The role of distributive justice for family firm governance and succession

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The President:

Prof. Dr. Thomas Bieger
Acknowledgments

I have started this dissertation after having worked for a couple of years as a lawyer in business law. The pivotal experience that made me change my career direction is that I learned about cooperative interest-based negotiations and mediation during my LL.M. studies at Columbia University, New York. Both include a non-adversarial communication where parties discuss their interests in a self-responsible manner to find a solution to the common good. Particularly, in delicate discussions between parties that have an enduring relationship this approach is very helpful as it aims to make communication efficient and problem-solving and not positional or competitive.

I realized that especially for family firms this is the right approach as family firms are confronted with many challenging issues (organization of the family, the company, ownership and wealth) that need to be addressed in an interest-based and cooperative manner in order to be sustainable. I was aware that in order to follow the approach of interest-based consultancy and to become a valuable consultant for family firms I needed to learn more about family firms, about their functioning, the interests of the involved parties and the challenges they face.

By now, my understanding of family firms has enhanced substantially and I thank Professor Thomas Zellweger and Dr. Frank Halter for giving me the opportunity to work with them at the Center for Family Business of the University of St.Gallen (CFB-HSG) with family firms, scholars, practitioners and students and to write a dissertation about justice and governance in family firms. During my work at the University I came in touch with so many people who find deep pleasure in questioning and learning, a very fertilizing ground to never become satisfied and to always improve, I am very grateful for that.

I thank my husband, Dieter Streuli, for being my husband, my comrade and ally in the battlefield of life, for supporting and challenging me to dare to leave the capsule and to float in a most peculiar way, so that Major Tom can reach the stars. I thank my whole family Kissling-Rissling-Streuli and my friends for their love, they are my life. And most importantly, I hope that Marie, my little daughter, will never cede to learn and question and find her own way in life. Your parents’ love will be with you.

Zürich, May 2017

Sonja Kissling Streuli
Executive summary

This dissertation sheds light on the correlation between justice and governance in family firms. It shows that current governance of family firms impacts incumbents' choice of a justice principle in family firm succession and that incumbents’ choice of a justice principle in family firm succession in turn impacts future governance of family firms. Justice principles are allocation norms according to which resources are divided between people. The two justice principles that this dissertation focuses on are equity and equality. If a good is allocated according to the justice principle of equality, it is divided evenly between the parties to the distribution. If a good is allocated according to the justice principle of equity, the good is assigned based on merit to the one who deserves it most. The two justice principles play a role in succession as incumbents often struggle with the question of how to transfer the family firm to the next generation: Shall they treat their descendants equally or favor the entrepreneurially most skilled among their descendants when transferring ownership and management of the family firm? This dissertation is composed out of three papers that tackle the correlation between governance and justice as follows:

The first paper looks at the current governance structure of the firm and investigates how family influence in the different governance bodies (ownership, management, board of directors) determines the choice between equity and equality. Based on responses of 1’528 incumbents, it finds through logistic regression analysis that increasing family influence in ownership will favor equity-ownership transfers as well as equity-management transfers. It further reveals that increasing family influence in management will increase the likelihood of equality-management transfers. It discloses an ambiguous role of family board members, depending on whether their presence is combined with family influence in ownership or management. Combined with increasing family influence in ownership, increasing family influence in the board of directors will mitigate the likelihood of equity-management transfers, whereas combined with increasing influence in management it will mitigate the likelihood of equality-management transfers.

The second paper analyzes three different succession options – succession according to equity, succession according to equality as well as a succession form that encompasses both principles (equity-management transfer and equality-ownership transfer) – and carves out in a dynamic approach the
particular challenges that arise in the family firm under an agency perspective (adverse selection, moral hazard). That paper is a conceptual one that combines justice and agency considerations in family business succession.

The third and last paper deals with perceived injustice. Based on organizational behavior and organizational justice theory it explains that both, not only under- but also over-rewarded descendants change their behavior in order to restore justice. Based on survey responses of 1’528 respondents it shows that perceived injustice in family firm succession leads to so called injustice reduction mechanisms undertaken by the under- and the over-rewarded descendant: The under-rewarded is likely to show behaviors such as shirking, free-riding, resistance to change as well as legal claiming. The over-rewarded is likely to have less job satisfaction, to increase the salary of the under-rewarded and to tolerate less work effort of the under-rewarded. The paper investigates mediating effects of anger and envy on the side of the under-rewarded and guilt on the side of the over-rewarded. The paper finds that family cohesion has no moderating effect.

Overall the three dissertation papers reveal the interplay between justice and governance in family firms. A topic family firms must deal with in order to be sustainably successful for generations.
Zusammenfassung


Das zweite Paper analysiert drei verschiedene Nachfolgeformen - die Nachfolge nach dem Verdienstprinzip, die Nachfolge nach dem Gleichheitsprinzip und die Nachfolge, bei der Management nach Verdienst und


Insgesamt erheilen die drei Beiträge das Wechselspiel zwischen Gerechtigkeit und Governance in Familienunternehmen. Ein Thema, mit welchem sich Familienunternehmen beschäftigen müssen, um nachhaltig und über Generationen erfolgreich zu sein.
# Table of content

Acknowledgements ........................................................................................................ III
Executive summary ........................................................................................................ IV
Zusammenfassung ........................................................................................................... VI
List of figures ................................................................................................................. XI
List of tables ................................................................................................................ XI

1 **Introduction** ........................................................................................................... 1

2 **Framing the dissertation topic** ............................................................................. 4

2.1 Definition of family firms ...................................................................................... 4
2.2 Family firms’ transgenerational intent ................................................................. 6
2.3 Different transition forms (evolutionary, devolutionary, recycles) ....................... 7
2.4 Ownership and management transfer ................................................................... 9
2.5 Succession decision of incumbent ....................................................................... 10
2.6 Distributive justice in family firm succession ..................................................... 10

2.6.1 Competing family and firm norms in succession ............................................ 12
2.6.2 Increasing family influence ............................................................................ 16

2.7 Why important? ..................................................................................................... 17

2.7.1 Better understanding of current governance structures ..................................... 18
2.7.2 Better understanding of future governance structures and challenges ........... 18

2.8 Understanding governance in family firms ......................................................... 20

2.8.1 Governance, governance challenges and instruments in general .................... 20
2.8.2 Four areas of governance in family firms ....................................................... 22

2.9 Relation between distributional justice principles and governance ................. 30

2.9.1 Impact of current governance on choice of justice principle ............................ 31
2.9.2 Impact of choice of justice principle on future governance ............................... 33

2.10 Overview of papers ............................................................................................. 37
# How family influence determines incumbent’s choice between the justice principles of equity and equality in family firm succession

3.1 Abstract ................................................................. 40
3.2 Introduction ............................................................. 40
3.3 Theoretical background .................................................. 44
  3.3.1 Choice between conflicting distributional justice principles in family firm succession .......... 44
3.4 Hypotheses development .................................................. 48
  3.4.1 Ownership succession ................................................ 49
  3.4.2 Management succession ............................................. 54
  3.4.3 Moderating effects .................................................... 57
3.5 Methodology ............................................................... 62
  3.5.1 Sample and data collection ......................................... 62
  3.5.2 Measures .............................................................. 65
  3.5.3 Data analysis .......................................................... 70
  3.5.4 Analytical procedures and results ................................ 72
3.6 Discussion ................................................................. 77
  3.6.1 Contribution to family firm governance ....................... 78
  3.6.2 Contribution to family firm succession ....................... 81
  3.6.3 Contribution to justice theory ................................. 83
3.7 Future research and limitations ....................................... 83
3.8 Conclusion .................................................................. 86

# Relation between governance structures, agency issues, and justice principles in family firms

4.1 Abstract ........................................................................ 87
4.2 Introduction .................................................................. 87
4.3 Theoretical foundations ................................................... 90
  4.3.1 Succession .............................................................. 90
  4.3.2 Justice in family business succession ......................... 92
  4.3.3 Agency perspective .................................................. 99
4.4 Governance structures resulting from different justice principles ........................................... 104
  4.4.1 Scenario I: Application of the equity principle ...... 104
  4.4.2 Scenario II: Application of the equality principle... 111
  4.4.3 Scenario III: Application of equality to ownership and equity to management .......... 119
4.5 Conclusion .................................................................. 127
4.6 Limitations and future research ...................................... 130
What goes around comes around – descendants harm the family firm following perceived injustice

5.1 Abstract ................................................................. 132
5.2 Introduction .......................................................... 133
5.3 Theoretical background ............................................ 138
  5.3.1 Three different types of justice ............................... 138
  5.3.2 Distributional justice and perceived injustice .......... 141
  5.3.3 Consequences of perceived injustice ....................... 143
  5.3.4 Consequences of perceived injustice in organizations ................................................ 144
5.4 Hypotheses development ........................................... 146
  5.4.1 Injustice reduction mechanisms following perceived injustice in family firm succession .......... 146
  5.4.2 Injustice reduction mechanisms of the under-rewarded descendant ........................................ 148
  5.4.3 Injustice reduction mechanisms of the over-rewarded descendant ....................................... 154
  5.4.4 Moderating effects of family cohesion ................. 159
  5.4.5 Mediating effects of emotions ........................... 162
5.5 Methodology .......................................................... 165
  5.5.1 Sample and data collection ..................................... 165
  5.5.2 Measures .......................................................... 168
  5.5.3 Data analysis ....................................................... 175
  5.5.4 Analytical procedures and results ....................... 178
5.6 Discussion ............................................................. 186
  5.6.1 Contributions to theory ........................................ 188
  5.6.2 Future research ................................................. 191
  5.6.3 Limitations .......................................................... 193
  5.6.4 Conclusion ........................................................ 193

6 Concluding chapter ...................................................... 194
  6.1 Revisiting the key findings of the three papers .......... 194
  6.2 Contribution to theory ............................................ 195
  6.3 Contribution to practice ......................................... 198
  6.4 Limitations .............................................................. 202
  6.5 Future research ....................................................... 203
  6.6 Conclusion .............................................................. 205
  6.7 25 proposed thinking patterns ............................. 207
References..................................................................................................................................... 209
Curriculum Vitae......................................................................................................................... 234

List of figures

Figure 1: Different transition forms in family firms according to Gersick et al., (1999) ................................................................................................................................. 8
Figure 2: Goals and norms of family and firm in succession .............................. 14
Figure 3: Competing justice principles in family firm succession ............... 15
Figure 4: Family firms’ goals and understanding of success ...................... 22
Figure 5: Governance areas in family firms ....................................................... 23
Figure 6: Relation between justice and governance in family firms .......... 31
Figure 7: Agency issues in equity succession (paper 2) .............................. 110
Figure 8: Agency issues in equality transfers (paper 2) .............................. 118
Figure 9: Agency issues in mixed transfers (paper 2) ................................. 126
Figure 10: Proposed model (paper 3) ............................................................... 165

List of tables

Table 1: Dissertation structure ......................................................................................... 3
Table 2: Summary of the three dissertation papers ......................................................... 37
Table 3: Descriptive statistics and correlations of variables (paper 2) .......................................................... 71
Table 4: Logistic regression models (paper 2) ................................................................. 73
Table 5: Descriptive statistics and correlations of variables in under-rewarded scenario (paper 3) ..................................................................................................................... 176
Table 6: Descriptive statistics and correlations of variables in over-rewarded scenario (paper 3).......................................................... 177
Table 7: Models of under-rewarded scenario (paper 3).............................. 179
Table 8: Models of over-rewarded scenario (paper 3)................................. 180
Table 9: Overview of hypotheses and results (paper 3)............................... 185
1 Introduction

“Gouverner, c’est prévoir” said the French publisher Emile de Girardin in the 19th century. People who are in charge with decisions correspondingly need to anticipate the impact of their action. Decision-makers are hence required to foresee the challenges, risks and opportunities of their choices. In intra-family successions, it is up to family firm incumbents to decide about how to transfer the company to the next generation. How do they know about the impact of their decisions?

On the one hand, practical experiences will help incumbents to foresee some consequences. In this regard one cannot underestimate their own experiences, i.e. the experiences they made when taking over the firm from their parents. Incumbents learn from the faults of their parents and will try to make up for them in own succession processes. Also, successions in other, often befriended, family firms will set an example. Fortunately, within the last decade a wide public became more aware of the fact that family firm succession processes have to be addressed and planned actively. Consequently, there is an increasing number of consultants in the field of family firm succession.

On the other hand, it is theory and academic work that will help to foresee consequences. Academics analyze situations and try to derive statements that are generally applicable. Theory hence reduces reality and provides for general rules that will help to foresee interrelations and the consequences of one’s action. “To understand is to perceive patterns”.\(^1\) Fully aware that such thinking

\(^1\) Sir Isaiah Berlin.
patterns do not fit individual situations, theory helps us to reduce life’s complexity and gives us orientation. That is the aim of the following dissertation. The dissertation shall provide for some thinking patterns (see chapter 6.7) for family firms and their consultants with regard to justice and governance in family firms. It deals with two allocation norms, equity and equality, that are regularly applied in family firm succession and looks at the interplay between these justice principles and governance in family firms (see Table 1 for the structure of the dissertation).
Table 1: Dissertation structure

<table>
<thead>
<tr>
<th>Chapter</th>
<th>Introduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chapter 2</td>
<td>Framing the dissertation topic</td>
</tr>
<tr>
<td></td>
<td>– Definition of family firms</td>
</tr>
<tr>
<td></td>
<td>– Family firms’ transgenerational intent</td>
</tr>
<tr>
<td></td>
<td>– Different transition forms (evolutionary, devolutionary, recycles)</td>
</tr>
<tr>
<td></td>
<td>– Ownership and management transfer</td>
</tr>
<tr>
<td></td>
<td>– Succession decision of incumbent</td>
</tr>
<tr>
<td></td>
<td>– Distributive justice in family firm succession</td>
</tr>
<tr>
<td></td>
<td>– Competing family and firm norms in succession</td>
</tr>
<tr>
<td></td>
<td>– Why important?</td>
</tr>
<tr>
<td></td>
<td>– Understanding governance in family firms</td>
</tr>
<tr>
<td></td>
<td>– Relation between distributional justice principles and governance</td>
</tr>
<tr>
<td></td>
<td>– Overview of papers</td>
</tr>
<tr>
<td>Chapter 3</td>
<td>Paper 1: How family influence determines incumbent’s choice between the justice principles of equity and equality in family firm succession</td>
</tr>
<tr>
<td>Chapter 4</td>
<td>Paper 2: Relation between governance structures, agency issues, and justice principles in family firms</td>
</tr>
<tr>
<td>Chapter 5</td>
<td>Paper 3: What goes around comes around – descendants harm the family firm following perceived injustice</td>
</tr>
<tr>
<td>Chapter 6</td>
<td>Concluding chapter</td>
</tr>
<tr>
<td></td>
<td>– Revisiting the key findings of the three papers</td>
</tr>
<tr>
<td></td>
<td>– Contribution to theory</td>
</tr>
<tr>
<td></td>
<td>– Contribution to practice</td>
</tr>
<tr>
<td></td>
<td>– Limitations</td>
</tr>
<tr>
<td></td>
<td>– Future research</td>
</tr>
<tr>
<td></td>
<td>– Conclusion</td>
</tr>
<tr>
<td></td>
<td>– 25 proposed thinking patterns</td>
</tr>
</tbody>
</table>
2 Framing the dissertation topic

2.1 Definition of family firms

Family firms represent about 65-90% of the companies in the world (La Porta, Lopez-de-Silanes, & Shleifer, 1999; Sharma, Chrisman, Pablo, & Chua, 2001; Zellweger, 2017). The percentage of family firms varies in particular also because there is no unified definition of family firms (Chua, Chrisman, & Sharma, 1999).

In order to be qualified as a family firm, the majority of definitions considers the degree of influence of the family in the family firm, meaning its presence in the different governance bodies (Astrachan, Klein, & Smyrnios, 2002; Faccio & Lang, 2002; La Porta et al., 1999). In general, definitions require that a certain percentage of the ownership stake of the company lies in the hand of a family (Ward & Dolan, 1998). The intent is to make sure that the family can control the company via shareholder rights. The required threshold of stock in small and mid-sized companies is often set at the simple majority (51%). Contrary, in family firms with dispersed ownership, i.e. listed family firms, a lower threshold is accepted, e.g., 20% to 25%, as such threshold also allows to control the company (Anderson & Reeb, 2003; Villalonga & Amit, 2006; Zellweger, 2017). Some definitions require that the family is moreover present in the board of directors and/or the management (Chua et al., 1999). A recent study of the Center for Family Business inquired about the percentage of family firms among small and medium-sized companies in Switzerland (Andric et al., 2016) and used a definition that added the percentage of family members present in ownership, board of directors and management and defined as family firms, firms in which a percentage of 100% of family
influence was reached. 75% of the small and medium-sized companies in Switzerland are according to this definition family firms (Andric et al., 2016). Other definitions include a transgenerational dimension and qualify firms as family firms only if they have already experienced intra-family succession and passed from one generation to the other (Daily & Thompson, 1994), or if firms at least have a corresponding intention (Barach & Ganitsky, 1995).

Increasingly, definitions do not only comprise factual or objective, but also interpretive or subjective information and therewith provide for more elaborate conceptualizations of family firms. For instance, according to the “essence” approach, family involvement must produce certain distinctiveness (Chrisman, Chua, & Sharma, 2005). So, two firms might have the same family involvement but one of them is not considered as a family firm as it lacks the intention, familiness, or behavior that is considered as essence of the family firm (Chrisman et al., 2005). Astrachan and colleagues offer with the F-PEC scale a non-dichotomous definition of family firms that considers the three dimensions of power, experience and culture to differentiate between family firms (Astrachan et al., 2002; Klein, Astrachan, & Smyrniotis, 2005).

In view of this myriad of definitions, every research contribution needs to specify the type of family firm it works with. This dissertation focuses on family influence in the governance bodies of the firm and investigates how ownership and management is passed on to the next generation. It therewith deals with family involvement and transgenerational intentionality (Chrisman et al., 2005). The first paper focuses on incumbents’ succession decisions and investigates how increasing family influence in different governance bodies, i.e. ownership, board of directors and management, impacts incumbents’
choice between the justice principles of equity and equality in succession. Correspondingly, the first paper applies a dynamic view of family influence – without requiring a specific, initial degree of family involvement. The second paper is a conceptual one and assumes that the family is in full possession of ownership and management and that the firm is passed on within the family. Also, the third paper is based on a scenario where respondents assume that the family has 100% of ownership and management, and transfer the firm to the next generation.

2.2 Family firms’ transgenerational intent

The dissertation is concerned with intra-family succession. In intra-family succession leadership is transferred to the next family generation (Sharma et al., 2001). Family firm incumbents generally prefer this form of succession over others, such as passing on the family firm to a non-family employee or selling the company externally (Andric et al., 2016). The family firm constitutes a financial asset of the family and gives family members moreover the opportunity to satisfy non-financial, socio-emotional needs (Gómez-Mejía, Takács Haynes, Núñez-Nickel, Jacobson, & Moyana-Fuentes, 2007; Zellweger, Nason, Nordqvist, & Brush, 2013). For instance, such socio-emotional assets are the collaboration between family members, the ability to commonly exercise authority (Schulze, Lubatkin, & Dino, 2003a), family’s reputation and status, the perpetuation of family values through the business and the preservation of the family dynasty (Casson, 1999). Intra-family succession is hence a means for the family to keep financial and socio-emotional wealth within the family.
2.3 Different transition forms (evolutionary, devolutionary, recycles)

Intra-family succession leads to different forms of family firms over time. According to Gersick, Lansberg, Desjardins, & Dunn (1999) family firms run through the following stages: Starting with the controlling owner stage whereby the founder of the family firm owns and manages the company, the family firm is then passed down to the descendants of the controlling owner and enters the stage of sibling partnership. In this stage, the descendants of the founding owner take over management and ownership of the family firm. The next transfer leads to the cousin consortium stage, whereas different family lines own and manage the company. Zellweger (2017) adds the family enterprise stage as further development stage. In this stage family and business have grown, so that a family with multiple members controls a portfolio of business activities. Over time, family firms might run through all stages (controlling owner to family enterprise) and therewith undergo evolutionary transitions (Gersick et al., 1999). Or, family firms remain in a certain stage and do a recycle, e.g., from controlling owner to controlling owner (Gersick et al., 1999). Lastly, also devolutionary transitions happen where family firms move to a less complex structure (e.g., from cousin consortium to controlling owner) (Gersick et al., 1999).
Figure 1: Different transition forms in family firms according to Gersick et al., (1999)

Considering the different stages the family firms run through, the fundamental and starting question of this dissertation was:

Why do some family firms run through evolutionary transitions, while others through devolutionary transitions or recycles?
As the succession event determines whether the family firm effects an evolutionary or devolutionary transfer or a recycle, we have to take a closer look on what actually happens in intra-family succession.

2.4 Ownership and management transfer

Succession in family firms includes *ownership succession* (Ward & Dolan, 1998) and *management succession* (Brockhaus, 2004). Ownership and management succession are often interdependent. Especially in early stages of the family firm, ownership and management are not separated and passed on together from one generation to the next (Gedajlovic, Lubatkin, & Schulze, 2004; Gersick et al., 1999). For instance, imagine the founder who transfers the shares of the family business to his or her daughter at the moment the daughter becomes the CEO of the firm. In this example, ownership and management transfer happen simultaneously. In other family firms, ownership and management transfers are effected sequentially. In these cases, incumbents gradually move away from active involvement, i.e. they first transfer operative responsibility to descendants and at a later time the shares of the family firm (Dyer & Handler, 1994; Le Breton-Miller, Miller, & Steier, 2004). In family firms of later stages (cousin consortium, family enterprise), ownership and management transfers become more and more independent. In these stages, often a large number of family members at different age classes own the company (Zellweger, 2017). The different life cycles of the family members imply that their individual succession processes occur at different times and ownership is not passed on at once from one generation to the next. This timely dimension in family firm succession entails that ownership and management transfers are considered separately and happen irrespective of each other (Gedajlovic et al., 2004).
2.5 Succession decision of incumbent

In intra-family succession, family firm *incumbents decide* on how they transfer ownership and management to the next generation, i.e. they determine to what degree descendants participate in owning and managing the firm in future. Naturally, the scope of decision-making and the options of incumbents are limited by facts: An increasing number of descendants is unwilling to take over the family firm as they wish to proceed their own career path or follow own projects (Sieger, Fueglistaller, & Zellweger, 2016). Some incumbents have multiple descendants, others have none. Or, they have children that are too young to succeed in the business and timing imposes other succession forms. And sometimes succession decisions are not even in the hand of the incumbents as unexpected events, for instance a sudden illness or even a sudden death (Handler, 1994), hinder them to take part in the succession process. Despite all these circumstances, often incumbents of family firms actually decide on how ownership and management is passed on to their descendants. And hereinafter we look at the normative foundations on which family firm incumbents reach these succession decisions.

2.6 Distributive justice in family firm succession

As in family firm succession the two functions of ownership and management are transferred to the next generation, family firm succession hence constitutes an *allocation* or *distribution*. In allocations, people generally try to achieve outcomes that are perceived as just by the involved parties (Homans, 1958). This drive for justice stems from a moral imperative to act justly and strengthens social cohesion and solidarity within society (Greenberg, 1990a; Montada, 1998).
To find out what people consider as just, justice theory has dealt with different aspects of distributions (Cohen-Charash & Spector, 2001; Colquitt, Conlon, Wesson, Porter, & Ng, 2001; Cropanzano, Bowen, & Gilliland, 2007). It has conceptualized justice focusing on the outcome of allocations (distributional justice), on the process of the allocation (procedural justice), and lastly on interactional elements of the process (interactional justice) (Bies & Moag, 1986; Colquitt et al., 2001; Gilliland, 1993; Greenberg, 1990a; McFarlin & Sweeney, 1992). This dissertation focuses primarily on distributional justice. Distributional justice theory explains that allocations can be effected according to different allocation norms, called distributive justice principles, such as equity, equality, or need, and investigates what justice principles people choose in different allocation situations (Breugst, Patzelt, & Rathgeber, 2015; Deutsch, 1975; Frohlich, Oppenheimer, & Eavey, 1987; Herreiner & Puppe, 2007; Tornblom & Foa, 1983). What justice principle people consider as fair depends on the context of the allocation situation (Deutsch, 1975; Walzer, 1983). So, the question that emerged in connection my dissertation was:

What justice principles do incumbents choose in family firm succession?

As the appropriateness of the justice principles depends on the allocation context (Deutsch, 1975), we have to comprehend the context of family firm succession to unfold which justice principles incumbents choose and consider as fair when transferring ownership and management to the next generation.
2.6.1 Competing family and firm norms in succession

Family firms have the idiosyncrasy that two systems meet, the family and the business (De Massis, Chua, & Chrisman, 2008; Dyer & Handler, 1994; Sharma et al., 2001; Tagiuri & Davis, 1996). Each of these systems has a unique set of goals, values, norms, and rules of conduct (Lansberg, 1983). This duality of the family business becomes visible also in the family firm succession context (Zellweger, Richards, Sieger, & Patel, 2016), as the two systems call for the application of different justice principles in distributions.

From the family perspective, succession risks to result in conflicts between family members (Barach & Ganitsky, 1995). Succession deals with passing on the family firm and inevitably family members have to deal with own mortality or the death of close family members (Handler, 1994). Succession includes furthermore a confrontation with oneself, as it touches personal life and career plans and an assessment of own skills and abilities (Chrisman, Chua, & Sharma, 1998). Succession also implies reviewing family relationships, the relationship between parents, couples, parents and children, or between siblings. This emotionally intense situation often rips open old wounds and endangers family cohesion (Friedman, 1991; Handler, 1994). Overall, succession provides fertile ground for conflicts between family members (Kidwell, Kellermanns, & Eddleston, 2012). Correspondingly, the family goal in succession is to preserve family cohesion and harmony (Barach & Ganitsky, 1995; Le Breton-Miller et al., 2004; Morris, Williams, Allen, & Avila, 1997; Sharma et al., 2001).
With regard to distributions, families choose in general – in order to achieve the goals of family cohesion and harmony – the justice principle of equality (Drake & Lawrence, 2000; Kidwell, Eddleston, Cater, & Kellermanns, 2013; Lansberg, 1983). In contexts in which the fostering and maintenance of social relations is the common goal, the justice principle of equality is the dominant allocation norm (Deutsch, 1975). The application of the justice principle of equality signifies the parties to the distribution that they all have the same value (Deutsch, 1975). Hence parents will try to treat their children equally with regard to the allocation of resources, such as love, time, money etc. (Tornblom & Foa, 1983). Applied to the family business succession context, such family logic calls for the application of the justice principle of equality where ownership and management are divided equally between descendants.

From the business perspective, succession determines the prospective leaders of the company (Le Breton-Miller et al., 2004). Succession therefore is surrounded by uncertainty about the company’s future strategy and performance (Gersick et al., 1999; Lansberg, 1988). The business goal in succession is therefore to guarantee for future profit of the company (Le Breton-Miller et al., 2004; Sharma et al., 2001). To achieve that goal, allocations in the business context are based on merit. Hence the justice principle of equity is pertinent in business decisions in order to ensure firm’s performance (Deutsch, 1975; Kidwell et al., 2013; Lansberg, 1983). Applied to the family business succession context, the business norm of equity would lead to a succession form that favors the descendant who deserves it more, i.e. is more competent (Chrisman et al., 1998).
Figure 2: Goals and norms of family and firm in succession

The institutional overlap between family and firm hence creates tensions in family firm succession (Barach & Ganitsky, 1995; De Massis et al., 2008; Lansberg, 1983; Sharma et al., 2001; Tagiuri & Davis, 1996). Family firm incumbents want to save family harmony but at the same time maintain firm performance. They try to achieve both, family and business goals (Kammerlander, 2016; Tagiuri & Davis, 1996; Zellweger et al., 2016). But these goals call for the application of different justice principles (Ayres, 1990; Deutsch, 1975; Kabanoff, 1991; Sharma et al., 2001). In order to save family harmony, incumbents should choose the justice principle of equality. Contrary, to maintain firm performance family firm incumbents will be inclined to apply the justice principle of equity in succession. The struggle of incumbents between the family norm of equality and the business norm of equity manifests itself in questions of the following nature:
Shall I pass on the family firm to all my descendants equally?
That means, shall all descendants succeed in ownership?
Shall they receive the same number of shares?
Shall the management of the company be shared by descendants?
Or, shall only the most competent descendant take over the management?
Shall descendants managing the family firm receive a bigger ownership stake or even all shares in the company?

Figure 3: Competing justice principles in family firm succession

These examples show that equality and equity considerations clash in family-internal succession. In practice, incumbents often combine the two justice principles to a certain degree. For instance, they attribute ownership evenly to all descendants, but management to only one of them. Or, they make the successor-manager to the majority shareholder (e.g., 51%) and his or her
siblings to minority shareholders. Despite these combination, in every succession there remains a tension between the family norm of equality and the business norm of equity. And succession decisions of the incumbent hence constitute a commitment, a commitment to the family norm or the business norm. So, the question arises:

Do incumbents of family firms choose the business norm of equity or the family norm of equality in succession?
(Paper 1)

2.6.2 Increasing family influence

As initially mentioned, there is no dichotomous definition of family firms. Family firms have different stages and in those stages the influence of the family varies. Increasing family influence in the firm provides the family with more power and legitimacy (Chrisman, Chua, Pearson, & Barnett, 2012). Hence, there is a positive relationship between the family’s influence in the firm and the adoption of family norms (Chrisman et al., 2012). Accordingly, the degree to which family norms influence succession depends on the degree of family influence in the governance bodies of the family firm, i.e. ownership,
board of directors and management. Correspondingly, the first paper of this dissertation will respond to the following question:

How does increasing family influence in the governance bodies of family firms impact the choice between the application of the justice principles of equity and equality when transferring ownership and management to the next generation?

(Paper 1)

Assumingly, increasing family influence in the governance bodies of the family firm boosts the application of the family norm of equality, and equality successions are more frequent in family firms where family influence is high. Contrary, we can assume that the business norm of equity is more pertinent if family influence in the firm is low. In its first paper, this dissertation will analyze family influence and its impact on the choice of the justice principle more thoroughly and come up with some surprising findings.

2.7 Why important?

Why is it important that we know how family influence in the different governance bodies (ownership, board of directors, management) impacts the choice between the justice principles of equity and equality in succession?
2.7.1 Better understanding of current governance structures

To know how family influence impacts the choice between equity and equality successions will provide us with a better understanding of current governance structures in family firms. I will help us to identify whether and how the primacy of family norms in succession depends on the level the family influences the different governance bodies. This will enable us to differ between types of family firms that favor the application of family norms in succession and types of family firms that favor the application of business norms. This knowledge paves the way for theory and practice to better address and mitigate possible negative effects of family influence in succession (Schulze et al., 2003a).

2.7.2 Better understanding of future governance structures and challenges

Moreover, knowledge about the justice principle chosen in succession will help us to understand future governance structures and challenges of family firms.

With regard to future governance structures, the choice of the justice principle will answer the question of why some family firms go through evolutionary transitions, while other through devolutionary or recycles (Gersick et al., 1999). The transition stages result, at least partly, from the application of different justice principles: If the justice principle of equality is applied in succession, descendants will share ownership and management in future. Correspondingly, the number of family members present in the company will increase and the family firm experiences an evolutionary transfer. Contrary, if the justice principle of equity is applied in family firm succession, the family
firm is transferred to the most competent descendant, the one who contributes the most to future success of the company. The justice principle of *equity* therewith leads to *recycles* or *devolutionary transfers* if, in the latter case, the firm previously was transferred according to the justice principle of equality and then goes back to a less complex family structure.

These different transition forms result in *different governance challenges* (Carney, 2005). Therefore, knowledge about the justice principle chosen in succession will help to understand the governance challenges the family firm meets in future. For instance, the justice principle of equality will lead to a governance structure where multiple family members share power in the organization of the family firm. Correspondingly, issues resulting from conflicting interests of the family members, different degrees of dedication or competence will affect governance of the family firm (Lubatkin, Schulze, Ling, & Dino, 2005; Schulze, Lubatkin, & Dino, 2002; Schulze, Lubatkin, Dino, & Buchholtz, 2001). The second and the third paper are dedicated to investigating the governance challenges that arise from the application of the justice principles of equity and equality in succession in more detail. Paper 2 and paper 3 therewith deal with the following question:

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*What governance challenges result from the choice of the justice principles of equity and equality in family firm succession?*

*(Paper 2 + 3)*
2.8 Understanding governance in family firms

As the second and the third paper of this cumulative dissertation deal with governance structures and challenges, this chapter shall beforehand convey a basic understanding of the concept of governance, and particularly of governance in family firms. It will help to understand the significant impact of distributive justice on family firm governance. First, this chapter explains governance, governance challenges and governance instruments in general and specific to family firms. Thereafter, it illustrates how governance and the topic of justice in family firm succession are interrelated.

2.8.1 Governance, governance challenges and instruments in general

Governance in general can be thought of as the set-up of an organization, its chain of responsibilities (Aguilera & Crespi-Cladera, 2012; Cadbury, 2002; Zellweger, 2017). Governance therewith includes all formal and informal rules about who makes decisions and about how these decisions are made and implemented.

The term governance itself is unbiased. The governance of an organization is good if it ensures that the activities of the organization and its members are directed at achieving the organization’s goals. This implies that the procedures within the organization are clearly defined and run smoothly. Proof of good governance is when the company achieves its goals. Contrary, the governance of an organization is bad if the activities of the company and its members are not directed at achieving the organization’s goals and the procedures within the organization are unclear and disturbed. Correspondingly, governance challenges constitute situations in which there is a risk that governance bodies
do not act in the interests of the company and/or procedures are impaired. Governance instruments lastly are means by which governance challenges are mitigated.

Governance shall help organizations to achieve their goals. As each organization sets its own goals and is embedded in a different internal and external context, governance systems need to be customized to meet the organizations’ specific needs (Hilb, 2016).

