value	Tuckey
	Mean	Median	Mean	Median		
Consumer Staples	58.5	57.1	62.1	61.3	0.64	a
Materials	43.1	35.9	55.8	67.0	0.09	abc
Consumer Discretionary	54.1	61.7	51.8	54.4	0.32	ab
Utilities	NA	NA	51.7	49.3	NA	abcd
Energy	55.8	54.5	55.8	45.7	0.30	abcd
Communication Services	41.9	34.55	50.1	51.9	0.38	abcd
Financials	33.2	26.9	50.0	48.6	0.05	abcd
Real Estate	39.7	32.8	50.1	52.4	0.08	abcd
Industrials	43.3	43.6	43.3	47.4	0.15	bcd
Health Care	40.3	46.2	39.6	37.1	0.40	cd
Information Technology	33.0	40.1	40.1	38.7	0.16	d
Overall ESG score	42.9	44.3	47.2	47.9	0.09	

By the same approach, Table 5.2 reports the mean and median values of the ESG scores for family firms and non-family firms within each country. The result suggests that the most prominent difference in ESG scores between family firms and their non-family counterparts is in Finland and Denmark. Family firms in Finland have, on average, 12.3 lower ESG scores than non-family firms, while family firms in Denmark have 10.9 lower ESG scores than non-family firms.

Table 5.2: ESG Scores for Firms within each Country

	Family Firms		Non-family Firms		p-value	Tuckey
	Mean	Median	Mean	Median		
Finland	47.8	51.3	54.7	60.1	0.08	a
Denmark	44.1	44.5	53.2	55.0	0.06	a
Norway	43.9	46.3	49.4	47.4	0.79	ab
Sweden	42.8	42.8	43.3	43.1	0.86	b

Furthermore, Table 5.3 shows the effect on the ESG scores if the family is highly involved in the firm's decision-making processes versus less involved in the decision-making processes. First, we notice that if the family firm has a family member as CEO, the average ESG score is approximately 14 points lower than if the CEO is a family outsider. Second, if the firm is founded by a family

member of the controlling family, the ESG score is on average 7.2 points higher. Third, whether a family member is chairman of the board does not seem to determine their ESG score. The same holds for the predictor family's name in the firm's name. More interestingly, whether the firm is majority-owned by a family or not does not seem to have a remarkable influence on the ESG score.

Table 5.3: ESG Scores for Different Governance Structures

	Mean	Median	Max	Min
Family CEO	29.2	30.5	57.6	8.1
External CEO	43.8	45.6	82.6	7.3
Family Founder	48.6	51.7	78.2	8.9
External Founder	41.4	39.9	83.4	11.2
Family Chairman of the Board	41.2	46.9	75.0	11.5
External Chairman of the Board	46.9	46.9	93.4	9.6
Family Firm Name	46.1	50.9	76.5	7.9
Other Firm Name	46.3	46.0	93.4	12.3
Board Control Below 1/3	47.3	47.5	93.1	8.7
Board Control Above 1/3	34.9	36.2	71.8	8.4
Ownership Votes Above 50%	44.2	44.7	82.6	7.3
Ownership Votes Below 50%	42.9	45.6	75.0	8.4

Finally, correlation matrices for all relevant variables are available in Appendix A3 (Table A3.1, A3.2, and A3.3).

5.2 Family Ownership and ESG Ratings

Table 5.4 reports the results from the regression models used to test hypothesis 1, which predicted that family firms exhibit lower ESG ratings than their non-family counterparts.

Table 5.4: OLS Regressions for Hypothesis 1

	<i>Dependent variable:</i>	
	ESG score (1)	ESG score (2)
Family Firm	-0.041** (0.015)	-0.046** (0.103)
Total Assets	0.063*** (0.005)	0.073*** (0.005)
Leverage	-0.127*** (0.034)	-0.017 (0.034)
Board Size	0.026*** (0.003)	0.016*** (0.003)
ROA	0.1305** (0.139)	0.113 (0.134)
P/B	0.002 (0.001)	0.016 (0.001)
Constant	-1.06*** (0.123)	-
Industry Dummy	No	Yes
Observations	528	528
Adjusted R ²	0.515	0.932
Std. Error	0.153	0.146
F Statistic	77.387***	344.4***
<i>Note:</i>	*p<0.1; **p<0.05; ***p<0.01	
	<i>Control variables are winsorized at 2.5% level</i>	

Indeed, we find evidence that family firms are associated with lower ESG scores than non-family firms at a 5% significant level. In model 1, we only control for firm-specific effects. We find that ESG scores are typically 4.1 points lower in family firms. In model 2, we also consider that ESG scores may systematically differ between industries. The result confirms that the adverse ESG scores for family firms are not only present in specific industries but rather an overall effect. The negative coefficient of 4.6 points translates to a very similar impact, i.e., family ownership would cause a decline in a firm's ESG score by approximately 4%. Even if not reported, we also controlled for

country-fixed effects by including country dummies. The result confirmed that the adverse ESG scores for family firms are an overall effect in the Nordic market, even if Table 5.2 suggests that the effect is most prominent in Finland and Denmark.

