РАЗДЕЛ 3 КОРПОРАТИВНОЕ УПРАВЛЕНИЕ ВО ФРАНЦИИ

SECTION 3 NATIONAL PRACTICES OF CORPORATE GOVERNANCE: FRANCE

OWNERSHIP STRUCTURE AND VOLUNTARY DISCLOSURES: THE CASE OF FRENCH-LISTED FIRMS

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Abstract

This paper investigates the relationship between ownership structure and voluntary earnings disclosures under high ownership concentration of French-listed firms. The findings show that French managers are less likely to make voluntary disclosures when they are controlled by a large shareholder or by a family, suggesting that low legal protection leads to expropriation of minority shareholders. The results also show that the proportion of foreign institutional investors in capital is likely to mitigate this relationship since institutional investors signal good minority shareholders' protection to the market.

Keywords: Voluntary earning disclosure, ownership structure, controlling shareholder, institutional investors, occasional disclosure

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1. Introduction

There has been an ongoing interest in corporate voluntary disclosures in recent years due to the market growing need for financial information. One of the components of voluntary disclosures is unregulated earnings announcements. These disclosures are not required by law. This paper provides evidence on whether voluntary disclosures are influenced by concentrated ownership structures, as is the case of most French-listed firms.

In France, three forms of earnings announcements are unregulated: quarterly earnings announcements, earnings forecasts, and earnings pre-announcements including profit warnings. French-listed firms are required to release their annual reports in the BALO (BALO refers to Bulletin des Annonces Légales et Officielles). They must also release their net income half-yearly and report their revenue only quarterly. Where the regulation S-X from the SEC (SEC refers to Securities Exchange Commission) compels firms to disclose annual and quarterly reports under a homogenizing form (10-K and 10-Q forms), the AMF (AMF stands for Autorité des marchés financiers) requires the quarterly announcements to only include revenues. Earnings forecasts and earnings pre-announcements are both expectations about yet-to-be-released earnings. The former are reported before the fiscal year end, whereas the latter are disclosed after the fiscal year end and before annual reports' releases. They are issued by managers to inform the market about the forth-coming of either good or bad news.

Ownership structure in France is concentrated. While separation of ownership and control is the main

form of corporate governance in the US and the UK, the control of most French firms is concentrated in the hands of families or individuals. Under concentrated ownership structure, conflicts of interests arise between controlling and minority shareholders. The decisions of controlling shareholders may result in the expropriation of minority shareholders (Shleifer and Vishny, 1997). A substantial fraction of these large shareholders holds more voting rights than cash flow rights. The controlling shareholders have, then, more power to expropriate minority shareholders. Moreover, when shareholders effectively control a company, they also control all company reporting policies. The case of French-listed firms is therefore worth studying because of its corporate governance environment. Besides, voluntary disclosures deserve special attention in the European context because firms in these countries have less incentive for regular disclosures than their Anglo-American counterparts.

The purpose of this paper is to show how corporate ownership structure in France affects the frequency of voluntary disclosures. It is expected that the relation between ownership concentration and voluntary disclosures in France to be different from that in the U.S. This paper shows that ownership concentration and voluntary disclosures are negatively associated. Furthermore, French managers occasionally provide voluntary disclosures to inform the market about their good performance because they might take advantage from stock price increases. The results are generally robust to control for firm size, leverage, US-listing and high-tech industry.

The remainder of this paper is organized as follows: Section 2 presents an overview of the literature that deals with ownership structure and voluntary disclosure interactions. It examines also the literature regarding voluntary disclosures and firm characteristics. Section 3 describes the sample, data and variables used in this study. This is followed by the empirical findings and discussions in section 4. The last section concludes the paper.

2. Literature Review and Hypotheses Development

2.1 Ownership structure and voluntary disclosures

Agency theory provides insights into the determinants of companies' disclosure choices. Jensen and Meckling's (1976) positive agency theory provides a framework linking disclosure behaviour to corporate governance. Corporate disclosures are considered a tool to control the agency costs arising from conflicts of interests between managers and shareholders or between large and small shareholders.

