DOES MANAGEMENT ENTRENCHMENT EXPLAIN AGENCY COSTS OF EQUITY: EVIDENCE FROM FRENCH FIRMS

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Abstract

The purpose of this study is to examine the effect of the management entrenchment on the agency costs of equity. We conduct tests on 120 French companies over the period 2000-2014 in order to test the impact of the main factors that can intensify the conflicts between shareholders and managers. We use three alternative measures of agency costs of equity, namely asset utilization, operating expenses and administrative expenses. According to the empirical results, the CEO age, his dual role of executive and chairman, and the discrepancy between ownership and voting rights are relevant determinants of agency conflicts between shareholders and managers. Furthermore, we find that, the manager's seniority and his ownership constitute internal governance mechanisms for the French companies.

Keywords: Agency Costs, Managerial Entrenchment, Ownership Structure, Free Cash Flow
JEL Codes: G30, G32, G34, G35, G38

1. INTRODUCTION

The conflictual relationship between shareholders and managers is the main concern for companies in which ownership and control are separated (*Berle and Means (1932), Jensen and Meckling (1976*)). In other words, such conflict arises from the fact that the manager does not possess all of the company's equity and, therefore, does not receive all of its benefits. On the other hand, when the company declares bankruptcy, managers risk losing their position. As a result, they will tend to reduce their efforts and transfer the resources of the company for their own account (*Harris and Raviv (1991)*). In these circumstances, an agency conflict can occur when the manager does not maximize shareholder value. These continue to be sources of enormous costs, even in developed countries, for the shareholders and investors in general.

Corporate governance covers different theories whose aim is to study the various factors contributing to the intensification of conflicts between the different stakeholders. These theories have the same assumptions of neoclassic economics, such as agency and property rights theory as well as competence-based theories, which are mainly the evolutionary and resource-based theory of the firm (*Hodgson (1998*)). Through these theories, we are examining a question that it has not been studied well enough in the context of French companies, in particular the identification of the determinants of agency conflicts between managers and shareholders regardless of the disciplinary mechanisms allowing for the reduction of these conflicts. To achieve the objective of the study, the rest of the paper is organized as follows. The second section reviews the previous empirical literature on the determinants of agency conflicts between managers and shareholders. The third section describes the data and methodology that we employ in our study. The fourth section reports on an empirical study of the French context. The last section concludes by discussing the various implications of our approach.

2. THE LITERATURE REVIEW

A large amount of the theoretical literature identified the different factors that could potentially intensify agency conflicts and allowing managers to escape from controls.

2.1. The relationship between CEO age and agency conflicts

The age of a CEO is an important variable in our study because it allows to take into account his experience and somehow his entrenchment (*Mtanios (1997*), *Paquerot (1996)*). Therefore, it is important to know whether the CEO age is relevant for the success of an organization. Indeed, the assumption about the CEO age predicted that firm value follows a downward trend with growing age because of the neurophysiological changes documented in the cognitive ability of an ageing person.

The literature also explains these changes. In a longitudinal study covering seven age cohorts over a period of 35 years, *Schaie (1996)* found that inductive reasoning, speed of perception, the ability of digital reasoning and verbal memory demonstrates a long-term decrease with age. Decreases are generally small for those aged between 20 and 60 years, but it becomes particularly serious beyond 60. According to classical theory, *Shleifer and Vishny (1989)* found that it would be easier for older CEOs to work around governance controls, so that they can take specific decisions that other managers will not be able to properly implement. At the same time, CEOs honor implicit contracts with internal shareholders in order

to expand their power and to make them irreplaceable.