Family firms follow economic and non-economic goals (Zellweger et al., 2013; Zellweger et al., 2016). Their main goals are threefold: First, as all firms, they aim at maintaining/increasing financial profit. Second, family firms wish to preserve family cohesion and harmony (Chrisman et al., 2012). And third, family firms strive for passing on the family firm to the next generation, in order to keep financial and socio-emotional wealth within the family (Chua et al., 1999; Habbershon, Williams, & MacMillan, 2003; Wiklund, Nordqvist, Hellerstedt, & Bird, 2013). The governance system in family firms must be designed in such a way that it enables family firms to meet these three supreme goals of firm profit, family harmony, and intra-family succession. In the event these three goals are realized, the family firm is successful (Le Breton-Miller et al., 2004).
2.8.2 Four areas of governance in family firms

In order to achieve these goals (profitable company, family harmony, intra-family succession), family firms have to deal with structuring four areas of governance (Zellweger, 2017). These are 1) the company, 2) the family, 3) ownership, and 4) wealth.
2.8.2.1 **Corporate governance**

Corporate governance structure, i.e. the set-up of companies and their decision structure, is prescribed by binding law. Many family firms have the legal form of stock corporations. In those corporations, the responsibilities are appointed by law to three governance bodies: *Shareholders, board of directors, and management*:\(^2\) The shareholders are the owners of the company and have financial (right of dividend) and non-financial rights (information and decision rights). They elect board members which on their behalf lead the company. The board of directors defines the company’s strategy and its mission and

\(^2\) For Swiss law see Articles 620 et seqq. of the Swiss Code of Obligations.
vision (Hilb, 2016). The implementation of the strategy is executed by the management. In the annual report, the board of directors gives an account of its activities to the shareholders. Shareholders can approve or reject the annual report of the board of directors as well as the annual financial statement in their annual meetings. As law does not distinct between family firms and non-family firms, both have the same governance bodies. However, they differ in the composition of these governance bodies in so far as shareholders, board members and members of the management, are – to a certain degree – family members.

**Corporate governance challenges.** In research, corporate governance challenges are analyzed with help of the *principal-agency theory* (Fama & Jensen, 1983; Jensen & Meckling, 1976; Shleifer & Vishny, 1997). The theory explains that in the event of a separation of ownership and management, i.e. these functions are not executed by the same person, there will be conflicts of interests and information asymmetry between the owner (principal) and the manager (agent). Because of information asymmetry, the owner might engage managers that do not come up with the required skills, so called *adverse selection* (Fama, 1980). Furthermore, managers are tempted to pursue own goals and act opportunistically (Jensen & Meckling, 1976). For instance, they might simply do not show the necessary effort and engage in free-riding and shirking (Eisenhardt, 1989). Such behavior of agents is subsumed under the term *moral hazard* (Fama, 1980).

In its beginnings, principal-agency theory expected *family firms* to have no agency issues as the family was considered as one unified actor with no diverging interests and full transparency (Jensen & Meckling, 1976).
Thereupon, family scholars engaged in a stimulating debate on what agency challenges family firms meet (Gomez-Mejia, Nunez-Nickel, & Gutierrez, 2001; Morck & Yeung, 2003) and found for instance, that altruism of family members leads to adverse selection and moral hazard in family firms (Schulze et al., 2001). As a result of altruism, family members are engaged in the company that are not competent or family members that take advantage of their membership to the family to exploit resources of the company (Buchanan, 1975; Karra, Tracey, & Nelson, 2006; Lubatkin et al., 2005; Schulze et al., 2002, 2003a). Correspondingly, the agency issues of adverse selection and moral hazard also arise in family firms. Furthermore, research established that the family cannot be considered one unified actor as family members have diverging goals. As mentioned, family firms have both economic and non-economic goals. While one can assume that the economic interests of family members fit, one cannot suppose that their non-financial goals are congruent (Schulze et al., 2001). Correspondingly, there is a risk of conflicting interests among family shareholders that leads to governance issues.

**Corporate governance instruments.** In order to prevent risks resulting from the separation of ownership and management, owners try to align the interests of the agent with their own interests (Jensen & Meckling, 1976). This is commonly made via compensation schemes that aim to reduce conflicts of interests. Moreover, monitoring systems are established that will decrease moral hazardous behavior of the agent and reduce information asymmetry (Jensen & Meckling, 1976). As family firms also meet the governance challenges of adverse selection and moral hazard, they need to install the same governance instruments as non-family firms. For instance, family firms can reduce agency issues in appointing independent (especially family-external)
board members to the board of directors as they will improve monitoring effectiveness of the board (Corbetta & Salvato, 2004; Miller & Le Breton-Miller, 2006). In contrast to shareholders of widely held or publicly listed firms, family shareholders often cannot escape from these governance issues as family firms regularly are privately hold and hence there is no market where family shareholders could sell their shares (Schulze et al., 2001).

2.8.2.2 Family governance

The goal of family governance is to foster the relationship between family members and the relationship between family members and the firm. In this area, no governance bodies are prescribed by law. Often family firms with a complex family situation, i.e. numerous family members, create family committees or councils with special duties. For example, there might be a committee that takes care of educating the next generation about the family firm and organizes corresponding seminars or workshops. Or, family firms have a special social committee that prepares social gatherings of the family. To provide for common ground, families often feel the need to work out a declaration, often called family constitution, in which they lay down common values as well as communication and decision-making guidelines.

Family governance challenges. The biggest challenge of family governance is to maintain identification of family members with both, the family and the firm. Good family relations are important for the family to be able to transfer the family firm to the next generation (Sharma et al., 2001). Whereas in early stages of the family firm (Gersick et al., 1999) there is usually a strong link between family members and the company, such connection risks to be lost in later generations. Family governance must correspondingly ensure that family
members come together to talk and to be educated about the family firm to establish a strong connection between the family members and the company.

**Family governance instruments.** As mentioned above, establishing a family constitution will help family members to find common ground. Important is the process of establishing the family constitution not necessarily the resulting document. The process will enable family members to put themselves in the shoes of each other and to learn to work together to achieve a mutual goal. Regular social gatherings help to create new common memories and provide for an exchange of thoughts that increases understanding of each other. Educational seminars about the family firm will support the bonding between the family and the firm. Some families write a book about the company to treasure the memory of the family firm and pass on the knowhow to the next generation.

2.8.2.3 **Ownership governance**

Another area that family firms should structure to be successful is ownership. Family shareholders must define how ownership is transferred within the family and possibly to third persons. They need to agree on whether they can sell or buy stock from or to other family members, whether in-laws are able to become shareholders, what happens if family shareholders get divorced, whether family shareholders can exit the firm and how ownership is handed over to the next generation. To establish corresponding rules, shareholder agreements have to be established as well as marriage contracts and contracts of inheritance. In shareholder agreements family shareholders often additionally agree on how they execute their shareholder rights towards the company. Often families decide to speak with one voice at the annual
shareholder meeting and to meet before the annual meeting to agree on how they will vote on the agenda items. Moreover, in such shareholder agreements family shareholders determine for instance, how the board of directors shall be composed, e.g., if each family line has the right to elect one board member.

Ownership governance challenges. The two biggest risks in ownership governance is that 1) families do not establish governance instruments (contracts) at all, or that 2) families establish contracts but do not understand them or do not emotionally agree to them. The latter case arises if contracts are established by lawyers and consultants without involving all family members. Such advisors often elaborate extremely detailed and sophisticated contracts; however, these contracts do in many cases not reflect the convictions of the family members. What is needed is that advisors and family members develop the guidelines with regard to ownership transfers jointly in physical meetings. Only such process can ensure 1) that family members understand what is agreed on in the contract and 2) that the contract fully expresses their will. If these two conditions are not met, conflict and litigation are highly likely.

Ownership governance instruments. Law determines shareholder rights and how these rights are exercised towards the company. If family shareholders wish to grant each other additional rights (e.g., preemption rights) they have to enter into a shareholder agreements. Further, they need to establish marriage and inheritance contracts to define how ownership is passed on in the event of divorce or death.
2.8.2.4 Wealth governance

The last area family members have to organize is their wealth. Here the family needs to define how much profit is reinvested in the company and how much is dispersed among family members in form of dividends. The family needs to decide whether they pool dividends and engage in joint investment activities or whether family members individually manage their assets. Family members must determine the degree to which they separate their wealth from family and business (family office, trust etc.) and what external advisors they engage to administer their wealth. Lastly, also the administration of common philanthropic activities falls in this area of governance.

Wealth governance challenges. The biggest challenge for the family firm is that family members become dependent on dividends to meet their day-to-day needs. Retirement plans and lifestyle of family members should not depend on dividend payments, so that the company maintains the freedom to reinvest earnings. Further, if family members jointly engage in (other) investment activities, the challenge is to find the right structure. Engaging external specialists is costly and the family needs to set the right incentives in order to attract competent and trustworthy advisors that act in the interests of the family members.

Wealth governance instruments. Depending on the degree the family intends to separate its wealth from family and business they might establish a single-family office or join a multi-family office or transfer their wealth into a trust. In order to mitigate principal-agency issues they need to establish a monitoring
system to reduce information asymmetry and a compensation policy that aligns the interests of the agents with their own (Jensen & Meckling, 1976).

In sum, in order that the family, the business and succession are successful, the four areas – company, family, ownership and wealth need to be structured. If these four areas are well organized (good governance) and governance challenges are met, the family firm will be successful and prepared for succession. However, not every family firm needs the same sophistication of governance. The level of governance in each area depends on the stage of the family firm (controlling owner – sibling partnership – cousin consortium – family enterprise) and therewith on the complexity of the family and the firm (Zellweger, 2017).

2.9 Relation between distributional justice principles and governance

The basic topic of the dissertation is the relation between justice principles applied in succession and governance in family firms. As explained above, justice principles are allocation norms that incumbents use when passing on ownership and management to the next generation. The dissertation focuses on the justice principle of equity (merit based succession) and equality (all descendants equally succeed in the company). In its three papers, the dissertation deals with how family influence in different governance bodies impacts the choice between equity and equality in succession (paper 1), and what governance challenges result from such choice (papers 2 and 3). Paper 2 focuses on agency issues arising out of the choice between equity and equality over time. Paper 3 addresses the governance challenges that result from perceived injustice. The papers are summarized in Table 2. In a nutshell, the key finding is that the current governance of the family firm impacts the choice
of the justice principle (equity or equality) and the choice of the justice principle impacts future governance of the family firm.

Figure 6: Relation between justice and governance in family firms

In this chapter, these relations will be explained separately for each governance area. The three dissertation papers do not explicitly deal with all four governance areas (corporate, family, ownership, wealth) but focus on corporate governance. Nevertheless, as the four governance areas are closely intertwined, in practice one cannot consider one without the others. To provide an overview of the interplay between justice and governance in family firm, hence hereinafter the insights of the three papers are applied to all four areas of governance.

2.9.1 Impact of current governance on choice of justice principle

2.9.1.1 Corporate governance

As mentioned, family firms have by law the same governance bodies as non-family firms. What is different is that family members hold positions in ownership, board of directors and management. Their presence will have the following impact:
Increasing family influence in ownership will favor equity transfers with regard to ownership and management transfers. *(Paper 1)*

Increasing family influence in management will favor equality transfers with regard to management. *(Paper 1)*

Family influence in board of directors has an ambiguous role depending on whether paired with family influence in ownership or management. Family influence in the board of directors will weaken the tendency that increasing family influence in ownership will favor equity transfers whereas it weakens the tendency that increasing family influence in management will favor equality transfers. *(Paper 1)*

### 2.9.1.2 Family governance

The choice of a justice principle is a value commitment. Value statements form often part of family constitutions; hence these documents may give a hint to what degree equality and equity considerations play a role in succession. For instance, the family constitution might provide for certain conditions that family members must meet to be allowed to work in the family firm. Such provision would be an indication that the family, at least partly, applies the justice principle of equity with regard to employment in the family firm.

### 2.9.1.3 Ownership governance

Shareholder agreements as well as matrimonial and inheritance contracts indicate according to what justice principle ownership will
be transferred to the next generation. If family incumbents die without inheritance contracts or wills, ownership is, by law, split equally between descendants. If they wish to favor the most competent descendant in ownership, other heirs must renounce inheritance rights and such renouncements generally require the establishment of matrimonial and/or inheritance contracts as well as shareholder agreements.

2.9.1.4 Wealth governance

- How family firms organize their wealth has an impact on the choice of the justice principle. For example, it is likely that incumbents that have no other assets than the family firm will tend to pass on the family firm according to the justice principle of equality. This is the only way to ensure that all descendants receive a share of the economic wealth of the family. Contrary, if incumbents have other assets (e.g., real estate), it is more likely that they apply the justice principle of equity in family firm succession as they are able to bequeath non-successor descendants with other assets of financial or emotional value (e.g., holiday home).

2.9.2 Impact of choice of justice principle on future governance

2.9.2.1 Corporate governance

- The choice of a justice principle leads to different compositions of the governance bodies. If the justice principle of equality is applied multiple family members succeed in ownership, board of directors
and management. Contrary, if the justice principle of equity is applied, only one of the descendants succeeds in these governance bodies. \textit{(Paper 2)}

- As ownership is regularly divided equally between the descendants, while management is transferred based on merit to the most competent descendant the \textit{most common governance structure} is equality-ownership and equity-management. \textit{(Paper 1)}

- The application of different justice principles favors the occurrence of \textit{moral hazard} and \textit{adverse selection} in family firms to a different degree. \textit{(Paper 2)}

- \textit{Perceived injustice} in succession leads to governance challenges. The under-rewarded descendant is likely to engage in moral hazardous behaviors such as free-riding and shirking. The over-rewarded descendant is tempted to tolerate and even promote such behavior out of a feeling of guilt. \textit{(Paper 3)}

- \textit{Governance instruments} (such as monitoring, compensation incentives, family specific governance instruments, e.g., the establishment of a family constitution) need to be established to mitigate agency issues resulting from the different justice principles and perceived injustice.

\textbf{2.9.2.2 \textit{Family governance}}

- Justice principles applied in succession define future roles of the family members (family member – shareholder – board member – manager). \textit{(Paper 2)}
The future roles have an impact on the interests of the family members and their commitment to the firm.

The choice of a justice principle therewith impacts the relationship between family members and their relationship to the firm. (*Paper 2*)

Perceived injustice provokes the feelings of anger and envy on side of the under-rewarded descendant and guilt on side of the over-rewarded descendant. Those feelings are likely to create conflict between family members. (*Paper 3*)

Family cohesion is not able to mitigate the relationship between perceived injustice and resulting, firm-damaging behavior of descendants. (*Paper 3*)

Early disclosure of the justice principle of choice is necessary to mitigate agency issues resulting from perceived injustice. (*Paper 2*)

### 2.9.2.3 Ownership governance

The choice of the justice principle determines who will succeed in ownership. (*Paper 2*)

Equality transfers will lead to more complex ownership structures where decision-making processes must be clarified. Governance instruments such as shareholder agreements become important to prevent that conflicts of interests lead to stalemate. (*Paper 2*)

In equity transfers only the most competent descendant succeeds in ownership. This succession form conveys much power to the succeeding descendant. Risks are that the descendant exploits such
power to the detriment of stakeholders of the firm, or that the firm becomes heavily dependent on the descendant. Governance instruments must be established to mitigate such risks.

2.9.2.4 Wealth governance

On a micro-level the justice principle chosen in succession determines the assets that are available to each descendant, and whether they equally share and manage family wealth or whether some descendants are favored and others discriminated. On a macro level, the justice principle applied in succession defines how wealth is distributed in societies.

This chapter was designed to introduce the concepts of distributional justice and governance and to establish the relationship between the two concepts in family firm succession. The findings of the three papers were incorporated in this introduction. The three papers are summarized in more detail in Table 2. Thereafter follow the three dissertation papers.

2.10 Overview of papers

Table 2 shows a summary of the three dissertation papers.
### Table 2: Summary of the three dissertation papers

<table>
<thead>
<tr>
<th>Paper 1: How family influence determines incumbent's choice between the justice principles of equity and equality in family firm succession</th>
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<tbody>
<tr>
<td><strong>Research question</strong></td>
</tr>
<tr>
<td><strong>Research gap</strong></td>
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</table>
| **Main theoretical constructs** | – Family firm succession  
– Family influence  
– Family firm governance  
– Justice theory (distributional justice) |
| **Methodology & sample** | Logistic Regression / Questionnaire / Respondents: 1’528 incumbents |
| **Findings** | – Increasing family influence in ownership leads to equity ownership and management transfers  
– Increasing family influence in management favors equality management transfers  
– Increasing family influence in board of directors is ambiguous: It weakens the tendency that increasing family influence in ownership favors equity management transfers, but also weakens the tendency that increasing family influence in management favors equality management transfers |
| **Contribution** | Sheds light on how current governance structures impacts choice of justice principle in family firm succession |
| **Authorship** | – Sonja Kissling Streuli  
– Miriam Bird |
| **Status/external recognition** | Accepted and will be presented at the Annual Meeting of the Academy of Management (AoM) 2017, Atlanta |
**Paper 2: Relation between governance structures, agency issues, and justice principles in family firms**

| Research questions | 1. How does the choice of a justice principle in succession influence the governance structure of the family business?  
2. How does the corresponding governance structure change over time (dynamic approach)?  
3. What consequences does the choice of a justice principle have under an agency perspective? |
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<tr>
<td>Research gap</td>
<td>Impact of the choice of the justice principles of equity and equality in succession on family firm governance and governance challenge</td>
</tr>
</tbody>
</table>
| Main theoretical constructs | – Family firm succession  
– Family firm governance / principal agency theory |
| Methodology & sample | Conceptual paper |
| Findings          | The choice of one of the justice principles of equity and equality leads to different governance structures. Each governance structure has distinct governance challenges/agency issues. Correspondingly, these governance challenges/agency issues depend on the choice of the justice principle in succession |
| Contribution      | Connecting justice principles applied in succession with governance challenges/agency issues while applying a dynamic approach, i.e. investigating how governance challenges/agency issues change over time |
| Authorship        | Sonja Kissling Streuli |
| Status/external recognition | – Winner of the Roleski award for the best paper on family systems constructs  
– Presented at the International Family Research Academy (IFERA) 2015, Hamburg  
– Accepted at Annual Meeting of the Academy of Management (AoM) 2015, Vancouver |
<table>
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<th><strong>Paper 3: What goes around comes around – negative effects of perceived injustice in succession on the family firm</strong></th>
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<tr>
<td><strong>Research question</strong></td>
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<td><strong>Research gap</strong></td>
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</tbody>
</table>
| **Main theoretical constructs** | – Family firm succession  
– Organizational justice/organizational behavior  
– Injustice reduction mechanisms  
– Under- and over-rewarded descendants |
| **Methodology & sample** | Regression analysis (incl. moderator & mediator analysis) / Questionnaire / Respondents: 1’528 incumbents |
| **Findings** | – Perceived injustice leads on the side of the under-rewarded to:  
  o Shirking  
  o Free-riding  
  o Resistance to change  
  o Legal claiming  
– Perceived injustice leads on the side of the over-rewarded to:  
  o Less job satisfaction  
  o Salary increases towards the under-rewarded  
  o Toleration of less work effort of under-rewarded  
– Family cohesion is not able to mitigate these effects |
| **Contributions** | Shows that under- as well as over-rewarded descendant reverts to behavior that is detrimental to the firm |
| **Authorship** | Sonja Kissling Streuli |
| **Status/external recognition** | – Winner of the EQUA-Best Research Idea Award  
– Accepted and will be presented at the Annual Meeting of the Academy of Management (AoM) 2017, Atlanta  
– Accepted at the International Family Research Academy (IFERA) 2017, Zadar |
3 How family influence determines incumbent’s choice between the justice principles of equity and equality in family firm succession

Sonja Kissling Streuli, Miriam Bird

3.1 Abstract

When confronted with the decision of how to pass on ownership and management, incumbent family business owners can choose between two different justice principles: Equality and equity. While equality typically represents the justice principle that prevails in the family sphere, equity is the prevalent justice principle in the business sphere. Our paper investigates which justice principle incumbents intend to choose when passing on the business within the family, and how the related preferences alter depending family influence in ownership and management. Based on survey responses of 1’528 owner-managers, we found that ownership and management are passed on according to different justice principles. Surprisingly, an increased family influence in ownership leads to a preference for the equity principle in management and ownership succession. With our study, we contribute to the literatures of family business succession, justice and governance.

3.2 Introduction

Intra-familial succession is a key event in the family business life cycle (Chrisman, Chua, & Sharma, 2003; De Massis, Chua, & Chrisman, 2008; Handler, 1994; Lansberg, 1988; Le Breton-Miller & Steier, 2004; Zahra &
In succession, family firms transfer ownership and management to the next generation. Succession literature has long dealt with the question of how management and ownership are handed over to the next generation (Sharma et al., 2001). An important factor to consider in the succession process is distributional justice as family internal succession implies the allocation of goods, i.e. ownership and management to the next generation. There are several justice principles according to which goods, resources or assets, can be allocated to individuals. In family firm succession, mainly two justice principles compete: the justice principle of equity and the justice principle of equality. Incumbents essentially have to consider in the succession process whether they shall apply the justice principle of equity and select the most capable descendant as sole successor or whether they shall apply the justice principle of equality and equally split ownership and management among descendants (Deutsch, 1975; Van der Heyden, Blondel, & Carlock, 2005).

In family firms the choice between these justice principles is not clear as family firms embrace two different systems, i.e., the family and the business system (Bhappu, 2000; Greenwood, Raynard, Kodeih, Micelotta, & Lounsbury, 2011; Miller, Le Breton-Miller, & Lester, 2011; Zellweger et al., 2016). Within those two systems, two different justice principles are embedded (Kets de Vries, 1993; Lubatkin, Ling, & Schulze, 2007). In the family, the upbringing of the children is the main goal, the fostering and maintenance of enjoyable social relations (Deutsch, 1975; Drake & Lawrence, 2000; Kabanoff, 1991, Tyler, 1994). Hence, in distributional processes parents aim to treat their children equally (Drake & Lawrence, 2000). Contrary, within the business logic, goods are distributed according to the justice principle of equity (Thornton, Ocasio,
& Lounsbury, 2012). Economic productivity is the primary concern and resources are assigned based on merit to the most capable descendant (Deutsch, 1975; Leventhal, 1980; Tyler, 1994).

So far, there exists a scarcity of research investigating how incumbents deal with this dilemma of competing justice principles in family firm succession. One could argue that in firms that are influenced by families, the family norm of equality prevails whereas in non-family firms the business norm of equity is dominant. Since we believe that reality is more nuanced and in our article, we investigate how family influence determines the intended choice between the justice principle of equity over equality in family firm succession. More concretely, our study attempts to answer the following research question: *How does family influence in different governance bodies impact incumbents’ intended choice between the justice principles of equity and equality when passing on ownership and management to the next family generation?* In our article, we distinguish between ownership and management succession as these governance functions supply different degrees of economic and socio-emotional wealth to family members and therewith constitute different resources (Gómez-Mejía et al., 2007; Zellweger et al., 2013).

We draw on justice (Deutsch, 1975; Fehr & Gächter, 2000), family business (Astrachan et al., 2002; Gersick et al., 1999) and agency theory (Lubatkin et al., 2007; Schulze et al., 2003a) to develop our theoretical framework of whether family influence in ownership and management influences incumbents to choose equity versus equality transfers in ownership and management succession. We further test whether *female family owners* and *family influence in the board of directors* moderates these baseline effects.
Employing survey responses of 1’528 incumbents of Swiss small and medium-sized enterprises, we find empirical evidence that increasing family influence in ownership increases the likelihood that incumbents intend to choose the justice principle of equity in ownership as well as management succession while increasing family influence in management increases the likelihood of the application of the justice principle of equality in management successions.

Our contributions are at least threefold: First, we contribute to family firm governance literature (Aguilera & Crespi-Cladera, 2012; Gersick et al., 1999; Lubatkin et al., 2005; Schulze et al., 2001) as we show how family influence in different governance bodies impacts the intended choice between the family norm of equality versus the business norm of equity in family firm succession. We thereby contribute to previous findings that “family influence” cannot be lumped together and that family firms have to be distinguished based on the governance body the family exercises its influence on (Faccio & Lang, 2002; La Porta et al., 1999; Villalonga & Amit, 2006). Further, the choice of the justice principle determines future governance structures in family firms and therewith is a reason why family firms run through evolutionary transitions, devolutionary transitions or recycles (Gersick et al., 1999).

Second, we contribute to the literature on family firm succession (Barach & Ganitsky, 1995; Bennedsen, Nielsen, Perez-Gonzalez, & Wolfenzon, 2007; De Massis et al., 2008; Ward & Dolan, 1998) by providing evidence under which circumstances incumbents intend to choose the justice principle of equity versus the justice principle of equality in family firm succession. The study clarifies what drives incumbents’ justice perceptions and how this is rooted within the firm’s exposure to the family. Our findings help theory and practice...
to tackle different perceptions of (in-)justice and entitlements of the parties involved (Kabanoff, 1991; Lerner, 1987; Van der Heyden et al., 2005).

Lastly, according to justice theory, justice is a relative, context-dependent, and individual construct (Breugst et al., 2015; Colquitt & George, 2011; Deutsch, 1975; Fondacaro, Jackson, & Luescher, 2002; Tornblom & Foa, 1983) and correspondingly, what is perceived as fair depends on the specific circumstances of the allocation, the parties to the allocation and the resources to be distributed. We extend this stream of literature by shedding light on how the choice for a justice principle is effected in the family firm succession context and thereby differentiate between ownership and management succession to find out whether and to what extent these goods are allocated according to different justice principles.

3.3 Theoretical background

3.3.1 Choice between conflicting distributional justice principles in family firm succession

In every distribution, there are several distributive justice principles available, e.g., equality, equity, need, seniority, or first-come-first-serve (Messick, 1999), according to which allocators may determine the outcome of an allocation. In view of this multidimensional concept of distributive fairness – what factors influence which justice principle is applied?

Primarily, such choice depends on the context of the distribution (Leventhal, 1980). In family firms two different contexts meet. The family context and the business context. It has been argued that in the context of the family, where
interpersonal relations and group solidarity are of primary concern, the *justice principle of equality* prevails (Deutsch, 1975; Leventhal, 1980). Within the nuclear family, the upbringing of the children is the major goal besides fostering and maintenance of stable social relations (Deutsch, 1975; Lubatkin, Schulze, Ling, & Dino, 2005; Miller et al., 2011; Schulze et al., 2001; Morek, Wolfenzon, & Yeung, 2005). Family members’ interaction is characterized by its unconditional nature (Friedland & Alford, 1991) and therefore parents allocate resources independent of children’s contributions. Such *resources* can be classified in different categories, such as for instance love, money, goods, status, information, and services (Tornblom & Foa, 1983). It would contradict the very essence of the family, if parents allocated these resources to their children based on economic rationale (Clark & Chrisman, 1994). Parents follow the justice principle of equality as they further aim at preventing rivalry and conflict and seek to preserve harmony among the siblings (Von Schlippe & Kellermanns, 2008). In fact, research has shown that the relationship quality among siblings and parents was highest when siblings were treated equally (Boll, Ferring, & Filipp, 2005). Although it has been argued that in close relationships other justice principles as for instance need play a role (Clark & Chrisman, 1994), it has been established that the justice principle of equality serves as a default rule in families in Western societies, especially in the context of allocations made in case of parents death (Drake & Lawrence, 2000; Simon, Rau, & Fellows, 1980). The egalitarian treatment of children is the result of societal efforts in the last century to overcome primogeniture and discrimination of female and non-marital children (Drake & Lawrence, 2000; Simon et al., 1980).
Contrary, distributional processes within the *business context* most commonly apply the *justice principle of equity* (Deutsch, 1975). This phenomenon must be viewed against the background of the economic system dominant in the Western world. Capitalism is the economic and social order that developed at the end of the 18th century and continuously shapes economic exchange relations (Friedman, 1982; Pryor, 2010). Capitalism defines how the means of productions are to be distributed among various parties in order to increase profit. The argument put forth by capitalist theory is that division of labor, competition and individuals’ rational self-interest lead to the economic well-being of the whole society (Smith, 1776). Meritocracy, is intrinsically tied to capitalism and constitutes a departure from feudal structures. The allocation of resources to those who contribute more serves hereby as an incentive. Such merit-based allocation – to those who are able to use the allocated resources most effectively (Baldridge & Schulze, 1999; Deutsch, 1975; Walzer, 1983) – is assumed to be socially justified as it will result in increasing prosperity of the whole society with compensating benefits also for less advantaged members of society (Rawls, 1971).

In *family business succession*, the family norm suggests a succession according to the equality principle, whereas the business norm calls for the justice principle of equity (Bhappu, 2000; Lansberg, 1983; Lubatkin et al., 2005; Miller et al., 2011; Titus, Rosenblatt, & Anderson, 1979; Zellweger et al., 2016). In case incumbents choose the justice principle of equality they transfer ownership, respectively management equally to all their descendants. Contrary, if incumbents choose the justice principle of equity, they transfer the business to the most capable descendant who is able to employ the allocated resources – the family firm – most effectively.
Given that family firms are exposed to both, the family and the business context, the two justice principles of equality and equity are competing (Rosenblatt, de Mik, Anderson, & Johnson, 1985). In the following, we will investigate how family influence in different governance bodies influence the intended choice of justice principles in the context of family firm succession. Our aim is to reveal the degree of family influence that determines the choice between the family norm of equality and the business norm of equity (Astrachan, Klein, & Smyrnios, 2002; Cliff & Jennings, 2005; Klein, Astrachan, & Smyrnios, 2005; Tagiuri & Davis, 1996).

Besides the context, it has been established that the choice of a justice principle depends on the type of resources allocated (Tornblom & Foa, 1983). Tornblom & Foa (1983) found for instance that the justice principle of equity is most prominent when status is involved or that in money distributions, the justice principles of equity and equality are equally appropriate (Tornblom & Foa, 1983). In family firm succession, ownership and management provide economic and non-economic or socio-emotional resources to descendants (Gómez-Mejía et al., 2007; Zellweger et al., 2013). Both functions offer family members income (salary or dividends), information rights or status. However, ownership and management differ in terms of the quantity of economic and non-economic resources provided and the necessary services required of family members in return for these resources. As ownership and management therewith include different types of resources, it is highly likely that they are allocated according to different justice principles (Tornblom & Foa, 1983).
Further, scholars argue that individuals’ choice for a specific justice principle is partly motivated by *self-interest* and *altruism* (Fehr & Gächter, 2000; Homans, 1958; Karni & Safra, 2002; Montada, 1998). Self-interested behavior is associated with the goal to increase one’s own welfare while altruistic behavior is associated with the goal to increase the welfare of others (Fehr & Gächter, 2000; Lubatkin et al., 2007; Lubatkin et al., 2005; Meeker, 1971; Schulze, Lubatkin, & Dino, 2002). So, it might be that the decision for a certain justice principle is made in order to obtain benefits for oneself, or in order to provide such benefits to others.

Lastly, the choice for a particular justice principle in succession may be made out of *practical reasons*. For instance, Drake & Lawrence (2000) argue that the supremacy of the justice principle of equality in the Western society is to some degree due to its high feasibility to implement. Equal inheritance distributions are objectively measurable and hence easy to effect (i.e. half of assets). Contrary, distributions based on the justice principle of equity include a complex and subjective assessment of the merits (e.g., capabilities) of the possible recipients (Drake & Lawrence, 2000).

In sum, the choice of the justice principle in family firm succession is influenced by the context, the resources allocated, self-interest, altruism and feasibility.

### 3.4 Hypotheses development

Family business scholars have investigated how the presence of family influence in a business impacts the firm strategy and consequently its performance (Garcia-Castro & Aguilera, 2014; Miller & Le Breton-Miller, 2006; Zellweger, Eddleston, & Kellermanns, 2010). The overall goal of such
studies has been to explore whether and under which conditions such family influence has a positive or negative impact on firm performance. Scholars thereby distinguish between different kinds of family firms and differentiate whether and to what extent the family is present in the governance functions of ownership, management and board of directors (Anderson & Reeb, 2003, 2004; Chua et al., 1999). Research has shown that there exist firms in which all these governance functions are concentrated within the hand of a single owner manager or some family members while in other firms, the family influence is limited to a controlling function. Often, the different governance structures of family firms result from the transitions between generations and move from a controlling owner to a sibling partnership and then to a cousin consortium stage (Gersick et al., 1999).

In acknowledging that families exercise their influence in different governance functions (Astrachan et al., 2002; Cliff & Jennings, 2005; Klein et al., 2005; Tagiuri & Davis, 1996), we hereinafter differentiate between those functions to investigate how this influences the intended choice between the justice principle of equity and equality in family firm ownership and management succession.

3.4.1 Ownership succession

3.4.1.1 Family influence in ownership

We argue that increasing family influence in ownership increases incumbents’ likelihood to choose ownership successions according to the justice principle of equality due to the following reasons.
First of all, family owners prefer family internal transfers of ownership over family external transfers (Dehlen, Zellweger, Kammerlander, & Halter, 2014; Wiklund et al., 2013). It is the common norm in Western societies, and also manifested in law, that distributions of inheritance in families are effected according to the justice principle of equality (Drake & Lawrence, 2000).

Besides parents’ moral and legal obligation, also altruism and the nurturing identity of parents speak in favor of the equality principle (Schulze et al., 2003a). Parents wish to equip their children with resources that can provide them with potential gains over a longer time period. This goal is better served if they bequeath their children with an ownership stake in the family firm, as such a tied transfer (tied as the transfer of wealth is concentrated in business ownership) prohibits children from spending the resource quickly and inefficiently (Bruce & Waldman, 1991). A tied transfer therefore constitutes an efficient response to the Samaritan’s dilemma (Buchanan, 1975). It allows parents to act altruistically towards their children without spoiling them.

Additionally, a high ownership share held within the family often implies that the larger share of the family’s wealth is concentrated within the firm (Anderson & Reeb, 2003). Especially in small and mid-sized companies family’s wealth is concentrated within the company and family incumbents usually have no other assets to transfer to their children (Anderson, Mansi, & Reeb, 2003; Duran, Kammerlander, van Essen, & Zellweger, 2016). Moreover,

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3 This norm is also reflected in Swiss intestacy rules that apply in the event the decedent left no other instructions in a will.
4 The Samaritan’s dilemma explains the situation of parents (Samaritans) who with their good actions spoil and ultimately harm their children as the latter get accustomed to parents’ altruism and cannot help themselves.
having all children in ownership positions will increase socioemotional wealth of the whole family and ensure legacy of the firm (Gómez-Mejía et al., 2007; Zellweger, Nason, & Nordqvist, 2012).