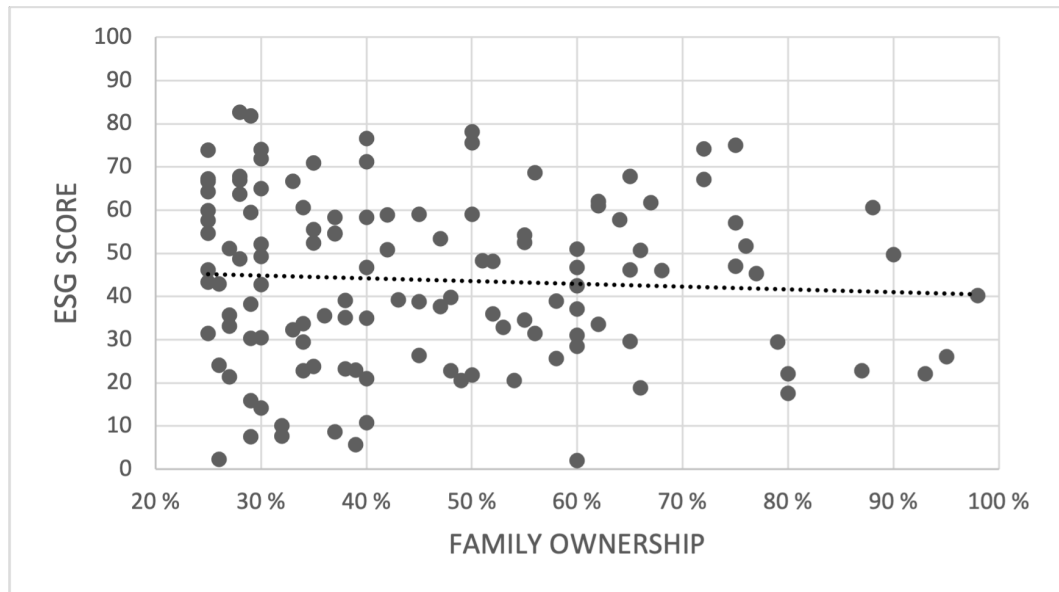
Total assets, our proxy for firm size, is positively associated with ESG scores with a coefficient of 0.063. The evidence is as expected. Large firms have more resources to expand and tend to experience more public scrutiny, or better ESG ratings reflects their capacity to generate good sustainability reports (Crace & Gehman, 2022). Next, leverage is negatively associated with ESG scores with a coefficient of -0.127. Model 2 confirms that this is an industry-wide effect. Our evidence suggests that real estate and financials are the two industries that tend to have higher leverage and thus lower ESG ratings. Industries with high leverage are prone to induce agency costs of debt and financial distress, limiting resources available to fund ESG activities. Finally, board size positively correlates with ESG scores with a coefficient of 0.016. This evidence is consistent with the ones from Said et al. (2009). They suggest that large boards exercise better monitoring and share a broader exchange of innovative ideas and experience, making firms more likely to engage in ESG.

The empirical evidence suggests that the complex nexus of family goals and business objectives in family firms may influence their propensity to invest in ESG initiatives. Even if the family firms tend to be smaller and have higher leverage (Table 4.4), their ESG ratings are not only dependent on these financial characteristics. The family firm dummy is still significant at a 5% level. Consistent with our theoretical arguments when developing our first hypothesis, we argue that family firms' desire to retain family control may materialize in adverse ESG scores. Families can appropriate private benefits of control and neglect other stakeholders' interests. However, we cannot suggest which type of personal benefits families may appropriate from their firms. This supports the necessity further to investigate how family firms prioritize their ESG initiatives, which we will do when we examine the results from hypothesis 2.

Family Ownership Stake. Figure 5.1 provides the trend line of a plot on family ownership stake and ESG score for all family firms in our sample. As ascertained

by figure 5.1, we find no evidence that a higher percentage of family ownership reinforces the adverse impact on the ESG scores for family firms.

Figure 5.1: A plot of Family Ownership Stake and ESG Score



The evidence contradicts the ones of Rees & Rodionova (2015) and Berrone et al. (2010). However, we employ a higher ownership stake as the minimum requirement to qualify as a family firm compared to the benchmark in previous studies. Thus, the family owners are more likely to possess more real power in the firm, ascertained by the fact that 91,5% of the family firms in our sample can influence firm decisions through involvement in management or on the board of directors. Hence, the extent to which they can enforce control over the firms' behavior seems to play a more crucial role in determining their ESG ratings. This evidence supports the necessity further to investigate the internal governance structure of family firms, which we will do when examining the results from hypothesis 3.

5.3 The Determinants of ESG Ratings in Family Firms

Table 5.5 reports the results from the ten regression models used to test hypothesis 2, which predicted that family firms prioritize ESG activities differently than non-family firms. We expected this to materialize in the ten ESG category scores. After controlling for firm-specific and industry wide-effects, we find evidence that aligns with our prediction. Notably, the decline in ESG ratings for family firms is driven by adverse performance in the workforce, management, and shareholder scores. If the firm is family-owned, it will typically cause a decline of approximately 5% in the workforce score, 9% in the management score, and 10% in the shareholder score. For the other category scores, we find no evidence that family firms exhibit different ESG ratings than non-family firms. Hence, when decomposing the total ESG ratings, we find causality in the same direction as for hypothesis 1. It strengthens the robustness of our evidence.