Corporate governance problems take different forms: one when corporate ownership is concentrated and the other one when it is diffused. In particular, when ownership and control are separated as is the case in US and UK companies, agency costs arise from conflicts of interests between managers and shareholders (Jensen and Meckling, 1976). When ownership structure is controlled by a large shareholder or by a family, conflicts between the controlling and minority shareholders are deemed to be more important (Shleifer and Vishny, 1997). French firms are subject to the second nature of agency problem. The conflicts of interests between large and small shareholders exist because large shareholders often own more control rights than cash flow rights. This cash-control divergence positively affects the controlling owners' incentives to expropriate other shareholders. La Porta *et al.* (1998) show that civil law countries such as France, offer low legal protection of external investors than common law countries. Besides, French firms may opt for dual-class shares, pyramiding and cross holdings, which are likely to enhance agency costs (Boubaker, 2005).

Ownership structure is likely to influence financial disclosures. The accounting literature suggests that the reporting incentives of managers affect accounting information quality and production. Fama and Jensen (1983) argue that in widely-held firms the potential of conflicts between principal and agent is greater, than in family-controlled firms. To reduce these conflicts some shareholders, especially institutional ones, compel managers to disclose more corporate information in order to accurately assess firm performance. Linkages between ownership structure and voluntary disclosures have been found in several other studies (McKinnon and Dalimunthe, 1993; Ho and Wong, 2001; Chau and Gray, 2002; Healy *et al.*, 1999; Healy and Palepu, 2001). As share ownership is concentrated, accounting information production decreases and controlling shareholders are likely to expropriate minority shareholders rather than issuing information about firm performance.

A strand of the literature argues that a separation between cash flow rights and voting rights is common among public corporations around the world. La Porta *et al.* (1999) report such evidence for over 600 firms in 27 wealthy countries. Studies on European countries show a typical ownership structure characterized by separation of cash flow and voting rights. In France, shareholders can receive double voting rights on their stocks when the latter have been registered for at least two years[41]. These dual-class shares increase the dissociation between cash flow and control rights. La Porta *et al.* (1999) point out that France has a civil law system with low minority investor protection, controlling shareholders might, then, try to expropriate minority shareholders and exploit private control benefits. Under highly ownership concentration, large shareholders are able to obtain private information from the company and they are likely to be closely allied to managers. Consequently, the incentives to provide information to the market are reduced.

[41] As stated in the Art. 225 – 123 of the French commercial law.

It is important to shed light on the active role that plays institutional investors in corporate governance structures. These investors act either as traders or owners. First, when they act as traders, they are considered transient investors having incentives to emphasize short-term profits at the expense of the long-term corporate governance issues. They may encourage managers to exercise myopic discretion in reporting a firm's financial performance. Second, once they act as owners, they may take on the role of a large shareholder who will monitor the company on behalf of small shareholders (Short and Keasey, 1997). This will lower the quality and production of accounting information. Elgazzar (1998) shows that the proportion of institutional investors is positively associated to frequent pre-emptive earnings disclosures. These findings are consistent with those of Bushee and Noe's (2000) who emphasize the importance of these actors in influencing managers' decisions. A distinction is made between foreign and local institutional investors. The former have been found to be more cautious about the monitoring of management behavior and offer a better guarantee for minority protection than the latter. In case of repurchase program announcements in France, Ginglinger and L'Her (2002) find that the proportion of foreign institutional investors is strongly and positively associated to price reactions. They suggest that these investors contribute to the adoption of international standards and have stressed their importance in ensuring that companies follow their corporate governance best practice recommendations.

This paper consequently hypothesizes that the threat of expropriation by controlling shareholders in French firms lowers the frequency of voluntary earnings disclosures and hence, the existence of a disclosure policy. However, the high proportion of foreign institutional investors are likely to encourage voluntary disclosures' releases given that they are supposed to provide good minority protection in civil law countries as France.

2.2 Firm characteristics and voluntary disclosures

A large number of empirical studies in the voluntary disclosure literature finds that voluntary disclosures are not only associated to ownership structure; firm characteristics are also likely to influence the disclosure policy. They include firm performance, firm size, industry type, US-listing and leverage.