Further, also practical reasons speak in favor of the justice principle of equality. Today, most firms are legal entities in form of stock corporations or limited liability companies which allow for shared ownership. Therefore, shares can be divided without difficulties and the justice principle of equality is easy to implement.

Lastly, incumbents generally believe that holding an ownership stake – different from management – does not require special skills or abilities of their offspring and therefore considerations with regard to children’s capabilities lose in importance (Chrisman et al., 1998; Le Breton-Miller et al., 2004).

Hence, we argue that with increasing family influence in ownership, incumbents intend to choose the justice principle of equality in ownership succession. Correspondingly, we propose the following hypothesis:

*Hypothesis 1a. Increasing family influence in ownership increases the likelihood that incumbents intend to choose the justice principle of equality when transferring ownership in family firm succession.*
3.4.1.2 Family influence in management

We argue that increasing family influence in management will increase the likelihood of the application of the *justice principle of equality* in ownership transfers.

Strong family influence in management is usually found in family firms in early stages, i.e. owner-manager run firms or sibling partnerships (Gersick et al., 1999). In the event that managers are family members, they can directly impact the course of the business, as they have the decision-making power and are involved in the day-to-day business (Anderson, Mansi, & Reeb, 2003; Anderson & Reeb, 2003; Sharma & Manikutty, 2005). As family managers will introduce family norms and values into the firm, family’s presence in management will shape firm behavior (Chrisman et al., 2005; Gomez-Mejia et al., 2001; Schulze et al., 2002, 2001).

In later generations, family firms tend to professionalize (Chua, Chrisman, & Bergiel, 2009; Sharma, Chrisman, & Chua, 1997; Stewart & Hitt, 2012). Family firm professionalization is multi-dimensional and includes that family firms delegate management to non-family members (Daily & Dalton, 1992; Gedajlovic et al., 2004). Professionalization therewith implies a shift towards the justice principle of equity, whereas family firms evaluate performance of managers and reward them based on merit (Chua et al., 2009; Stewart & Hitt, 2012). As long as family managers are around, family norms will by contrast strongly influence decision making in the family firm. Stewart & Hitt (2012) explain that family norms constitute a cultural impediment to professionalization, as incumbents are expected to display their wealth
amongst their kin and to provide family members with responsible positions in the family firm. Overall, strong family influence in the management and the therewith connected strong presence of family values indicates the application of the justice principle of equality.

Further, family managers often feel remorse as they have not spent enough time with their descendants. Family managers work day and night and are regularly not emotionally available for their children (Kets de Vries, 1993). This kind of behavior leads to feelings of guilt and incumbents deal with those feelings by bribing family members (Kets de Vries, 1993), first with a teddy bear, then with expensive vacations and lastly with ownership in the family firm. Hence passing on ownership equally to the descendants is a means to make up for incumbents’ absence from family life (Schulze et al., 2002).

So, we argue that management presence of family is a sign that ownership will be passed on according to the justice principle of equality. Even though managers themselves do not have the power to transfer ownership of the company, a strong presence of family members in the top management team will increase the likelihood that family norms prevail and ownership is passed on according to the justice principle of equality.

*Hypothesis 1b. Increasing family influence in management increases the likelihood that incumbents intend to choose the justice principle of equality when transferring ownership in family firm succession.*
3.4.2 Management succession

3.4.2.1 Family influence in ownership

Family owners indirectly appoint the management\(^5\) and generally wish to keep the management of the family firm within the family (Andric et al., 2016). Whether they thereby apply the justice principle of equity or equality is unclear, there are arguments in favor of both justice principles.

On the one hand, the application of the justice principle of equality is likely, as one can observe – considering the issues of adverse selection in family firms – that family norms influence management succession in general. Also, altruism and the nurturing identity of family incumbents speak in favor of equality transfers as in transferring management equally, incumbents are able to pass on a steady income and corresponding privileges to all descendants (Schulze et al., 2002). Lastly, when management (and ownership) is transferred to all descendants equally, there is no separation of ownership and management what reduces corresponding agency issues resulting from conflicts of interests (Schulze et al., 2002).

However, we argue that increasing family influence in ownership will increase the likelihood of management transfers according to the justice principle of equity out of the following reasons.

\(^5\) Owners have by law the power to appoint members of the board of directors and the board of directors in turn elects the members of the management.
Family owners, as owners in general aim to increase their shareholder value. Only continued wealth creation guarantees the continued and transgenerational existence of the family firm (Habbershon et al., 2003). Hence, family owners aim to select a successor manager that is competent and can ensure that the future of the firm is in good hands. Moreover, a high ownership stake of the family is a sign that a high amount of family’s wealth is concentrated within the firm (Anderson et al., 2003; Zellweger et al., 2016). This undiversified wealth position means that family members highly depend on firm performance. Increasing endowment effects result from the fact that families not only fear the loss of financial but also socioemotional wealth (Gómez-Mejía et al., 2007). The management of companies requires special skills and capabilities (Bennedsen, Nielsen, Perez-Gonzalez, & Wolfenzon, 2007; Kets de Vries, 1993), and it is unlikely that all descendants possess the necessary talent and competence. Acknowledging this risk of adverse selection, family firms nowadays often establish requirements which descendants must fulfill to work in the family firm (Verbeke & Kano, 2012). So, it is likely that family owners revert to the justice principle of equity in management succession and allocate management based on merit to the descendant who is most able to increase family’s financial and socioemotional wealth (Deutsch, 1975; Sharma et al., 2001).

Also, the justice principle of equality is less easy to implement in management than in ownership transfer. Sharing of management tasks among descendants often leads to conflicts that endanger family harmony and the survival of the firm (Kidwell et al., 2012; Ward & Aronoff, 1992).
Accordingly, we argue that with increasing family influence in ownership the likelihood of the application of the justice principle of equity increases since the family is highly concerned with maintaining its financial and socioemotional wealth. These arguments lead us to posit following hypothesis:

*Hypothesis 2a. Increasing family influence in ownership increases the likelihood that incumbents intend to choose the justice principle of equity when transferring management in family firm succession.*

### 3.4.2.2 Family influence in management

For this particular context, some of the above-mentioned reasoning will also apply. While altruism, alignment of interests, the nurturing identity of parents and the risk of losing financial and socioemotional wealth speak in favor of the justice principle of equality (Lubatkin et al., 2005; Schulze et al., 2002), the difficulty of dividing management tasks among descendants speaks in favor of the justice principle of equity.

In addition, there are further arguments that must be considered in case of family influence in management and that let us suggest that increasing family influence in management will increase the likelihood of management transfers according to *the justice principle of equality*.

First, in family-managed firms the degree of closeness of family members is usually very high and family and company are very much intertwined (Gersick et al., 1999). Therefore, family values, reflected in the justice principle of equality, are more prevalent in the business. Further, if management is split
among descendants, shared management enables descendants to also share the burdens that family firm management brings along (Schulze et al., 2002). Incumbents know about the downsides of family firm management and may hope that a shared responsibility will ease such burden for their descendants (Munoz-Darde, 1998; Ward, 1997). The role of incumbents, their personality and motivation strongly influence succession process (Dyer, 1986; Le Breton-Miller et al., 2004). Incumbents who manage the family firm will due to their experience and their tacit knowledge see more opportunities than pure family owners to divide management tasks among their descendants, which increases feasibility of shared management. Lastly, incumbents are more likely to believe that skills can be acquired and that experience will teach their children how to manage the company (Ward & Aronoff, 1992). Correspondingly, they are in general less afraid of losing financial or socioemotional wealth when transferring the company to their offspring. Hence, we posit the following:

*Hypothesis 2b. Increasing family influence in management increases the likelihood that incumbents intend to choose the justice principle of equality when transferring management in family firm succession.*

### 3.4.3 Moderating effects

In the following we analyze more thoroughly the nature of family influence and discuss two boundary conditions that we expect to influence the baseline relationship.
3.4.3.1 Female family owners’ role in ownership and management succession

We argue that the presence of female family owners increases the likelihood of the application of the *justice principle of equality* in both, *ownership and management succession*.

Within the entrepreneurship research field, it has been established that female entrepreneurs follow different rationales in business decisions (Brush, de Bruin, & Welter, 2009) and hence it has been termed that entrepreneurial processes are highly gendered (Eddleston & Powell, 2008).\(^6\)

With regard to distributional processes men and women were found to display different behavior (Cohen-Charash & Spector, 2001). Previous research found that females’ major concern in a distribution process is to maintain the welfare of group members (Leventhal & Lane, 1970). In their interaction with others, females tend to be more relationship-oriented while men will exhibit a more competitive stance (Ahl, 2002; Kahn, O’Leary, Krulewitz, & Lamm, 1980). Applying these considerations to the family context and the parenting style of men and women, fathers will be more inclined to apply a merit based award system, contrary, mothers will aim to treat their children equally. Further, at least according to traditional role models, mothers are expected to have a stronger nurturing identity than fathers (Baumrind, 1991). We therefore expect that female family owners will be more inclined than their male counterparts to intend to choose the justice principle of equality in intra-family ownership.

\(^6\) For instance, Sexton & Bowman-Upton (1990) established that female entrepreneurs have different perceptions with regard to risk taking.
succession (Kahn et al., 1980). They will transfer ownership equally as therewith they prevent rivalry and conflicts between siblings and at the same time make a provision for their children’s future. Correspondingly:

_Hypothesis 3a. Increasing presence of female family owners reinforces the positive relationship between increasing family ownership and the likelihood that incumbents intend to choose the justice principle of equality when transferring ownership in family firm succession._

Increasing presence of female family owners will also increase the likelihood of applying the justice principle of equality in management succession. Females wish to provide descendants with the same opportunities in life. Equal management transfer will offer female owners the opportunity to provide descendants with a steady income and a purpose in life (Lubatkin, Durand, & Ling, 2007; Miller et al., 2011). Moreover, it has been established that relationship quality with mothers deteriorated when descendants felt disfavored (Boll et al., 2005). Because of their concern for maintaining good relationships with descendants, females will try to avoid discrimination of their descendants. Hence, our arguments lead us to following hypothesis:

_Hypothesis 3b. Increasing presence of female family owners weakens the positive relationship between increasing family ownership and the likelihood that incumbents intend to choose the justice principle of equity when transferring management in family firm succession._
3.4.3.2 Family board members’ role in management succession

We argue that increasing family influence in the board of directors is ambivalent in management succession: Combined with family influence in ownership, it will increase the likelihood of management transfers according to the justice principle of equity, contrary, combined with increasing family influence in management it will increase the likelihood of management transfers according to the justice principle of equality.

The board of directors has two primary functions. On the one hand, it has a monitoring function towards the management. On the other hand, it provides resources to the company in form of knowledge and expertise (Hillman & Dalziel, 2003). In governance literature, the monitoring function refers to the responsibility of the board members to control the management on behalf of the shareholders (Hillman & Dalziel, 2003). As agency theory posits, managers and shareholders have different interests (Jensen & Meckling, 1976). Hence the board’s duty is to supervise the actions of the managers in the company and make sure that they do not contravene the interests of the shareholders (Berle & Means, 1932; Eisenhardt, 1989; Fama & Jensen, 1983; Jensen & Meckling, 1976). In order to fulfill their duties effectively it has been stipulated (Daily, 1995) that board members should be firm-external, i.e. not serve or have served in the company. Correspondingly, there is a preference for these so called “independent directors” in governance literature (Daily, 1995) with regard to the board of directors’ monitoring function.

The board of directors is responsible to elect the management and to plan leadership succession. Independent board members thereby often prevent
unqualified or incompetent family members from taking on the CEO position (Anderson & Reeb, 2004; Corbetta & Salvato, 2004; Shleifer & Vishny, 1997). Therefore, independent board members are expected to act as guarantors for merit-based decisions, whereas family board members are regularly suspected to give preference to family norms. We argue, that family board members’ influence is more nuanced and heavily depends on the family influence in the other governance bodies, i.e. ownership and management. As explained above, in management succession, family owners prefer to choose the justice principle of equity when handing over ownership. The presence of family board members will reinforce this tendency as they are elected and instructed by the owners and therewith act as “extended arm” of the family owners. So, we put forth the following hypothesis:

Hypothesis 4a. Increasing family influence in the board of directors reinforces the positive relationship between increasing family influence in ownership and the likelihood that incumbents intend to choose the justice principle of equity when transferring management in family firm succession.

Contrary, we argued that family influence in management is associated with the application of the justice principle of equality in management succession. We explained that with family influence in management, the influence of family norms is very high as family and company are so closely connected. In these situations, family presence in the board of directors is not able to mitigate but will further promote the dominance of family values and increases the likelihood of incumbents to choose the justice principle of equality. Correspondingly, we posit the following:
Hypothesis 4b. Increasing family influence in the board of directors reinforces the positive relation between increasing family influence in management and the likelihood that incumbents intend to choose the justice principle of equality when transferring management in family firm succession.

3.5 Methodology

3.5.1 Sample and data collection

To empirically test how family influence determines the choice between the justice principles of equity and equality, we collected survey responses from small- and medium-sized enterprises (SMEs). SMEs are firms defined as firms with less than 250 employees. Data collection was conducted in January and February 2016 via physical mail to randomly chosen managers of 38‘049 privately held SMEs located in Switzerland. The distribution of the survey participants deviates slightly from the sector and size structure of the overall Swiss SME landscape reflected in the most recent statistics on corporate structure (STATENT) of the Swiss Federal Statistical Office (SFSO) from the year 2013. Construction and industrial firms are slightly overrepresented in our sample, while SMEs from service sectors are underrepresented. In addition, micro firms with fewer than ten full-time equivalents (FTEs) are underrepresented in the survey compared to their actual frequency in Switzerland.

7 We excluded the following sectors from the analysis: Agriculture/forestry, energy/water supply, finance/insurance, public administration.
In total, we received 1’528\textsuperscript{8} survey responses. We further limited the sample to owner-managers of SMEs, who indicated that they were managers of the company owning a minimum stake of 20% in the company. Correspondingly our final sample consists of 1’234 respondents who can be qualified as key informants (e.g., Kellermanns et al., 2008). The final sample represents about 0.22% of the total SMEs in Switzerland (561’619: Schweizerische Eidgenossenschaft, 2014). As regards the characteristics of the firm, the average number of employees is 25.1. As regards the characteristics of the owner-manager, they have an average age of 54 years, an average tenure of 16.7 years and 9.33% are female. 77.4% of the owner-managers are married and they have on average 2 children. In the light of these owner-manager characteristics, we believe to have a reliable sample to analyze distributive justice questions in family internal succession.

As dependent and independent variables stem from the same respondents, we must address common method variance. First, we point out that the independent variables are fact-based (e.g., % of family ownership, % of family members in the management) and correspondingly common method bias is less likely (Chang, van Witteloostuijn, & Eden, 2010). The questionnaire was further subdivided in the sections A-E. Thus, independent and dependent variables were not inquired in the same section. In section C, we asked about succession plans and included a scenario assuming family internal succession to investigate the justice principle of choice (constituting our dependent variable). The demographic characteristics of the respondent, information

\textsuperscript{8} This corresponds to a response rate of 4.02%. We ascribe the low response rate to the fact that the questionnaire was rather long.
about the family situation and the firm characteristics were inquired in separate sections.

The survey was drafted so that respondents could not make assumptions about the studied relationships (Podsakoff, MacKenzie, Lee, & Podsakoff, 2003). Moreover, we applied two post-hoc tests: Harman’s single factor test and the marker variable test (Lindell & Whitney, 2001).

First, to conduct the Harman single factor test, we entered all variables of Model 3 (independent, dependent, control and moderating variables), separately for the two dependent variables ownership and management succession, into an exploratory factor analysis using principal component factor analysis (Podsakoff et al., 2003). For ownership succession, five factors have an eigenvalue greater than one, all accounting for 57.72% of the total variance. The first factor explains only 19.43% of the total variance what indicates that no single factor accounts for the majority of the variance. Regarding management succession, six factors have an eigenvalue greater than one, all accounting for 65.06% of the total variance. As only 19.4% of the total variance are explained by the first factor, again no single factor accounts for the majority of the variance.

Further, we conducted the marker variable test (Lindell & Whitney, 2001) investigating the correlation between our dependent variables (justice principles applied in ownership and management transfer) and another variable that should be uncorrelated with our dependent variables, called marker variable (Homburg, Klarmann, & Schmitt, 2010). This variable is then used to correct the correlation matrix for common method bias. We assessed the
correlation between the marker variable “existence of a family charter” and the intended choice of the justice principle when transferring ownership \( (r = -0.0404) \), respectively management \( (r = -0.0108) \). This predictor has insignificant correlations with the dependent variables. Overall, the statistical significance and correlations do not change, which provides further evidence that common method bias is not present (Van Doorn & Verhoef, 2008).

### 3.5.2 Measures

#### 3.5.2.1 Dependent variables

In order to examine what justice principle respondents intend to choose in family internal succession, we provided them with a case vignette. This methodology is often used in justice research (Drake & Lawrence, 2000). For example Drake & Lawrence (2000) used hypothetical inheritance vignettes that varied children’s needs and deservedness to inquire adults’ judgements about inheritance distributions to children. Vignettes allow to manipulate some critical factors (e.g., existence of more than one descendant) that is needed to inquire value judgments. The wording of our vignette was as follows:

> “Assuming that you transfer your business to your descendants (you own 100% of the business), how would you transfer management, respectively ownership (i.e., your shares in the company)? Assume that all descendants are interested in taking over management, respectively ownership. Please choose only one answer for each column, management (ownership):

I transfer management (ownership):
1) to the descendant with the highest entrepreneurial capabilities,
2) to all descendants equally,
3) to the eldest son,
4) to the eldest daughter.”

Separate columns were provided for answering the above-mentioned questions for management and ownership succession.

Options 3 and 4 take into account that in some families the traditional justice principle of primogeniture (i.e., the first born) may still play a role, however, as the results show this justice principle was elected only by a small minority (2.62% in management succession; 2.61% in ownership succession). We therefore excluded it from the main analysis.

We then created a dichotomous variable as dependent variable, i.e. for transfer of ownership and transfer of management, whereby “0” indicates equity transfers and “1” equality transfers, which we coded separately for ownership and management succession. Overall, 83.27% of the respondents stated that they would transfer management according to the justice principle of equity. In contrast, a 66.16% of all owner-managers stated that they transfer ownership according to equality.

3.5.2.2 Independent variables

Family influence in ownership. We asked for the ownership share held by family members (measured in %). We computed the logarithm (log) of this variable as it has a skewed distribution.
Family influence in management. We computed this variable by dividing the number of family managers by the total number of managers.

3.5.2.3 Control variables

We controlled for the following variables on industry-, firm-, family- and individual level that have been found to be important in prior studies of family business and justice research.

Industry. Industry may be a critical driver of the type of successor chosen (Le Breton-Miller et al., 2004), hence we computed a dummy variable and considered companies active in the secondary sector (manufacturing) being equal to “0”, while firms of the tertiary sector (services) were coded as “1”.

Firm age. We measured firm age as the number of years since the company was founded. We controlled for firm age as with increasing firm age the family firm will be more inclined to the justice principle of equity. Over time family firms adopt more professional governance structures (Barry, 1989; Gersick et al., 1999) and the boundaries between family and firm become succinct. Therewith family norms will be less dominant (Sonfield & Lussier, 2004; Stewart & Hitt, 2012), and the family becomes more business oriented (Cabrera-Suarez, Saa-Perez, & Garcia-Almeida, 2001; Klein et al., 2005; Lumpkin & Dess, 1996; Zellweger et al., 2012).

Firm size. Firm size was measured as the number of employees. In small firms more than one successor, i.e. equality transfers, might just be not feasible as there is not enough work for multiple family members, hence we controlled for firm size.

Performance. We measured performance by computing the average relative growth rate in operating revenues for the period between 2013 and 2015.
Market patterns and performance influence succession patterns (Miller, Steier, & Le Breton-Miller, 2003). Incumbents of low performing companies may consider it a better choice to apply the justice principle of equity and hand over the company to the descendant that most capable of turning the company around.

**Family cohesion.** Family cohesion reflects the quality of the relationship between the family members and refers to the degree of connectedness and emotional bonding in the family (Dyer & Handler, 1994; Fondacaro et al., 2002; Lansberg & Astrachan, 1994). Family cohesion will correspondingly vary depending on the relationship between the individuals (Wiklund et al., 2013). Competitive behavior and merit-based decisions jeopardize relationships and are hence unlikely to create cohesion (Kidwell et al., 2012; Sorenson, 1999). High family cohesion will therefore call for the application of the justice principle of equality. Contrary, where family cohesion is low, equal sharing of ownership and management is less likely (Barach & Ganitsky, 1995). We assessed family cohesion via four items from the FACES III scale (Olson, 1986, 1991). Respondents could indicate on a seven-point scale within the range: “I strongly to I completely agree”. The construct consisted of six items: 1) “family togetherness is very important”, 2) “family members feel very close to each other”, 3) “when our family gets together for activities, everybody is present”, 4) “family members ask each other for help”, 5) “family members consult other family members on their decisions”, and 6) “family members like to spend their free time with other” (see also Zellweger et al., 2015). The Cronbach’s alpha reaches 0.916 and signals high reliability of our construct.

**Region.** What is perceived as fair is culturally dependent (Carney, 2005; Meindl, 1989). The extent to which culture influences successions based on
merit as opposed to kinship differs (Gupta & Levenburg, 2010: “competitive succession”). Switzerland comprises different cultures what is reflected by the situation that there are three main languages spoken: German, French, and Italian (a small minority speaks Rhaeto-Romanic). People from the German speaking part are said to put a higher emphasis on equity and competition than people from Latin Switzerland, the French and Italian speaking part (Hofstede, 2016). Hence, we controlled for region and coded a dummy variable whereas 0 represents questionnaires sent out in the German-speaking region (76.79%) and 1, questionnaires that were sent out in the French and Italian regions of Switzerland (23.21%).

**Age of respondent.** We controlled for age of owner-managers as individuals might change their justice judgments with increasing age. We asked respondents in which year they were born and such was deducted from 2016.

**Gender.** Male and female act differently in distributional processes as females are more likely than males to apply the justice principle of equality (Ahl, 2002; Cohen-Charash & Spector, 2001; Kahn, Krulewitz, O’Leary, & Lamm, 1980; Leventhal & Lane, 1970). Correspondingly we controlled for gender on an individual level and coded a dummy variable whereas “0” denotes to male and “1” to female.

### 3.5.2.4 Moderating variables

**Female family owners.** We computed this variable by dividing the number of female family owners by the total number of owners (Wiklund et al., 2013).

**Family influence in board of directors.** We computed this variable by dividing the number of family members of the board of directors by the total number of members of the board of directors.
3.5.3 Data analysis

Descriptive statistics including number of observations, means, standard deviations, and correlations for all variables used in the logistic regression analysis can be found in Table 1.

The table shows acceptable levels of correlation between independent and control variables being lower than 0.2 (Hair, Black, Babin, Anderson, & Tatham, 2006). The Variance Inflation Factors (VIF) values are all below the accepted threshold of 4 (Hair et al., 2006) with the highest VIF amounting (2.16) indicating that multicollinearity is not a major concern for our study.
Table 3: Descriptive statistics and correlations of variables

<table>
<thead>
<tr>
<th>Obs</th>
<th>Mean</th>
<th>Std. Dev.</th>
<th>VIF</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
<th>11</th>
<th>12</th>
<th>13</th>
<th>14</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Ownership succession</td>
<td>1046</td>
<td>0.662</td>
<td>0.473</td>
<td>n.a.</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Management succession</td>
<td>1076</td>
<td>0.167</td>
<td>0.373</td>
<td>n.a.</td>
<td>0.279*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Family influence in ownership</td>
<td>1258</td>
<td>3.387</td>
<td>1.961</td>
<td>2.08</td>
<td>-0.117*</td>
<td>-0.110*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Family influence in management</td>
<td>1228</td>
<td>56.153</td>
<td>43.625</td>
<td>1.92</td>
<td>-0.023</td>
<td>0.001*</td>
<td>0.601*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>Female family owners</td>
<td>1234</td>
<td>14.873</td>
<td>25.458</td>
<td>1.27</td>
<td>0.053</td>
<td>0.018</td>
<td>0.260*</td>
<td>0.354*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>Family influence in board of directors</td>
<td>953</td>
<td>57.974</td>
<td>41.997</td>
<td>2.16</td>
<td>-0.063</td>
<td>-0.026</td>
<td>0.651*</td>
<td>0.649*</td>
<td>0.342*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>Industry</td>
<td>1228</td>
<td>0.541</td>
<td>0.499</td>
<td>1.08</td>
<td>0.001</td>
<td>-0.046</td>
<td>-0.070*</td>
<td>-0.004</td>
<td>0.100*</td>
<td>-0.052</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>Firm age</td>
<td>1214</td>
<td>43.440</td>
<td>35.735</td>
<td>1.13</td>
<td>-0.102*</td>
<td>-0.062*</td>
<td>0.190*</td>
<td>0.085*</td>
<td>0.069*</td>
<td>0.131*</td>
<td>-0.197*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td>Firm size</td>
<td>1258</td>
<td>25.137</td>
<td>32.894</td>
<td>1.15</td>
<td>-0.021</td>
<td>-0.089*</td>
<td>0.049</td>
<td>-0.151*</td>
<td>-0.070*</td>
<td>-0.069*</td>
<td>-0.151*</td>
<td>0.277*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>Performance</td>
<td>1106</td>
<td>0.057</td>
<td>0.393</td>
<td>1.03</td>
<td>-0.004</td>
<td>0.006</td>
<td>-0.031</td>
<td>-0.013</td>
<td>0.057</td>
<td>-0.017</td>
<td>0.056</td>
<td>-0.117*</td>
<td>-0.020</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>11</td>
<td>Family cohesion</td>
<td>1194</td>
<td>5.307</td>
<td>1.335</td>
<td>1.01</td>
<td>0.065*</td>
<td>0.034</td>
<td>0.054</td>
<td>0.078*</td>
<td>0.082*</td>
<td>0.041</td>
<td>-0.001</td>
<td>-0.002</td>
<td>0.012</td>
<td>0.003</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>12</td>
<td>Region</td>
<td>1258</td>
<td>0.232</td>
<td>0.422</td>
<td>1.05</td>
<td>0.083*</td>
<td>0.093*</td>
<td>-0.034</td>
<td>0.048</td>
<td>-0.009</td>
<td>-0.042</td>
<td>0.016</td>
<td>-0.022</td>
<td>-0.040</td>
<td>-0.052</td>
<td>0.048</td>
<td>1</td>
</tr>
<tr>
<td>13</td>
<td>Age respondent</td>
<td>1132</td>
<td>53.965</td>
<td>9.994</td>
<td>1.05</td>
<td>-0.067*</td>
<td>-0.040</td>
<td>0.075*</td>
<td>0.083*</td>
<td>0.009</td>
<td>0.046</td>
<td>0.029</td>
<td>0.046</td>
<td>-0.064*</td>
<td>-0.054</td>
<td>-0.023</td>
<td>0.048</td>
</tr>
<tr>
<td>14</td>
<td>Gender respondent</td>
<td>1136</td>
<td>0.093</td>
<td>0.291</td>
<td>1.13</td>
<td>0.027</td>
<td>0.004</td>
<td>0.004</td>
<td>0.044</td>
<td>0.329*</td>
<td>0.061</td>
<td>0.134*</td>
<td>-0.054</td>
<td>-0.096*</td>
<td>-0.011</td>
<td>0.035</td>
<td>0.034</td>
</tr>
</tbody>
</table>

*p<0.05*
3.5.4 Analytical procedures and results

To test our hypotheses, we employed *logistic regressions* (Stata command: *logit*) because the dependent variable is of dichotomous character. Table 4 displays the results of the tested models, both for ownership as well as management succession. Model 1 contains only control variables. In Model 2, the independent variables are added. In Model 3 the moderating variables are added and Model 4 reports results from the full model, including interactions between the independent variables and the moderators.

In Models 1-4 we take equity as the base outcome, therefore a *negative coefficient* indicates that there is a likelihood for the equity principle while a positive coefficient indicates that the choice of the equality principle is more likely.

To test model fit, we used in a first step the Wald to check whether including the two independent variables (Model 2) increased model fit between Model 1 and Model 2. The Wald test confirmed such increase in model fit for both dependent variables, ownership transfer (Model 2: p < 0.01) and management transfer (Model 2: p < 0.001). Further, we investigated whether the Pseudo R-squared increased. Pseudo R-squared increased with each model. Considering the Bayesian Information Criterion (BIC), we found that Model 4 with the smallest values is preferred over the other models.

Table 4 displays the results of the four models for the transfer of ownership and management.
### Table 4: Logistic regression models

<table>
<thead>
<tr>
<th>Control variables</th>
<th>Model 1 Ownership</th>
<th>Model 2 Ownership</th>
<th>Model 3 Ownership</th>
<th>Model 4 Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ownership</td>
<td>Management</td>
<td>Management</td>
<td>Management</td>
<td>Management</td>
</tr>
<tr>
<td>Industry</td>
<td>0.005</td>
<td>-0.410*</td>
<td>0.013</td>
<td>-0.391</td>
</tr>
<tr>
<td>(0.158)</td>
<td>(0.209)</td>
<td>(0.162)</td>
<td>(0.215)</td>
<td>(0.180)</td>
</tr>
<tr>
<td>Firm age</td>
<td>-0.007**</td>
<td>-0.007*</td>
<td>-0.006**</td>
<td>-0.006</td>
</tr>
<tr>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.004)</td>
</tr>
<tr>
<td>Firm size</td>
<td>0.000</td>
<td>-0.008</td>
<td>0.002</td>
<td>-0.006</td>
</tr>
<tr>
<td>(0.002)</td>
<td>(0.004)</td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.004)</td>
</tr>
<tr>
<td>Firm performance</td>
<td>0.033</td>
<td>0.009</td>
<td>0.017</td>
<td>0.074</td>
</tr>
<tr>
<td>(0.197)</td>
<td>(0.211)</td>
<td>(0.198)</td>
<td>(0.212)</td>
<td>(0.202)</td>
</tr>
<tr>
<td>Family cohesion</td>
<td>0.122*</td>
<td>0.043</td>
<td>0.141*</td>
<td>0.061</td>
</tr>
<tr>
<td>(0.053)</td>
<td>(0.078)</td>
<td>(0.078)</td>
<td>(0.079)</td>
<td>(0.063)</td>
</tr>
<tr>
<td>Region</td>
<td>0.506</td>
<td>0.547*</td>
<td>0.346</td>
<td>0.308</td>
</tr>
<tr>
<td>(0.201)</td>
<td>(0.210)</td>
<td>(0.212)</td>
<td>(0.241)</td>
<td>(0.277)</td>
</tr>
<tr>
<td>Respondent age</td>
<td>-0.018*</td>
<td>-0.011</td>
<td>-0.016**</td>
<td>-0.012</td>
</tr>
<tr>
<td>(0.008)</td>
<td>(0.011)</td>
<td>(0.009)</td>
<td>(0.011)</td>
<td>(0.010)</td>
</tr>
<tr>
<td>Respondent gender</td>
<td>0.172</td>
<td>-0.432</td>
<td>0.226</td>
<td>-0.523</td>
</tr>
<tr>
<td>(0.303)</td>
<td>(0.428)</td>
<td>(0.312)</td>
<td>(0.442)</td>
<td>(0.361)</td>
</tr>
</tbody>
</table>

### Independent variables

<table>
<thead>
<tr>
<th>Model 1 Ownership</th>
<th>Model 2 Ownership</th>
<th>Model 3 Ownership</th>
<th>Model 4 Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Family influence in ownership</td>
<td>(H1a, H2a)</td>
<td>-0.185***</td>
<td>-0.327***</td>
</tr>
<tr>
<td>(0.053)</td>
<td>(0.070)</td>
<td>(0.070)</td>
<td>(0.064)</td>
</tr>
<tr>
<td>Family influence in management</td>
<td>(H1b, H2b)</td>
<td>0.002</td>
<td>0.012***</td>
</tr>
<tr>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.003)</td>
<td>(0.004)</td>
</tr>
</tbody>
</table>

### Moderator variables

| Female family owners | 0.010* | -0.006 | 0.109 | 0.019 |
| (0.004) | (0.006) | (0.139) | (0.028) |
| Family influence in board of directors | -0.003 | -0.002 | 0.030 | 0.011 |
| (0.003) | (0.004) | (0.019) | (0.010) |

### Interaction effects

| Female family owners x Family influence in ownership | (H3a, H3b) | -0.019 | 0.000 |
| (0.030) | (0.007) |
| Female family owners x Family influence in management | 0.000 | -0.000 |
| (0.000) | (0.000) |
| Family influence in BoD x Family influence in ownership | (H4a) | -0.009* | -0.009** |
| (0.004) | (0.005) |
| Family influence in BoD x Family influence in management | (H4b) | 0.000 | 0.000 |
| (0.000) | (0.000) |

### Constant

| 1.175* | -0.740 | 1.418* | -0.599 | 1.453* | 0.605 | 1.217* | -0.252 |
| (0.569) | (0.710) | (0.588) | (0.761) | (0.658) | (0.891) | (0.669) | (0.919) |

### Observations

| 791 | 814 | 773 | 701 | 618 | 637 | 618 | 637 |

### Pseudo R2

| 0.025 | 0.032 | 0.040 | 0.064 | 0.044 | 0.077 | 0.055 | 0.109 |

### Log likelihood

| -216.07 | -473.52 | -129.86 | -162.26 | -711.67 | -350.46 | -3997.55 | -3705.65 |
| -101.22 | -131.27 | -481.36 | -312.96 | -388.17 | -229.33 | -382.38 | -222.27 |
| 12.56* | 21.68** | 4.82* | 14.31** | 0.740 | 0.196 |

*** p<0.001, ** p<0.01, * p<0.05, + p<0.1
3.5.4.1 Ownership succession

With regard to intra-family ownership succession, 66.16% of the respondents preferred to apply the justice principle of equality (33.84% equity), see Table 3. Model 3 in Table 4 shows that higher family influence in ownership is contrary to our hypothesis negatively and significantly related to the choice of the justice principle of equity ($\beta = -0.154$, $p < 0.05$) and not equality. Hence H1a is rejected. Family influence in management is unrelated to the choice of the justice principle of equality in ownership succession ($\beta = 0.002$, $p > 0.1$), correspondingly H1b is rejected.