Note that the regressions 1-10 on the next page have the following dependent variables:

- | | |
|-----------------------------------|---|
| (1) <i>Emission score (E)</i> | (6) <i>Product responsibility score (S)</i> |
| (2) <i>Innovation score (E)</i> | (7) <i>Workforce score (S)</i> |
| (3) <i>Resource use score (E)</i> | (8) <i>CSR strategy score (G)</i> |
| (4) <i>Community score (S)</i> | (9) <i>Management score (G)</i> |
| (5) <i>Human rights score (S)</i> | (10) <i>Shareholder score (G)</i> |

Table 5.5: OLS Regressions for Hypothesis 2

	<i>Dependent variable:</i>									
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Family Firm	-0.010 (0.024)	0.006 (0.029)	-0.037 (0.026)	0.007 (0.026)	0.027 (0.030)	-0.038 (0.029)	-0.048** (0.021)	-0.014 (0.023)	-0.095*** (0.024)	-0.102*** (0.029)
Total Assets	0.082*** (0.007)	0.061*** (0.008)	0.079*** (0.007)	0.068*** (0.007)	0.070*** (0.008)	0.029*** (0.008)	0.052*** (0.006)	0.091*** (0.007)	0.060*** (0.007)	0.008 (0.008)
Leverage	-0.010 (0.047)	-0.055 (0.055)	-0.108** (0.049)	-0.178*** (0.050)	-0.132** (0.058)	-0.212*** (0.055)	-0.061 (0.040)	-0.096** (0.045)	-0.186** (0.047)	-0.038 (0.055)
Board Size	0.016*** (0.005)	0.005 (0.006)	0.023*** (0.006)	0.020*** (0.006)	0.022*** (0.007)	0.028*** (0.006)	0.018*** (0.005)	0.021*** (0.005)	0.021*** (0.005)	-0.005 (0.006)
ROA	0.252*** (0.084)	0.031 (0.100)	0.195** (0.089)	0.116 (0.089)	0.210** (0.104)	0.125 (0.100)	0.020 (0.072)	0.216*** (0.081)	0.011 (0.084)	-0.058 (0.100)
P/B ratio	0.001 (0.002)	0.001 (0.002)	0.0003 (0.002)	-0.001 (0.002)	0.003 (0.002)	-0.002 (0.002)	0.003* (0.002)	-0.001 (0.002)	-0.001 (0.002)	0.004 (0.002)
Constant	-1.368*** (0.123)	-1.028*** (0.145)	-1.365*** (0.130)	-1.099*** (0.130)	-1.113*** (0.152)	-0.281* (0.146)	-0.647*** (0.105)	-1.614*** (0.118)	-0.791*** (0.123)	0.404*** (0.146)
Industry Dummy	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	528	528	528	528	528	528	528	528	528	528
Adjusted R ²	0.429	0.172	0.392	0.297	0.270	0.131	0.295	0.494	0.287	0.020
Std. Error	0.235	0.279	0.249	0.251	0.292	0.280	0.202	0.227	0.236	0.280
F Statistic	66.928***	19.203***	57.727***	38.159***	33.482***	14.248***	37.666***	86.758***	36.317***	2.799**

Note: *p<0.1; **p<0.05; ***p<0.01

The initial evidence from hypothesis 1 suggested that family firms tend to be guided by private benefits, not reconciling with certain ESG activities. However, we could not suggest which types of private benefits they may appropriate from their firms. Now, with new evidence, we can discuss the private benefits that could exist in family firms. We did expect a negative effect on shareholder score (G) and management score (G) for family firms since prior researchers have criticized the current governance practice of family firms (Bertrand & Schoar, 2006; Carney, 2005; Rees & Rodionova, 2013). Therefore, we will first propose the economic intuition behind these findings.

Shareholder Score (G). The shareholder score consists of two different components; the firm's ability to treat all shareholders equally and the firm's use of takeover defenses (Refinitiv, 2022). For the former component, our evidence suggests that the agency conflict between minor non-family shareholders and family shareholders is major in family firms. Large family owners may expropriate the interest of non-family shareholders, making decisions that benefit themselves and thus aid in protecting SEW. For the latter component, our evidence suggests that family firms are more likely to deploy control-enhancing mechanisms to deter takeovers. Justified by the implication of the behavioral agency theory, family firms' desire to protect SEW is predominant. Even if takeovers may result in prospective financial wealth (Campbell et al., 2007), they will resist takeovers as it may lead to loss of family control and dilution of the family firm's identity. Consequently, the adverse shareholder score for family firms propounds that they may have a detrimental impact on their shareholders.