Performance: Analytical literature, based mainly on the models of Verrecchia (1983) and Dye (1985), predicts a positive relationship between good news and corporate disclosures. In accordance with these models, several studies have tested this prediction. Empirically the results are mixed. Miller (2002) shows that disclosure increases around the time of increased earning performance. Firms that report large earnings increases have incentives to enhance disclosure both prior to and concurrent with the earning realisation (Miller and Piotroski, 2000, Lev and Penman, 1990, Penman, 1980, and Lang and Lundholm, 1993). However, Skinner (1994, 1997) argues that firms disclose voluntarily their earnings to inform the market about negative news. Accordingly, firm performance is measured by the ratio of return on assets and the sign of the relationship is not expected.

Firm Size: Firm size and voluntary disclosures have been found by several studies to be positively associated (e.g., Lev and Penman, 1990, Lang and Lundholm, 1993; Miller and Piotroski, 2000; Kasznik *et al.*, 2001; Soffer *et al.*, 1999; Debreceny *et al.*, 2002; Xiao *et al.*, 2004). Large firms are mostly held by institutional investors and attract market participants' attention. Furthermore, Raffournier (1995) suggests that firms reporting regular financial information experience less costs than do small firms. Firm size is measured by the logarithm of total assets and it is expected to positively influence voluntary disclosures.

Industry Type: Industry type also affects disclosure choices particularly when the reported information is specific to the firm itself and not common to the industry. Haven *et al.* (2002) show that high-tech firms voluntarily disclose information because, investors might not expect their future earnings easily. Consequently, firm value is subject to large price fluctuations. Furthermore, Wallace *et al.* (1994) and Kasznik and Lev (1995) suggest that industry effects could explain the different levels of disclosure among firms. Industry dummies are therefore included in this study to control for the industry effects.

US-Listing: US-listing is also introduced among firm characteristics. When firms are listed on US markets, they adopt large disclosure strategies (Joos, 2000; Raffournier, 1995; Elgazzar *et al.*, 1999 and Xiao *et al.*, 2004). Disclosure requirements of US markets are greater than those of French stock exchange. US-listed firms have to abide by US Generally Accepted Principles (GAAP) leading to a higher level and quality of disclosures than those listed on the French market. US-listing is introduced as a dummy variable.

Debt Level: Companies can reduce agency costs of debt by adopting a disclosure policy. According to the free cash flow problem of Jensen (1986), managers are likely to invest cash in negative net present value projects. Shareholders will then force entrepreneurs to have enough accumulated debt to reduce the cash available at the discretion of managers. Information release would then be high in order to satisfy the informational needs of debt-holders (Lang and Lundholm, 1993; Xiao *et al.*, 2004). However, some authors show a negative relationship between voluntary disclosures and debt level (Wallace *et al.*, 1994 and Eng and Mak, 2003). Firms with high debts are more likely to provide debt-holders with more private information; there is then less need for additional public disclosure. Leverage is measured by the ratio of long-term debt to total assets.

3. Research Methods

3.1 Sample and data selection

The sample includes all industrial and commercial listed firms included in the SBF 250's index at the exception of 43 financial and insurance firms since they are subject to specific disclosure requirements. The final sample includes 207 firms. The sample period goes from 1998 to 2001. Data related to voluntary earnings disclosures are hand-collected for the whole sample. Voluntary disclosures are located in press financial releases. The sample covers all industry sectors (excluding for financial ones as mentioned earlier). The cash flow and voting rights are collected from the annual reports. Lastly, accounting and financial data are extracted from the Worldscope database.

3.2 Variables and method

This study examines voluntary disclosure's frequency. The dependant variable DISCFREQ is a dummy variable coded as 1 if the company has regularly issued earnings announcements from 1998 to 2001; it equals 2 if the company occasionally provides voluntary earnings announcements; and 0 if no voluntary earning announcement is reported. Ownership concentration is measured by the percentage of voting rights owned by the largest shareholder, then by the second important shareholder and by the Herfindahl index (Demsetz and Lehn, 1995). It is calculated by summing the squared percentages of shares held by each shareholder. To test for the existence of relationships between institutional investor's ownership and voluntary earnings disclosures, we include two variables: the proportions of French and foreign institutional investors. Multinomial regression analysis is used to examine the relationship between ownership concentration and voluntary disclosure's frequency in France.