Furthermore, *Haug and Eggers (1991), Resnick et al. (2003)* and *Raz et al. (2005)* showed that the oldest CEOs seemed to disturb the management of their firms. These authors report that the physical volumes of the lateral prefrontal cortex (Note1) as well as the hippocampus (Note2) indicate a decrease with age. These places in the brain's grey matter are responsible for instabilities in its memory and cognition. All these age-related changes seem to have an impact on the CEO decision. However, the hypothesis of the specificity of the human capital of the company predicted their experience compensates for this effect. In other words, increased knowledge allows improving the company's performance and maximizing shareholder value and thus decreasing the agency costs of equity (Cline and Yore (2016)

2.2. The relationship between CEO tenure and agency costs of equity

From a theoretical perspective, the CEO tenure allows them to accumulate considerable experience (*Buchanan (1974), Vance (1983*)). In other words, seniority of the CEO in their functions may be a breeding ground for their entrenchment. They have the time needed to forge relationships with various partners, to consolidate their negotiating power, extend their dominance and form a relational network internal to the company. This seniority allows them, as a result, to influence decision-making in their favor (*Hermalin and Weisbach, (2003*)).

Hill and Phan (1991) found that the relationship between CEO compensation and firm size reinforces the managerial seniority. They will have more power to structure their compensation programs in order to improve their own interests. Consequently, former CEOs should have greater incentives to increase firm size in order to benefit from higher earnings. Thus, we expect that when seniority increases, managerial capacity increases, which in turn, leads to a greater administrative and discretionary expenditure. In the same line of thinking, *Brockman and Thistle (2009)* showed that the CEO tenure is positively, linked to their equity detention and their remuneration. These authors also asserted that firm value tends to decrease when seniority increases as it becomes more complicated to deny them the decision-making process after building their reputation over time. Moreover, *Chen et al. (2012)* showed that longer CEO tenure may not always, produce positive results and it is more likely for them to be entrenched in their positions over time. This situation allows them to form coalitions and accumulate power. As a result, they tend to have more control over the internal control mechanisms and are more likely, therefore, to pursue their own interests rather than shareholders' interests.

2.3. Managerial ownership as an entrenchment mechanism

To our knowledge, no study was able to establish the relationship between higher levels of managerial ownership and agency conflicts. Several studies give conflicting results. In accordance with the interest convergence theory (*Jensen and Meckling (1976)),* the managerial ownership constitutes a great incentive to manage the company taking into account shareholders' interests. In other words, at high levels of managerial ownership, the agency problems can be largely, mitigated due to the full alignment between managers' and shareholders' interests. Similarly, *Turong (2006)* examined the impact of the managerial ownership on the resolving agency conflicts. Examining a sample of 500 Australian companies, the author found a significant, positive relationship between managerial ownership and asset utilization. The most significant outcome of this result is that with high levels of managerial ownership, the use of firm's assets will be more efficient, thereby reducing the agencies costs. In addition, several researchers have incorporated the highest level of managerial ownership to capture the entrenchment effects. They found that managers benefit from decision-making prerogatives at the general meetings of shareholders as well as an influence on decision making by board members. This power allows them to resist from attacks of the different stakeholders, in particular large shareholders (*Allen and Panian (1982), Jensen and Warner (1988), Hermalin and Weisbach (1988), Mörck and al (1988), McConnell and Servaes (1990) and Rashid (2015*)).

Han and Suk (1998) renewed the above investigations and found that the effect of aligning interests of managers and shareholders dominates if managerial ownership is less than 41.8%. The authors showed also that, with managerial ownership levels greater than 41.8%, managers are able to control the board of directors and, therefore, their entrenchment strategy will prevails which increases agency conflicts with shareholders. In other words, managers will have sufficient power to continue their private profits at the expense of shareholders. Another study conducted by *Charreaux (1997),* based on a sample of 106 listed French companies, shows that higher levels of managerial ownership are a breeding ground for entrenched manager to maximize his utility function at the expense of the shareholder wealth. These results are confirmed by the work of *Gelb (2000) and Mamoghli et al (2007).*

Likewise, *Larcker and Tayan (2011)* argued that usually, the purpose of the managerial ownership is to provide incentives that motivate executives to improve firm performance. However, it can also be a potential to encourage undesirable behaviors. This is true when manager looks forward to increasing the value of his shares using other means than the improvement of operational, financing and investment decisions. According to these authors, four strategies can be used: (i) manipulate accounting results to inflate the share price. (ii) Manipulate the timing of option awards to increase their intrinsic value. (iii) Handling the disclosure of public information to fit more favorable allocation dates. (iv) The use of privileged information to gain an advantage in selling or to insure its interests when these actions occur.