Management Score (G). The management score reflects the companies' commitment and effectiveness in following best governance principles. It assesses firms' compliance with independency, diversity, committees, and compensations (Refinitiv, 2022). Consistent with evidence from Rees & Rodionova (2015), we suggest that family firms forego management improvements to retain family control. We give two arguments that provide support for this suggestion. First, family firms are often argued to select and promote decision-makers based on the potential they bring to sustain the family's culture and prevailing norms (Singal & Gerde, 2015). Ultimately, they may be reluctant to embracing diversity

initiatives. For instance, they may favorite family members in recruiting processes for top positions, regardless of the competence and skills they bring to the company. Second, one should expect that compensations for executives in non-family firms are higher than in family firms. Consistent with agency theory, compensations are a remedy for agency conflicts. Since the manager-owner agency conflict is minor in family firms, high management compensations are against its purpose. Even if this is probably true, our evidence mirrors a common opinion in the literature; the compensation structure in family firms is unevenly distributed (Samara et al., 2018). We suggest that family altruism may lead to a desire for family enrichments (Chua et al., 2015; Jaskiewicz et al., 2017), leading to asymmetric treatment of firm insiders. Consequently, family firms' power to influence the internal governance structure of their firms may lead to a decline in their management scores.

Workforce Score (S). Furthermore, it is interesting that family ownership would cause a decline in the workforce score by 5%, as prior research shares divided empirical evidence for how family firms treat their workforce. Indeed, this suggests the necessity to examine the underlying forces and provide evidence from the Nordic market. Therefore, Table 5.6 report the results from a regression using interaction terms between the family firm dummy variable and the four subcategories that constitutes the total workforce score.⁸

We find that family ownership would cause a decline in the diversity and inclusion score by 12%. On the other subcategories, we find no evidence that family firms underperform. Due to missing data, the statistical power of the regression may be reduced and thus produce biased estimates.⁹ Despite this, the evidence gives substance to proposing an economic argument.

The workforce score assesses the firms' commitment to taking equal care of the employees (Refinitiv, 2022). The adverse workforce score for family firms strengthens the arguments provided for the management score; at least some asymmetric treatment of family insiders (management and employees) exists in family firms. With SEW as the main frame of reference for family firms,

⁸Women employees are the proxy for diversion and inclusion. Average training hours are the proxy for career development and training. Trade union representation is the proxy for working conditions. Lost working days are the proxy for health and safety (Refinitiv, 2022).

⁹150 observations are removed from the regression due to NA.

Table 5.6: OLS Regression on the Workforce Category Score

	<i>Dependent variable:</i>
	Workforce Score
Diversity and Inclusion*Family Firm	-0.12** (0.005)
Working Conditions*Family Firm	0.07 (0.006)
Career Development*Family Firm	0.04 (0.002)
Health and Safety*Family firm	-0.07 (0.005)
Constant	0.567*** (0.140)
Observations	378
Adjusted R ²	0.491
Residual Std. Error	0.104
F Statistic	3.357**

Note: *p<0.1; **p<0.05; ***p<0.01

distrust may arise of those outside the family circle (Jennings et al., 2017). Thus, nepotism may lead to inappropriate staffing decisions or favoritism of family members. For instance, in case of necessary downsizing, the practice in family firms may be socially irresponsible. In particular, scholars have found that family members are unlikely to be dismissed (Samara & Arenas, 2017; Verbeke & Kano, 2012). If so, family firms will undermine the ESG requirements of fair treatment and no discrimination, which corresponds to displaying a lower workforce score than non-family firms. Nevertheless, family firms perform similarly to non-family firms on requirements for working conditions, career development, and health and safety (Table 5.6). It might suggest that family owners invest time and resources in introducing employees to the prevalent norms and values of the firms (Samara & Arenas, 2017) or just that they are eager to invest in a talented workforce and want to prevent loss of human capital.

Theoretical Implications. Based on our evidence from hypothesis 2, family firms are less likely to adopt ESG initiatives that concerns internal stakeholders of

their firms (shareholders, management, and their workforce). Consistent with evidence from Anderson & Reeb (2003), principal-principal agency conflicts between family insiders and outsiders may exist. The family members are the dominant principal, who can extract private benefits at the expense of non-family members. Examples of private benefits are expropriation of non-family shareholders, nepotism, favoritism, diversion, and management entrenchment. The private benefit consumption is an auxiliary to maintain family control and thus preserve SEW. We agree with a common opinion in the literature; families' desire to retain control might be the critical determinant of their behavior (Chrisman et al., 2012, Dick et al., 2021, Gomez-Mejia et al., 2007). In turn, agency conflicts hinder effective decision-making and limit the financial resources available to fund ESG activities.