4. Analysis and Discussion

4.1 Descriptive statistics

Table 1 presented below shows that 43.5% of the sample firms disclose at least one voluntary earning announcement each year and 36.2% occasionally disclose their earnings voluntarily. The sample includes 63.8% family-controlled firms, and 81.2% are controlled either by a family or by individuals. These statistics show that ownership structure of French firms is concentrated in hands of individuals or families compared to the widely held firms in the US. Furthermore, only a small proportion of French firms are listed on the US markets (12.5%); family-controlled firms are not inclined to have foreign investors in their capital. Finally, high-tech companies represent a small proportion (18.8%) of the total sample.

Table 1. Summary Statistics of Nominal Variables

		Percentage	Frequency	Total
DISCFREQ	Frequent	43.5	90	207
	Occasional	36.2	75	
	No disclosure	20.3	42	
FAMILY	Family controlled	63.8	132	207
	Other control	36.2	75	
CONTROL[42]	Controlled	81.2	168	207
	Not controlled	18.8	39	
USQUOT	US-listing	12.5	26	207
	Non US-listing	87.5	181	
HIGHTECH	High-tech industry	18.8	39	207
	Other industries	81.2	168	

Table 2. Descriptive Statistics

	Panel A: DISCFREQ = 1		Panel B: DISCFREQ = 2		Panel C: DISCFREQ = 0	
	Mean	SD	Mean	SD	Mean	SD
AH	0.153	0.152	0.236	0.192	0.305	0.179
VR1	0.343	0.219	0.453	0.241	0.572	0.184
VR2	0.086	0.094	0.077	0.081	0.085	0.098
FRII	0.147	0.137	0.131	0.150	0.133	0.173
FORII	0.220	0.163	0.16	0.166	0.080	0.094
LOGTA	7.928	1.931	7.273	1.907	5.662	1.445
LEVERAGE	0.879	4.700	1.884	5.548	2.770	8.994
ROI	-0.484	33.374	9.46	33.992	8.402	9.176

[42] According to the French legislation, a two-thirds majority is required to overtake any decision at the special shareholders general meeting. Shareholders that own one third of the shares can block these decisions. The first large shareholder is an important shareholder then, if he holds at least a third of the shares. The firm is controlled when the first large shareholder owns more than a third of shares.

Summary statistics of dummy variables are presented for 207 listed French firms. DISCFREQ takes the value of 1 if the firm discloses frequently its earnings, 2 if it issues occasionally voluntary earnings announcements and 0 otherwise. FAMILY equals 1 if the company is controlled by a family, CONTROL equals 1 if the company is controlled either by a family or by individuals, USQUOT is coded as 1 if the firm is listed on US market, and 0 otherwise and HIGHTECH equals 1 if the firm belongs to high-tech sector and 0 otherwise.

Panels A and B of Table 2 report descriptive statistics about firms that disclose frequently and occasionally their earnings respectively, whereas panel C provides statistics about non disclosing firms. Concentration index is larger for firms of panel C (30.5%) compared to lower levels for panel B (23.6%) and panel A (15.3%). The same result is observed for the voting rights of the largest shareholder. Tests of mean differences between the three groups are statistically significant at the 1% level. It is argued that as the ownership concentration decreases, the level of earnings announcements increases. Furthermore, foreign institutional investors' ownership is on average greater for firms embracing frequent earnings announcements than for other groups of firms. Lastly, unlike firms that disclose occasionally their earnings, firms with frequent voluntary disclosures seem to belong to high-tech industry and are US-listed.

Descriptive statistics are reported for 207 listed French firms. Panels A, B and C report statistics for the frequent, occasional and non-disclosing group, respectively. AH is the concentration index which equals the squared sum of shares percentages; VR1 is voting rights of the first large shareholder; VR2 is voting rights of the second large shareholder; FRII is the proportion of shares owned by the French institutional investors; FORII is the percentage of shares held by foreign investors; LOGTA is the log of total assets; LEVERAGE is the ratio of total debt to total assets; and ROI is the return on invested capital

Table 3. Tests For Mean Difference

	T-test: 1 Versus 0	T-test: 2 Versus 0	T-test: 1 Versus 2
AH	-5.843***	-2.151***	-2.508***
VR1	-7.172***	-3.010***	-2.573***
VR2	0.049	-0.554	0.602
FRII	0.550	-0.174	0.698
FORII	6.729***	3.918***	1.247
LOGTA	4.773***	2.189***	1.690*
LEVERAGE	-1.610	-0.628	-0.962
ROI	-2.824***	0.558	-1.461
USQUOT	5.471***	1.455	2.687***
HIGHTECH	4.078***	0.934	2.269**