We found that the presence of female family owners ($\beta = 0.010$, $p < 0.05$) and family cohesion ($\beta = 0.143$, $p < 0.05$) are positively associated with incumbents’ intention to choose the principle of equality. Contrary, increasing firm age ($\beta = -0.005$, $p < 0.05$) and increasing age of the respondent ($\beta = -0.017$, $p < 0.1$) are associated with equity transfers.

3.5.4.2 Management succession

With regard to intra-family management succession, 83.27% chose the justice principle of equity and only 16.73% the justice principle of equality, see Table 3. Model 3 in Table 4 shows that in line with our argumentation, with increasing family influence in ownership, incumbents are more likely to choose the justice principle of equity when transferring management, hence H2a is supported ($\beta = -0.305$, $p = 0.001$). As we expected, higher family influence in management is associated with the choice of the justice principle of equality ($\beta = 0.014$, $p < 0.01$), H2b is therewith confirmed.
Further, the service sector ($\beta = -0.573$, $p < 0.05$) and increasing firm age ($\beta = 0.009$, $p < 0.05$) increase the likelihood for the application of the justice principle of equity in management transfers.

3.5.4.3 Moderating effects

Model 4 in Table 4 shows that the presence of female family owners has no moderating effect on the relationship between increasing family influence in ownership and the choice of the justice principle in ownership and management succession, hence H3a (ownership succession: $\beta = -0.019$, $p > 0.1$) and H3b (management succession: $\beta = 0.000$, $p > 0.1$) are rejected.

With regard to management transfers, model 4 of Table 4 shows that increasing family influence in the board of directors will, combined with increasing family influence in ownership, reduce the likelihood for the choice of the equity justice principle ($\beta = -0.009$, $p < 0.01$), hence H4a is rejected. Also, H4b is rejected as increasing family influence in the board of directors reduces the positive relationship between increasing family influence in management and the choice of the equality principle ($\beta = 0.000$, $p < 0.05$).

3.5.4.4 Robustness tests

We tested the robustness of our findings. First, model 3 of Table 4 was re-estimated including the values for the *primogeniture* choice (first-born) of incumbents. This test proved that with regard to ownership succession intentions of incumbents, increasing family influence in ownership significantly increases the likelihood of the application of the justice principle of equity ($\beta = -0.151$, $p < 0.05$). Again, increasing family influence in
management had no effect on ownership succession intentions. With regard to management succession, this robustness test confirmed significance of our findings and that increasing family influence in ownership increases the likelihood of equity management successions ($\beta = -0.273$, $p < 0.01$), and increasing family influence in management increases the likelihood of management successions according the justice principle of equality ($\beta = 0.012$, $p < 0.01$).

Second, model 3 of Table 4 was run under the condition that incumbents had full ownership of the company (100% of shares). This test confirmed that in ownership succession, increasing family influence in ownership significantly increases the likelihood of equity transfer intentions of incumbents ($\beta = -0.249$, $p < 0.05$). Again, increasing family influence in management has no effect on ownership succession intentions. With regard to management succession intentions, the test confirmed that increasing family influence in ownership leads to equity transfers ($\beta = -0.252$, $p < 0.05$), whereas increasing family influence in management to equality transfers ($\beta = 0.016$, $p < 0.01$).

Lastly, we run model 3 of Table 4 under the condition that incumbents had at least two children. With regard to ownership succession intention of incumbents, increasing family influence in ownership induces equity successions, even though this effect was just insignificant ($\beta = -0.144$, $p = 0.063$). Increasing family influence in management had again no effect on ownership intentions. In management succession, both effects remained significant, such that increasing family influence in ownership increases the likelihood that incumbents intend to transfer management according to the justice principle of equity ($\beta = -0.242$, $p < 0.05$) and increasing family influence
in management increases the likelihood that incumbents intend to transfer management according to the justice principle of equality ($\beta = 0.015$, $p = 0.001$).

### 3.6 Discussion

The following key insights can be summarized from our findings.

*First*, family influence in ownership is associated – with regard to both ownership and management succession – with an increasing likelihood of the application of the justice principle of equity. We observe from the results that the majority of incumbents in general intends to pass on ownership according to the equality principle (83.27%) and management according to the equity principle (66.16%). Thereby, increasing family influence in ownership makes the choice of the justice principle of equity more likely. We expected this result with regard to management succession because of families’ wish to protect family’s financial and socioemotional wealth (Anderson et al., 2003; Gómez-Mejía et al., 2007; Zellweger et al., 2016), but did not with regard to ownership succession as we believed that here the family norm of equality is prevalent (Drake & Lawrence, 2000). We assume that increased family influence in ownership hence strengthens the awareness that owners have responsibilities (such as the organization of the company, election of the board of directors, approval of the annual statement etc.) that require special entrepreneurial skills from successors. It is true that in practice one can observe this equity dimension of ownership, as it finds its expression for instance in family constitutions that set certain conditions for family members to become owners (e.g., with regard to age, attitude as well as adherence to certain family and business values) (Verbeke & Kano, 2012).
Second, family influence in management is associated with equality transfers in management succession. We expected that as in family-managed firms, typically family firms in early stages, the degree of closeness of family members is usually very high and family and company are very much intertwined so that family values are more dominant, and the family norm of equality is likely to prevail over the business norm of equity. This finding might help to understand why some agency issues are more prevalent in certain stages of the family firm and if the family is represented in the management.

Third, our study confirms our expectation that family board members have an ambiguous influence but shows that such influence is exactly opposite from what we expected. Family influence in the board of directors reduces – and not increases – the positive relationship between family influence in ownership and the application of the justice principle of equity in management succession. Further, family influence in the board of directors reduces – and not increases – the positive relationship between family influence in management and the application of the justice principle of equality in management succession.

3.6.1 Contribution to family firm governance

We contribute to family firm governance literature as we show how the composition of the governance bodies in family firms influences incumbent’s choice of justice principle in succession. Our findings suggest that family influence is not necessarily associated with a rejection of merit based decisions and that “family influence” cannot be lumped together (Faccio & Lang, 2002; La Porta et al., 1999; Villalonga & Amit, 2006) as increasing family influence in ownership will result in the application of the justice principle of equity
while increasing family influence in management will lead to equality transfers.

Moreover, the justice principle applied in succession also *influences future governance structures* of family firms as it determines the prospective leaders of the company (Chrisman et al., 1998; Sharma et al., 2001). We learned from our study that incumbents in general transfer ownership according to equality and management according to equity. As a consequence, the most common governance structure of family firms in future corresponds to an evolutionary transition of ownership and a recycle transition with regard to management (Gersick et al., 1999). This implies that because of equality-ownership transfers more family members become present in ownership, while because of equity-management transfers there will be a sole family manager. This governance structure induces an own set of capabilities and challenges (Baldridge & Schulze, 1999; Carney, 2005).\(^9\) Descendants will share ownership, and as their economic and non-economic preferences are unlikely to match completely (Schulze et al., 2001), there is a risk of stalemate resulting from conflicts of interests. Conflicts of interests are reinforced by the circumstance that the descendants take over different roles in the family firm. Only one of them succeeds in management, while all descendants succeed in ownership. Such different degree of involvement in the family business creates tensions (Jensen & Meckling, 1976) that source in a confusion among the descendants over who does what in the business (Danes, Zuiker, Kean, & Arbuthnot, 1999; Ward & Aronoff, 1992).

\(^9\) We can draw from the results that 50.64% of the intended transfers are equality-ownership & equity-management transfers; 33.59% of the intended transfers are equity-ownership & equity-management transfers; and 15.77% of the intended transfers are equality-ownership & equality-management transfers.
Furthermore, our findings show that family board members’ influence with regard to the application of business or family norms in management succession depends on family’s presence in other governance bodies. Family board members act somewhat like a counterweight to family influence in other governance bodies: In family firms that are family owned, family board members mitigate the emphasis on business norms in management succession. That might result from the special role that family board members take over. Family board members are mandated to foster the relation between family and business and to implement family values on a strategic level. Hence, they may appease family’s business orientation to maintain good family relationships. With this stance family board members are however less apt to fulfill their monitoring function towards managers (Hillman & Dalziel, 2003). Contrary, the finding that in family managed firms, family board members will weaken the emphasis on the family norm of equality in management succession suggests that family board members are more critical towards family managers than towards non-family managers. Family board members might think that family managers must particularly excel to deserve to manage the family firm and therewith family’s financial and socio-emotional wealth. In this constellation, family board members might be able to perform their monitoring function towards family managers (Hillman & Dalziel, 2003). Our study therewith shows that the role of family board members is ambiguous and partly (i.e. family board members combined with family managers) challenges the widespread assumption that only non-family board members can mitigate the “negative” influence of family norms. It certainly shows that the composition of ownership and management must be considered when compiling the “ideal” composition of the board.
Overall, the findings contribute to family governance research as it shows that the degree to which family norms permeate decision-making in family firms strongly depends on the governance body the family exercises its influence on. Such validity of family norms in family firms has proven to have positive as well as negative impact on the firm (Eddleston & Kellermanns, 2007; Lansberg & Astrachan, 1994). Family norms can lead to lower agency costs as these shared values align the goals and create high trust between family members (Dyer, 2006). However, family norms may also generate agency costs resulting from opportunism, shirking, and adverse selection sourcing from altruism (Dyer, 2006; Schulze et al., 2002, 2001). This study indicates that family influence and therewith the positive and negative effects of family norms might vary depending on the governance body the family exercises its influence on.

3.6.2 Contribution to family firm succession

This paper also contributes to family firm succession research in shedding light on the challenges incumbents face in the succession process (Dyer, 1986; Taylor & Norris, 2000). We showed whether incumbents choose the justice principle of equity or equality in ownership and management succession and how incumbents’ justice perceptions are rooted within the firm’s exposure to the family (Aldrich & Cliff, 2003). The study revealed that incumbents have a norm conflict between the justice principles of equity and equality, especially when passing on ownership. This study therewith delineates family firm incumbents’ struggle in succession decisions and unfolds the extent to which the justice principles of equity and equality are competing in family firm succession. Our study helps to address and tackle this dilemma of incumbents in family firm succession in theory and practice.
Further, as mentioned above, the choice of one of the justice principles will result in different governance structures. With the future governance structure also the context of the succession changes (Barach & Ganitsky, 1995; De Massis et al., 2008). Depending on the justice principle of choice, the number of participants (descendants), the tasks and the intergenerational dynamics (Miller et al., 2003) in succession vary. For instance, if the justice principle of equality is applied and all descendants succeed in ownership and management, main concerns in the succession process are to develop all descendants according to their needs, to split management tasks according to the skills of the individual descendants, and to establish clear responsibilities and efficient decision making processes (Le Breton-Miller et al., 2004). Contrary, if the justice principle of equity is chosen and only one successor succeeds in the family firm, the focus of succession is more on successor’s personal relationship with the incumbent (Chrisman et al., 2005; Lansberg & Astrachan, 1994), and on how other descendants are excluded from succession and can be compensated for not being considered. The succession process and the tasks to be completed therewith depend on the justice principle applied in succession.

Moreover, our study highlights the role of female family owners in succession. It shows that the presence of female family owners will increase the likelihood that incumbents pass on ownership of the family firm according to the justice principle of equality. In future, the presence of females in family firms will increase (Andric et al., 2016), and therewith, the tendency that ownership in family firms is passed on according to the justice principle of equality can be expected to intensify.
3.6.3 Contribution to justice theory

Lastly, the paper contributes to justice theory that considers justice as a relative, context-dependent, and individual construct (Breugst et al., 2015; Colquitt et al., 2001; Deutsch, 1975; Fondacaro et al., 2002). We demonstrated that the *justice principles dominant in family business succession* context in Switzerland are equity and equality. The paper confirms that different governance roles are passed on in accordance with different justice principles (Tornblom & Foa, 1983): Management succession is strongly associated with the justice principle of equity while ownership succession predominantly with the justice principle of equality. The study also deals with other factors that, besides pure justice considerations, influence the choice of a justice principle and offers self-interest, altruism, and the practicability of the allocation norm as elements affecting incumbents’ selection of a justice principle (Drake & Lawrence, 2000; Montada, 1998).

These contributions are not only relevant for theory but also for practice. They will help individuals involved in the succession process, such as family members, members of the board of directors or management, attorneys, consultants and others to address the difficult topic of distributional justice in ownership and management succession and we hope it will serve as reference with regard to what justice principles are applied in family firm succession.

3.7 Future research and limitations

As our study shows, the most common succession type in family firms is “equality-ownership/equity-management”. *Future research* could hence focus on this governance type and elaborate on the capabilities and challenges (e.g.,
agency issues) that arise out of such a split of justice principles in succession. One could further investigate how the selection of a justice principle is related to family firms’ performance. Fittko & Kormann (2014) observed for instance that the majority of the large and old family firms in Germany originate from equality transfers whereas the small and old family firms predominantly stem from equity transfers and conclude that equality transferred firms have a greater growth potential. Future research will be able to reveal the pros and cons of equity versus equality transfers and could more closely investigate the circumstances that support the choice for one of the justice principles.

Further, it would be interesting if researchers repeated our study over time. Switzerland is currently revising its inheritance law and will decrease statutory shares of children. That will leave incumbents more freedom to favor one of their children in ownership succession and it might be that this change in law will have an impact on moral perceptions and therewith incumbents become more likely to apply the justice principle of equity. It would be interesting to compare such data to other cultural contexts and investigate what justice principles incumbents of other countries prefer and how such preference changes over time. In family firms of countries where a succession according to the justice principle of primogeniture is currently the dominant succession form, one might observe that the justice principle of equality will gain momentum in family business succession.

Lastly, future research could investigate, for instance by using case study methodology, how divergent justice perceptions in succession will result in perceived injustice and how injustice perceptions of family members’
influence their behavior within the firm (Adams, 1965; Ambrose, Seabright, & Schminke, 2002; Cropanzano et al., 2007; Greenberg, 1990b).

This paper has several limitations which constitute further important avenues for future research. First, the paper only deals with distributional justice and focuses on “pure” forms of the justice principles of equality and equity (i.e. in equality transfers, ownership or management respectively is split 50:50 between descendants while in equity transfers the successor receives 100% of ownership and management). The paper therewith does not factor in that equality and equity considerations can be mixed in family firm succession (e.g., successor manager receives majority of ownership and other descendant becomes minority shareholder (60:40), or ownership transfers with merit components, i.e. descendants can become owners only if they have certain education levels or showed special interest in the company). Our aim was to understand the main differences between the two justice principles of equity and equality and therefore we used these pure manifestations of the justice principles. Future research could hence analyze to what degrees the different justice principles are realized in management and ownership succession in practice. Further, we excluded other distributional justice principles such as need (Colquitt et al., 2001) as well as the other two types of justice (Cohen-Charash & Spector, 2001; Cropanzano et al., 2007). Hence future research would be well advised to consider other distributional justice principles as well as elements of procedural and interactional justice, such as the degree to which descendants have a say in the succession process (Leventhal, 1980; Thibaut & Walker, 1978) and the extent to which they were treated with respect (Bies & Moag, 1986; Cropanzano, Prehar, & Chen, 2002).
We further did not include other circumstances that could influence the application of justice principles such as succession laws, inheritance taxes, the relevance and roles of other heirs (e.g., spouses) and other assets of the family that could be allocated to the descendants as compensation for not being considered in the transfer of the business. Future research should consider how these aspects play into distributional justice considerations. Finally, our survey asked for transfer intentions of the respondents, and the results therewith lack verification in practice.

### 3.8 Conclusion

To conclude, current governance structures in family firms impact the choice of the justice principle in succession. Such choice has a major effect on the family business, as it shapes its future governance structure. Empirical research regarding how family influence determines the choice of a justice principle and a structural analysis of corresponding governance challenges and capabilities has been lacking so far. The paper attempts to start closing that gap and to provide a basis for future research on the relevance of distributional justice in succession.
4 Relation between governance structures, agency issues, and justice principles in family firms

Sonja Kissling Streuli

4.1 Abstract

In intra-familial successions family firm incumbents must choose according to which justice principle they transfer the family business – ownership and management – to the next generation. The most prevalent justice principles in Western societies are equity and equality. Each choice leads to different governance structures that entail particular consequences, such as agency issues. In the following I will analyze three different succession forms – succession according to equity, succession according to equality as well as a succession form that encompasses both principles – and carve out in a dynamic approach the particular challenges that arise in the family business under an agency perspective. This paper is a conceptual one that combines justice and agency considerations in the family business succession.

4.2 Introduction

Family firm succession is a key moment for business and family as it influences future performance of the company as well as the relationships between the involved family members (Le Breton-Miller et al., 2004). In every family firm succession (Ayres, 1990; Lansberg & Astrachan, 1994), the incumbent is concerned with two questions: 1) How shall I distribute the family business (ownership and management) between my descendants? And 2), at what point in time shall I transfer the business? The first question implies a choice between
the different principles of distributional justice that are in line for the transfer of the family business in Western societies: Equity and equality (Deutsch, 1975; Lansberg, 1983). The second question regarding the moment of the transfer of the family business concerns the process and hence affects the topic of procedural justice (Thibaut & Walker, 1978; Van der Heyden et al., 2005).

The application of different distributional justice principles lead to different governance structures in the family firm. Governance structures encompass the composition of ownership and management in the family firm. Successions based on the justice principle of equity lead to a different composition of ownership and management than successions based on the justice principle of equality. Hence, the composition of ownership and management of family firms in future depends on the choice of the justice principle in succession. Governance structures in non-family as well as in family firms are often investigated with an agency approach as one can therewith systematically analyze the relation between owners and managers of the company (Fama, 1980; Fama & Jensen, 1983; Jensen & Meckling, 1976). Hence, the three topics of succession, justice and agency are interrelated and the interplay of those forces defines governance of family firms.

In this paper I will present three different succession forms – succession according to equity, succession according to equality as well as a succession form that encompasses both principles – and carve out the particular consequences each choice has on the governance of the family business under an agency perspective. That course of action shall outline answers to three research questions: 1) How does the choice of a justice principle in succession influence the governance structure of the family business? 2) How does the
corresponding governance structure change over time (dynamic approach)? And 3) what consequences does the choice of a justice principle have under an agency perspective? Each of the three scenarios concludes with specific propositions.

The paper contributes therewith to three different streams of research. First, the paper contributes to family firm governance literature (Jensen & Meckling, 1976; Schulze, Lubatkin, & Dino, 2003b; Schulze et al., 2001) in investigating and distinguishing between governance structures and challenges that arise from the application of different justice principles in family firm succession. The paper thereby applies a dynamic approach and demonstrates that the governance structures and challenges resulting from the application of different justice principles change over time. The paper therewith initiates a more differentiated analysis of the agency issues that trouble family firms.

Second, the paper adds to family business succession research (Barach & Ganitsky, 1995; Handler, 1994; Sharma et al., 2001). The transition periods in family firms are the most sensitive and challenging situations in the development of the family firm (Gersick et al., 1999). This paper shows that the choice of the justice principle is a pivotal component of family firm succession that has a major impact on family firms’ future. The paper explains that the justice principle chosen in family firm succession decides about future roles of family members and hence determines whether the family firm develops from a controlling ownership stage to a sibling partnership stage and undertakes an evolutionary transition or whether the family firm undergoes a recycle and remains in a controlling ownership stage (Gersick et al., 1999).
Third, the paper adds to social justice research as it investigates elements of distributive and procedural justice in a context that so far has received little notice, the family business succession context (Cohen-Charash & Spector, 2001; Cropanzano et al., 2007; Greenberg, 1990a). The paper shows the influence of equity and equality considerations in family firm succession and addresses the mitigating role of elements of procedural justice.

The paper intends to show in a structured way the challenges that the application of different justice principles in family firm succession has. In theory and practice it is very important to understand the sources and reasons for different governance structures of family businesses. For theory, in order to analyze their consequences in a conceptual and empirical way and for practice, in order to procure solution approaches to family businesses that struggle with the challenges arising out of the different governance structures.

4.3 Theoretical foundations

The paper touches the three different research streams of succession, justice and governance (agency theory). All of them will be dealt with in more detail in this section in order to lay a sound foundation for the subsequent analysis of the three mentioned scenarios demonstrating the governance structures and challenges resulting from the choice of different justice principles in family firm succession.

4.3.1 Succession

The family business research field devoted major efforts to the study of succession. A successful succession is considered as basis for the future
success of the family business (Le Breton-Miller et al., 2004). Therefore, elements were identified that are key for a successful transfer of the family business, such as health and prospects of the firm, the relationship between successors and incumbents as well as personal characteristics of the involved family members (Barach & Ganitsky, 1995; Handler, 1994; Lansberg, 1988; Lansberg & Astrachan, 1994; Morris et al., 1997).

It is an idiosyncrasy of family businesses that they intent to transfer the firm to the next generation (Astrachan et al., 2002; Chrisman et al., 2012; Miller & Le Breton-Miller, 2003). Out of family-internal transfers different governance structures arise (Gersick et al., 1999; Ward & Dolan, 1998): Over generations family businesses might turn from owner controlled firms to sibling partnerships and later on to cousin consortiums (Gersick et al., 1999). However, it was noticed that not all family businesses follow such “expansion”. Besides these evolutionary transitions – as Gersick et al. (1999) called it – also recycles or even devolutionary transitions exist, where the amount of family members involved in the business stagnates or even decreases.

Lacking so far is a closer discussion of the source and the reasons that lead to different transition forms and correspondingly to different governance structures and challenges. I argue that the application of different justice principles in succession is one very important reason for the type of transition happening in family businesses (recycles or evolutionary or devolutionary transitions) and the development of corresponding governance structures in different family generations.
4.3.2 Justice in family business succession

In the everyday life of every human distributive questions turn up. People have to decide how they allocate economic goods such as money, natural resources, or food as well as non-economic goods such as love, status, or time (Tornblom & Foa, 1983). Also family firm succession is a distributive process (Kets de Vries, 1993), as ownership and management are distributed among descendants.

As all goods are scarce or costly to give, people establish norms and processes according to which goods are distributed. It has long been recognized that thereby the ideal of justice is of fundamental significance and hence social theorists have investigated what people consider as fair in specific situations (Cropanzano et al., 2007; Greenberg, 1990a). If people perceive that the allocation of goods is not in congruence with their internal believe system they consider the distribution as unfair (Cropanzano, Byrne, Bobocel, & Rupp, 2001; Meindl, 1989). Such perceived unfairness (also called injustice or inequity) damages social interaction and is source of conflict (Adams, 1965). Justice is considered hence as basic requirement for the effective functioning of social entities and the personal satisfaction of individuals (Greenberg, 1990a; Moore, 1978; Okun, 1975). In management theory the topic gained interest in the study of the functioning of organizations and the elements that maintain the feelings of justice in an organization, e.g., equitably payment (Greenberg, 1990b; Jaques, 1961).

When analyzing justice in distributions, scholars make a difference between principles that focus on the outcome of an allocation, and guidelines that are
concerned with the process (Colquitt et al., 2001; Greenberg, 1987, 1990a). The two concepts are named *distributive* and *procedural justice*. Distributive justice will give an answer to the question of what *outcome* of a division of goods is regarded as fair, whereas procedural justice is concerned with the fairness of the *process* itself (Thibaut & Walker, 1978; Walker, Lind, & Thibaut, 1979).

### 4.3.2.1 Distributive justice

Distributive justice theory explains that the outcome of an allocation can be determined by different allocation norms, so called distributive justice principles (Colquitt et al., 2001; Cropanzano et al., 2007; Deutsch, 1975). The appropriate distributive justice principle is chosen depending on the context of the allocation (Colquitt et al., 2001; Cropanzano et al., 2007; Deutsch, 1975). Justice is therefore a relative concept (Breugst et al., 2015; Deutsch, 1975; Kabanoff, 1991). This paper deals with intra-familial succession in family firms and hence has to establish what justice principles are dominant in this context.

In the family business context in general, two different systems meet, the family and the business (Dyer & Handler, 1994; Lansberg, 1983). These systems follow different goals and correspondingly different allocation norms (Ayres, 1990; Baldridge & Schulze, 1999; Deutsch, 1975; Fondacaro et al., 2002; Leventhal, 1980; Van der Heyden et al., 2005).

In the *family* system, the goals are personal support and development as well as the preservation of family harmony (Deutsch, 1975; Lansberg, 1983). It has been established that parents therefore will, in order to achieve these goals, try
to treat their children equally in allocations, especially with regard to inheritance distributions (Deutsch, 1975; Drake & Lawrence, 2000; Lansberg, 1983). Accordingly, in the family context, the *justice principle of equality* is applied, where goods are distributed evenly between the descendants, independent of other factors such as merit (Fondacaro et al., 2002). Contrary, in the business system, economic productivity is the primary goal and people are rewarded for their achievements (Adams, 1965; Deutsch, 1975; Festinger, 1957; Homans, 1961). This is based on the notion that scarce resources should be assigned to those who are most able to use them (Deutsch, 1975). Allocations in the business context are hence effected based on merit applying the *justice principle of equity*.

Applied to the family firm succession context, the family system would call for the application of the justice principle of equality, while the business system would suggest the application of the justice principle of equity. If the justice principle of equality is applied, ownership and management are split evenly between descendants. Contrary, when the justice principle of equity is applied, the family firm is transferred considering the “merits” of the descendants. Merits that are generally of relevance in family firm succession are skills, education, experience, and motivation of the descendants (Adams, 1965; De Massis et al., 2008; Titus et al., 1979), i.e., their overall competence. So, when the justice principle of equity is applied in succession, the family firm is transferred to the most competent descendant.¹⁰

¹⁰ A pitfall of the concept of equity in the family business succession context is that the family firm is handed over to the successor descendant at a moment where the prove of his or her merit at least partly lies in the future. Incumbent needs to analyze the competence of the descendant at the time of succession, however only time will show whether such assessment was right. It may well be that a descendant is considered as veritable successor at the time of the succession
As the two justice principles of equity and equality are due to the institutional overlap between family and firm competing in family firm succession (Lansberg, 1983), the paper will exhibit three succession forms that encompass the two justice principles to different degrees. The first scenario deals with a succession according to the justice principle of equity, the second with a succession according to the justice principle of equality, and the third with a succession form that considers both principles, i.e., the justice principle of equality in ownership succession and the justice principle of equity in management succession.

4.3.2.2 Procedural justice

Distributional justice theory regards the outcome when evaluating the fairness of a distribution (Colquitt et al., 2001). However, there are other aspects that people consider when analyzing the fairness of an allocation, such as the process of the allocation (Cohen-Charash & Spector, 2001; Colquitt et al., 2001; Walker et al., 1979). Consequently, procedural justice theory was developed as a distinct category of justice. Especially Thibaut & Walker (1978) put procedural justice in the light of research. They analyzed the elements that enhance the fairness of judicial processes and thereby stressed the importance of process control of the participants. Scholars of different fields followed the call and put up efforts for the study of the different elements of procedural justice (Fondacaro et al., 2002; Masterson, Lewis, Goldman, & Taylor, 2000; McFarlin & Sweeney, 1992). Leventhal (1980: 16) explained that procedural

but later brings the company into ruin. So, the merit considered when applying the justice principle of equity, is partly uncertain.
justice does not focus on the outcome but “on the individual’s cognitive map of events that precede the distribution or reward, and the evaluation of those events”. He defined six rules that support fairness of the distributional process (consistency, bias-suppression, accuracy, correctability, representativeness, ethicality). These elements of procedural justice were incorporated and integrated in the subsequent research activity while the range of the elements was further broadened and specified. At the end of the last century researchers addressed the importance of the interpersonal treatment that people receive in the distribution process and qualified interactional justice as either part of procedural justice or as a separate third category of justice (Bies & Moag, 1986; Colquitt et al., 2001; Cropanzano et al., 2002; Skarlicki & Folger, 1997).

In family business literature, procedural justice is considered to be able to establish trust, commitment, and family harmony (Van der Heyden et al., 2005), and therefore strengthens family relations and family harmony (Fondacaro, Dunkle, & Pathak, 1998; Fondacaro et al., 2002). In family firm succession, fair process includes that succession must be anticipated long in advance and managed as planned process (Lansberg, 1983; Le Breton-Miller et al., 2004). The process must acknowledge the different roles of family members and integrate their interests (Lansberg, 1988). The process must further be able to establish a shared vision of the family firm in future (Le Breton-Miller et al., 2004).

A fundamental element of procedural justice in the succession process is timing (Schulze et al., 2002). Timing decides about whether there is an heir at all, whether there is an interested, experienced or trained heir (Handler & Kram, 1988). Timing determines when responsibilities are transferred and the
successor follows in ownership and management (Dyer & Handler, 1994). This paper deals with the timing of the disclosure of the justice principle applied by incumbents in succession. In the three succession scenarios, the paper argues that the timing of disclosure influences fairness perception of the descendants. Early disclosure of the justice principle in succession can lower sunk costs of the descendants as it enables them to take a decision for or against the family firm and follow a different career path (Von Schlippe & Kellermanns, 2008). If incumbents disclose the justice principle of choice very late in the succession process, corresponding wrong expectations of family members and false hopes are likely to generate conflicts (Dunn, 1999).

4.3.2.3 Injustice

Often descendants perceive succession as unfair. Felt injustice is a discrepancy of “what is perceived to be and what is perceived should be” (Adams, 1965: 272). Such felt injustice is – as justice – the result of a comparative process (Festinger, 1954). People feel that compared to others, they have not received to what they are entitled to. Injustice is therewith a perceived violation of entitlement (Mikula, 1993) where the result of a distribution is analyzed in a comparative process (relative deprivation).

In succession, descendants might receive less than they feel entitled to and consider themselves as under-rewarded (Adams, 1965). For instance, imagine a situation where an incumbent has two children, descendant A and B. Descendant A feels entitled to an equal ownership share as descendant B as he or she is of the opinion that all children should be treated equally. However, in succession the incumbent allocates all shares based on the justice principle of equity to descendant B as such descendant will manage the firm in future. In
this situation, incumbent and descendant A have conflicting justice perceptions and descendant A feels under-rewarded. At the same time, it might be that descendant B feels over-rewarded as he or she was – as descendant A – of the opinion that with regard to ownership succession the justice principle of equality should apply. Descendant B in such case considers to have received more than deserved (Homans, 1961). Both descendant hence perceive the succession decision as unjust.

Both, the under-rewarded and the over-rewarded descendant are said to be motivated to reduce injustice felt (Adams, 1965; Festinger, 1957; Homans, 1961). There are different mechanisms available that allow a person to reduce felt injustice. Based on the equation that a fair outcome is an outcome where input is equivalent to outcome, Adams (1965) namely suggests that the person feeling under-rewarded can reduce injustice in the following ways: 1) by reducing own input, 2) by increasing own outcome, 3) by increasing the input of the other, or 4) by reducing the outcome of the other. The person who feels over-rewarded behaves like a mirror image to the under-rewarded person, he or she reduces the injustice felt by: 1) increasing own input, 2) reducing own outcome, 3) reducing the input of the other, or 4) increasing the outcome of the other.

The paper investigates these mechanisms of the under- and the over-rewarded in the three succession scenarios and considers perceived injustice as one source of agency costs (called hereinafter moral hazard II; see chapter 4.3.3.2).
4.3.3 Agency perspective

Using the three scenarios described below – a succession according to equity, a succession according to equality and a succession that encompasses both justice principles, this paper wants to demonstrate that the application of different justice principles leads to different governance structures and correspondingly to different governance challenges. Research has long tried to understand governance challenges in firms using agency theory (Fama & Jensen, 1983; Jensen & Meckling, 1976; Schulze et al., 2001).

Agency theory explains that in the event of a separation of ownership and management, the principal (= owner) engages a manager (= agent) and delegates to such person decision making power (Fama, 1980; Jensen & Meckling, 1976). Based on the assumption that both parties are opportunistic utility maximizers, their interests will to a certain extent diverge (Jensen & Meckling, 1976). Two issues that arise from the divergent interests of principal and agent are adverse selection and moral hazard (Chrisman, Chua, & Litz, 2004; Fama, 1980; Jensen & Meckling, 1976).

Adverse selection and moral hazard appear on different points in time. Adverse selection is considered a circumstance in which the principal inadvertently engages an agent who lacks the ability or commitment or whose interests are not in congruence with those of the principal (Chrisman et al., 2004; Eisenhardt, 1989). Moral hazard defines circumstances after contracting in which the agent does not act in the best interest of the incumbent but engages in behaviors, such as free-riding and shirking (Eisenhardt, 1989; Fama, 1980; Jensen & Meckling, 1976). Such actions of the manager result in costs, called
agency costs (Chrisman et al., 2005; Jensen & Meckling, 1976). The principal will try to control adverse selection and moral hazard in implementing appropriate governance instruments as counter-measures. In general, these governance instruments will consist of compensation incentives and monitoring (Jensen & Meckling, 1976), however this paper will discuss in the three scenarios outlined below further governance instruments that mitigate agency issues.

Owner managed businesses were first said to have no agency issues as owner and manager are the same person and their interests naturally do not conflict (Jensen & Meckling, 1976). One argued that same applies to family firms, as family members typically share the same interests and were hence regarded as one unified actor. Scholars from the family business field (Chrisman et al., 2004; Schulze et al., 2002, 2003b, 2001) rejected this view and explained that governance challenges also arise in the family business context:

4.3.3.1 Adverse selection

Research established that adverse selection also happens in family businesses (Lubatkin et al., 2005; Schulze et al., 2002). In family businesses, adverse selection is regularly not the result of divergent interests and asymmetric information because incumbents generally know about the ability, or inability, of the family members. Contrary, adverse selection results from altruism of family incumbents (Karra et al., 2006; Lubatkin et al., 2007; Schulze et al., 2003a). Family incumbents engage family members in order to share with them financial and socio-emotional wealth of the family firm (Gómez-Mejía et al., 2007). Incumbents may further wish to provide family members via an employment with a certain standard of living (Chrisman et al., 2004). Any
resulting decreasing economic performance of the family business is correspondingly covered by the interest of the incumbent. The financial loss is hence not result of a conflict of interest as it is assumed in classical agency theory (Chrisman, Chua, Kellermanns, & Chang, 2007; Chrisman et al., 2004; Jensen & Meckling, 1976). The loss is generated as family incumbents follow non-economic goals (Lansberg, 1983; Zellweger et al., 2013). Adverse selection is therefore triggered by altruism and a lack of self-control (Chrisman et al., 2004). Altruism is defined as a utility function in which the welfare of one individual is positively linked to the welfare of others (Bergstrom, 1989). Altruism can create agency problems as it induces the incumbent to be generous and to give advantages to descendants without them having merited the rewards (Baldrige & Schulze, 1999). Consequently, there is a risk that such action harms the company. It might even harm descendants if they get accustomed to privileged treatment and lose (or not gain) the ability to look for themselves and to live independently. This occurrence is termed the Samaritan’s dilemma (Buchanan, 1975).