However, we support the proposal that SEW can be a “double-edged sword” (Cruz et al., 2014). None of the category scores that deal with external stakeholders have a significant family dummy variable.¹⁰ Hence, family firms show the same level of ESG engagement related to external stakeholders as non-family firms. Even if they abstain from ESG activities threatening family control, they comply with ESG requirements that pose the highest threat of damaging the family's reputation. For instance, initiating eco-friendly behavior, respecting human rights conventions, and ensuring safety and health in society are essential factors to having the license to operate. Thus, firms that fail to initiate such behavior risk damaging their legitimacy and reputation (Berrone et al., 2010; Garcés-Ayerbe et al., 2021; Giannarakis et al., 2014). We argue that the risk of losing SEW is too significant to avoid complying with such requirements. Nevertheless, it does not imply superior performance compared to non-family firms. Adopting such behavior beyond regulatory compliance requires large investments, which may come at the expense of their private benefits. It is, however, surprising that the community score for family firms does not reflect superior performance. Other scholars have found that family firms tend to be very committed to the local community (Niehm et al., 2008; Fitzgerald et al., 2010; Tsai & Goshal, 1998). Nevertheless, it might be that

¹⁰Emission score, innovation score, resource Use score, community score, human rights score, product responsibility score, and CSR strategy score addresses compliance to demands from external stakeholder (see Appendix A1 for a description of the category score).

family firms think they care more about the local community, even if they, in reality, do not care more than other firms. Otherwise, it might only be valid for private firms that more often work and live in the same area (Craig & Dibrell, 2006).

5.4 The Impact of Family Involvement

Table 5.7 reports the results from the first regression model used to test hypothesis 3, which predicted that a higher degree of family involvement reinforces the adverse ESG scores for family firms.

Table 5.7: OLS Regression for Hypothesis 3 (ESG Score)

<i>Dependent variable:</i>	
ESG score	
Family Votes	-0.006 (0.019)
Family CEO	-0.193*** (0.054)
Family Chairman	-0.038 (0.034)
Presence on Board	-0.387*** (0.145)
Family Founder	0.089* (0.043)
Family Firm Name	-0.027 (0.050)
Constant	0.518*** (0.035)
Observations	126
Adjusted R ²	0.157
Std. Error	0.179
F Statistic	4.578***

Note: *p<0.1; **p<0.05; ***p<0.01

As expected, an increase in family ownership stake does not significantly influence the ESG rating. However, the extent to which the controlling family can exert significant influence over the firm's behavior is highly decisive for

their ESG ratings.

We find that if the CEO is a family member of the controlling family, this will typically cause a decline in ESG score by approximately 19%. Similarly, the extent to which the family can control the board has an adverse effect on the ESG score. For instance, if the family controls 1/5 of the board, this will typically cause a decline in the ESG score by $-0.387 \times 0.20 = 7.7$ points. While if the family controls 1/3 of the board, this will typically cause a decline in the ESG score by 12.7 points. More precisely, the average ESG rating is negatively affected by 3.87% for every 10% increase in family presence on the board. On the contrary, the ESG score is expected to rise by approximately 8% if the firm is founded by a member of the controlling family.

Even if not reported, we perform the regression several times to address the possibility of multivariate problems, which is necessary since the governance variables employed often possess a high threat of multicollinearity (Berrone et al., 2010). Since the predictor family chairman of the board is insignificant, we omit it from the regression (correlation coefficient with family presence on the board is 0.558). The same holds for the predictor family's name in the firm's name (correlation coefficient with family founder 0.668). In doing so, we ensure that the other variables retain their significance. Eventually, the results remain stable and thus will not interfere with our interpretation. Therefore, we will review all significant variables to provide an economic argument.

Family CEO. Our evidence is consistent with the implications of the agency theory. The manager-owner agency conflict diminishes when the CEO is a family member. The core of the problem is directly addressed by narrowing the separation between ownership and daily control (Berzins et al., 2018). Hence, family owners will exercise their influence on the firm's daily operations more effectively. In turn, we argue that the emphasis on preserving SEW becomes more dominant. This will reinforce the family firms' desire to retain family control and thus their ability to appropriate private benefits, which again reinforces the adverse effect on family firms' ESG ratings.

Family Presence on the Board. Even if the CEO is not a family member, our evidence suggests that family firms have unique prerequisites to ensure

alignment of interest between decision-makers and the controlling family. It agrees well with prior research, which often argues that family firms actively monitor to retain private benefits (Arregle et al., 2007). Monitoring is efficient in family firms. Even if they pay the cost of monitoring, their ownership stake is large enough to extract a high enough proportion of the benefit from improvements. In family firms, the benefit refers to the preservation of SEW. Thus, we argue that monitoring is an auxiliary to pursue family-centered goals.

Family Founder. Interestingly, other scholars have also found that whether the firm is founded by a family member or acquired at a later stage by a family matter for the firm's performance (e.g., Berrone et al. 2012; Bingham et al. 2011; Block & Wagner, 2013; Dick et al., 2021; Mishra et al., 2001) Consistent with our findings, we argue that family-founded firms are positively associated with ESG ratings since the family's desire for a transgenerational vision increases. Consistent with evidence from Bingham et al. (2011), longevity for future generations is usually initiated and perpetuated by the founder. For such firms, firm survival is paramount (Dyer & Whetten, 2006). Therefore, they comply with pressure from external stakeholders since it amplifies the chances of transferring a well-reputed and long-term orientated business to future generations. On the other hand, firms acquired by a family at later stages are more likely to comply with ESG initiatives that offers a "low-hanging fruit" opportunity (Rees & Rodionova, 2013). It is more likely that these firms are short-term investment objects for the family. Alternatively, if it is a long-term investment, the family's identity will not be as closely tied to the firm's identity as for family-founded firms (Berrone et al., 2012). In such cases, they may appreciate a stable cash flow to sustain a privileged lifestyle and ensure personal wealth (Barth et al., 2005) and oppose excessive ESG investing, if it does not yield private benefits.