T-tests for equality of means between the three groups of firms are presented in table 3. AH is the concentration index which equals the squared sum of shares percentages; VR1 is voting rights of the first large shareholder; VR2 is voting rights of the second large shareholder; FRII is the proportion of shares owned by the French institutional investors; FORII is the percentage of shares held by foreign investors; LOGTA is the log of total assets; LEVERAGE is the ratio of total debt to total assets; ROI is the return on invested capital; USQUOT is coded as 1 if the firm is listed on the US market, and 0 otherwise; and HIGHTECH equals 1 if the firm belongs to high-tech sector, and 0 otherwise. *, **, and *** represent coefficients' significance levels respectively at 10%, 5%, and 1%.

4.2 Discussion

It is noted that the econometric estimation of the model has included year dummies[43] and industry dummies as additional control variables. All estimated coefficients of these dummy variables at the exception of high-tech companies are statistically insignificant at usual levels. Accordingly, they will be omitted from the results presented below. The model is estimated as follows:

$$DISCFREQ = \alpha_0 + \alpha_1 AH + \alpha_2 VR1 + \alpha_3 VR2 + \alpha_4 CONTROL + \alpha_5 FORII + \alpha_6 FRII + \alpha_7 LEVERAGE + \alpha_8 LOGTA + \alpha_9 ROI + \alpha_{10} USQUOT + \alpha_{11} HIGHTECH + \varepsilon$$

Where,

DISCFREQ = a dummy variable that equals 1 for frequent earnings announcements; 2 for occasional disclosures; and 0 for the non-disclosing group.

AH = the sum of the squared percentages of shares held by each shareholder.

VR1, VR2 = the percentage of voting rights held by the first and second large shareholder, respectively.

CONTROL = a dummy variable that equals 1 if the firm is controlled either by a family or by individuals; and 0 otherwise.

FORII, FRII = the percentage of shares held by foreign and French institutional investors, respectively.

LEVERAGE = the ratio of total debts to total assets.

LOGTA = the log of total assets.

ROI = the return on invested capital;

USQUOT = a dummy variable that equals 1 if the firm is listed on the US market; and 0 otherwise.

HIGHTECH = a dummy variable that equals 1 if the firm belongs to high tech industry.

Table 4 shows that the voting rights of the first large shareholder are negatively and statistically

[43] Year dummies are introduced to control for time trend.

associated to the probability of issuing voluntary earnings disclosures. Share ownership concentration, as measured by the Herfindahl index, is also negatively related to the disclosure policy. Given that family ownership dominates the control of French-listed firms, it would be interesting to learn whether family-control affects the level of voluntary earnings disclosures. The results presented in equation (2) of table 4 back up the argument that controlled shareholders do not pay attention to minority shareholder interests and are able to obtain private information internally. The hypothesis stating that firms are less likely to make voluntary disclosures under the power of a large shareholder is then, confirmed. Eng and Mak (2003), Chau and Gray (2002), Ho and Wong (2001) find the same results as well. As shown in equation (1) of table 4, the proportion of foreign institutional investors and voluntary disclosures are positively and significantly associated. These investors enhance the firm's disclosure quality. This result is similar to that presented by Ginglinger and L'Her (200). French institutional investors, however, own generally a large percentage of the company shares and are more able to obtain private information from the company. The coefficient is insignificant and negative. Another complementary explanation is that French institutional investors act as owners and not as traders, therefore, the need for corporate disclosures may decrease. We test the effects of firms' characteristics on the frequency of voluntary disclosures. Occasional earnings disclosures are significantly associated to good performance, whereas frequent disclosures are not (see table 4). French firms occasionally disclose their earnings when they are doing well. Controlling owners are perceived to report accounting information for self-interested purposes, suggesting the reported earnings could lose their credibility. Furthermore, as expected the findings show that large firms and those listed on the US market are more likely to make voluntary disclosures. These firms are required to follow International Accounting Standards (IAS), which tend to encompass a broader scope than the domestic market. The relation between leverage and voluntary earnings disclosures is subject to debate in literature. Our findings show that leverage negatively affects voluntary earnings dissemination. One intuition of this result is that the agency costs of free cash flow are controlled by debt, which plays a substitutive role for controlling management or owner expropriation. As a consequence, the control effect of debt reduces voluntary disclosure's level. This result is in contrast to that found by Raffournier (1995) on Swiss companies. The author shows that firms increase their disclosure level to get external financing. Our finding is however, consistent with Eng and Mak (2003) arguing that leverage lessens incentives for voluntary disclosures because it helps control the free cash flow problem in Singapore.