4.3.3.2 Moral hazard

As mentioned, moral hazard defines circumstances after contracting in which the agent engages in behaviors, such as free-riding or shirking, that contravene the interest of the incumbent (Chrisman et al., 2004; Jensen & Meckling, 1976). Hereinafter the paper differs between two sources of moral hazard: Opportunistic behavior in conflicts of interest (moral hazard I) and perceived injustice in succession (moral hazard II).

Moral hazard I. Agency theory explains that one source of moral hazardous behaviors of managers (free-riding and shirking) is opportunistic behavior of
managers in the event there is a *conflict of interest* between principal and agent (Fama, 1980; Jensen & Meckling, 1976). Agents work only for a distinct time frame for the company. Correspondingly agents’ interests, goals and behaviors are contrary to those of the principal short-term oriented (Berle & Means, 1932; Fama, 1980; Jensen & Meckling, 1976; Walsh & Seward, 1990). In practice, this short-term orientation might hinder agents for instance to seize investment opportunities in order to uphold profitability of the company in the short term. Further, agents might excessively use perquisites of the company – as they are not owners they do not suffer the corresponding financial burden.

*Moral hazard II.* Apart from opportunistic behavior in a conflict of interest between principal and agent, there is another and less discussed reason for moral hazardous behavior of family managers: The second source of moral hazard is *perceived injustice*. Only few family business researchers have recognized the relation between perceived injustice and moral hazardous behavior of family members so far. Baldridge & Schulze (1999: C5) realized that: “agency problems may arise from efforts to relieve perceived injustices”, and Lubatkin et al. (2007: 961) propose: “Violations of procedural and distributive justice are positively associated with the firm’s agency costs”. This paper argues that agency issues emerge independent of an opportunistic human nature in a conflict of interests solely as a reaction to unfair treatment. In chapter 4.3.2.3 was stated that under- as well as over-rewarded descendants engage in mechanisms to restore justice. As Adams (1965) elaborated, the under-rewarded person will attempt to increase own outcome, lower own inputs, decrease other’s outcome or to increase other’s input (for the over-rewarded person such applies reversely). For instance, the under-rewarded descendant might reduce work effort following perceived injustice in
succession (= reduce own input), or the under-rewarded might excessively use company perquisites to make up for perceived injustice (increase own outcome). Herewith the circle between justice and agency completes itself: Free-riding and shirking of family members can in certain circumstances be the consequences of felt injustice and an attempt to compensate for unjust treatment (Adams, 1965; Lubatkin et al., 2007).

These deliberations clarify the relations between succession, justice and agency issues. Hereinafter, governance challenges of three different succession forms will be analyzed: 1) if ownership and management in family businesses are transferred in congruence with the distributive justice principle of equity; 2) if ownership and management in family businesses are transferred in congruence with the distributive justice principle of equality, and 3) if ownership is transferred according to the distributive justice principle of equality and management according to the distributive justice principle of equity. Such procedure aims to clearly distinct between the governance challenges resulting from the application of the different distributional justice principles and to explain the corresponding agency issues. The paper thereby considers the time dimension of the succession process and hence applies a dynamic approach (Gersick et al., 1999; Ward & Dolan, 1998). The paper further integrates elements of procedural justice and especially considers the influence of the timing of the disclosure of the justice principle of choice by the incumbent as governance instrument able to mitigate agency issues.
4.4 Governance structures resulting from different justice principles

Let us assume that there are one incumbent and two descendants, descendant A and descendant B, in the family firm succession. Both descendant work and wish to succeed in the family firm.

4.4.1 Scenario I: Application of the equity principle

If the incumbent applies the justice principle of equity, the family firm is transferred based on merit to the most competent descendant. There is a “the winner takes it all” dynamic, in which the winner takes over management and ownership of the firm. The family firm will so move from an controlling owner stage to an controlling owner stage, and its transition form will be a recycle (Dimaggio et al., 1983; Gersick et al., 1999).

With a dynamic look on the succession process, there will be a first phase where the incumbent analyzes descendant A and B in order to elect the “winner” of the family firm. After that choice, there will be a phase in which ownership and management is divided between incumbent and chosen descendant. The incumbent will maintain ownership, whereas the descendant takes over the management of the company, until they reach the last stage of succession in which the chosen successor owns and manages the company alone before entering him- or herself in the succession process (Cabrera-Suarez et al., 2001; Friedman, 1991; Handler, 1994). Categorized in the two classes of adverse selection and moral hazard, the following governance challenges arise in this process.
4.4.1.1 Adverse selection

In intra-familial succession family members are favored over non-family members (nepotism), hence there is always a risk of adverse selection (Jaskiewicz, Uhlenbruck, Balkin, & Reay, 2013). However, as in our scenario two descendants compete for succession, such risk of adverse selection is limited. The incumbent will assess the skills, efforts, education and motivation of descendant A and B and choose the one that is more competent than the other to lead the company to profitability in future. The assessment of the descendants will nevertheless cause agency costs. Such costs arise as both descendants work in the family firm during the assessment period. In this case, positions need to be created and tasks have to be shifted so that both descendants can work in the family firm. Moreover, the time that the incumbent or possibly involved consultants dedicate to assess the competence of the descendants has to be considered as agency costs. Lastly, expenses are generated in connection with the training and education of the descendants. All these costs can be ascribed to the agency costs that arise to prevent adverse selection.

4.4.1.2 Moral hazard

Before succession, the incumbent is at the same time owner and manager. Classical agency costs therefore do not exist. Governance challenges might emerge out of the lack of internal and external monitoring (Walsh & Seward, 1990) what can often be found in non-public owner managed companies (e.g., lack of independent board members).
During the assessment period, moral hazard issues that arise out of opportunistic behavior (moral hazard I) of the descendants are limited. As both, descendant A and B, wish to take over the family firm, they will work hard and give their utmost in order to show their ability to take over the family business. They are not likely to risk succession in engaging in moral hazardous behavior and showing poor performance. In contrast, their ambition is to proof their abilities in order to legitimize themselves as successors. Hence, they are not likely to engage in free-riding or shirking. The possibility of taking over the family business is incentive enough to exclude agency issues arising out of moral hazardous behavior. Accordingly, other incentives, such as performance-based salary or else, will not enhance performance of descendants.

Once the successor is chosen among the descendant A and B, he or she will take over management tasks, while the incumbent is still the owner of the company. This results in a separation of ownership and management. Here classical moral hazard agency issues arise out of conflicts of interest (moral hazard I). But what are the interests of the incumbent and the newly selected successor? Corresponding findings in non-family businesses speak of a long-term orientation of the principal and a short-term risk-averse attitude of the agent (Fama, 1980; Jensen & Meckling, 1976). In family firms, the situation is different (Gomez-Mejia et al., 2001). Especially if one looks at the family succession context. Agents are the sons and daughters of incumbents and therewith the future owners of the company. That changes the supposed short term orientation of the agent. Successor will take into account future ownership. Contrary to predictions in traditional agency theory – where managers are supposed to take fewer investment risks in order not to jeopardize
their position (Fama, 1980; Fama & Jensen, 1983; Jensen & Meckling, 1976) – this can entail a strong investment activity of the successor.

Also, the presumed long-term orientation of incumbents is challenged in the family firm succession context. Most of incumbents’ estate will be bound in the business. In order to finance retirement incumbents might become dependent on dividend payments (Miller & Le Breton-Miller, 2006) and the successor descendant becomes the financial insurance policy of his or her parents (Dunn, 1999). Especially once incumbents give up working for the firm and lose the corresponding salary.

Another point of conflict is that the successor manager wishes to participate in the profit he or she gains for the company. If the successor will not be offered the option to participate in positive performance, in form of ownership and consequent dividend payments or a performance based salary, free-riding or shirking are likely to arise as the successor will try to skim his or her profits in another way. The interests of incumbents and successors are hence likely to diverge. A simultaneous transfer of ownership and management is able to mitigate these agency issues.

Also, moral hazardous behavior out of perceived injustice can incur (moral hazard II) in the event the non-successor descendant stays employed in the family firm. For instance, descendant A might consider the choice of descendant B as unfair and feels under-rewarded. Perceived injustice then leads to free-riding and shirking of descendant A as such behaviors are ways to compensate for the injustice experienced. Successor descendants might aggravate these agency issues as they – out of a feeling of guilt – will allow for
the moral hazardous behaviors of non-successor descendants (Adams, 1965). Establishing clear business objectives, monitoring and pay incentives will work as governance instruments that help to mitigate the consequences of injustice perceived in succession. Further, an early disclosure of the justice principle of choice by the incumbent will moderate the relationship between experienced injustice and negative behaviors of both, the under- and over-rewarded descendant. Early commitment to one of the justice principles by the incumbent can lower sunk costs of the non-successor descendant as it allows the non-successor descendant to follow a different career path (Von Schlippe & Kellermanns, 2008). Timing as element of procedural justice is therewith another governance instrument that is able to mitigate agency costs.

Consolidated this amounts to the following propositions (see also Figure 7):

**Proposition 1a.** In the event that succession is conducted in accordance with the justice principle of equity the risk of adverse selection is limited. Agency costs arise nevertheless in connection with the assessment and training of the descendants.

**Proposition 1b.** Before the choice of the successor moral hazard I agency issues will not arise because the prospect of taking over the family business will mitigate opportunistic behavior of descendants. Other incentives, such as performance based salary or else are of no impact on the performance of the descendants.

**Proposition 1c.** After the successor is chosen, there are moral hazard I agency issues resulting from a separation of ownership and management between
incumbent and successor descendant. Means to moderate these issues are besides monitoring and performance based salary, the simultaneous transfer of ownership and management.

Proposition 1 d. There are moral hazard II agency issues arising out of perceptions of injustice. Besides other governance instruments, early disclosure of the justice principle applied in succession can moderate corresponding agency issues.
Figure 7: Agency issues in equity succession

Equity succession (ownership & management)

- Selection process (competition)
- Training

Altruism

Adverse selection

Conflicts of interests

- Selection process (competition)
- Time of transfer of ownership
- Performance-based salary

Phase I: Pre-choice stage

Phase II: After-choice stage

Moral hazard I

- Time of disclosure of justice principle (input, assessment period)
- Monitoring
- Performance-based salary

Injustice

Moral hazard II
4.4.2 Scenario II: Application of the equality principle

If the justice principle of equality is applied, the incumbent transfers the family firm to both descendants, descendant A and descendant B. The family firm will correspondingly move from an controlling owner stage to sibling partnership stage, and its transition form will be evolutionary (Dimaggio et al., 1983; Gersick et al., 1999).

With a dynamic look on the succession process, in a first phase, both of the descendants will work in the family business and gradually get engaged in the management of the company. First there will be a separation of ownership and management where the incumbent holds ownership and descendant A and B manage the company. Then ownership will be transferred to the descendants so that both become principals as well as agents. If the descendants again apply the justice principle of equality in their own succession, the company will move from a sibling partnership stage to a cousin consortium stage (Gersick et al., 1999). Hence, in contrast to equity successions, with equality successions the number of the family members engaged in the family business increases. As opposed to non-family firms, where the number of shareholders generally increases with the need for capital, the number of shareholders in family firms increases with each family generation. Categorized in the two classes of adverse selection and moral hazard, the following agency issues arise.

4.4.2.1 Adverse selection

Both, descendant A and B succeed in the family business. There is no selection according to their abilities, education, experience or effort. Hence, in the event the justice principle of equality is applied in family firm succession, the risk of
adverse selection, i.e. the risk of engaging and keeping family members employed that not have the necessary competence to lead the family firm, is high (Lubatkin et al., 2005; Schulze et al., 2002, 2003a). In order to mitigate corresponding agency issues, incumbents need to educate descendants, monitor their performance and set financial incentives. Further agency costs arise as incumbents are likely to create unnecessary positions to accommodate both descendants in the firm.

4.4.2.2 **Moral hazard**

*Before ownership succession*, the risk that descendant A and B engage in moral hazardous behaviors is high (*moral hazard I*).

First, successor descendants do not need to prove their abilities. They have secured future ownership and do not risk to lose it because of poor work performance. Buchanan (1975) explains that such guaranteed ownership spoils descendants. As the benefits are secured, descendants feel entitled to them but are not willing to work for them (Lubatkin et al., 2007).

Also, conflicts of interests between the incumbent as principal and descendant A and B as agents are source of moral hazardous behavior of descendants. As mentioned before, the incumbent is likely to rely on dividend payments in order to finance retirement. Contrary, descendants may wish to reinvest profits in order to create wealth in the future. The interest of the incumbent to extract a maximum amount of dividends collides with the interests of the successor descendants to reinvest financial means in the family business. Furthermore, successful successors want to have a share of the profits of the company. If
they do not get such share via dividends or performance-based salaries they are likely to free-ride and shirk.

To *mitigate these agency issues*, incumbents must establish governance instruments such as monitoring and compensation incentives. Another instrument that alleviates agency issues resulting from moral hazard is the simultaneous transfer of ownership and management to the descendants. In this case, free-riding and shirking will diminish out of two reasons. First, because descendant A and B immediately feel poor performance in their pockets and therefore have a higher level of personal responsibility. Second, because the descendants are incentivized to monitor each other more closely as they realize that poor performance of the other descendant has a negative impact on the company performance and correspondingly on the firm value and the distribution of dividends. In contrast to widely held firms, where monitoring is said to decrease with a growing shareholder basis – the shareholders of widely held firms are supposed to be more diversified and less focused on the single investment (Ang, Cole, & Lin, 2000) – descendants will not reduce monitoring. In contrast to shareholders of widely held firms, family shareholders are generally not diversified and the family firm regularly constitutes their greatest financial asset (Fama, 1980; Miller & Le Breton-Miller, 2006; Walsh & Seward, 1990).

*Once the ownership is transferred* to descendant A and B there is a two-owner-two-manager governance structure (= sibling partnership, later cousin consortium). Here the likelihood arises that the siblings have different interests (*moral hazard I*) (Friedman, 1991; Lubatkin et al., 2007; Schulze et al., 2001). In order that conflicts between siblings do not lead into stalemate, the
descendants need to establish governance structures, decision making processes as well as bonding mechanisms that ensure that the company remains fully operative (Friedman, 1991; Ward & Aronoff, 1992).

The danger of conflicting interests increases with every family generation as the number of family members involved in the company rises (Gersick et al., 1999). The establishment of special family firm specific governance instruments, such as family councils, or written family agreements, such as a family constitution or a family shareholder agreement will help to meet the needs of an increasing number family shareholders.

A further mechanism that helps to reduce agency issues is to facilitate the exit of family members. Such exit is facilitated in two ways. First, the exit of the firm should not be equivalent to the exit of the family and the loss of family ties. For instance, the family member that leaves the company (ownership and management) should not be excluded from family celebrations. Second, the exit of the family firm is facilitated if the financial damage of the exit is not too high. In general, family shareholders that wish to sell their shares, have to offer them to other family members at a discount to the actual value of the shares. Depending on the amount of such discount, the exit from the family firm becomes more or less attractive. In any case, such share buy-back of the family, requires that the other family members have enough financial means to finance the transaction. Many families hence build up a special fund that allows to pay the exit of family shareholders.

Lastly, moral hazard issues arise if descendants perceive the succession according to the justice principle of equality as unjust (moral hazard II). If, for
instance descendant B considers him- or herself more competent than descendant A, it is very likely that descendant B feels under-rewarded and perceives succession as unjust. In order to balance out this injustice perceived, descendant B is likely to reduce own input or to increase own outcome (Adams, 1965). Free-riding and shirking therewith become a way to make up for injustice experienced. Also, non-family members might perceive the succession as unjust. In the event of perceived injustice, the family firm hence risks to lose competent employees, family members as well as non-family members (Baldridge & Schulze, 1999; Lansberg, 1983). Such agency issues are mitigated by rewarding special achievements of employees and corresponding compensation incentives. Moreover, an early disclosure of the justice principle of choice by the incumbent will prevent wrong expectations and decrease sunk costs of all involved parties.

It has to be mentioned that successions according to the justice principle of equality cannot endure over several generations. First the application of the justice principle of equality cannot survive in management succession, as the number of family members will over time generally exceed the number of management jobs that the family firm can offer to family members. As a result, there is a separation of ownership and management at some point (see for corresponding governance challenges scenario III). Furthermore, the justice principle of equality can also with regard to ownership transfers not be maintained. Family members will unlikely have the same amount of offspring. For instance, if descendant A has three children and descendant B has only one child, the latter will inherit a bigger ownership stake than the children of descendant A. Thus, at some point, some family members will have more shares than others. Majority shareholders control decision making and hence
the distribution of dividends and the election of board members. They may then misuse their controlling position in the firm to extract benefits at the expense of minority shareholders (Morck & Yeung, 2003; Villalonga & Amit, 2006). In order to keep up with the equality principle families tend to revert to “tribalism” (Von Schlippe & Kellermanns, 2008), and provide each family line (i.e. the family lines of descendant A and B) via contracts, such as family constitutions and shareholder agreements, with the same amount of decision-making power. For instance, a shareholder agreement could be established that guarantees the family lines of descendant A and B the same voting power at the annual general meeting of shareholders.

In a nutshell, agency issues in family businesses that are passed on in accordance with the equality principle can be summarized as follows (see also Figure 8):

Proposition 2a. In the event that succession is conducted in accordance with the justice principle of equality the risk of adverse selection is high. Agency costs arise mainly out of position creation and the training and monitoring of descendants.

Proposition 2b. Before the transfer of ownership to the descendants, moral hazard I agency issues arise out of conflicting interests between the incumbent and the descendants. Future ownership is not able to mitigate these agency issues. Besides monitoring and performance based salary, the simultaneous transfer of ownership and management can moderate these
agency issues, but the latter results in other agency issues (see Proposition 2c).

**Proposition 2c.** Once ownership is transferred to descendants, moral hazard I agency issues arise out of conflicting interests between descendants. Besides monitoring and performance based salary these can be moderated by establishing family firm specific governance instruments to align divergent interests (special family agreements and governance bodies, exit facilitating mechanisms).

**Proposition 2d.** There are moral hazard II agency issues arising out of perceptions of injustice. Besides other governance instruments, early disclosure of the justice principle applied in succession can moderate corresponding agency issues.

**Proposition 2e.** The justice principle of equality cannot be maintained over several generations.
Figure 8: Agency issues in equality transfers

- **Equality succession (ownership & management)**
  - Training
  - Performance-based salary
  - Monitoring

- **Altruism**
  - Time of transfer of ownership
  - Performance-based salary
  - Monitoring

- **Conflicts of interests**
  - Before transfer of ownership from incumbent to descendants
  - After transfer of ownership from incumbent to descendants
  - Time of disclosure of justice principle
  - Performance-based salary
  - Monitoring
  - Family firm specific gov. instr.

- **Injustice**

- **Adverse selection**

- **Moral hazard I**

- **Moral hazard II**
4.4.3 Scenario III: Application of equality to ownership and equity to management

If in ownership succession, the justice principle of equality is applied while in management succession, the justice principle of equity is applied, both, descendant A and B become shareholders of the company. Contrary, only the most competent of them, let us assume that this is B, succeeds in management. With regard to ownership, the transition form of the family firm is evolutionary, whereas with regard to management, the transition leads to a recycle (Dimaggio et al., 1983; Gersick et al., 1999).

With a dynamic look on the succession process, the two descendants join the family business in order to compete for the management position in the company. After an assessment period, descendant B is chosen as manager successor. There will be a period where ownership and management is divided between the incumbent and descendant B. In a last step, the incumbent transfers ownership of the company to both descendants, and descendant A and B become equal owners of the company. With regard to agency issues the following applies:

4.4.3.1 Adverse selection

Besides the clear preference of family members (nepotism) (Jaskiewicz et al., 2013), the equity approach will guarantee that the most able of the descendants will take over the management of the company. After the assessment period, one of the descendants is chosen as successor. The risk of adverse selection is hence limited. Costs arise as described above in connection with the assessment of the descendants. The time the incumbent or consultants dedicate to assess
the competence of the descendants, education and training of the descendants as well as possible position creation result in agency costs. It has to be mentioned that this third scenario is different from the first scenario: As ownership is distributed according to equality the pool of possible manager successors increases with each generation (Le Breton-Miller et al., 2004), so that the risk of adverse selection decreases over time.

4.4.3.2 Moral hazard

As explained in chapter 4.3.3.2, moral hazard agency issues arise either out of opportunistic behavior following a conflict of interest (moral hazard I) or out of perceived injustice in succession (moral hazard II). Most of these issues are elaborated on in scenario I and II.

Before succession, the descendants compete for the management position. They are expected to work hard in order to prove their merit. However – and this in contrast to scenario I – it is questionable if their efforts are as high as in the event that they fight for all or nothing (ownership and management of the company). Ownership is passed on according to the justice principle of equality and hence not tied to the management position. That will reduce eagerness of descendant A and B and increase the likelihood of moral hazardous behaviors (moral hazard I) of descendants (Buchanan, 1975). However, the incentive of management succession is strong and will be able to reduce corresponding agency issues. Additional governance instruments, such as performance-based salary or monitoring, will further mitigate agency issues.

Once the incumbent has chosen the successor and descendant B succeeds into management of the company, classical agency issues arise out of the separation
of ownership and management and diverging interests between incumbent and descendant B, e.g., with regard to the re-investments and the sharing of profits (Dunn, 1999), see scenario I and II. Governance instruments need to be established that address these conflicts of interests.

After ownership is transferred to both descendants, they replace the incumbent as principal. Both descendants are now principals but only descendant B is the agent. Tensions might arise because of the different roles the descendants now have (Tagiuri & Davis, 1996). Different degrees of involvement and commitment to the family firm as well as information asymmetries (Jensen & Meckling, 1976; Schulze et al., 2001) might generate conflicts of interests. There is a risk that descendants have conflicting views on the re-investment of profits. Descendant B may wish to reinvest profits while the descendant A depends on dividend payments to maintain his or her living standard. Family firm specific governance instruments, such as family constitutions, must ensure efficient decision making processes. In practice, families often tackle for example the issue of dividend distributions by contractually setting a minimum dividend payout ratio in the family constitution or the shareholder agreement. Also, the facilitation of the exit of family shareholders will prevent that conflicts in the family lead to stalemate in the firm (see scenario II).

Moreover, also in this scenario, injustice perceived in succession will lead to agency issues if both descendants remain employed in the family firm (moral hazard II). For instance, if descendant A considers the choice of descendant B as manager successor as unfair, descendant A is likely to engage in free-riding and shirking in order to restore justice (Adams, 1965). Descendant B might tolerate such behaviors of descendant A, as he or she feels over-rewarded and
guilty towards descendant A (Adams, 1963; Regan, 1971). Contrary, if descendant B feels under-rewarded as he or she expected to receive a majority stake in the company, then descendant B is likely to free-ride and shirk in order to make up for experienced injustice.

Agency issues generated by descendant B are mitigated by monitoring through descendant A. Descendant A will closely monitor the performance of the successor out of several reasons. First because most of his or her estate will be bound in the company and descendant A is therefore very much concerned about how his or her wealth is invested. Second, generally ownership stakes in family businesses are hard to sell (see scenario II). Shares are regularly tied to preemption rights of other family members, which often imply a price deduction. The inability to exit the family firm and to invest financial resources in another way will increase monitoring activities of descendant A.

Agency issues generated by descendant A are mitigated by performance based salary and monitoring through the management successor descendant B.

In the event of perceived injustice, monitoring activities should not be effected by the over-rewarded – as over-rewarded descendants will tolerate moral hazardous behavior of under-rewarded descendants. Again, early disclosure of the justice principle of choice by incumbents will mitigate moral hazardous behavior by descendants resulting from perceived injustice as it will help descendants to lower sunk costs and follow other career paths, if necessary.
Another already discussed mechanism to reduce agency issues arising out of conflicts of interest is to facilitate the exit of the family business (see scenario II).

The policy of equal ownership stakes of family members cannot be maintained over generations. It is improbable that descendants have the same number of children and consequently, over time, some family members will have a bigger ownership stake than others. Agency issues might arise because now family shareholders with a bigger ownership stake are able to dominate decision making of the company (Morck & Yeung, 2003; Villalonga & Amit, 2006). In order to keep up with the equality principle in ownership families often assign to each family line contractually the same amount of decision-making power (see scenario II: tribalism) (Von Schlippe & Kellermanns, 2008). One manifestation of such tribalism is that every family line has the right to appoint among its members one member of the board of directors. Over time such outflow of the equality principle in ownership is hard to be maintained. Especially, in the event that the family firm becomes publicly listed the pressure from non-family shareholders increases to select board members solely based on their competence and to not favor family shareholders in the board.

Lastly, it has to be mentioned that the use of both justice principles, equity and equality, leads to confusion (Le Breton-Miller et al., 2004). If ownership is transferred according to equality and management according to equity, the roles of the family members in the governance bodies have different sources of legitimacy. Family owners are owners because of their kinship ties to the incumbent. Contrary family managers are engaged because of their
competence to lead the company to future success. Requirement profiles and performance measures become blurred and create tensions between family members (Baldrige & Schulze, 1999; Kidwell et al., 2012; Lansberg, 1983; 1994b). Family owners might not acknowledge family managers’ work and efforts, and contrary family managers expect more from family shareholders than they could and would from non-family shareholders.

In sum, the agency issues resulting from an equality transfer of ownership and an equity transfer of management can be resumed as follows (see also Figure 9):

**Proposition 3a.** In the event that management is transferred in accordance with the justice principle of equity and ownership in accordance with the justice principle of equality the risk of adverse selection is medium. Agency costs arise in connection with the assessment of the descendants. With each generation, the pool of possible successors grows and the risk of adverse selection decreases.

**Proposition 3b.** Before the choice of the successor the risk of moral hazard I agency issues resulting from divergent interests between incumbent and descendants is limited. The prospect of taking over the family business will moderate opportunistic behavior of descendants, but to a lesser extent than when ownership and management are both transferred according to the justice principle of equity.

**Proposition 3c.** After the manager successor is chosen there are moral hazard I agency issues arising from conflicting interests between incumbent
and successor, which are after the ownership transfer to both descendants replaced by moral hazard I agency issues arising from conflicting interests between the two descendants. That implies that the simultaneous transfer of ownership and management is not able to mitigate moral hazard I agency. Agency issues can be moderated – besides monitoring and performance based salary – by family firm specific governance instruments (special family agreements and governance bodies, exit facilitating mechanisms).

Proposition 3d. There are moral hazard II agency issues arising out of perceptions of injustice. Besides other governance instruments, early disclosure of the justice principle applied in succession can moderate corresponding agency issues.

Proposition 3e. The justice principle of equality cannot be maintained over several generations.
Figure 9: Agency issues in mixed transfers

Equity in management succession – equality in ownership succession

- Selection process (competition)
- Training
- Growth of family

Altruism → Adverse selection

Conflicts of interests

- Selection process (competition)
- Time of transfer of ownership
- Performance-based salary
- Performance-based salary

Phase I: Pre-choice stage → Phase II: After-choice stage → After transfer of ownership to descendants

- Time of disclosure of justice principle (input, assessment period)
- Performance-based salary
- Monitoring
- Family firm specific gov. instr.

Injustice → Moral hazard II

Moral hazard I

- Family firm specific gov. instr.
- Exit facilitating mechanisms
- Performance-based salary
- Monitoring
4.5 Conclusion

This is a conceptual paper that outlines the consequences that the choice of the justice principles of equity or equality in succession has on governance of family firms over time. Each family internal succession touches the question of distributional justice as it implies the allocation of management and ownership to the next generation. In distributions in the family context the justice principle of equality is dominant as here the fostering and maintenance of social bonds are the main objectives (Deutsch, 1975). Contrary, in competitive environments such as the business, goods are allocated based on merit to the one who contributes more (Deutsch, 1975). In family firms the two systems of family and firm overlap (Lansberg, 1983), and correspondingly both norms, equity and equality, play a role in family firm succession.

In order to elaborate on the consequences of the choice of the different justice principles of equity and equality, three scenarios are described. One in which the family business – ownership and management – is transferred according to equity, one in which such functions are transferred according to equality, and one in which ownership is transferred according the equality principle and management according to the equity principle. The latter case is the most common in our cultural environment (see paper 1, chapter 3). All three scenarios assume that there is one incumbent and two descendants (siblings) and that it is up to the incumbent to choose either the justice principle of equity or equality. In reality, the choice of the incumbent is limited by factual or legal restrictions. If the equity principle is selected only the most competent among the descendants replaces the incumbent in ownership and management. Contrary, if the choice falls on the equality principle both descendants succeed
the incumbent in management and ownership. In the third scenario, ownership is transferred according to equality and both siblings become owners but only one of them takes over the management as in this regard the equity principle is applied.

The consequences of the resulting governance structures are approached under an agency perspective (Jensen & Meckling, 1976). Agency issues arise out of the fact that ownership and management are in the hand of different people (principal and agent) and can be classified in the two subsections of adverse selection and moral hazard (Fama, 1980; Fama & Jensen, 1983; Jensen & Meckling, 1976). Whereas adverse selection refers to problems that arise in connection with the employment of the agent (pre-contracting), moral hazard issues arise after contracting. Moral hazard is further split in two categories. The first category encompasses moral hazard issues arising out of divergent interests and the opportunistic behavior of the parties (moral hazard I). The second category includes moral hazard issues that have their source in perceived injustice (moral hazard II).

The paper analyzes the agency issues in each of the three scenarios and thereby differentiates between different succession stages.

Agency costs to prevent adverse selection arise from the employment and the assessment of the descendants. Moral hazard issues (moral hazard I) are generated by different interests of incumbent and descendants or by conflicts between the descendants. Governance instruments that are able to mitigate these agency issues, are besides the traditional governance instruments of monitoring and compensation incentives (Fama & Jensen, 1983), a
simultaneous transfer of ownership and management as well as the establishment of family firm specific governance instruments (such as family contracts, e.g., family constitutions), or lastly the facilitation of an exit of family shareholders.

Agency issues further arise in connection with perceived injustice (moral hazard II). It was shown that descendants, if they feel under- or over-rewarded in succession seize different injustice reducing mechanisms in order to reestablish justice. These agency issues are likely to arise in all three scenarios. It is offered that they can be moderated by known agency instruments (Jensen & Meckling, 1976), such as monitoring or compensation incentives as well as by elements of procedural justice such as the early disclosure of the justice principle designed to apply in succession by incumbents.

This paper combines the three research streams of family business succession, justice and governance and makes several contributions. First, it establishes the relation between the choice of a justice principle in the succession and the corresponding governance structure of the family business. Although scholars consider succession as key element for future success of the family firm and as distinguishing feature in relation to non-family firms (Chua et al., 1999; Le Breton-Miller et al., 2004), a closer discussion of governance structures resulting from the application of different justice principles has been lacking so far. Second, agency issues in family business have previously almost exclusively been discussed from a static point of view. In this paper, a more dynamic approach is adopted in which governance and agency issues were investigated taking into account the succession process and different transition forms of family firms (Gersick et al., 1999; Handler, 1994). Lastly, agency
issues resulting from perceived injustice have been introduced, therewith the paper offers, in addition to altruism (Karra et al., 2006; Schulze et al., 2002) another source of firm damaging behavior of family members. The paper hence adds on to an emerging research stream investigating the relation between agency issues and justice (Baldridge & Schulze, 1999; Lubatkin et al., 2007).

4.6 Limitations and future research

This conceptual paper has several limitations: First, this paper only investigates the two different justice principles of equity and equality although there are others that are likely to influence the incumbent, e.g., the justice principle of need (Cropanzano et al., 2007; Deutsch, 1975). Furthermore, the paper leaves out contextual elements such as the willingness of descendants to succeed in the family business, intestate succession laws, family relationships etc. Also, it focuses exclusively on the family business and does not take into consideration other economic and non-economic goods of the incumbent (such as the family home) that can be distributed in a case of inheritance and have an impact on the overall assessment of the fairness of the allocation.

Future research should be influenced in three ways. First, as governance structures in family firms and therewith their challenges change over time, future discussions of agency issues in family firms should specify in what transition stage the family firm finds itself. Second, empirical investigations of the governance structures in light of their origin regarding the justice principle applied in the succession are needed and third, such investigations should especially focus on consequences perceived injustice has on the behavior of family members involved in the family firm.
Overall, justice considerations fundamentally shape governance in family firms. Future research dedicated to analyzing the relationship between justice and governance will be able to provide insights that are fruitful for theory and practice.
5 What goes around comes around – descendants harm the family firm following perceived injustice

Sonja Kissling Streuli

5.1 Abstract

A pitfall in succession is the just allocation of the family business to the descendants. Very often children perceive incumbents’ decision regarding ownership and management transfer as unfair. Some believe to be under-rewarded, others over-rewarded. This paper deals with the consequences of injustice perceived by descendants in succession, on the family firm. Findings suggest that not only family relations suffer but that the family firm becomes target of so called injustice reduction mechanisms, behaviors of descendants designed to restore justice, that have predominantly detrimental effects on the business. Based on survey responses of 1’528 respondents I quantitatively investigate the occurrence of these injustice reduction mechanisms. Under-rewarded descendants are expected to feel anger and envy and show behaviors such as shirking, free-riding, resistance to change, or legal-claiming. Contrary, perceived injustice is expected to lead the over-rewarded to feel guilty and to result in the following behaviors: More work effort, less satisfaction, salary increase for the under-rewarded and a toleration of less work quality of the under-rewarded. I further test moderating effects of family cohesion. The paper aims to contribute to family business succession, governance and organizational justice literature.
5.2 Introduction

Moro is a food company in the third generation. Moro is producer and distributor of high-quality fresh fruits and vegetables. Since a couple of years Arthur Moro is CEO of the company. His younger brother Danny Moro leads the company’s packaging division. Their father is still in the board of directors and sole owner of the company. Arthur and Danny get along very well with each other. Arthur is more decisive than his brother, while Danny is more considered. Since early childhood they know that they will be co-owning the company and expect that they will share ownership equally. After the death of their father they however learn that their father left the majority of the shares to Arthur.