2.4. CEO duality and agency conflicts

Surveillance capability of CEOs through the company's board of directors has attracted attention following the collapse of the Maxwell publishing group since the end of the 1980s, the UK branches of BCCI in 1991 due to losses, fraud and suspicion of involvement in criminal activities and Poly Peck in the United Kingdom. As a result, the Cadbury code (1992)

was a response to major corporate scandals associated with governance that developed and published some recommendations to reform the board of directors. This report recommends that management responsibility should be divided in order to avoid excessive decision-making powers. In the early 2000s, a wave of bankruptcy of large companies such as Enron and WorldCom have confirmed the ineffectiveness of controlling members in the board of directors when their power is consolidated by the CEO (*Rose (2005)*). Following this series of collapses, the disciplinary role of the board of directors raised a broad debate among researchers and economists. The ability to run and control depends on certain attributes such as the distribution of power among the Chairman of the board of directors and the CEO (*Pearce and Zahra (1991), Finkelstein and Hambrick (1996) and Kakabadse and al (2006)*).

Theoretical studies do not provide a consensus about as to whether or not that CEO duality may lead to better performance. Indeed, some academics found that this situation would be effective as the CEO has a better knowledge of the business environment he manages. Others consider that this situation constitutes an abuse of power since the role of the Chairman of the board of directors is to monitor the CEO, leading often to agency conflicts (*Fama and Jensen (1983), Jensen* (*1993) and Rashid (2012)*). Similarly, merging both functions is a major constraint for the board independence and reduces the likelihood of effectively performing its mandate efficiently. (*Bebchuk and al (2002)*). In the same vein, *Baysinger and Hoskinsson (1990)* showed that the board of directors may approve the situation by advocating the interests of executives.

Most of these studies agrees on the ineffectiveness of a dual structure of the Board of directors. However, other researchers have found that (CEO) duality reduces the cost of information sharing and is an important tool for management and planning (*Brickley and al (1994)*). These authors suggest that a strategy of an independent presidency does not constitute a good governance practice that would definitely improve the results of companies. Other authors have found that the accumulation of functions has no influence on the conflictual relationship between shareholders and executives. For example, *Florackis and Özkan (2004),* based on a sample of UK listed companies have shown that CEO duality has no impact on agency costs. *Mcknight and Weir (2008)* confirmed this result in the same British context.

2.5. The separation between ownership and control

The separation between ownership and control is considered as a dominant factor explaining managerial entrenchment. By increasing their participation and their voting rights, the CEOs will have the opportunity to appropriate some company funds for their own account at the expense of the shareholder wealth «private control benefits». According to *Shleifer and Vishny (1997),* the latter is one of the main reasons for the presence of blockholders around the world. Likewise, *Bebchuk et al. (2000)* showed that the Multiple Voting Shares guarantee most shareholders the largest portion of the voting rights. As a result, the power of such shareholders to extract private benefits will be greater. In the French context, which is characterized by higher capital concentration, discrepancy between ownership and control takes two forms namely double voting rights as well as pyramidal structures. When managerial ownership in a majority position and if their voting rights exceed their property rights, this guarantees for managers a decision-making power which influences the decisions taken by members of the board of directors. Therefore, *Bebchuk, al (2000), Claessens and al (2002), Lemmon, and Lins (2003)* found that this position induces a managerial entrenchment motivation and leads to increased agency costs.