To strengthen the robustness of our results, we run a final regression to analyze the importance of internal governance for each of the ten category scores. The regression results are presented in Table 5.8. The empirical evidence provides highly robust results, as we find causality in the same direction as for hypothesis 2. To exemplify, we find that founder-controlled family firms typically exhibit 18.7% higher emission scores, 13.6% higher resource use scores, and 13.7%

higher human rights scores than other family firms. Hence, the expected rise in ESG ratings for founder-controlled family firms holds for ESG initiatives that deal with external stakeholders of crucial importance for maintaining the family's reputation. Thus, both family-founded firms and other family firms tend to downgrade ESG initiatives that affect internal stakeholders.

Note that the regressions 1-10 on the next page have the following dependent variables:

- | | |
|-----------------------------------|---|
| (1) <i>Emission score (E)</i> | (6) <i>Product responsibility score (S)</i> |
| (2) <i>Innovation score (E)</i> | (7) <i>Workforce score (S)</i> |
| (3) <i>Resource use score (E)</i> | (8) <i>CSR strategy score (G)</i> |
| (4) <i>Community score (S)</i> | (9) <i>Management score (G)</i> |
| (5) <i>Human rights score (S)</i> | (10) <i>Shareholder score (G)</i> |

Table 5.8: OLS Regressions for Hypothesis 3 (Category Scores)

	<i>Dependent variable:</i>									
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Family Votes	0.014 (0.030)	0.007 (0.030)	0.009 (.032)	0.058 (0.032)	0.023 (0.032)	0.014 (0.033)	-0.005 (0.024)	0.035 (0.032)	-0.029 (0.027)	-0.038 (.029)
Board Presence	-0.488* (0.222)	-0.573* (0.227)	-0.439 (0.237)	-0.307 (0.236)	-0.633*** (0.238)	-0.681** (0.246)	-0.502** (0.177)	-0.534 (0.239)	-0.293 (0.203)	0.041 (0.219)
Family CEO	-0.266*** (0.083)	-0.085 (0.085)	-0.231* (0.089)	-0.206* (0.088)	-0.275** (0.089)	-0.257** (0.092)	-0.209** (0.066)	-0.216* (0.089)	-0.117 (0.076)	-0.085 (0.082)
Family Founder	0.187** (.065)	0.089 (0.067)	0.136** (.070)	0.076 (0.070)	0.137** (0.070)	0.033 (0.072)	0.082 (0.052)	0.116 (0.070)	0.046 (0.060)	0.031 (0.065)
Family Firm Name	-0.031 (0.077)	-0.038 (0.079)	-0.108 (0.082)	-0.023 (.082)	-0.105 (0.082)	0.004 (0.085)	-0.036 (0.061)	0.052 (.083)	0.002 (0.070)	0.005 (0.076)
Family Chairman	-0.047 (0.052)	-0.051 (0.053)	-0.046 (0.056)	-0.016 (0.056)	0.012 (0.056)	-0.050 (0.058)	-0.010 (0.041)	0.007 (0.056)	-0.007 (0.048)	-0.135 (0.052)
Constant	0.522 *** (0.054)	0.374*** (0.055)	0.486*** (0.057)	0.448*** (0.057)	0.634*** (0.058)	0.587* (0.059)	0.618*** (0.043)	0.442*** (0.058)	0.525*** (0.049)	0.514*** (0.053)
Observations	126	126	126	126	126	126	126	126	126	126
Adjusted R ²	0.153	0.046	0.087	0.045	0.129	0.098	0.124	0.076	0.014	0.034
Std. Error	0.273	0.279	0.291	0.291	0.293	0.280	0.218	0.294	0.250	0.273
F Statistic	4.525**	2.984**	2.636**	1.82	3.752**	3.024**	3.865**	2.524*	1.30	1.62

Note: * p<0.1; ** p<0.05; *** p<0.01

Theoretical Implications. In the discussion after reporting the result from hypothesis 2, we proposed that principal-principal conflicts exist between family insiders and outsiders in family firms. It becomes especially evident when family members are heavily involved in the firm's decision-making processes. Early studies on agency theory suggested that agency conflicts in family firms are non-exciting (e.g., Jensen & Meckling, 1976), especially since ownership and control overlap and concentration of ownership give monitoring advantages. Indeed, our evidence confirms that the traditional manager-owner agency problem may be minor in family firms (Berzins et al., 2018) and that family firms may actively monitor the firm's behavior. Over decades, scholars have then suggested that the possibility of opportunistic behavior of the family principals is very low (Li & Zuo, 2020). However, our evidence comes in defense of more recent research on agency theories. The existence of family members within the governance structure gives rise to unique agency challenges, which distinguishes family firms from the broader corporate landscape (Li & Zuo, 2020). From this agency perspective, strong family involvement reinforces the families' ability to appropriate private benefits of control and neglect the interest of other internal stakeholders (Chrisman et al., 2012). Many scholars agree that this is especially evident for public-traded firms (Villalonga & Amit, 2006). We argue that the focus on preserving SEW is dominant in the absence of other control mechanisms and thus harms the purpose of the governance function. In other words, high presence of family outsiders in a firm may be vital to engaging in E, S, and G activities. Family outsiders can offer an external and objective point of view.