Family-internal succession is a distributional process in which incumbents allocate the family firm, i.e. ownership and management of the firm, to their descendants. They must choose which of their children follow in their footsteps. One main goal of incumbents is that succession is perceived as fair by their descendants to prevent conflict and to enable a smooth succession (Dyer, 1986, Kidwell, Kellermanns, & Eddleston, 2012; Taylor & Norris, 2000). However, this objective is often not achieved and the allocation decision results in perceived injustice (Friedman, 1991). Some descendants might think that they did not receive what they deserve and consider themselves as under-rewarded. In the introduction example above, Danny feels under-rewarded. Danny thinks that his father should have divided ownership equally between him and Arthur, but his father bequeathed the majority of the shares to Arthur who at the same time takes over the management of the family firm. Danny
feels discriminated as he believes that a father should treat his children equally. Additionally, also Arthur perceives the succession solution of his father as unjust. As Danny, he thinks that their father should have divided ownership equally between him and his brother. Now that he learned that he becomes the majority shareholder, he feels to have received more than deserved. He feels not under- but over-rewarded (Taylor & Norris, 2000). The example shows that allocation decisions of incumbents might at the same time produce a situation in which some descendants feel under- and others over-rewarded. Both, under- and over-rewarded descendants perceive injustice. This paper investigates the consequences of injustice perceived by descendants that are directed against the family firm.

Family business researchers have recognized that justice is an important aspect in family firm succession. It has been discussed that a common understanding of what is just is a key factor for a smooth transition (Dyer, 1986; Le Breton-Miller et al., 2004; Morris et al., 1997; Taylor & Norris, 2000; Van der Heyden et al., 2005), as otherwise feelings of injustice create conflict and rivalry between descendants that endanger the survival of the family firm (Ayres, 1990; Dyer & Handler, 1994; Friedman, 1991; Kidwell et al., 2012; Taylor & Norris, 2000; Van der Heyden et al., 2005). Family business governance scholars have indicated that perceived injustice might result in moral hazardous behavior and thereby create agency costs (Baldridge & Schulze, 1999; Lubatkin et al., 2007). Kidwell and colleagues (2012) have argued that perceived distributive fairness creates a climate that fosters family members’ positive contributions and prevent the “Fredo” effect, i.e. inhibit family members to become an impediment for the family firm.
However, a deeper conceptual discussion of perceived injustice in family firms as well as quantitative empirical investigations of its consequences have been lacking so far. That led Gagné, Sharma, & De Massis (2014) to the conclusion that in family business research “the justice stream is virtually dry”. They suggest using findings of organizational behavior literature to enlighten the role of perceived injustice in family firms. Following their call, this paper intends to answer the following research question: *What impact has injustice perceived by descendants in family firm succession on the family firm?* The consequences of injustice perceived in family firm succession are analyzed by drawing from organizational justice research. “Injustice is hurtful to individuals and harmful to organizations” (Russell Cropanzano, Bowen, & Gilliland, 2007: 34) and therefore organizational justice as part of the organizational behavior research stream investigates what people believe to be just in the workplace (Colquitt, Conlon, Wesson, Porter, & Ng, 2001; Greenberg, 1990; Greenberg, 1990). Organizational justice researchers have investigated behaviors that people who perceive injustice apply in the workplace and proved that people who perceive a situation as unjust will change their behavior in order to restore justice. The theoretical foundation of these so-called injustice reduction mechanisms lies in the definition of injustice presented in the seminal work of Adams (1965).

In building the hypotheses I draw from these findings of organizational justice research and investigate whether some of the injustice reduction mechanisms that were established to be undertaken by under- or over-rewarded employees will also apply to under- and over-rewarded descendants in the family business succession context. I thereby test whether family cohesion is able to moderate
the relationship between perceived injustice and injustice reduction mechanisms.

The paper therewith intends to contribute to three research streams. First, it adds to *family business succession* research (Barach & Ganitsky, 1995; Le Breton-Miller et al., 2004; Sharma et al., 2001) in empirically investigating whether injustice perceived in succession will have consequences for the business post succession as family members engage in injustice reduction mechanisms addressed at the firm to reduce injustice. I thereby would like to again raise awareness that succession decisions cannot be regarded as isolated phenomenon but have profound and enduring effects on the family firm. I further address the role of family cohesion in situations of perceived injustice and will answer the question whether it can mitigate its effects.

Second, I intend to contribute to *family business governance* research in offering empirical data to the hypothesis that, besides altruism, an important source of moral hazardous behavior and adverse selection is perceived injustice in succession (Baldridge & Schulze, 1999; Lubatkin et al., 2007). Perceived injustice can explain firm-damaging (and self-destructive) behaviors of family members in family firms. Consequently, family firms have to design a governance system that prevents perceived injustice in succession and mitigates negative consequences of perceived injustice on the family firm.

Third, the paper aims to add to *organizational justice* theory in extending its findings to the family business context (Cropanzano et al., 2007; Greenberg, 1990a). As most firms are family firms (La Porta et al., 1999; Sharma et al., 2001; Zellweger, 2017), it is important to investigate the ramifications of
family members’ behavior on the firm in the event of perceived injustice in succession. I thereby extent the focus in three ways. First, I look at behaviors of the under- and the over-rewarded. Detrimental behaviors of the latter have received little attention of organizational justice theory (Cropanzano et al., 2007; Greenberg, 1987, 1990b). In the family business succession context, such behaviors gain importance as the over-rewarded is typically the successor of the firm and his or her feelings and behaviors will correspondingly determine firm decisions. Second, I look at justice perceptions that are generated by incidents outside the firm (or in the intersect of the family and the firm) and investigate consequences within the firm. Third, the paper’s focus is not restricted to the exchange situation of the dyadic relationship (incumbent - descendant) but investigates how perceived injustice is reciprocated outside this relationship, i.e. to the family firm. In terms of social exchange theory (see e.g., Blau, 2009; Ekeh, 1974; Homans, 1958, 1961; Thibaut & Kelley, 1959), the paper deals with an indirect or generalized form of social exchange in which perceived injustice results in behaviors that are not directed to the party causing the pain but to third parties not directly involved in the exchange situation (Bosse, Phillips, & Harrison, 2009; Ekeh 1974; Wade-Benzoni, 2002).

In short, this paper will provide for empirical results on the effects of perceived injustice in family firm succession. This is helpful for theory to further examine the consequences of perceived injustice in family firm succession but will also raise awareness in people dealing with family firm succession in practice to consider and address injustice perceived by descendants in succession planning.
5.3 Theoretical background

5.3.1 Three different types of justice

Social interaction always implies the exchange of economic and non-economic resources (Leventhal, 1980). In these exchanges the parties distribute resources, such as money, love, status, information, or services (Tornblom & Foa, 1983) to each other. Distributions imply decisions about to whom goods are allocated and in what way such goods are divided between possible recipients (Clark & Chrisman, 1994; Konow, 2003; Masterson et al., 2000; Walzer, 1983). As people aim to achieve just allocations, justice forms part of every social interaction (Masterson et al., 2000; Montada, 1998).

Justice theory now deals with the question of justice in two ways. First, in a normative approach scholars try to answer the question of how goods should be distributed to achieve an ideal state (Konow, 2003). Others, like this study, focus on what distributions people actually perceive as fair and what they do if they consider situations as unfair (Cropanzano et al., 2007).

In searching for answers regarding what distributions are perceived as fair by the people, justice theory first focused on the outcome of the distribution (distributional justice) (Adams & Jacobsen, 1964; Cropanzano, Prehar, & Chen, 2002; Deutsch, 1975; Homans, 1958). It was recognized that there are multiple justice principles at hand according to which the outcome of an allocation can be determined, e.g., equality, equity, seniority, “first come first served” etc. (Deutsch, 1975; Messick, 1995; Walzer, 1983). What determines which justice principle is appropriate is particularly the context of the decision (Leventhal, 1980; Leventhal & Anderson, 1970). Leventhal (1980) argues that
people use in distributions the justice principle of equality if their primary concern are interpersonal relations and group solidarity. Deutsch (1975) explains that the equality rule supports cooperative systems where the fostering or maintenance of enjoyable social relations is the common goal. Drake & Lawrence (2000) found that in inheritance distributions, parents by default apply the justice principle of equality. Contrary, in the business context economic productivity is the primary goal (Deutsch, 1975) and goods are allocated based on merit to those who are able to use them in the most efficient and effective way (Baldridge & Schulze, 1999; Deutsch, 1975; Walzer, 1983).

But not only the context but also culture, personality traits and the type of resources to be allocated will influence the election of a justice principle (Carney, 2005; Meindl, 1989; Tornblom & Foa, 1983). So, when distributing estate assets to descendants, Western societies prefer equality transfers while other cultures consider the justice principle of primogeniture as appropriate (Drake & Lawrence, 2000). Males are more inclined than females to apply the justice principle of merit (Kahn et al., 1980). And grades are awarded based on merit, while social welfare is given to the ones in need (Deutsch, 1975). These examples show that distributional justice is a relative concept.

In a further step, research understood that people assess the fairness of an allocation not based on the outcome alone, but that they evaluate in their fairness judgment also the process of the allocation decision (procedural justice) (Leventhal, 1980; Thibaut & Walker, 1978; Walker et al., 1979). Scholars determined procedural elements that influence peoples’ fairness appraisal, especially in a context where they have limited own decision power, i.e. legal process (Thibaut & Walker, 1978; Walker et al., 1979). Initially
numbered among the elements of procedural justice it was later recognized that treating people in a fair and respectful manner constitutes a separate third type of justice, besides distributional and procedural justice, called *interactional justice* (Barclay, Skarlicki, & Pugh, 2005; Bies, 2005; Cropanzano et al., 2002). Due to this separation, more formal elements, such as consistency of the justice principle chosen in allocation processes (Barclay et al., 2005; Cohen-Charash & Spector, 2001; Leventhal, 1980), are discussed within the concept of procedural justice, and more social elements, such as whether people are treated with dignity, within the concept of interactional justice (Bies & Moag, 1986; Bosse et al., 2009).

Family-internal succession is an allocation process in which family firm incumbents distribute power and control (De Massis et al., 2008), i.e., management and ownership, to the next generation. All three types of justice will thereby shape justice perceptions of family members. First, distributional justice principles decide about how ownership and management of the company are passed on to the next generation. Distributional justice principles that suggest themselves are equity, equality, need or also the principle of primogeniture (first-born) (Ayres, 1990; Van der Heyden et al., 2005). Culture and personality of the incumbent will decide which justice principle will be applied (Baldrige & Schulze, 1999; Deutsch, 1975; Fondacaro et al., 2002; Friedman, 1991; Leventhal, 1980, see also chapter 3). Besides distributional justice also procedural and interactional justice will play a pivotal role in succession (Barnett, Long, & Marler, 2012; De Massis, 2012; Fondacaro et al., 1998; Van der Heyden et al., 2005). Important elements of procedural justice that will influence justice perceptions among family members are the timing of the transfer of ownership and management as well as the degree to which
descendants have a say in the process (Sharma et al., 2001). Further, interactional justice elements, i.e. understanding and respectful treatment, will be key as succession is a very sensitive topic for all involved family members (De Massis et al., 2008). It is likely to reopen old wounds (Lansberg, 1988) and implies drastic changes in professional and personal life of family members (Brockhaus, 2004). In sum, family business research has dealt with distributional, procedural and interactional justice elements that support success or failure of succession (Barach & Ganitsky, 1995; Sharma et al., 2001). However, family business research has not investigated concrete outcomes of a violation of the three types of justice in succession. This study focuses in a first step on distributional justice and the consequences distributional injustice perceived by descendants has on the family firm.

5.3.2 Distributional justice and perceived injustice

The seminal work of Adams (1965) provides for the conceptual basis of what people perceive as fair and what they do in the event they consider an outcome as unfair. Adams sees humans’ behavior as exchange of goods (Ekeh, 1974). According to Adams, exchange situations, or distributions, are considered as fair if parties believe that the outcome received from the exchange corresponds to the input given into the exchange (Adams, 1965; Homans, 1961). Individuals will thereby assess own input and outcome and the input and outcome of the other party to the exchange. The latter hence serve as a reference value (Festinger, 1954). As the amount of inputs and outcomes of people are different, people consider a situation to be fair if they proportionally receive the same and hence the following equation can be made (Adams, 1965):
For example, it is considered as fair if someone who works more receives a higher salary (Greenberg, 1988a). Here a bigger input (work) leads to a higher outcome (salary). People who work less and receive a lower salary will not consider the situation as unfair. In contrast, if such equation cannot be made, the situation is unfair: The situation in which someone who works less than another person receives a higher salary than such person is regarded as unfair.

People hence perceive an allocation as unfair if they do not receive the outcome they feel entitled to (Adams, 1965; Mikula, 1993). They base such feelings of entitlement on the justice principle they consider as applicable in a given situation. In the example with the salary, people consider the justice principle of equity as relevant where the allocation of wages is based on merit. What justice principle people consider as relevant and correspondingly what outcome they feel entitled to, depends on culture, context, resource to be distributed and the individual (Deutsch, 1975; Festinger, 1954; Tornblom & Foa, 1983). Correspondingly injustice is relative and not an objectively determinable consequence of a distribution. This relativity of the justice concept is the reason and primary source of perceived injustice and conflict. Because of the relativity of the justice concept it is highly likely that at least one person to an allocation has a divergent view on how the allocation should be effected.
5.3.3 Consequences of perceived injustice

Perceived injustice has several consequences. First, perceived injustice will result in emotions and such emotions motivate a change in the behavior of people (Adams, 1965; Barclay et al., 2005; Mikula, Scherer, & Athenstaedt, 1998; Weiss, Suckow, & Cropanzano, 1999). These behaviors are aimed to reduce injustice and are consequently summarized in the term *injustice reduction mechanisms* (Adams, 1965; Barclay et al., 2005; Mikula, Scherer, & Athenstaedt, 1998; Weiss, Suckow, & Cropanzano, 1999). Adam’s equation gives us the options how people who perceive injustice can reestablish a just situation (Adams, 1965; Festinger, 1957; Homans, 1961). Namely, in order to restore justice, they can work with each factor of the equation.

The *under-rewarded* person has the following options:

1. Reduce own input
2. Increase own outcome
3. Increase input of other
4. Reduce outcome of other

Like a mirror image of the under-rewarded person, the *over-rewarded* has the following options to retrieve justice:

1. Increase own input
2. Reduce own outcome
3. Reduce input of other
4. Increase outcome of other
5.3.4 Consequences of perceived injustice in organizations

Based on Adam’s equation organizational justice theory empirically established the occurrence of these injustice reduction mechanisms in the workplace (Colquitt et al., 2001; Greenberg, 1990). They proved that employees who consider the ratio between their input and outcome as unfair will change their behavior (Greenberg, 1988a, 1990b). Possible outcomes of employees in the employment relationship are of financial and non-financial value, such as salary (Adams & Jacobsen, 1964), office type (Greenberg, 1988a), respectful treatment by supervisor (Skarlicki & Folger, 1997), or overall workplace satisfaction (McFarlin & Sweeney, 1992). The inputs of employees are their job performance, such as work effort, work quality, or productivity (Adams & Jacobsen, 1964) as well as their general behavior, such as organizational citizenship behavior at the workplace (Lee & Allen, 2002; Zhang, Lepine, Buckman, & Wei, 2014).

It was shown that if the ratio between input and output at the workplace is unbalanced, employees will consider the situation as unfair and that both, under- and over-rewarded will engage in injustice reduction mechanisms. For instance, the under-rewarded was found to revert to workplace sabotage (Ambrose et al., 2002), workplace deviance (Bennett & Robinson, 2000), or counterproductive work behavior (Cohen-Charash & Spector, 2001). Such behaviors reduce own input and decrease the outcome of the other (i.e. employer), what corresponds to the first and forth injustice reduction mechanism of the under-rewarded named above. Further, Adams & Jacobsen (1964) as well as Greenberg (1988) found that the over-rewarded will show
more work effort and therewith increase own input, what corresponds to the first injustice reduction mechanism of the over-rewarded named above.

Injustice reduction mechanisms undertaken by employees target either directly their supervisor or the company in general (Cropanzano et al., 2002; Ekeh, 1974; Skarlicki & Folger, 1997). Same applies to injustice perceived, as such might emanate from the supervisor or the company. Employees may perceive behaviors of individuals as unjust or general procedures and processes of the company (Bies & Moag, 1986; Colquitt et al., 2001). It might therefore be that employees perceive a decision of the supervisor as unjust but direct injustice reduction mechanisms against the company. This form of exchange is predicted by social exchange theory (Ekeh, 1974). According to social exchange theory there are on the one hand exchanges in a dyadic interaction A-B and on the other hand there are exchanges that affect third persons, e.g., A gives something to B whereupon B gives something to C (Ekeh, 1974; Homans, 1958, 1961). The latter exchanges are called indirect or generalized forms of exchange (Barnett et al., 2012; Ekeh, 1974; Homans, 1958).

In the following, I will draw from these findings in organizational justice theory and investigate whether descendants who feel unjustly treated in family firm succession will undertake injustice reduction mechanisms that affect the family firm (Gagné et al., 2014). Thereafter, I will discuss some indirect effects, the moderating role of family cohesion and mediating role of the emotions anger, envy on side of the under-rewarded and guilt on side of the over-rewarded.
After the death of their father, Arthur and Danny Moro continue their work in the family firm. Danny is disappointed that his father only left him a minority stake in the company. Why did he do that? Was it that his father doubted his abilities as shareholder? Danny always knew that his father felt a little closer to Arthur as their personality was similar. However, he never thought that this would impact ownership succession decisions. Arthur feels that his brother is doubting the succession decision of their father. He himself does not know more about their father’s considerations. Arthur has nothing to do with his father’s decision, however, he feels a bit guilty. Also, Arthur fears that the relationship to his brother will deteriorate.

5.4 Hypotheses development

5.4.1 Injustice reduction mechanisms following perceived injustice in family firm succession

In family firm succession, the two main inputs descendants can place on the table are on the one hand their kinship to the incumbent and on the other hand their competence to lead the family firm. The outcome of the descendants is their degree of participation in ownership and management of the company. If kinship is the input incumbents consider as relevant, incumbents will hand over the firm equally to their descendants. Contrary, if incumbents focus on competence, they will hand over the firm to the most competent of their descendants. In family firm succession these two allocation norms or distributive justice principles – the justice principle of equality and the justice principle of equity are competing and cause different feelings of entitlement (Drake & Lawrence, 2000; Rosenblatt et al., 1985, see also paper 1 in chapter
3). In family firm succession, the *under-rewarded* person is the one of the descendants who feels to have received less than to what he or she feels entitled to (Adams, 1965). Contrary, the *over-rewarded* person is the one of the descendants who feels to have received more than he or she deserves (Adams, 1965).

In the introductory example, Danny considers himself as under-rewarded as he believes that he should have received the same number of shares as his brother Arthur. Arthur by contrast perceives to be over-rewarded as he also is of the opinion that Danny should have received the same number of shares as he did. Both descendants consider kinship and therewith the justice principle of equality as applicable whereas their father effectuated the allocation based on merit.

Both, the under-rewarded as well as the over-rewarded descendant will engage in *injustice reduction mechanisms* to reduce perceived injustice (Adams, 1963). These injustice reduction mechanisms will be directed against the company if descendants are employed in the family firm. As established in organizational justice and social exchange literature (Ekeh, 1974; Molm, 2003; Skarlicki & Folger, 1997), injustice reduction mechanisms are not necessarily directed at the one who caused the unjust situation, i.e. the incumbent, but also at third parties. If family members are employed in the family firm, they have the chance to restore justice through actions at the workplace.

Hereinafter possible injustice reduction mechanisms that are directed at the family firm, are elaborated for each, the under-rewarded person and the over-rewarded person, separately:
5.4.2 Injustice reduction mechanisms of the under-rewarded descendant

5.4.2.1 Shirking (reduce own input)

In line with Adam's (1965) equation, organizational justice literature has established that there is a relation between peoples’ job performance and their perception of fairness (Dittrich & Carrell, 1979; Janssen, 2001; Masterson, Lewis, Goldman, & Taylor, 2000; Zhang, Lepine, Buckman, & Wei, 2014). Greenberg (1988) for instance empirically proved that under-rewarded employees will lower job performance. He randomly assigned 198 employees of a large insurance company to offices of either higher, lower, or equal-status coworkers while their own offices were being refurbished. Employees who were reassigned to higher status offices raised their performance whereas those who were reassigned to lower status offices lowered their performance (Greenberg, 1988a). Hence, employees who considered themselves as under-rewarded (lower status office) adjusted their work effort to reduce injustice. Ambrose et al. (2002) found that injustice was the most common cause of workplace sabotage, a term that encompasses all behavior of employees that is likely to damage organization’s operations or the working relationships within the firm.

Typical occurrence of lower job performance is shirking. Shirking is a conscious reduction of work effort and manifests itself in less willingness to take over new tasks and responsibilities. Shirking is a phenomenon known and extensively discussed in agency theory (Jensen & Meckling, 1976; Walsh & Seward, 1990) and integrated in family business governance literature (Chrisman, Chua, & Litz, 2004; Schulze, Lubatkin, & Dino, 2002; Schulze et
Dealing with consequences of the separation of ownership and management agency theory considers shirking as a behavior pattern exhibited by managers that results from the fact that they have interests and risk-exposures different from owners (Fama, 1980; Fama & Jensen, 1983). In order to achieve their goals managers are said to act opportunistically and shirk in the event that they personally do not profit from fulfilling their responsibilities or tasks (Eisenhardt, 1989). This paper suggests that the source of shirking of family members working in the family firm (not only managers) is perceived injustice. If family members feel under-rewarded, shirking will help them to reduce injustice perceived in succession. As under-rewarded descendants received a lower outcome in succession than expected, lowering job performance (= their input) will help them to restore the balance between input and outcome (Adams, 1965). Therefore, the following hypothesis is made:

_Hypothesis 1. Descendants who feel under-rewarded in family firm succession and work in the family business are likely to shirk._

### 5.4.2.2 Free-riding (increase own outcome)

Organizational justice literature has also established that perceived injustice of employees leads to employee theft (Greenberg, 1990b). Greenberg’s study (1990b) study was effected in a company that was, because of a loss of large manufacturing contracts, forced to cut wages by 15%. After the wage cut employees reported feeling underpaid and stole over twice as much as they did when they felt equitably paid. Greenberg reflects that these acts of theft can be interpreted as “unofficial transfers of outcomes from the employer to the employee” (p. 566). It allows employees to increase their outcome without
increasing their input and therewith restore the, in their view, just relation between their input and outcome. In the study of (Greenberg, 1990b) perceived injustice led to illegal behavior. A milder form of theft is free-riding. Free-riding means that someone consumes resources without contributing in return – such person free-rides on the work of others – and is a construct often discussed in agency theory and applied to the family business context (Baldrige & Schulze, 1999; Lubatkin et al., 2007; Schulze et al., 2003a, 2001). Family business research shows that free-riding can result from altruism and a lack of self-control and creates agency costs (Chrisman et al., 2003). But altruism might not be the primary source of free-riding behavior of family members. Through the consumption of family firm resources and perquisites family members can increase their outcome of succession. Therewith they can restore justice. Hence, the following hypothesis is made:

_Hypothesis 2. Descendants who feel under-rewarded in family firm succession and work in the family business are likely to free-ride._

### 5.4.2.3 **Resistance to change (increase input of other)**

Organizational change is strongly connected to justice perception of employees (Cobb, Folger, & Wooten, 1995). For instance, it was found that justice mediates the relationship between supervisors’ transformational leadership and employee cynicism about organizational change (Wu, Neubert, & Xiang Yi, 2007). Bernerth, Armenakis, Feild, & Walker (2007) investigated effects of justice on change commitment of employees following a spin-off and found that procedural and interactional justice predicted organizational cynicism. Folger & Skarlicki (1999) explained how perceived injustice will lead to
resistance to change. As employees face great uncertainty in organizational change, change is connected to a heightened sensibility of the employees (Folger & Skarlicki, 1999). Their support for change is only achieved if they trust the leadership of the company and their working environment (Folger & Skarlicki, 1999). Such trust is shaken in the event that employees feel unjustly treated, and consequently they will resist change (Folger & Skarlicki, 1999).

Resistance to change implies that the leaders of the company have to increase their efforts and work harder to convince employees to undertake the envisaged change. With regard to Adam’s equation (1965) one can say, that perceived injustice results in behavior of under-rewarded employees that induces the over-rewarded supervisors to increase their input. Correspondingly resistance to change is an injustice reduction mechanisms aimed to increase the input of the over-rewarded.

In family firm succession, support for change is pivotal as succession alters so many areas of family and business life (Barach & Ganitsky, 1995; Gersick et al., 1999; Miller et al., 2003). Succession entails changes in the relationships of family members, fathers and mothers retire, and other family members take over new functions in ownership or management (Gersick et al., 1999). Succession affects not only the family but many areas in the firm. Often, succession is reason for long-term non-family employees to leave the company what implies further changes in the staff (Kidwell et al., 2013; Lubatkin et al., 2007). Changes also affect the strategy of the business as successor managers commonly introduce new products, services, processes such as IT solutions, or enter new geographical markets (Sharma et al., 1997).
So far, family business research dealt with resistance to change by incumbents (Kets de Vries, 1993). Incumbents, especially founders, risk to become fixated on a formula for success and inflexible (Brockhaus, 2004; Ward, 1997). Such attitude also prevents incumbents from succession planning (Dyer & Handler, 1994). But not only incumbents’ resistance to change has a negative impact on the firm but also descendants’ resistance to change. Often under-rewarded descendants have managerial functions in the firm and their behavior will influence overall performance of the company. As family members, they further serve as examples for other employees of the company. If under-rewarded family members do not support change in the family firm, change and succession itself will be more difficult to manage. Hence, resistance to change of employed family members is likely to be a stumbling block for successful succession (Barach & Ganitsky, 1995; De Massis et al., 2008; Sharma et al., 2001). Other family members, especially the over-rewarded, must increase their input to encourage change. Hence resistance to change is a means for the under-rewarded descendant to make up for injustice perceived in succession. Correspondingly, the following hypothesis is made:

_Hypothesis 3. Descendants who feel under-rewarded in succession firm succession and work in the family business are likely to resist change (e.g., new products)._ 

### 5.4.2.4 Legal claiming (decrease outcome of other)

Organizational injustice was found to be a predictor of employee legal-claiming behavior (Goldman, 2003). For example, Bies & Tyler (1993) found that the increasing "litigation mentality" among employees is influenced
largely by the perceived fairness of their dealings with the organization. In a survey of 141 employed workers, they found that the perceived fairness was the primary factor influencing whether employees consider a litigious response (Bies & Tyler, 1993). Lind, Greenberg, Scott, & Welchans (2000) investigated actual legal claiming behaviors and found in structured interviews with 996 fired workers that wrongful-termination claims were strongly correlated with the way workers felt they had been treated at the time of termination. Youngblood, Trevino, & Favia (1992) analyzing archival and interview data suggested that especially perceived procedural justice dominates the motivation for filing claims. Overall, under-rewarded employees engaged in legal-claiming as retaliation for perceived unfairness (Goldman, 2003; Lind et al., 2000). In the language of Adams (1965) legal-claiming can be qualified as an attempt of the under-rewarded to reduce the outcome of the other and increase at the same time own outcome.

In practice, there are abundant legal claims following inheritance disputes. Where there’s a will there’s a war titled once the Guardian. That legal-claiming constitutes an attempt to reduce injustice and therefore can be considered as injustice reduction mechanism offers an accurate explanation for the myriad of legal claims of under-rewarded descendants also in family firm succession. For instance, in the introductory example, Danny might initiate an inheritance action against his father or brother in order to receive the same number of shares of the company as Arthur. Or, Danny finds a pretext under which he can sue the company. Through legal claiming, under-rewarded descendants try to decrease the outcome of the over-rewarded and at the same

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time increase own outcome. Legal claiming is hence a means to restore justice and the following hypothesis is made:

Hypothesis 4. Descendants who feel under-rewarded in family firm succession are likely to engage in legal-claiming.

5.4.3 Injustice reduction mechanisms of the over-rewarded descendant

The paper so far addressed four behaviors of under-rewarded descendants that have a negative impact on the firm. Hereinafter, the injustice reduction mechanisms of the over-rewarded are illustrated, three of which with a possible detrimental effect on the firm and one with a possible positive impact (more work effort).

5.4.3.1 More work effort (increase own input)

As stated above, organizational justice researchers established that employees who feel unjustly treated will revert to diverse behaviors that are detrimental to the business (Colquitt et al., 2001; Cropanzano et al., 2007; Greenberg, 1987). However, perceived injustice is also able to evoke behavior that is beneficial for the company.

Organizational justice research has established that employees who consider themselves over-rewarded will increase work effort (Adams, 1965). Greenberg (1988) observed that employees who were temporarily moved to higher-status offices than their position actually warranted, increased their performance. Adams & Jacobsen (1964) gave students a proof-reading task. The students
who were made to believe that they are not experienced enough for the job and correspondingly overpaid, produced significantly better quality work than other students who thought that their experience was adequate. So, independent of whether the outcomes of employees were of economic or non-economic value, in the event they felt over-rewarded the employees increased performance. In terms of Adams (1965), over-rewarded employees will increase their input following perceived injustice. Increased work effort helps over-rewarded employees to restore a just proportion between the outcome gained in the exchange with the employer and the input invested in such exchange. Same will apply in family firm succession.

Over-rewarded descendants in family firm succession believe to have received more than deserved. For instance, descendants might feel over-rewarded as they have received a bigger ownership stake in the company than they consider as fair (such as Arthur Moro in the introductory example). In such event, the over-rewarded descendant will try to make up for injustice perceived through increased work effort (Adams, 1965). Through such increased input, over-rewarded descendants restore a just relationship between input and outcome in family firm succession. Hence the following hypothesis is made:

_**Hypothesis 5. Descendants who feel over-rewarded in family firm succession and work in the family business are likely to increase work effort.**_

### 5.4.3.2 Less job satisfaction (reduce own outcome)

Job satisfaction constitutes in the work environment a non-economic _outcome_ (Greenberg, 1988b). Like salary, job satisfaction is a personal outcome of the
employee out of the employer-employee relationship (McFarlin & Sweeney, 1992). Justice was found to be a predictor for job satisfaction (Cohen-Charash & Spector, 2001; Colquitt & George, 2011). McFarlin & Sweeney (1992) showed that distributive justice was a more powerful predictor of job satisfaction than was procedural justice, whereas Masterson, Lewis, Goldman, Taylor, et al. (2000) found that procedural justice is a stronger predictor of job satisfaction than interactional justice. Overall perceived justice will positively affect job satisfaction while perceived injustice will negatively affect job satisfaction (Adams, 1963; Colquitt et al., 2001; Greenberg, 1987).

Contrary to the other hypotheses in this paper, this hypothesis does not deal with a behavioral reaction to perceived injustice but with a more attitudinal or emotional one (Cohen-Charash & Spector, 2001). Nevertheless, job satisfaction constitutes an outcome that is altered following perceived injustice (Adams, 1965).

It has been established that in family firms, conflicts within the family have an impact on job satisfaction of incumbents (Boles, 1996). Same will apply to over-rewarded descendants in the family business succession context. This means that perceived injustice in succession is a trigger for reduced job satisfaction of the over-rewarded descendant (Adams, 1965). Reduced job satisfaction will restore the just balance between input and outcome in family firm succession. Justice is hereby not restored by an action or the behavior of the over-rewarded but through the loss of satisfaction. Justice consequently works as an attractor that not only guides peoples’ behaviors but also their emotions and attitudes (Adams, 1965). Hence, the following hypothesis is made:
Hypothesis 6. Descendants who feel over-rewarded in family firm succession and work in the family business are likely to have less job satisfaction.

5.4.3.3 Salary increase to under-rewarded descendant (increase outcome of other)

A possible injustice reduction mechanism of the over-rewarded is to increase the outcome of the under-rewarded (Adams, 1965). This injustice reduction mechanism has not been discussed to a great extent in organizational justice literature as detrimental injustice reduction mechanisms of the under-rewarded – and not the over-rewarded – have been more in the center of attention (Cropanzano et al., 2007; Greenberg, 1990a). It has been suggested that over-rewarded peoples’ threshold to react to perceived injustice is higher than the one of under-rewarded people (Adams, 1963).

However, injustice reduction mechanisms undertaken by the over-rewarded may as well be detrimental for the firm. In family firms, over-rewarded descendants regularly have key positions in the firm. One possible injustice reduction mechanism of the over-rewarded successor is to raise the salary of the under-rewarded family member employed in the firm. With such salary increase, the over-rewarded is able to increase the outcome of the under-rewarded and to recompense the under-rewarded for injustice experienced in succession. Family business research has so far explained undeserved financial rewards to family members by altruism (Karra et al., 2006; Lubatkin et al., 2007; Schulze et al., 2002, 2001). However, the deeper reason for such
allegedly altruistic behavior of family members is often perceived injustice. To financially compensate under-rewarded descendants is a means for over-rewarded descendants to reestablish justice. Over-rewarded descendants are hence likely to induce salary increases even though they themselves did not cause discrimination (Ekeh, 1974; Wade-Benzoni, 2002). Therefore, the following hypothesis is made:

**Hypothesis 7. Descendants who feel over-rewarded in family firm succession and work in the family business are likely to give salary increases to under-rewarded descendants.**

### 5.4.3.4 Toleration of less work effort (reduce input of other)

As mentioned before, job performance constitutes an input of the employee. Perceived injustice will reduce job performance of the employee (Dittrich & Carrell, 1979; Janssen, 2001; Masterson et al., 2000; Zhang et al., 2014). Hypothesis 1 explains that this applies also to the family firm succession context and shows how shirking of under-rewarded descendants is a consequence of perceived injustice. In general, such behavior would provoke counter-measures of the employer. However, in the event such employer is a family member who feels over-rewarded he or she is tempted to tolerate the change in the work attitude of the under-rewarded descendant. Such toleration constitutes an approval of the input reduction of the under-rewarded person in terms of Adams' equation (1965). Again, so far altruism has been considered as main reason that common work standards are not applied to family members (Lubatkin et al., 2005). However, often the deeper reason for tolerating low
performance of family members, is perceived injustice. Hence the following hypothesis is made:

Hypothesis 8. Descendants who feel over-rewarded in family firm succession and work in the family business are likely to tolerate less work effort of the under-rewarded.

