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Reporting strategies: What makes family firms beat around the bush? Family-related antecedents of annual report readability☆

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ABSTRACT

We investigate the heterogeneity of reporting strategies across family firms by focusing on the readability of annual reports. Adopting the socioemotional wealth perspective, we introduce three family-related antecedents of annual report readability to accounting and family business literature: *family power, the overlap between family and firm name,* and *generational stage.* Our findings, based on the textual analysis of 288 annual report readability increases at higher levels of family power, decreases at later generational stages, and when the firm carries the family name.

1. Introduction

Academic interest in accounting research in the family business field is growing (Prencipe, Bar-Yosef, & Dekker, 2014; Salvato & Moores, 2010; Songini, Gnan, & Malmi, 2013). In recent years, scholars have explored whether family firms differ from non-family firms in their reporting strategies (e.g., Ali, Chen, & Radhakrishnan, 2007; Campopiano & De Massis, 2015; Cascino, Pugliese, Mussolino, & Sansone, 2010; Prencipe, Markarian, & Pozza, 2008; Shujun, Baozhi, & Zili, 2011). However, in light of the fact that the variance among family firms may be even greater than between family and non-family firms (Chrisman & Patel, 2012), the following research question remains unanswered: *What drives heterogeneous reporting strategies across family firms?*

With the aim of moving a step forward in this field of inquiry, and in line with studies on the "readability/reading ease manipulation" in accounting narratives (Brennan, Guillamon-Saorin, & Pierce, 2009; Merkl-Davies & Brennan, 2007), we focus on a key aspect of reporting strategies, i.e., annual report readability (Lawrence, 2013; Lehavy, Li, & Merkley, 2011; Li, 2008; Lo, Ramos, & Rogo, 2017). The notion of "readability" generally refers to the extent to which a document is easy to understand in terms of its composition and text-based style (Courtis, 2004; Merkl-Davies & Brennan, 2007). A growing number of recent studies claim that the readability of annual reports is a key element of communication between managers and stakeholders (De Franco, Hope, Vyas, & Zhou, 2015; Lang & Stice-Lawrence, 2015; Lo et al., 2017; Lundholm, Rogo, & Zhang, 2014; Stone, 2011). Managers can help investors reduce processing costs by making information more readable, as disclosure readability increases the investors' ability to understand the firm's business strategies, activities, and results (Bonsall & Miller, 2017; Guay et al., 2016; Lang & Stice-Lawrence, 2015; Loughran & McDonald,2014). In addition, financial report readability plays a significant role in improving perceptions of the management's reliability in the long run (Lawrence, 2013; Lundholm et al., 2014; Rennekamp, 2012).

Since the annual report is the primary source of information for external parties (Dawkins & Fraas, 2013; Jeanjean, Lesage, & Stolow, 2010; Jeanjean, Stolow, Erkens, & Yhon, 2015), a natural concern arises when managers deliberately obfuscate some important information to alter stakeholder perceptions (Brennan et al., 2009; Courtis, 2004; Li, 2008; Merkl-Davies & Brennan, 2007; Stanton & Stanton, 2002). Building on the recent theoretical article of Gómez-Mejía, Cruz, and Imperatore (2014), and incorporating the socioemotional wealth (SEW) logic in reporting strategies, we argue that the readability of annual reports among family firms depends on the emphasis placed on the specific dimension of SEW that family principals prioritize, i.e., "family control and influence" vs. "family identity". Thus, we introduce three family-related antecedents that may enable understanding the variation in annual report readability among family firms: family power, the overlap between firm and family name, and generational stage. Relying

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on a hand-collected sample of 288 annual reports of Italian listed family firms in the period 2008–2013, we find that annual report readability increases at higher levels of family power, decreases at later generational stages, and when the firm carries the family name.

This study contributes to family business literature by providing evidence of the heterogeneity of family firms in their reporting strategies. We respond to the call for research to grasp the heterogeneity of family firms in any business aspect (Chrisman, Sharma, & Taggar, 2007). In doing so, we contribute to establishing the SEW perspective as an emerging theoretical approach to understand the reporting strategies of family firms (Gómez-Mejía, Cruz, Berrone, & De Castro, 2011). Second, in line with studies on the "readability/reading ease manipulation" in narrative reporting, we also respond to recent calls in accounting literature seeking novel insights on reporting issues in the context of family firms (Gómez-Mejía et al., 2014; Prencipe et al., 2014). Indeed, we propose three new drivers of the variance in the readability of annual reports, contributing to a deeper understanding of reporting strategies in listed family firms.

The remainder of the paper is structured as follows. The next section introduces the SEW logic to annual report readability in family firms, followed by a set of three hypotheses. We then describe the research methodology, i.e., the sample, data collection, textual analysis, variables, regression models, and robustness tests. Thereafter, we present the results and discuss our findings and their implications.

2. Theoretical development

2.1. Annual report readability in family firms: a SEW approach

In the last decade, the SEW approach has emerged as a new theoretical lens to investigate decision-making in family business and understand the distinctive features of this type of organization. Socioemotional wealth refers to the affective endowments of the family business and includes a variety of potential non-economic returns that family members obtain from owning and managing their firm, such as family control and influence, a sense of shared identity and emotional attachment, the creation and maintenance of social ties, the perpetuation of the family dynasty (Berrone, Cruz, & Gómez-Mejía, 2012; Gómez-Mejía, Haynes, Nuñez-Nickel, Jacobson, & Moyano-Fuentes, 2007; Gómez-Mejía et al., 2011).