5.5 Endogeneity Issues

We acknowledge that our findings, and the corresponding interpretation, are only accurate if endogeneity issues do not threaten the models. We put forth three arguments for why endogeneity issues may exist in our models. First, we may face selection bias. Due to the limited availability of ESG ratings in the Thomson Reuters Eikon Refinitiv database, we cannot establish an entirely random selection process (Stock & Watson, 2015). Hence, we cannot ensure that our sample represents the total population of firms in the market. Second, we only use data for 2021. The lack of ESG ratings over a longer time horizon makes us unable to check for time-fixed effects. In turn, this can induce biased estimates. However, we alleviate parts of the problem by checking for industry-fixed effects and country-fixed effects. Third, we may face omitted variable bias if critical explanatory variables are excluded from our model or if they are incorrectly specified. However, we alleviate parts of the problem by including control variables based on empirical evidence from prior research (Fischer & Sawczyn, 2013).

6 Conclusion

This master thesis started by highlighting the competing arguments and conflicting results linking ESG to family firms. Our objective was to reconcile the discrepant findings and extend prior research. To our best knowledge, the determinants of ESG ratings in family firms have not been analyzed holistically until now. Hence, by drawing on the concept of SEW, our study improves the overall comprehension of the topic. We demonstrate how family firms' desire to protect SEW can affect their propensity to invest in ESG.

Le Breton-Miller & Miller (2014) did suggest that future researchers should address SEW's positive and negative outcomes. We can respond to this proposal. At first glance, family firms seem to be guided by family-centered goals that lead to more selfish behavior - which materializes in a lower ESG engagement than their non-family counterparts. However, this is only true for ESG initiatives that might constrain families' desire to retain control and thus often contradicts the interest of inside stakeholders. Family firms can perpetuate the family dynasty by appropriating private benefits at the expense of the firms' insiders. Despite this, they respond similarly to their non-family counterparts on ESG initiatives that concern external stakeholders and thus entail reputational benefits. Accordingly, we can confirm previous studies suggesting that founder-controlled family firms are especially worried about firm survival and thus comply with pressure from external stakeholders (Bingham et al., 2011; Dick et al., 2021). Hence, our response to Le Breton-Miller & Miller (2014) is that SEW reveals its dark side when family owners are concerned about maintaining family control. On the other hand, SEW reveals its bright side when the controlling family is concerned about long-term corporate reputation and ensuring wealth for future generations.

We do not interpret our results as evidence that the ESG engagement in family firms is worse than in non-family firms. Instead, we confirm the evidence of Cruz et al. (2014). The complex nexus of family and business goals in family firms may lead to the coexistence of irresponsible and responsible behavior at the same time. Nonetheless, our results yield some implications for business practices. The hesitance that stakeholders of family firms encounter concerning

ESG is not a symptom of irresponsibility. Instead, the controlling family endeavors to retain family control. Besides, family owners should be aware of the expediencies of investing in ESG. ESG engagement does not necessarily pose a risk of losing family control. Instead, it may be crucial to thrive in competitive markets and achieve longevity for future family generations. ESG engagement provides the opportunity to mitigate future risks, enhance the family's reputation, gain legitimacy, and improve stakeholder relations (Porter et al., 2019)

Future Research. The generalizability of our study is limited, which outlines several directions for future research. Our results are highly contingent upon ESG ratings from the Thomson Reuters Refinitiv database. Using an aggregate score from several ESG rating agencies could improve generalizability and yield other results. A more comprehensive methodology, yet more enlightening, is to fabricate ESG scores for private firms. While public firms are subject to ESG requirements by legislation and must generate yearly sustainability reports, private firms do not share the exact requirements. In turn, private firms may be interesting to study as they may highlight the differences in firms' behavior to a greater extent. Finally, we use SEW as our theoretical framework. However, it may be possible to highlight other perspectives using a different theoretical framework, such as the organization identity theory or stewardship theory.