A couple of months have passed. The relationship between Arthur and Danny has cooled. Besides work they do not spend much time together and do not talk about the family business. Danny is currently not very motivated. So far, he has been very enthusiastic about developing new packaging ideas to ensure freshness of their food products, but now... Arthur wants to give Danny some time to cope with the decision of their father. He works hard to keep the company on track. At the end of the year, Arthur learned that Danny increasingly uses his business credit card for private purposes. Arthur does not know what to do. Until now, working together with his brother was fun – but this situation is no longer tolerable...

5.4.4 Moderating effects of family cohesion

Family cohesion is a construct that reflects the quality of the relationship between the family members (Dyer & Handler, 1994; Fondacaro et al., 2002; Wennberg, Wiklund, Nordqvist, Hellerstedt, & Nordqvist, 2011; Wiklund et al., 2013). Good family relationships have a positive effect on the intra-familial succession process. Lansberg & Astrachan (1994) found that the relationship quality between incumbent and descendant is positively associated with the
extent of successor training. Sharma et al. (2001b) argued that there is a positive relationship between family harmony and the agreement among family members to continue the business. Friedman (1991) explained how especially sibling relationships are key for family firm succession. De Massis et al. (2008) describe how relational factors and conflicts among family members prevent intra-family succession. Overall, family cohesion has been found to substantially smooth intra-family successions.

Further, it has been established, that there is a relation between justice and family cohesion. For instance, Fondacaro, Dunkle, & Pathak (1998) examined family disputes of 240 study participants and found that procedural justice was positively associated with family cohesion. Later, Fondacaro et al. (2002) showed that procedural factors overshadow distributive justice in predicting family cohesion. It has to be pointed out that Fondacaro et al. (2002) did not differentiate between procedural and interactional justice and counted the elements of personal respect and trust among procedural justice elements. This research shows that justice perceptions of family members influence family cohesion.

I suggest that family cohesion acts as moderator in the relationship between injustice perceived by descendants in succession and the injustice reduction mechanisms undertaken by them.

High family cohesion will weaken the relationship between perceived injustice and injustice reduction mechanisms undertaken by the under-rewarded. Strong family relations lead to a higher level of empathy and inhibit descendants from assuming bad intent and parental favoritism (Friedman, 1991; Lansberg &
Under-rewarded descendants therefore will try to understand the reasoning of incumbents. Moreover, if family cohesion is high, family members have a high concern for other and protect each other from harm (Sorenson, 1999). Good relationships to other family members will correspondingly keep the under-rewarded from engaging in injustice reduction mechanisms directed against the company or other family members. When family bonds and cohesion are strong, family members are less likely to become “Fredos”, i.e. impediments, for the family firm (Kidwell et al., 2012). Hence, the following hypothesis is made:

Hypothesis 9a. High family cohesion will reduce the positive relationship between perceived injustice and injustice reduction mechanisms undertaken by the under-rewarded.

Contrary, high family cohesion will increase the positive relationship between perceived injustice and injustice reduction mechanisms on side of the over-rewarded. In families with high cohesion family members care for each other and act loyal towards each other (Lansberg & Astrachan, 1994). Family members of families with high cohesion link their own welfare to the welfare of other family members (Eddleston & Kellermanns, 2007). High family cohesion induces therefore altruistic behavior of family members (Lubatkin et al., 2005). Family members of families with high cohesion interact regularly (Olson, 1986, 1991) and share joys and burdens. They will know each other’s frame of mind. Thus, over-rewarded family members of families with high cohesion know about the pain of under-rewarded descendants and suffer with them. Because of this closeness, over-rewarded descendants of families with high family cohesion are motivated to a higher degree than over-rewarded
descendants of families with low family cohesion to reduce injustice.

Correspondingly:

_Hypothesis 9b. High family cohesion will increase the positive relationship between perceived injustice and injustice reduction mechanisms undertaken by the over-rewarded._

In sum, high family cohesion will have the _opposite effect_ on the over- and the under-rewarded person. Under-rewarded descendants from families with high cohesion are expected to engage in injustice reduction mechanisms to a lesser extent. Contrary, over-rewarded descendants from families with high cohesion are expected to increase injustice reduction mechanisms.

### 5.4.5 Mediating effects of emotions

Organizational justice research has established that besides behavioral consequences, perceived injustice has an impact on the feelings of the people.

#### 5.4.5.1 Emotions of the under-rewarded descendant

On the one hand, the under-rewarded person is said to _feel angry_ (Adams, 1965; Barclay et al., 2005; Kidwell et al., 2012; Mikula, 1993; Taylor & Norris, 2000). Anger results from perceived injustice and will result in retaliation behavior (Barclay et al., 2005; Mikula et al., 1998; Weiss et al., 1999). Anger is an out-ward focused emotion and signifies that the angry person blames another to be responsible for the outcome (Barclay et al., 2005). Correspondingly, retaliation behavior resulting from outward-focused
emotions is supposed to be directed against the perpetrator (Barclay et al., 2005).

On the other hand, perceived injustice provokes a feeling in under-rewarded people that is not directed against the perpetrator but against the one who is considered to be favored. This is the feeling of envy. As people evaluate their situation in comparison with others (Festinger, 1954), envy typically occurs if a person lacks another’s possession and desires it (Parrot & Smith, 1993). Sibling relationships are generally prone to provoke envy (Yoshimura, 2010), as siblings are each other’s reference group with regard to parental allocations (Festinger, 1954). So, in the context of family firm succession the under-rewarded descendant will feel anger and envy and these feelings will mediate the relationship between perceived injustice and injustice reduction mechanisms undertaken by the under-rewarded. Hence:

*Hypothesis 10a. The relationship between perceived injustice and injustice reduction mechanisms is mediated by the feeling of anger on side of the under-rewarded descendant.*

*Hypothesis 10b. The relationship between perceived injustice and injustice reduction mechanisms is mediated by the feeling of envy on side of the under-rewarded descendant.*

5.4.5.2 Emotions of the over-rewarded descendant

The over-rewarded person is expected to feel guilty (Adams, 1965; Barclay et al., 2005). Generally, guilt involves that the person feels responsible for the
outcome (Smith, Haynes, Lazarus, & Pope, 1993; Weiss et al., 1999). However, it has been advanced that guilt can also be generated in the absence of any own wrong-doing (Baumeister, Stillwell, & Heatherton, 1994). For instance, drawing from the known phenomena of survivor guilt (Lifton, 1967), justice researchers have established that in connection with perceived injustice people can feel guilty because of the mere perception that their rewards are larger than the rewards of someone else (Baumeister et al., 1994). Guilt however requires that the over-rewarded feels connected to the under-rewarded to some extent, as such guilt is said to have an interpersonal origin (Baumeister et al., 1994). Baumeister et al. (1994) make the example that receiving extra change from a pay telephone is unlikely to result in guilt, so the over-rewarded will only feel guilty if there is a salient other person that is under-rewarded. Guilt is associated with prosocial effects, such as altruistic behavior, reparation payments, confessions or apologies (Baumeister et al., 1994) as well as with antisocial effects, such as avoidance and withdrawal (Barclay et al., 2005; Baumeister et al., 1994).

In the succession context, descendants who consider themselves over-rewarded will feel guilty towards their siblings. They feel guilty even though they did not themselves generate the unjust succession (but the incumbent). In sum, guilt will mediate the relationship between perceived injustice and injustice reduction mechanisms undertaken by the over-rewarded. Correspondingly:
Hypothesis 10c. The relationship between perceived injustice and injustice reduction mechanisms is mediated by the feeling of guilt on side of the over-rewarded descendant.

Figure 10: Proposed model

5.5 Methodology

5.5.1 Sample and data collection

To empirically test whether people engage in injustice reduction mechanisms following perceived injustice in family firm succession, I included corresponding scenarios in a survey about succession that was sent out to managers of 38,049 small- and medium-sized enterprises (SMEs). SMEs are firms with less than 250 employees (additionally, a corresponding if-condition was included in the in Stata commands).
There were two versions of the survey, one version contained the over-rewarded scenario and the other version contained the under-rewarded scenario (see chapter 5.5.2.1). The two versions were randomly sent out to the respondent SMEs, so that one half of the addressees received the under-rewarded scenario and the other half the over-rewarded scenario. The goal thereby was to expose two groups to a different scenario but that these groups are alike in all other aspects, or at least do not systematically differ (Punch & Oancea, 2014).

The distribution of the survey participants deviates somewhat from the sector and size structure of the overall Swiss SME landscape reflected in the most recent statistics on corporate structure (STATENT) of the Swiss Federal Statistical Office (SFSO) dating from 2013. Construction and industrial firms are overrepresented in the survey, while SMEs from various service sectors are underrepresented. In addition, micro firms with fewer than ten full-time equivalents (FTEs) are underrepresented in the survey compared to their actual frequency in Switzerland.\(^{12}\)

Data collection was effected in January and February 2016 and achieved a total of 1’528 survey responses. This corresponds to a response rate of 4.02\%.\(^{13}\) 645 of the respondents who received the under-rewarded scenario answered the question of whether they perceive the scenario as unfair. 628 of the respondents who received the over-rewarded scenario answered the question of whether

\(^{12}\) The following sectors were excluded from the analysis: Agriculture/forestry, energy/water supply, finance/insurance, public administration.

\(^{13}\) The low response rate is ascribed to the fact that the questionnaire was rather long.
they perceive the scenario as unfair. These answers constitute the independent variables in the data analysis (see chapter 5.5.2.1).

As dependent and independent variables stem from the same respondents and the same survey, common method variance has to be addressed. To do so, two post-hoc tests were effected: Harman’s single factor test and the marker variable test (Lindell & Whitney, 2001).

To conduct the Harman single factor test, I entered all variables of Models 3 and 6 (see Table 7 and Table 8) into an exploratory factor analysis using principal component factor analysis (Podsakoff et al., 2003). For the under-rewarded scenario (Model 3), five factors have an eigenvalue greater than one, all accounting for 61.15% of the total variance. The first factor explains only 22.12% of the total variance what indicates that no single factor accounts for the majority of the variance. Regarding the over-rewarded scenario (Model 6), four factors have an eigenvalue greater than one, all accounting for 52.84% of the total variance. The first factor explains only 18.8% of the total variance what indicates that no single factor accounts for the majority of the variance.

Further, I conducted the marker variable test (Lindell & Whitney, 2001), including all other variables, to investigate the correlation between the dependent variable (injustice reduction mechanisms of under- and over-rewarded combined) and another variable that theoretically should be uncorrelated with the dependent variables, called marker variable (Homburg et al., 2010). This variable is then used to correct the correlation matrix for common method bias. I assessed the correlation between the marker variable
“existence of governance instruments” and the injustice reduction mechanisms undertaken by the under-rewarded ($r = -0.0321$), respectively by the over-rewarded ($r = -0.0292$). This predictor has insignificant correlations with the dependent variables. Overall, the statistical significance and correlations do not change, which provides further evidence that common method bias is not present (Van Doorn & Verhoef, 2008).

5.5.2 Measures

5.5.2.1 Independent variables

The independent variable is the likelihood of perceived injustice. Perceived injustice was provoked in confronting respondents either with the under- or the over-rewarded scenario. Respondents were then asked: “How likely do you perceive this decision as unjust?” They could answer on a seven-point scale that ranged from “not likely at all” to “very likely”.

In the scenarios, the respondents were put in the position of a descendant in a family firm succession context. They were informed that their father allocated ownership of the family firm according to the equity principle to the one of the descendants who also takes over the management. Further, it was written that such allocation contradicted their sense of justice, as according to their perception a transfer in compliance with the equality principle would have been just where ownership of the business is handed over equally to all descendants. In the scenarios, descendants and incumbent have therefore divergent perceptions of justice.

The wording for the scenario of the under-rewarded was:
“Assume the following scenario: Your family has a family business. Your father is sole-owner and manager of the business. You have a twin-brother. Your twin-brother has studied business management, has work experience outside the family business and is since a couple of years in the family business. He will succeed your father in managing the family business. Yourself, you are employed in the family business as case-handler with a normal salary. You are of the opinion that the shares in the company (ownership) should be handed over equally to you and your brother. After the decease of your father you learn however that your father left all the shares in the company (100%) to your brother alone.”

The wording for the scenario of the over-rewarded was:

“Assume the following scenario: Your family has a family business. Your father is sole-owner and manager of the business. You have studied business management, have work experience outside the family business and are since a couple of years in the family business. You will succeed your father in managing the family business. You have a twin-brother. Your twin is employed in the family business as case-handler with a normal salary. You are of the opinion that the shares in the company (ownership) should be handed over equally to you and your brother. After the decease of your father you learn however that your father left all the shares in the company (100%) to you alone.”
To exclude the consideration of the justice principle of primogeniture (allocation norm that favors the first-born), I included the fact that the brothers are twins. To also exclude need considerations, I stated that the discriminated brother has a “normal salary”. Lastly, I included the condition that the descendants are of the same gender, to exclude gender discrimination.

5.5.2.2 Dependent variables

The dependent variables are the injustice reduction mechanisms. Respondents were asked the following questions and could respond to the questions on a seven-point scale that ranged from “not likely at all” to “very likely”.

To inquire whether respondents engage in injustice reduction mechanisms, they were asked in the under-rewarded scenario: “How likely do you shirk from new tasks?” to learn whether under-rewarded persons show less work effort and engage in shirking, which is equivalent to a reduction of own input in terms of Adams (1965). In order to figure out whether under-rewarded persons will free-ride which is equivalent to an increase of outcome, respondents were asked: “How likely do you use available company resources more excessively?”. To inquire about under-rewarded’s resistance to change, an attempt to increase the input of the other, respondents were asked: “Your brother wants to introduce a new product. How likely do you oppose?”. And lastly, in order to find out about the increased likelihood of legal-claiming by under-rewarded descendants in order to reduce the outcome of the other, respondents were asked: “How likely do you file a legal suit to receive the same number of shares in the company as your brother?”.
When I tested the indirect effects (moderating effect of family cohesion and mediating effects of anger and envy) I created a combined variable of all the four items asked, called $IRM = injustice\ reduction\ mechanisms\ combined$ (see Table 7). For that purpose, the sum of the items was divided by the number of items answered. Cronbach’s alpha reaches $0.7572$ and average likelihood of the injustice reduction mechanism undertaken by the under-rewarded is $3.20$.

To learn whether respondents engage in injustice reduction mechanisms, they were asked in the over-rewarded scenario: “How likely do you show more work effort now?” in order to learn whether over-rewarded descendants will show more work effort and increase own input in terms of Adams (1965). To detect whether over-rewarded descendants’ job satisfaction and therewith their own outcome decreases, they were asked: “How likely do you have less job satisfaction?”.

To see whether over-rewarded persons are tempted to increase the salary and therewith the outcome of the other, the question was: “Your brother demands a pay increase. How likely do you approve the increase?”. And lastly, to investigate whether over-rewarded descendants will tolerate less work effort of the under-rewarded and therewith reduce input of other, they were asked: “Your brother works with less work quality now. How likely do you tolerate this behavior?”.

Again, when I tested the indirect effects (moderating effect of family cohesion and mediating effects of guilt) I created a combined variable of all the four items asked, called $IRM = injustice\ reduction\ mechanisms\ combined$ (see Table 8). For that purpose, the sum of the items was divided by the number of items answered. The average likelihood of the injustice reduction mechanism undertaken by the over-rewarded is $3.65$. Cronbach’s alpha reaches $0.5267$ and therefore a factor analysis (principal component) was effected what
showed that the item “more work effort” has an eigenvalue greater than 1 and accounts for 42.46% of the variance.

5.5.2.3 Control variables

I controlled for the following variables on industry-, firm- and individual level that have been found to be important in prior studies of family business and justice research.

**Industry.** Industry may be a critical factor for the type of successor needed (Le Breton-Miller et al., 2004), and hence of the type of succession that is considered as fair. I computed a dummy variable and considered companies active in the secondary sector (manufacturing) being equal to “0”, while firms of the tertiary sector (services) were coded as “1”. There were no firms of the primary sector.

**Firm size.** In small firms a separation of ownership and management might be less feasible, hence I controlled for firm size. Size was measured in counting the number of employees. The average number of employees is 27.3.

**Firm age.** Respondents were asked in which year their company was founded and such year was deducted from 2016. The average firm age is 43.9 years (1-328 years). For firm age was controlled as respondents from very old firms might be more inclined to the justice principle of equity, as in order to survive over a longer period of time companies must deliver above-average performance.

**Performance.** Performance might influence respondents’ justice perceptions. Respondents of companies with very low performance might perceive the company as burden and the scenario intended to evoke preferential treatment might in fact was not perceived as over-rewarding. Performance was measured
by taking the average growth rate of the total operating revenues of the years 2013-2015. I deducted the revenues of 2013 and 2014 from the revenues 2014 respectively 2015 and divided the result through the revenue of 2013, respectively 2014 to compute the relative average growth rate and then added the two results and divided it by two to calculate the average growth rate. The mean average growth rate is 0.058.

**Region.** What is perceived as fair is culturally dependent (Carney, 2005; Meindl, 1989). Accordingly, other cultures will make different justice judgments. For example individualistic countries, as the United States of America, will promote the application of the equity principle (Hofstede, 1984; Meindl, 1989). Contrary, more collectivistic countries are predicted to emphasize the justice principle of equality (Hofstede, 1984; Meindl, 1989). Switzerland comprises different cultures what is reflected by the situation that there are three main languages spoken: German, French, and Italian (a small minority speaks Rhaeto-Romanic). The French and Italian speaking part of Switzerland are often subsumed under the term “Latin Switzerland”. The German speaking part is said to have a stronger emphasis on equity (Hofstede, 2016). Hence a dummy variable was coded whereas 0 represents questionnaires sent out in the German language (76.85%) and 1, questionnaires that were sent out in the French and Italian language (23.15%).

**Age of respondent.** With age, people might change their justice judgments hence respondents were asked for the year they were born and such was deducted from 2016. The average age of the respondent is 54 years.

**Gender.** Respondents were asked whether they are male or female as with regard to distributional processes men and women were found to act differently (Cohen-Charash & Spector, 2001). It was recognized that females are more than males inclined to the justice principle of equality, as their major concern
is to maintain the welfare of the group members (Ahl, 2002; Kahn et al., 1980; Leventhal & Lane, 1970). Hence, I coded a dummy variable (1 = female). 10.15% of the respondents are women.

5.5.2.4 **Moderating variable**

*Family cohesion.* Family cohesion was assessed via four items from the FACES III scale (Olson, 1986, 1991). Respondents could indicate on a seven-point scale within the range: “I strongly to I completely agree”. The construct consisted of six items: 1) “Family togetherness is very important.” 2) “Family members feel very close to each other”, 3) “When our family gets together for activities, everybody is present”, 4) “Family members ask each other for help”, and 5) “Family members consult other family members on their decisions” 6) “Family members like to spend their free time with other” (Zellweger et al., 2015). Cronbach’s alpha reaches 0.9172 and average mean cohesion is 5.278.

5.5.2.5 **Mediating variables**

*Anger.* Respondents were asked „How likely is it that this decision makes you angry?” Respondents could answer the question on a seven-point scale that ranged from “not likely at all” to “very likely”.

*Envy.* Respondents were asked „How likely is it that you envy your brother for the ownership stakes?” Respondents could answer the question on a seven-point scale that ranged from “not likely at all” to “very likely”.

*Guilt.* Respondents were asked „How likely is it that you feel guilty towards your brother?” Respondents could answer the question on a seven-point scale that ranged from “not likely at all” to “very likely”.

5.5.3 **Data analysis**

Descriptive statistics including number of observations, mean, standard deviation, and correlations for all variables used in the regression analysis can be found in Table 5 and Table 6. The tables show acceptable levels of correlation between independent and control variables being lower than 0.2 (Hair, Black, Babin, Anderson, & Tatham, 2006). The Variance Inflation Factors (VIF) values are all below the accepted threshold of 4 (Hair et al., 2006) with the highest VIF amounting to 0.9897 (under-rewarded) and 0.9838 (over-rewarded) indicating that multicollinearity is not a major concern for the study.
### Table 5: Descriptive statistics and correlations of variables in under-rewarded scenario

| Variable                              | Obs | Min | Max | Mean | Std.Dev. | VIF | 1  | 2  | 3  | 4  | 5  | 6  | 7  | 8  | 9  | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 | 18 | 19 |
|---------------------------------------|-----|-----|-----|------|---------|-----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|
| Perceived injustice                   | 602 | 1   | 7   | 5.628| 1.763   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Shirking                              | 600 | 1   | 7   | 3.380| 1.941   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Free-riding                           | 594 | 1   | 7   | 3.816| 1.814   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Resistance to change                  | 601 | 1   | 7   | 2.612| 1.619   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Legal claiming                        | 898 | 1   | 7   | 3.018| 2.075   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Injustice Reduction Mechanisms (IRM) combined | 586 | 1   | 7   | 3.200| 1.413   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Compensation father                   | 274 | 0   | 100 | 59.964| 37.314  |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Compensation brother                  | 274 | 0   | 100 | 40.037| 37.314  |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| No compensation                       | 503 | 0   | 100 | 0.453| 0.498   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Family cohesion                       | 1341| 1   | 7   | 5.278| 1.343   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Anger                                 | 603 | 1   | 7   | 5.144| 1.834   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Industry                              | 1381| 0   | 1   | 0.550| 0.498   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Firm size                             | 1244| 0   | 250 | 27.289| 35.834  |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Firm age                              | 1365| 1   | 328 | 43.908| 36.022  |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Performance                           | 1274| 90  | 1023| 53.652| 10.253  |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Age respondent                        | 1417| 0   | 1   | 0.231| 0.422   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Gender                                | 1281| 0   | 1   | 0.101| 0.302   |     | 1  |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |

*p<0.05*
### Table 6: Descriptive statistics and correlations of variables in over-rewarded scenario

| Variable                                      | Obs. | Mean  | Std.Dev. | Min   | Max   | VIF  | 1   | 2   | 3   | 4   | 5   | 6   | 7   | 8   | 9   | 10  | 11  | 12  | 13  | 14  | 15  |
|-----------------------------------------------|------|-------|----------|-------|-------|------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| Perceived injustice                          | 589  | 5.171 | 1.969    | 1     | 7     | n.a. | 0.044| 1   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| More work effort                             | 586  | 4.329 | 1.951    | 1     | 7     | n.a. | 0.071| 1   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Less job satisfaction                        | 584  | 2.771 | 1.808    | 1     | 7     | n.a. | 0.141*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |
| Salary increase to under-rewarded            | 587  | 3.049 | 1.638    | 1     | 7     | n.a. | 0.049*| 0.166*| 0.103*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Tolerance of less work effort                | 585  | 2.478 | 1.599    | 1     | 7     | n.a. | 0.184*| 0.163*| 0.284*| 0.292*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Injustice Reduction Mechanisms (IRM) combined | 580  | 3.649 | 1.122    | 1     | 7     | n.a. | 0.388*| 0.608*| 0.676*| 0.646*| 0.638*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Family Cohesion                              | 1341 | 3.278 | 1.343    | 7     | n.a. | 0.133*| 0.018| -0.010| 0.167*| 0.051| 0.077| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Guilt                                        | 589  | 0.891 | 2.040    | 1     | 7     | n.a. | 0.166*| 0.148*| 0.332*| 0.362*| 0.226*| -0.421*| 0.164*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Industry                                     | 1381 | 0.550 | 0.498    | 0     | 1     | 0.908| 0.022| 0.051| 0.009| 0.041| 0.025| 0.044| -0.006| 0.043| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Firm size                                    | 1417 | 27.289| 35.834   | 0     | 250   | 0.905| 0.016| -0.010| -0.010| -0.019| -0.053| -0.025| 0.033| -0.136*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Firm age                                     | 1365 | 43.908| 36.022   | 1     | 328   | 0.872| -0.014*| 0.005| -0.027| -0.129*| -0.006| -0.055| 0.009| -0.179*| 0.248*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Performance                                  | 1244 | 0.058 | 0.377    | -0.65 | 7     | 0.971| 0.019| -0.073| 0.017| -0.034| -0.043| -0.053| 0.005| -0.059| 0.053| -0.025| -0.115*| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Age respondent                               | 1274 | 53.652| 10.251   | 24    | 90    | 0.983| -0.027| 0.032| 0.010| 0.034| -0.043| 0.006| -0.022| -0.086| 0.046| -0.058*| 0.050| -0.050| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Region                                       | 1417 | 0.231 | 0.422    | 0     | 1     | 0.982| -0.021| 0.103*| -0.123*| -0.021| 0.120*| 0.066| -0.002| 0.017| -0.062*| -0.030| -0.050| 0.050| 1   |    |    |    |    |    |    |    |    |    |    |    |    |
| Gender                                       | 1281 | 0.101 | 0.302    | 0     | 1     | 0.946| 0.053| 0.023| 0.086*| 0.007*| 0.032| 0.087*| 0.064*| 0.107*| 0.146*| -0.090*| -0.052| -0.011| -0.138*| 0.020| 1   |    |    |    |    |    |    |    |    |    |    |    |    |

*p<0.05*
5.5.4 Analytical procedures and results

To test the hypotheses, I employed simple regressions. Table 7 (Models 1-3) displays the models for the under-rewarded scenario and Table 8 (Models 4-6) for the over-rewarded scenario.

For the under-rewarded scenario: Model 1 contains the regressions from the independent variable together with the control variables on the injustice reduction mechanisms individually. Model 2 contains the regressions on the mean of the combined injustice reduction mechanisms (IRM) undertaken by the under-rewarded, testing the moderating effect of family cohesion. Model 3 tests mediation effects of anger and envy in establishing the four conditions required by Baron & Kenny (1986).

For the over-rewarded scenario: Model 4 contains the regressions from the independent variable together with the control variables on the injustice reduction mechanisms individually. Model 5 contains the regressions on the mean of the combined injustice reduction mechanisms (IRM) undertaken by the over-rewarded, testing the moderating effect of family cohesion. Model 6 tests the mediating effect of guilt (Baron & Kenny, 1986).
Table 7: Models of under-rewarded scenario

**IRM = Injustice Reduction Mechanisms combined (shirking, free-riding, resistance to change, legal claiming)**

<table>
<thead>
<tr>
<th>VARIABLES</th>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>H1_H2</td>
<td>H3_H4</td>
<td>IRM</td>
</tr>
<tr>
<td>Control variables</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry</td>
<td>0.007</td>
<td>-0.002</td>
<td>0.064</td>
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<tr>
<td>Firm size</td>
<td>0.009</td>
<td>0.044</td>
<td>-0.001</td>
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<td>Firm age</td>
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<td>-0.003</td>
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<td>-0.042</td>
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<tr>
<td>Region</td>
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<td>0.366*</td>
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<tr>
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<td>-0.312</td>
<td>0.029</td>
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<tr>
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<td></td>
</tr>
<tr>
<td>Perceived injustice</td>
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<td>0.344***</td>
<td>0.133**</td>
</tr>
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<td>Moderator variable</td>
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<tr>
<td>Family cohesion</td>
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</tr>
<tr>
<td>-family/organisational injustice</td>
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<tr>
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</tr>
<tr>
<td>Anger</td>
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<td>0.412***</td>
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</tr>
<tr>
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<td>1.052*</td>
<td>2.690***</td>
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<td>487</td>
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<tr>
<td>R-squared</td>
<td>0.134</td>
<td>0.138</td>
<td>0.058</td>
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</table>

Standard errors in parentheses

*** p < 0.001, ** p < 0.01, * p < 0.05, + p < 0.1
**Table 8: Models of over-rewarded scenario**

**IRM = Injustice Reduction Mechanisms combined (more work effort, less job satisfaction, salary increase, toleration of less work effort)**

<table>
<thead>
<tr>
<th>VARIABLES</th>
<th>Model 4</th>
<th>Model 5</th>
<th>Model 6</th>
</tr>
</thead>
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<td></td>
<td>More work effort</td>
<td>Less job satisfaction</td>
<td>Salary increase</td>
</tr>
<tr>
<td></td>
<td>H5</td>
<td>H6</td>
<td>H7</td>
</tr>
<tr>
<td>Control variables</td>
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</tr>
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<td>-0.031</td>
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<td>0.330***</td>
</tr>
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<td>Family cohesion</td>
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</tr>
<tr>
<td>Mediator variable</td>
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</tr>
<tr>
<td>Guilt</td>
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</tr>
<tr>
<td>R-squared</td>
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<td>0.12</td>
<td>0.181</td>
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</table>

Standard errors in parentheses

*** p<0.001, ** p<0.01, * p<0.05, + p<0.1
5.5.4.1 Under-rewarded

Table 7 shows that perceived injustice significantly increases the likelihood of all injustice reduction mechanisms predicted to be undertaken by the under-rewarded. Perceived injustice will lead to shirking and free-riding, correspondingly hypothesis 1 (Model 1: $\beta = 0.352$, $p < 0.001$) and hypothesis 2 (Model 1: $\beta = 0.344$, $p < 0.001$) are supported. Moreover, also hypothesis 3 (Model 1: $\beta = 0.133$, $p < 0.01$), and hypothesis 4 (Model 1: $\beta = 0.494$, $p < 0.001$) are supported as perceived injustice leads to resistance to change as well as legal claiming.

5.5.4.2 Over-rewarded

Table 8 shows that perceived injustice is not significantly correlated to more work effort, so hypothesis 5 (Model 4: $\beta = 0.062$, $p > 0.1$) is rejected. Contrary, perceived injustice will significantly increase the likelihood of less job satisfaction (Model 4: $\beta = 0.288$, $p < 0.001$), salary increases towards the under-rewarded sibling (Model 4: $\beta = 0.330$, $p < 0.001$), and toleration of less work effort (Model 4: $\beta = 0.141$, $p < 0.001$). Therewith hypotheses 6, 7, and 8 are supported.

5.5.4.3 Moderating effects of family cohesion

Model 2 in Table 7 tests the moderating effect of family cohesion in the relationship between perceived injustice of the under-rewarded and injustice reduction mechanisms (IRM) undertaken. As mentioned above, the IRM variable constitutes the mean of the behaviors of the under-rewarded resulting
from perceived injustice (shirking, free-riding, resistance to change, legal claiming). The first row of Model 2 only contains the control variables. The second row of Model 2 shows that perceived injustice significantly correlates to the combined injustice reduction mechanisms (IRM) undertaken by the under-rewarded ($\beta = 0.325$, $p < 0.001$). Unfortunately, family cohesion is not able to moderate the effect of perceived injustice on the injustice reduction mechanisms undertaken by the under-rewarded (Models 2: $\beta = 0.027$, $p > 0.1$), and hypothesis 9a is rejected.

Model 5 in Table 8 deals with the moderating effect of family cohesion between perceived injustice and the injustice reduction mechanisms (IRM) undertaken by the over-rewarded. Here the variable IRM combines the four behaviors of the over-rewarded (more work effort, less job satisfaction, salary increase, toleration of less work effort). The first row of Model 5 contains only the control variables, the second row shows that perceived injustice of the over-rewarded is significantly related to the combined injustice reduction mechanisms (IRM) (Model 5: $\beta = 0.215$, $p < 0.001$). Also in this relation, family cohesion has no moderating effect (Model 5: $\beta = -0.022$, $p > 0.1$) and hypothesis 9b is rejected.

5.5.4.4 Mediating effects of anger, envy, and guilt

According to Baron & Kenny (1986) the following four regressions have to be effected to establish mediation between three variables (independent – mediator – dependent variable): The mediation effect is proved and the mediator variable completely mediates the relationship between independent and dependent variable if in these four regressions the following conditions are
met: *First*, it is required that the independent variable significantly correlates with the dependent variable. *Second*, the independent variable has to significantly correlate with the mediator variable. *Third*, the mediator variable shows a significant effect on the dependent variable and *lastly*, the mediator variable needs to prove a significant effect on the dependent variable while controlling for the independent variable. To indicate complete mediation, the effect of the independent variable has to become zero in the last regression. Otherwise, partial mediation is indicated.

Model 3 in Table 7 deals with the mediating effects of the feelings of anger and envy in the relation between perceived injustice and injustice reduction mechanisms (IRM) of the *under-rewarded*. The first half of Model 3 deals with anger, while the second half of Model 3 with envy.

Testing the mediating effects of *anger* (Baron & Kenny, 1986), the first row of Model 3 indicates a significant correlation between perceived injustice and the IRM of the under-rewarded (Model 3: $\beta = 0.325$, $p < 0.001$). Further it indicates a significant correlation between perceived injustice and anger (Model 3: $\beta = 0.810$, $p < 0.001$), and between anger and IRM ($\beta = 0.405$, $p < 0.001$). The relation between anger and IRM remains significant in the fourth regression of Model 3 ($\beta = 0.412$, $p < 0.001$), while the effect between perceived injustice and IRM becomes insignificant (Model 3 $\beta = -0.008$, $p > 0.1$). Correspondingly the feeling of anger fully mediates the relation between perceived injustice and IRM undertaken by the under-rewarded. Hypothesis 10a is therewith supported.
With regard to the mediating effect of envy, Model 3 shows a significant correlation between perceived injustice and the IRM of the under-rewarded (Model 3: $\beta = 0.325$, $p < 0.001$). Also, it indicates a significant correlation between perceived injustice and envy (Model 3: $\beta = 0.489$, $p < 0.001$). Envy moreover passes the third step of the mediation test as it significantly effects IRM undertaken by the under-rewarded (Model 3: $\beta = 0.379$, $p < 0.001$). However, the last row of Model 3 shows that even though envy maintains its significant effect on IRM (Model 3: $\beta = 0.311$, $p < 0.001$), it cannot mediate the effect between perceived injustice and IRM, as such relationship remains significant (Model 3: $\beta = 0.174$, $p < 0.001$). Hence hypothesis 10b is not supported.