Table 4. Multinomial Logit Regressions

	Equation 1		Equation 2	
	Frequent	Occasional	Frequent	Occasional
Constant	-5.154***	-2.655**	-3.395***	-0.871
	(-3.44)	(-1.97)	-2.34	-0.64
VR1	-4.269***	-2.246**		
	(-3.62)	(-2.02)		
VR2	-1.533	-2.020		
	(-0.68)	(-0.85)		
AH			-2.684*	-0.509
			(-1.73)	(-0.41)
CONTROL			-2.512***	-2.344***
			(-3.09)	(-2.42)
FRII	-0.596	-1.011		
	(-0.42)	(-0.71)		
FORII	6.541***	5.139***		
	(3.68)	(3.01)		
LOGTA	0.778***	0.352**	0.771***	0.314**
	(4.22)	(2.18)	(4.29)	(2.05)
ROI	0.003	0.013	-0.003	0.012*
	(0.31)	(1.47)	(-0.34)	(1.66)
LEVERAGE	-0.002***	-0.0006	-0.002***	-0.0006
	(-2.71)	(-1.20)	(-2.86)	(-1.41)
USQUOT	3.859**	2.593	3.771***	2.349
	(2.29)	(1.48)	(3.12)	(1.46)
HIGHTECH	2.777***	1.125	2.431***	0.896
	(4.42)	(1.63)	(4.46)	(1.42)
Observations		207		207
Pseudo R2		0.255		0.244
Wald (Chi2)		69.7 (0.000)		88.42 (0.000)

Among industry sectors dummies, only firms belonging to high technology industry are likely to diffuse earnings voluntarily. The coefficients of HIGHTECH in both equations of table 4 are statistically significant at 1 percent level. This result supports the argument that such firms belong to a sensitive sector and they are inclined to have large price fluctuations leading them to inform constantly the market about their performance. The sample includes 207 listed French firms. Coefficients are estimated with Multinomial Logit models, using DISCFREQ as a dependent variable. It is coded as one for frequent disclosures, 2 for occasional disclosures and 0 for non-disclosing group. AH is the concentration index which equals the squared sum of shares percentages; VR1 is voting rights of the first large shareholder; VR2 is voting rights of the second large shareholder; FRII is the proportion of shares owned by the French institutional investors; FORII is the percentage of shares held by foreign investors; LOGTA is the log of total assets; LEVERAGE is the ratio of total debt to total assets; ROI is the return on invested capital; USQUOT is coded as 1 if the firm is listed on the US market, and 0 otherwise; and HIGHTECH equals 1 if the firm belongs to high-tech sector, and 0 otherwise. Z-statistics are mentioned under the coefficient values for each variable. . *, **, and *** represent coefficients' significance levels respectively at 10%, 5%, and 1%.

5. Conclusion

The main purpose of this study is to examine the relationship between concentrated ownership structure and the frequency of voluntary disclosures. The study uses multinomial logit to test the hypotheses. The empirical evidence supports the argument that ownership concentration is negatively associated to the existence of earning disclosure policies. Furthermore, when large voting rights are held by a controller of by a family, the probability of voluntary disclosures will be lessened. These holders do not pay attention to minority shareholder, withhold information and hence, expropriate them. The presence of foreign institutional investors tends to mitigate this relationship, since they signal good minority protection to the market.

It is important to point out that regular voluntary disclosures in opposition to occasional ones are strongly and positively related to the US-listed and to high-tech industry firms. The results also show that French managers occasionally disclose voluntary earning information when they are doing well, possibly for self-interested purposes. This could be harmful to the company's reputation and its information credibility in the market.

The study of French-listed firms examines the subject of voluntary earnings disclosures in an ownership context different from that of the US. Ownership structure in France raises especially conflicts of interest between large and small shareholders. The findings are consistent with the fact that regulators should understand the causes of lower incentives prior to establishing rules for both corporate disclosures and corporate governance.

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