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Appendix

A1 Description of the ESG Category Scores

Table A1.1: Description of the ESG Category Scores

Resource use score (E):	A company's performance and capacity to reduce use of energy, water, or materials, more eco-efficient and to find solutions by improving supply chain management.
Emission score (E):	A company's commitment and effectiveness in operational processes to reduce environmental emissions.
Innovation score (E):	A company's ability to reduce environmental costs and burden for its customers, thereby explore new technologies and processes, or eco-designed products to create new market opportunities.
Workforce score (S):	A company's effort to ensure job satisfaction, health and safety at the workplace, maintaining diversity and equal opportunities and develop opportunities for its workforce.
Human rights score (S):	A company's effectiveness in terms of respecting fundamental human rights conventions.
Community score (S):	A company's effort to be a good citizen, protecting health, and respecting business ethics.
Product responsibility score (S):	A company's capacity to produce quality goods and services, integrating health and safety, and data privacy.
CSR strategy score (G):	A company's practice to communicate that it integrates E,S and G dimensions into its daily decision-making processes.
Management score (G):	A company's effort towards following best practice corporate governance principles.
Shareholder score (G):	A company's effectiveness towards equal treatment of shareholders and use of anti-takeover devices.

Source: Refinitiv, 2022

A2 Model Diagnostics

Table A2.1: Variance Inflation Factors (VIF) for Multicollinearity

Regression for Hypothesis 1						
	Family Firm	Total Assets	ROA	Leverage	Board Size	
VIF	1.014	1.422	1.830	1.140	1.253	

Regression for Hypothesis 2						
	Family Firm	Total Assets	ROA	Leverage	Board Size	
VIF	1.016	1.978	1.221	1.394	1.290	

Regression for Hypothesis 3						
	Votes	Board Presence	CEO	Founder	Firm Name	Chairman
VIF	1.101	1.074	1.156	1.555	1.587	1.093

Table A2.2: Breusch-Pagan Tests for Heteroskedasticity

Dependent Variable	p-value
<i>Regression for Hypothesis 1</i>	
ESG score	0.37
<i>Regressions for Hypothesis 2</i>	
Resource Use Score	0.00
Emission Score	0.20
Innovation Score	0.00
Workforce Score	0.01
Human Rights Score	0.00
Community Score	0.00
Product Responsibility Score	0.70
Management Score	0.13
Shareholder Score	0.13
CSR Strategy Score	0.00
<i>Regression for Hypothesis 3</i>	
ESG score	0.86

Table A2.3: Breusch-Godfrey Test for Autocorrelation

Dependent Variable	p-value
<i>Regression for Hypothesis 1</i>	
ESG score	0.93
<i>Regression for Hypothesis 2</i>	
Resource Use Score	0.56
Emission Score	0.85
Innovation Score	0.56
Workforce Score	0.88
Human Rights Score	0.43
Community Score	0.48
Product Responsibility Score	0.51
Management Score	0.48
Shareholder Score	0.43
CSR Strategy Score	0.37
<i>Regression for Hypothesis 3</i>	
ESG score	0.83

A3 Correlation Matrices

Table A3.1: Correlation Matrix for Governance Variables

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) ESG score	1	-0.045	-0.078	-0.068	-0.135	0.031	-0.002
(2) Family Votes	-0.045	1	0.252	0.331	0.367	0.229	0.180
(3) Family Chairman	-0.078	0.252	1	0.558	0.175	0.326	0.251
(4) Board Presence	-0.068	0.331	0.558	1	0.175	0.338	0.277
(5) Family CEO	-0.135	0.367	0.023	0.175	1	0.216	0.240
(6) Family Founder	0.031	0.229	0.326	0.388	0.216	1	0.668
(7) Family Firm Name	-0.002	0.180	0.215	0.277	0.240	0.668	1

Table A3.2: Correlation Matrix for Control Variables

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) ESG score	1	-0.068	0.213	0.215	0.148	0.519	-0.102
(2) Family Firm	-0.068	1	-0.065	0.088	-0.043	-0.017	-0.001
(3) Total Assets	0.213	-0.065	1	0.011	0.456	0.239	-0.076
(4) ROA	0.215	0.088	0.011	1	0.051	0.075	0.136
(5) Leverage	0.148	-0.043	0.456	0.051	1	0.155	-0.329
(6) Board Size	0.519	-0.017	0.239	0.075	0.155	1	-0.097
(7) P/B	-0.102	-0.001	-0.076	0.136	-0.329	-0.097	1

Table A3.3: Correlation Matrix for Category Scores and Governance Variables

	Votes	Chairman	Presence on Board	CEO	Founder	Firm Name
Aggregate ESG score	-0.045	-0.078	-0.068	-0.135	0.031	-0.002
Resource Use Score	-0.024	-0.046	-0.033	-0.106	-0.029	-0.028
Emission Score	-0.006	-0.032	-0.008	-0.099	-0.104	-0.054
Innovation Score	0.016	-0.044	-0.042	-0.022	0.051	0.024
Workforce Score	-0.066	-0.056	-0.083	-0.147	0.011	-0.020
Human Rights Score	0.026	0.026	0.022	-0.093	0.076	0.015
Community Score	0.061	-0.001	0.021	-0.064	0.052	0.023
Product Responsibility Score	-0.022	-0.071	-0.076	-0.121	-0.009	-0.005
Management Score	-0.116	-0.091	-0.100	-0.105	-0.038	-0.031
Shareholder Score	-0.030	-0.177	-0.134	-0.077	-0.066	-0.049
CSR Strategy Score	0.016	-0.002	0.004	-0.074	0.081	0.070