Model 6 in Table 8 shows the four-step mediation test (Baron & Kenny, 1986) of the feeling of guilt on the relationship between perceived injustice and the combined injustice reduction mechanisms (IRM) of the over-rewarded. It shows a significant effect between perceived injustice and IRM undertaken by the over-rewarded (Model 6: $\beta = 0.215$, $p < 0.001$) as well as a significant effect between perceived injustice and guilt (Model 5: $\beta = 0.655$, $p < 0.001$). Further it establishes a significant relation between guilt and IRM (Model 6: $\beta = 0.219$, $p < 0.001$). This relation is significant (Model 6: $\beta = 0.153$, $p < 0.001$) also in the event that the perceived injustice variable is added. However, as the latter remains to have a significant effect on IRM (Model 6: $\beta = 0.115$, $p < 0.001$), guilt is not able to mediate the relationship between perceived injustice and IRM undertaken by the over-rewarded. Hence, hypothesis 10c is not supported.

Table 9 shows an overview of the hypotheses and the corresponding results.
### Table 9: Overview of hypotheses and results

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Injustice reduction mechanisms of under-rewarded descendant</strong></td>
<td></td>
</tr>
<tr>
<td>1. Shirking</td>
<td>✔</td>
</tr>
<tr>
<td>2. Free-riding</td>
<td>✔</td>
</tr>
<tr>
<td>3. Resistance to change</td>
<td>✔</td>
</tr>
<tr>
<td>4. Legal claiming</td>
<td>✔</td>
</tr>
<tr>
<td><strong>Injustice reduction mechanisms of over-rewarded descendant</strong></td>
<td></td>
</tr>
<tr>
<td>5. More work effort</td>
<td>✗</td>
</tr>
<tr>
<td>6. Less job satisfaction</td>
<td>✔</td>
</tr>
<tr>
<td>7. Salary increase to under-rewarded descendant</td>
<td>✔</td>
</tr>
<tr>
<td>8. Tolerance of less work effort</td>
<td>✔</td>
</tr>
<tr>
<td><strong>Moderating effects of family cohesion</strong></td>
<td></td>
</tr>
<tr>
<td>9a. High family cohesion will reduce injustice reduction mechanisms of under-rewarded descendant</td>
<td>✗</td>
</tr>
<tr>
<td>9b. High family cohesion will increase injustice reduction mechanisms of over-rewarded descendant</td>
<td>✗</td>
</tr>
<tr>
<td><strong>Mediating effects of anger, envy and guilt</strong></td>
<td></td>
</tr>
<tr>
<td>10a. Anger will mediate the relationship between injustice perceived and injustice reduction mechanisms undertaken by under-rewarded descendant</td>
<td>✔</td>
</tr>
<tr>
<td>10b. Envy will mediate the relationship between injustice perceived and injustice reduction mechanisms undertaken by under-rewarded descendant</td>
<td>✗</td>
</tr>
<tr>
<td>10c. Guilt will mediate the relationship between injustice perceived and injustice reduction mechanisms undertaken by over-rewarded descendant</td>
<td>✗</td>
</tr>
</tbody>
</table>
In a post hoc analysis it was found that family cohesion has a moderating effect on the relationship between guilt and IRM undertaken by the over-rewarded descendant ($\beta = -0.0392, p < 0.05$). Contrary to the argumentation with regard to perceived injustice, high family cohesion combined with guilt will hence result in decreasing injustice reduction mechanisms on side of the over-rewarded.

Additionally, under-rewarded respondents were asked whether they required a compensation for experienced injustice and if yes, who should compensate them, father or brother. 45.33% of the respondents answered that they require no compensation. Of the other 54.67%, 36.13% wish to receive 100% of the compensation from the father, 20.07% wish to receive 100% of the compensation from the brother and 28.83% wish to split the compensation between father and brother 50:50. One can draw from these findings that under-rewarded descendants will exhibit injustice reduction mechanisms vis-à-vis all parties involved in the allocation, the father – which seems obvious as he caused injustice – the brother and the family firm, which is less evident as these parties are not responsible for the injustice experienced by under-rewarded descendants.

5.6 Discussion

The paper aims to provide a conceptual and empirical basis for behaviors of descendants that result from perceived injustice in family firm succession and that affect the family business. The findings indicate that perceived injustice leads to injustice reduction mechanisms undertaken by the under-rewarded descendant that have alarming negative effects on the family business (shirking, free-riding, resistance to change, legal claiming). But not only the
under-rewarded is motivated to restore justice and thereby acts against the interests of the family firm, also the over-rewarded descendant proved to engage in behaviors that are detrimental to the firm. Worth particular mention, as it has a direct financial impact on the firm, is that the over-rewarded descendant will increase the salary of the under-rewarded family member working in the firm. This study proves that perceived injustice will not only result in negative feelings of the family members involved and harm family relationships but are very dangerous for the family firm, a consequence that has not received enough attention so far.

Further, the findings show that family cohesion cannot mitigate the effect between perceived injustice and injustice reduction mechanisms, neither of the under- nor of the over-rewarded. Family cohesion is therefore not able to mitigate damaging behaviors of the under-rewarded. Even though other studies have argued that good family relationships encourage family members to act as stewards for the family firm and enhance firm performance (Eddleston & Kellermanns, 2007; Kidwell et al., 2012). This proved not to apply to under-rewarded descendants in family firm succession. However, family cohesion will, against expectations, also not increase firm-damaging injustice reduction mechanisms of the over-rewarded. Overall, these findings suggest that although family members feel very close and consider family ties as important (Olson, 1986, 1991), they revert to injustice reduction mechanisms. Different conclusions can be drawn: One could conclude that injustice reduction mechanisms are somewhat independent of the quality of family ties. Correspondingly under- and over-rewarded descendants engage in injustice reduction mechanisms even though they have, and continue to have, good family relations. Also, injustice reduction mechanisms might even be
undertaken unconsciously by descendants without having a clear and conscious impact on family ties. Furthermore, especially from the under-rewarded’s perspective, injustice perceived in succession might be a disruptive experience that destroys formerly good family ties at once (Eddleston & Kellermanns, 2007). Lastly, it may be that rather than family cohesion, we need to consider the individual relationships between family members, i.e. the relationship between incumbent and descendant or the sibling relationship (Friedman, 1991) to understand how the quality of family bonds impacts perceived injustice and injustice reduction mechanisms.

5.6.1 Contributions to theory

The paper contributes to three research streams.

5.6.1.1 Contribution to family business succession

First, the paper adds to family business succession research in empirically proving that injustice perceived in succession is likely to have negative consequences for the business post succession as descendants engage in injustice reduction mechanisms addressed at the firm. I want to stress that perceived injustice therewith endurably affects the company and might influence the behavior of family members over generations (Wade-Benzoni, 2002). The study further showed no moderating effect of family cohesion in the relation between injustice perceived in succession and injustice reduction mechanisms. This finding indicates that some negative behaviors of family members happen independent of good family relations. We need to reconsider and differentiate in what constellations family cohesion positively influences family members’ behavior towards the firm and in what situations family
cohesion is no remedy. Further, the study provides an indication that family cohesion is in some situation a too comprehensive construct to understand individual family member’s behavior, and that we need to focus on individual family members’ relationship instead.

5.6.1.2 Contribution to family business governance

Second, the paper adds to family business governance research in offering another source or motive for moral hazard (shirking and free-riding) and adverse selection, two behaviors that, in family firm research, have so far nearly exclusively been discussed in connection with altruism (Lubatkin et al., 2005; Schulze et al., 2002, 2003a). Perceived injustice more often motivates family members’ behavior in family firms than it has been considered so far.

Perceived injustice explains moreover other behaviors of descendants that are detrimental to the firm, such as under-rewarded’s resistance to change or over-rewarded’s overcompensation of the under-rewarded. Family firms need to establish governance structures and instruments that address these risks of injustice perceived by descendants. The paper further raises awareness that not only under- but also over-rewarded descendants are likely to harm the firm following perceived injustice. As over-rewarded descendants generally become the decision-makers in the family firm, injustice perceived by over-rewarded descendants presents a major threat to the firm. The concept of the over-rewarded deserves correspondingly more attention in future research.
5.6.1.3 Contribution to organizational justice research

Third, the paper contributes to organizational justice research in showing how in family firms, issues that not directly happen in the firm, will nevertheless influence the work environment. In view of the myriad of family firms (La Porta et al., 1999; Sharma et al., 2001; Zellweger, 2017), and especially the multitude of sibling partnerships in family firms – in which relationship perceived injustice is highly likely (Ward, 1997) – organizational justice researchers have to deal with injustice perceived by descendants that affects the family business organization. Family members’ behavior will additionally have an influence on non-family employees. For instance, salary increases to under-rewarded descendants but not to non-family members are likely to reduce organizational justice climate in general and organizational citizenship behavior of non-family employees (Lee & Allen, 2002). Also, the paper demonstrates that behaviors resulting from perceived injustice will not rest in the dyad relationship between the parties to the exchange, i.e. the incumbent and the descendants, but will affect other parties to the exchange (Bosse, Phillips, & Harrison, 2009; Ekeh 1974; Wade-Benzoni, 2002). The study showed that both, the under- and the over-rewarded, will engage in such a generalized or indirect form of exchange (Blau, 2009; Ekeh, 1974; Emerson, 1976) and direct injustice reduction mechanisms against the family firm. This finding finds additional support by the fact that the study revealed that in the event that the under-rewarded respondents required a compensation, such compensation was requested not only from the father (59.96%), but also from the brother (40.04%). This is a clear proof that perceived injustice will prompt destructive and indirect forms of social exchange.
5.6.2 Future research

Future research might be able to identify other consequences that injustice perceived by descendants or other family members in succession has on the family firm. Especially, future research could focus on over-rewarded descendants as they are very influential and powerful family members and their actions have a significant impact on the firm. In this regard, future research will gain additional insight in examining the relation between injustice reduction mechanisms undertaken by the over-rewarded and the feeling of guilt.

Moreover, future research could focus on factors that mitigate the relation between perceived injustice and injustice reduction mechanisms. As mentioned, individual relationships between family members might be more suitable than family cohesion to explain the relation between perceived injustice and the behavior of descendants.

Furthermore, future research could investigate whether the violation of other types of justice, i.e. procedural or interactional injustice, leads to the same injustice reduction mechanisms in family firm succession as the violation of distributional injustice. Future research could analyze the interplay between the different types of justice in family firm succession. Organizational justice research found that depending on the context, certain types of justice have a greater influence on employees’ justice perceptions than others (Ambrose et al., 2002; Colquitt et al., 2001; Goldman, 2003; Leventhal, 1980; Walker et al., 1979). For instance, it was established that distributive justice is more decisive when people evaluate specific, person-referenced outcomes (such as salary),
whereas procedural justice is more important in the general evaluation of systems and authorities (Colquitt et al., 2001; Greenberg, 1990a; McFarlin & Sweeney, 1992). Masterson, Lewis, Goldman, Taylor, et al. (2000) differentiated between the parties of the distribution and found that interactional justice perceptions affect supervisor-related outcomes and procedural justice perceptions affect organization-related outcomes. So, the three different types of injustice might have other consequences also in family firm succession. For instance, future research might show that interactional justice affects the relationship between incumbent and descendants while distributional injustice has a greater impact on the company. Moreover, it would be interesting to learn, how procedural justice elements, such as having a say in the succession process or a planned versus an unplanned succession process (e.g., upon a sudden death of family firm incumbents), moderates the relationship between perceived distributional injustice and injustice reduction mechanisms undertaken by descendants.

As justice is a relative concept (Deutsch, 1975), perceived injustice partly depends on the cultural background of the allocation. Researchers could therefore test, how family firms from other cultural backgrounds deal with perceived injustice in succession.

Lastly, it would be very interesting to develop longitudinal data to learn whether perceived injustice is passed on to the next generation and what impact that has on the family business (Wade-Benzoni, 2002).
5.6.3 Limitations

These suggestions at the same time reveal the limitations of the present study. This study is limited to distributional justice and does not integrate elements of procedural or interactional justice. It hence provides no insight in the interplay between the three different types of justice. There are emotional, cognitive and other behavioral consequences of perceived injustice (Adams, 1965) that were not considered in this paper. The study further works with hypothetical scenarios and case vignettes and is therefore not able to provide for information on the actual behaviors of descendants following perceived injustice. This methodology was chosen to reduce complexity in family firm succession. It enables to create comparability between the cases but the hypotheses therewith lack verification in practice.

5.6.4 Conclusion

The paper has tried to connect family business and organizational behavior research in showing that the injustice reduction mechanisms found in organizational justice research are also applied by descendants who perceive injustice in family firm succession. The combination of these two research streams provides for fertile ground to better understand the influence of the family in the family firm and hopefully is used more frequently in future.
6 Concluding chapter

6.1 Revisiting the key findings of the three papers

This dissertation started with the question of why some families go through evolutionary transitions, while others through devolutionary or recycles. Evolutionary is a transition when a family firm moves from a controlling owner to a sibling partnership stage, or from a sibling partnership to a cousin consortium stage (Gersick et al., 1999). Through evolutionary transitions the family firm takes on a more complex structure, as multiple family members enter the family firm. Whereas in recycles (controlling owner to control owner) or devolutionary cycles the family firm remains in the same governance structure or moves to a less complex governance structure (Gersick et al., 1999). The dissertation explains that the different transition forms have their foundation at least partly in the application of the different justice principles of equity and equality in family firm succession. Equality transfers lead to evolutionary transition as the family firm is divided equally between the descendants. Contrary equity transfers lead to recycles or devolutionary transitions, as the family firm is handed over to only the most competent descendant. The dissertation shows that the reason for the different transition forms is the different use of the justice principles of equity and equality in succession.

In the first paper, we learn that while most incumbents pass on ownership according to the justice principle of equality, they apply the justice principle of equity in management transfers. The paper rebuts the presumption that family influence necessarily leads to the dominance of family values (equality) in
succession. Contrary, one has to regard family influence more distinguished and look at the different governance levels the family exercises its influence.

In the *second paper* the dissertation looks at the different governance structures and challenges that arise when applying the different justice principles of equity and equality in family firm succession under an agency perspective. This paper deals with three possible transition forms: equality transfers, equity transfers and a mixed transfer where ownership is passed on according to the justice principle of equality and management according to the justice principle of equity. The latter is the most common governance structure (see Paper 1, chapter 3). The paper conceptually explains that the agency issues of adverse selection, moral hazard and conflicts of interest depend on the justice principle chosen in succession.

Lastly, in its *third paper*, the dissertation deals with injustice perceived by descendants in succession and reveals its negative impact on the family firm. It shows that both descendants, not only the under-rewarded but also the over-rewarded, will adopt behavior that will harm the firm.

### 6.2 Contribution to theory

The dissertation conceptually and empirically establishes the relation between governance and justice in family firms. Hereinafter the main contributions of the three dissertation papers are summarized:

The main contribution of the *first paper* is that it deepens our understanding of how the *current governance structure* of family firms (Chrisman et al., 2012) impacts the choice of the justice principle in succession. The dissertation
thereby differentiates between family influence on different governance bodies, ownership, board of directors and management, and adds to literature that considers different forms of family involvement when investigating firms’ behavior (Astrachan et al., 2002; Klein et al., 2005). The first paper shows that the degree to which family norms permeate family firm succession decision depends on the governance body the family exercises its influence on. The dissertation therewith increases knowhow about intra-family succession and touches therewith the essence that distinguishes family firms from non-family firms (Ayres, 1990; Chua et al., 1999; Wennberg et al., 2011). It further contributes to family business succession literature through providing empirical data on how ownership and management are transferred in family firm succession in Switzerland.

The second paper adds in particular to governance literature in family firms (Lubatkin et al., 2005; Schulze et al., 2002, 2001). It shows that the different justice principles of equity and equality lead to different governance structures with specific governance or agency issues over time. The dissertation therewith reveals an additional source of agency issues (Ang et al., 2000; Jensen & Meckling, 1976): The different justice principles applied in succession. This paper explains that the occurrence of agency issues, such as adverse selection and moral hazard (Jensen & Meckling, 1976), depends on the justice principle chosen in succession. Justice is correspondingly a major, family firm specific source of agency issues that scholars have to consider alongside other types, such as altruism (Buchanan, 1975; Karra et al., 2006; Lubatkin et al., 2005; Schulze et al., 2002). Even though scholars have hinted at the connection between justice and agency issues before (Baldrige & Schulze, 1999; Lubatkin et al., 2007), their relation has not been discussed in
detail. The paper further raises awareness that academic analysis of agency issues needs to more clearly address the *dynamic nature of agency issues*. Governance structures are changing continuously over time and governance challenges change with them (Carney, 2005). Considering their different transition forms (Gersick et al., 1999), such dynamic approach is especially needed in family firms. For instance, the application of the equality principle is in general more likely to induce the agency issue of adverse selection. However, if ownership is passed on equally and management according to equity, with each generation the pool of possible successors grows and the risk of adverse selection decreases. This dynamic analysis of agency issues challenges the so far static approach and opens up new doors to investigate governance challenges. Lastly, the paper introduces *family firm specific governance instruments*, that beside monitoring and compensation incentives, can mitigate agency issues, such as the establishment of a family constitution, exit facilitating mechanisms, or the timing of the disclosure of the justice principle of choice in succession. The paper thereby deals with elements of distributional and procedural justice.

In its *third and last paper*, the dissertation introduces new concepts into *family business governance* and *succession* literature. The paper draws on organizational justice literature and explains how the concepts of *perceived injustice*, of *under- and over-rewarded descendants* as well as of *injustice reduction mechanisms* work in family firm succession (Adams, 1963). The paper reveals the negative impacts of perceived injustice by descendants in succession on the firm and therewith bridges the two systems of family and firm (Dyer & Handler, 1994; Harris, Martinez, & Ward, 1994). It raises awareness that not only the under-rewarded is likely to cause damage to the
firm but also the over-rewarded. So far, family business theory has focused on the under-rewarded who becomes an impediment to the family firm, known as “Fredo effect” (Kidwell et al., 2012), and the over-rewarded has been neglected. However, as the over-rewarded is generally the successor and future decision maker in the family firm the contribution that the over-rewarded descendant can turn into a “Fredo” as well is important (Kidwell et al., 2013).

The paper also adds to organizational behavior and organizational justice theory (Cohen-Charash & Spector, 2001; Greenberg, 1990a) as it deals with injustice reduction mechanisms in family firms and increases the knowhow about organizational behavior of family members working in the family firm. As 65-90% of the companies are family firms (Zellweger, 2017), the insight that following perceived injustice family members’ behavior is detrimental to the firm is crucial also for non-family business scholars.

In sum, the dissertation sheds light on the interplay between governance and justice in family firm succession and therewith adds to and draws from family business, succession, governance, organizational behavior and organizational justice theory. In 2014 (Gagné et al., 2014), stated: “the justice stream is virtually dry”. This dissertation pours water into the justice stream and hopefully generates a wave of attention towards the concepts of justice in family business research.

6.3 Contribution to practice

The first paper provides benchmarks. It shows that incumbents generally intend to pass on management according to the justice principle of equity whereas ownership according to the justice principle of equality. Such benchmarks show family firm incumbents in practice how succession is
effected in other family firms and are hence a helpful reference in succession processes. Family firm incumbents become aware whether they, with their succession decision, belong to the majority or the minority. Benchmarks thereby increase pressure for members of the minority to justify their decisions. For instance, as equal management transfer is the exception, incumbents who choose the justice principle of equality in management succession will feel obliged to better substantiate their choice. This leads to more reasoned decisions.

As the choice of the justice principle in ownership succession is less clear than in management succession, the paper further discloses that in ownership succession *incumbents are torn between the two justice principles*. They doubt whether there is a merit dimension in ownership succession and are undecided to what extent ownership and management transfers should relate.

The first paper further shows how family influence impacts the choice between equality and equity transfers. This awareness will support a more considerate *composition of governance* bodies in family firms. Simplified the first paper shows that family influence in ownership will increase the application of the business norm of equity in succession, while family influence in management favors the likelihood of the family norm of equality. Moreover, the impact of family members in the board of directors depends on whether their presence is combined with family ownership or family management. Knowledge of the fact that the degree to which family norms permeate family firms’ decision making, depends on the governance body the family exercises its influence on, will help to composite the governance bodies of the family firm in a way to achieve the right balance between family and business norms.
The second paper addresses agency issues resulting from the application of the different justice principles of equity and equality in succession. For practice, it is helpful to understand that each governance structure leads to agency issues. For instance, if equality is the justice principle of choice in succession, the risk of adverse selection increases and incumbents have to make sure that their descendants achieve the skills necessary to lead the company.

The second paper is especially helpful as it addresses the governance challenges in the most common family firm governance structure. As the most common succession form is an equity-transfer of management and an equality-transfer of ownership, there will be an evolutionary transition with regard to ownership and a recycle with regard to management (see paper 1, chapter 3). As a result, there are generally multiple family shareholders but only one family successor manager. Agency issues are generated by the fact that all descendants are shareholders (principals) but only one of them is managing the company (agent). Here information asymmetries and different interests are likely to cause conflicts between descendants, for example with regard to re-investments of profits in the family firm and dividend distributions. Also, this succession form might generate feelings of injustice among descendants. These issues need to be discussed in the family.

Family firm specific governance instruments that can prevent conflicts among descendants in such governance structures (equity-management, equality-ownership) is for instance the process of establishing a family constitution. Such process will help family members to generate common ground. Another procedural element that will mitigate negative behaviors of descendants
following perceived injustice is the early disclosure of the justice principle of choice in succession by the incumbent. Furthermore, the creation of exit opportunities for family shareholders will temper conflicts among descendants. Exit opportunities offer family members the choice to either sell their shares or to remain voluntary in the family firm. The likelihood that the successor manager exploits the company (moral hazard) is mitigated by the fact that family shareholders, in contrast to shareholders of widely held firms, will closely monitor the successor manager. Nevertheless, compensation schemes have to be established that align the interests of the successor manager with those of the successor shareholders.

In the long run, the distribution of ownership in accordance with the equality principle cannot be maintained, as shareholders have different numbers of descendants. Agency issues then arise as majority family shareholders can dominate decisions and exploit minority shareholders (Morck & Yeung, 2003). To maintain equal power between the family lines, later generation often agree that each family line has the same rights, for instance each line is entitled to send one of its members to the board of directors.

The third paper addresses the institutional overlap between family and firm (Lansberg, 1983) in the most prominent way as it shows how injustice perceived by descendants harms the firm. This paper raises awareness that family members have to actively address the difficult question of justice in succession. Otherwise, perceived injustice is likely to emerge and to endanger family relations as well as firm performance. In dealing with both, the behavior of the under- as well as the over-rewarded descendant, the paper reveals that not only the discriminated descendant is in pain, but also sheds light on the
unfortunate and complicated situation of the “favored” descendant. Most importantly, this paper will empower family business consultants to address the topic of justice in family firm succession. Generally, they shy away from the subject as they do not want to intrude the family sphere, a sphere they feel not responsible for as they deal with more technical questions of succession. The third paper however shows that perceived injustice has negative effects on the family firm and therewith will urge also business consultants to tackle the difficult question of justice. It therewith confirms previous findings of family business scholars that business and family are inextricably interconnected and that one cannot consult on business issues without taking into consideration the family.

6.4 Limitations

All three papers focus on distributional justice principles in succession, only paper 2 includes elements of procedural justice. Paper 1 and 3 apply a quantitative and paper 2 a conceptual approach. All three papers work with the assumption, that a family firm incumbent has two descendants and chooses one of justice principles of equity or equality in succession. Study 1 and 3 base on scenarios that were integrated in a questionnaire. After reading the respective scenarios, respondents were asked to indicate their transfer intentions (paper 1) and the likelihood that they revert to injustice reduction mechanisms (paper 3). Correspondingly, the empirical studies do not explore actual decisions of incumbents but provide hypothetical answers. This hypothetical approach has its limitations as it does not capture reality. However, it is very helpful as – similar to an experiment – it allows to manipulate some critical factors (e.g., existence of two descendants interested to take over the family firm). Applying this methodology helped to reduce the very complex setting of family firm
succession. Nevertheless, other important variables were not considered in this dissertation, such as the concrete situation of the succession, as e.g., the availability of other assets of incumbents that could be transferred in succession, or the existence of other justice principles that might play a role, such as need (Deutsch, 1975). Also, other aspects that determine whether people consider an allocation as fair, such as further components of procedural justice, as well as elements of interactional justice (Cropanzano et al., 2002), have received not enough attention.

6.5 Future research

The limitations point the direction to future research. The suggestions for future research are made in Chapters 3, 4 and 5. Hereinafter, I will summarize four ideas for future research.

First, it would be interesting to learn according to what justice principles successions are effected in different parts of the world and how culture influences the choice between different allocation norms and eventually performance of family firms.

Second, the ambiguous role of family boards should be analyzed in more detail. We have not yet enough knowledge about to what degree findings of corporate governance research can be transferred to the family business context. This applies for instance to the role that family internal board members have and the ideal ratio between family external and internal board members.

Third, future research could more closely analyze the most common governance structure of family firms (equality-ownership transfer / equity-
management transfer) and tackle the resulting governance challenges from different perspectives (agency or stewardship).

Lastly, especially injustice perceived by over-rewarded descendants might be a fruitful domain for future research. Over-rewarded descendants are generally the ones who follow as successor managers (CEO) into the family firm and are therewith able to shape the decisions of the company. Correspondingly, perceived injustice by over-rewarded descendant will be able to violate the interests of the family firm more strongly than perceived injustice by under-rewarded descendants.
6.6 Conclusion

“Some among the Great Goods cannot live together. That is a conceptual truth. We are doomed to choose, and every choice may entail an irreparable loss.”

This dissertation deals with the choice between equity and equality in family firm succession. It shows the current governance structures of family firms that influence such choice and the governance structures and challenges that result from such choice. As stated in the quote of Isaiah Berlin, choices may entail irreparable losses. Same applies to the choice between equity and equality in succession. Each choice entails a set of consequences for family firms’ governance. It determines the future roles of family members in the firm, the composition of the governance structures, perceived injustice and therewith lastly the success of family firms.

The dissertation does not opt for the application of one of the justice principles of equity or equality. This is a conscious decision. Decisive is not the choice of one of the justice principles but how family firms encounter the challenges that result from such choice. Family firms need to establish governance instruments that mitigate the possible negative effects of each justice principle. Family members must come together, face the critical questions that justice raises in family firm succession (who succeeds in ownership and management, how are these functions interconnected, to what extent are family members

treated equally and what decisions are based on equity?) and discuss solutions that are in the best interest of the family and the firm.

The aim of this dissertation was to provide for some thinking patterns. These follow in the next and last chapter. They shall give orientation in concrete succession planning situations. They shall help decision-makers in family firms to foresee the impact of their decisions and therewith to govern the family firm. They shall raise awareness that justice and governance are as much intertwined in family firms as the family and the firm. They shall serve family members as food for thought and basis for discussion. They shall empower family members and especially their consultants to dare to ask the pivotal question: “What do you perceive as just? Equity or Equality?”
6.7 **25 proposed thinking patterns**

1. In distributions, the family norm is equality
2. In distributions, the business norm is equity
3. In ownership succession, incumbents prefer equality transfers
4. In management succession, incumbents prefer equity transfers
5. Even tough in ownership succession, incumbents generally prefer the justice principle of equality, incumbents find themselves in a dilemma of how to imply equity considerations
6. Family’s impact on the choice of the justice principle must be considered in a more elaborate way. Depending on what governance body the family exercises its influence on, succession is more likely to be influenced by the family norm of equality or the business norm of equity
7. Increasing family influence in ownership favors equity ownership and management succession
8. Increasing family influence in management favors equality management succession
9. Increasing family influence in the board of directors is ambiguous. Paired with family influence in ownership it reduces the likelihood of equity management succession, paired with family influence in management it reduces the likelihood of equality management succession
10. High family cohesion favors equality ownership succession
11. The presence of female family members favors equality ownership succession (but not equality management succession)
12. The older the family firm the more likely are equity ownership transfers
13. The older the incumbent the more likely are equity ownership transfers
14. The older the family firm the more likely are equity management transfers
15. The choice of one of the justice principles equity or equality leads to different governance structures
16. The most common governance structure in family firms are equality-shareholders and equity-management
<p>| | |</p>
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<tbody>
<tr>
<td><strong>17.</strong></td>
<td>The fact that more family members are present in the family firm is a sign that the justice principle of equality played a role in succession</td>
</tr>
<tr>
<td><strong>18.</strong></td>
<td>The fact that different family lines have one representative in the board of directors follows from the application of the justice principle of equality in succession</td>
</tr>
<tr>
<td><strong>19.</strong></td>
<td>Each governance structure has its own specific challenges</td>
</tr>
<tr>
<td><strong>20.</strong></td>
<td>Equality transfers are not possible over several generations</td>
</tr>
<tr>
<td><strong>21.</strong></td>
<td>Perceived injustice has long-term damaging effects on the company</td>
</tr>
<tr>
<td><strong>22.</strong></td>
<td>Perceived injustice does not rest in the relationship between incumbent and descendant but impacts the relationship between siblings</td>
</tr>
<tr>
<td><strong>23.</strong></td>
<td>Under-rewarded descendants will harm the firm in order to make up for perceived injustice</td>
</tr>
<tr>
<td><strong>24.</strong></td>
<td>Over-rewarded descendants will harm the firm as well</td>
</tr>
<tr>
<td><strong>25.</strong></td>
<td>Family cohesion does not prevent these behaviors of descendants</td>
</tr>
</tbody>
</table>
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SONJA KISSLING STREULI

RA lic. iur., LL.M.; Mediator SAV
(Attorney at Law, Master of Laws)
Färberstrasse 28, 8008 Zurich, Switzerland
+41 79 285 14 34
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Date of birth February 23, 1980
Nationality Swiss / German
Civil status Married to Dieter Streuli, with daughter Marie

Interested in advising family firms in family, ownership and corporate governance; teaching activities; publication activities

PROFESSIONAL EXPERIENCE

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<tr>
<th>Date</th>
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<tr>
<td>today</td>
<td>FAMILY BUSINESS MATTERS, ZURICH</td>
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<tr>
<td>09/2017-</td>
<td>Family business governance consultant</td>
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<tr>
<td>06/2017-</td>
<td>CENTER FOR FAMILY BUSINESS (CFB-HSG), UNIVERSITY OF ST.GALLEN</td>
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<tr>
<td>03/2013-</td>
<td>Doctoral candidate and project manager:</td>
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<tr>
<td></td>
<td>- Doctoral thesis in business administration. Topic: Justice principles applied</td>
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<tr>
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<td>in family firm succession and their impact on governance</td>
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<tr>
<td></td>
<td>- Conduction of workshops with family firms: Input presentation, moderation</td>
</tr>
<tr>
<td></td>
<td>(inter alia Looser Holding, Bossard, Sigvaris)</td>
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<td></td>
<td>- Conduction of semi-annual meetings of the CFB-HSG sponsoring family firms:</td>
</tr>
<tr>
<td></td>
<td>Input presentation, moderation, organization</td>
</tr>
<tr>
<td></td>
<td>- Lectures on matrimonial, inheritance and company succession law and supervision of Bachelor and Master</td>
</tr>
</tbody>
</table>
theses
– Speeches for private organizations/companies (inter alia at Widenmoos; Zurich Bar Association; Consulta Succession Conference Lilienberg; Business Networking Day/Junior Chamber International (JCI))
– Organization of the conference “Familienunternehmen im Dialog (FiD)”.

01/2013  UMBRICH ATTORNEYS AT LAW, LAW FIRM, ZURICH
12/2008-
Associate lawyer:
– Consulting of international private clients and small and medium-sized companies in all legal aspects (international, contract, company, inheritance law)
– Negotiation of contracts with clients and counterparties
– Submissions to the court and conducted settlement discussions

09/2008  UNITED NATIONS, NEW YORK, USA
06/2008-
Externship at the Office of Legal Affairs / Office of the Under-Secretary-General:
– Practice in the areas of international law, UN-law, UN-procedure law
– Legal advice to UN entities

05/2008  BÄR & KARRER, LAW FIRM, ZURICH
04/2005-
Associate lawyer in the capital markets team:
– Drafting of prospectuses for the initial public offering of companies.
– Mergers & acquisitions (takeover offers, share purchase agreements)
– Corporate housekeeping and preparation of shareholder meetings and meetings of the board of directors

EDUCATION
2017  UNIVERSITY OF ST.GALLEN, ST. GALLEN
Completion of doctoral program (focus: Strategic management)
– Distinctions: EQUA-Best Research Question Award 2017; Award for best Family System
2011  **UNIVERSITY OF COLUMBIA, NEW YORK, USA**  
LL.M. (Master of Laws):  
– Teaching assistant for negotiation workshop  
  (sole LL.M. student allowed as teaching assistant)  
– Special interest in negotiation, conflict resolution, mediation

2007  **BAR EXAM, CANTON OF ZURICH**  
– Admitted to practice in Switzerland

2004  **UNIVERSITY OF ZURICH, ZURICH**  
Lic. iur. (J.D. equivalent):  
– Special interest in private and company law  
– Exchange semester at University of Geneva  
  (final examination in competition law and law making)  
– Distinction: Magna cum laude (within best 20)

1998  **CHRISTKÖNIG-KOLLEGIUM NUOLEN, NUOLEN**  
University-entrance diploma:  
– Type B (Latin)  
– Distinction: Award for best Matura (high school)  
  diploma of Canton Schwyz

**LANGUAGES**

<table>
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<th>Language</th>
<th>Knowledge Level</th>
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<tbody>
<tr>
<td><strong>GERMAN</strong></td>
<td>Mother tongue</td>
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<tr>
<td><strong>FRENCH</strong></td>
<td>Fluent in spoken and written</td>
</tr>
<tr>
<td><strong>ENGLISH</strong></td>
<td>Fluent in spoken and written</td>
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<tr>
<td><strong>ARABIC</strong></td>
<td>Beginner stage</td>
</tr>
</tbody>
</table>
PUBLICATIONS

- Halter, Frank & Kissling Streuli, Sonja (2014) Stolpersteine im Nachfolgeprozess
- Sieger, Philipp & Kissling Streuli, Sonja (2013) Psychologisches Eigentum - Das Gefühl zählt!
- Kissling Streuli, Sonja & Halter, Frank (2013) Informationsasymmetrien als Nachfolge-Hürden überwinden