Grounded in behavioral agency theory (Wiseman & Gómez-Mejía, 1998), the SEW approach contends that family decision-makers consider threats and risks according to a subjective view of what matters to their welfare, rather than drawing on economic evaluations that compare risks against financial returns. Accordingly, SEW preservation is considered the primary reference point for strategic decision-making in family firms. Moving from the seminal article of Gómez-Mejía et al. (2007), scholars have used the concept of SEW preservation to predict various family firm decisions, including accounting practices. Accounting contributions mostly focus on earnings management (Achleitner, Günther, Kaserer, & Siciliano, 2014; Martin, Campbell, & Gómez-Mejía, 2016; Pazzaglia, Mengoli, & Sapienza, 2013; Stockmans, Lybaert, & Voordeckers, 2010) with only scant attention to financial disclosure (for a review, see Prencipe et al., 2014).

However, the recent Gómez-Mejía et al. (2014) study has enabled moving a step forward in understanding financial disclosure in family firms by shedding light on the SEW-related mechanisms underlying the decision on the quality of financial reports. Family members consider this type of decision as a gamble in which SEW preservation is used as a reference point to estimate the costs and benefits of the gamble. More precisely, family principals are willing to bear the potential cost of the gamble (e.g., undesired attention of regulators) if they deem that a SEW reward is associated with it (e.g., reputational gains), whereas they are not willing to do so if they perceive that family SEW is under threat (Gómez-Mejía et al., 2014).

Specifically, Gómez-Mejía et al. (2014) argue that the evaluation of the advantages and potential drawbacks of decisions on the quality of financial reports depends on which dimension of SEW the family members prioritize. The scholars focus on two dimensions of SEW, i.e., "family control and influence" and "family identity", which represent not only two different types of non-economic utilities that family members obtain from owning the firm, but also two different reference points that explain heterogeneous behaviors in family firms (Berrone et al., 2012). The "family control and influence" dimension is related to the family principals' willingness to preserve and pass on to future generations direct or indirect family control and influence over the business. The "family identity" dimension is instead related to the family's close identification with the firm (Berrone et al., 2012; Gómez-Mejía et al., 2011; Zellweger, Kellermanns, Chrisman, & Chua, 2011; Zellweger, Nason, Nordqvist, & Bush, 2013). According to Gómez-Mejía et al. (2014), the quality of information disclosed is higher (i.e., more verifiable and credible) when family principals prioritize the "family identity" dimension of SEW. Conversely, the quality worsens (i.e., is less verifiable and credible) when family principals prioritize "family control and influence".

The reason lies in the strong role of reputational issues for the owning family when family identity is prioritized: the desire to protect the family's reputation and promote a positive image gives family members the incentive to disclose more transparent information. By contrast, when family control and influence are prioritized, family principals are assumed to alter non-family stakeholders' perceptions by engaging in impression management to preserve family control. Impression management refers to the management's opportunistic use of information disclosure to either improve the perception of corporate achievement or hide information that could negatively affect their position (Hooghiemstra, 2000; Leary & Kowalski, 1990). Accordingly, previous research argues that managers may not present transparent information and are incentivized to manipulate the readability of reports (Brennan et al., 2009; Courtis, 2004; Li, 2008; Merkl-Davies & Brennan, 2007).

Hence, the SEW lens enables grasping how and why family members decide to influence annual report readability – as a key aspect of the quality of financial reports – depending on which SEW dimension is emphasized and therefore used as a reference point in their reporting decisions. However, the antecedents that shape the prioritization of one SEW dimension over the other are still unclear. Thus, to understand which factors drive the emphasis on the aforementioned SEW dimensions and consequently influence annual report readability in family firms, our study focuses on three firm-specific antecedents: family power, overlap between firm and family name, and generational stage.

2.2. Annual report readability and family power

Family power refers to the degree of family involvement in ownership, corporate boards, and leadership (Astrachan, Klein, & Smyrnios, 2002; Klein, Astrachan, & Smyrnios, 2005; Mazzola, Sciascia, & Kellermanns, 2013). Prior research reports that family power is likely to affect accounting performance and financial disclosure (Anderson & Reeb, 2003; Audretsch, Chen, Chen, & Cheng, 2008; Hulsbeck, & Lehmann, 2013; Poutziouris, Savva, & Hadjielias, 2015; Sacristán-Navarro, Gómez-Ansón, & Cabeza-García, 2011; Villalonga & Amit, 2006).

We suggest that family power can influence annual report readability in family firms by shaping the prioritization of "family control and influence" vs. "family identity". We contend that when family power remains at moderate levels, family principals perceive themselves as vulnerable actors within the firm. A recent study suggests that when the family firm is under conditions of vulnerability (e.g., performance under aspiration levels), family principals are willing to deemphasize their family control preservation goals to foster financial goals with the final aim of safeguarding the firm's longevity and, in turn, their SEW endowment (Gómez-Mejía, Patel, & Zellweger, 2015). However, when the family members' position within the firm is