2.6. Agency costs of free cash flow

According to *Brigham and Ehrhardt (2014),* free cash flow represents the cash flows available for distribution to all of a firm's investors after the firm has paid all expenses (including taxes) and has made the required operational investments to support growth. Referring to agency theory, the existence of a surplus cash flow constitutes a means for managerial entrenchment. Indeed, *Jensen (1986)* argues that high free cash flow leads to potential conflicts between managers and shareholders. After having financed their profitable projects and disposing of an excess of liquidity, the remaining flow creates a more excitement for insiders. For the shareholders, liquidity should be paid in cash dividend. As far as the managers, their interests are to receive non-financial compensation referring to unprofitable investments. These opportunistic behaviors can be happened at the expense of the shareholders' wealth and leads to a decrease in shares value.

Likewise, the presence of free cash flow may lead to inefficient use of assets. According to Jensen, (1986) and Chung and al (2005), managers tend to invest free cash flow in projects that provide indirect personal benefits while ignoring the negative current value of invested projects. On average, these investment activities can generate lower returns than the actual capital cost. Therefore, the high free cash flow increases the inefficient asset utilization when managers invest in non-profitable projects while still satisfying their personal interests and create their own compensation (*Gul (2001) and Br-Bukit and Iskandar (2009)*). Accordingly, this is an overinvestment policy adopted by managers, will enable them to increase their discretionary power and will receive higher benefits (*Narayanan (1985) and Lambert and al (1991)*).

Studying agency conflicts in Malaysian listed companies, *Iskander et al. (2012)* examined the relationship between free cash flow and asset utilization ratio. The authors found that in the presence of a strong managerial ownership, asset utilization monitoring by companies with higher free cash flow is more efficient than by companies having a lower free cash flow. However, when such detention of capital is low, there no difference in the effect of controlling asset utilization with a higher or lower free cash flow. As a result, the extent of monitoring of managerial ownership on asset utilization depends on the level of their participation in the capital as well as cash flow level.

2.7. Intangible assets and agency conflicts

According to *Warren et al. (2014),* the accounting treatments of intangible assets are similar to capital

assets. The main problems covers the determination of the initial costs, calculating depreciation and certain intangible assets, are not recognized in the financial statements because it is difficult to quantify them in monetary value. Through the intangible assets, managers can improve their position by developing specific investments. The level of incompleteness of contracts seems to increase with the intensity of the intangible assets. In addition, drafting costs and taxation of incomplete contracts may worsen when managers possess greater expertise than the shareholders and creditors. In other words, from the shareholders' point of view, given that innovation project is risky and unpredictable. The agency cost associated with this project is likely to be high (Holmström (1989)).

3. DATA AND METHODOLOGY

3.1. The Sample

For the purpose of our study of agency costs, we use a sample of 120 French companies listed on the CAC index, All Tradable over the period 2000-2014. Data on financial variables came from the WorldScoop database. Furthermore, in order to obtain information, especially those related to the ownership structure and governance practice, we have used the web page of each company. Among these 120 companies, financial institutions are excluded from the sample because of different regulation imposed on these firms. We build a balanced panel of data with 1800 firm-year observations.

Our sample is representative of all sectors with slight difference accorded to services (25%) technology (22%) and Industrial activities (17%). According to turnover and market capitalization our data is shared between small, medium sized firms (53,3%) and large firms (46,7%).

Choice of Variables and assumptions to be tested

The Dependent Variables: There are several variables to measure agency conflicts. *Tirole (2006)* has pointed out to two important indicators of these conflicts: the choice of inefficient investment thus represents ineffective or insufficient efforts spent by managers. As a result, agency conflicts should therefore depend on inefficient asset utilization because of bad investments, high production costs and unnecessary benefits that managers have. The measures that we use in this study reflect these dependencies.

- *The asset utilization ratio* ***(AUR):*** This ratio is calculated as total sales divided by total assets. It reflects the efficiency of managers in using the company assets to create sales (*Truong and Heaney (2013)*). A high ratio means that the assets generate significant sales and indicates then lower agency costs. Conversely, a low ratio shows that managers take bad investment decisions with an insufficient effort resulted in a low income. In this case, managers consume excessive unproductive assets, like cars, fancy space offices and resort properties (*Ang and al (2000)*). Therefore, this ratio is negatively associated to agency conflicts level.
- *The Discretionary operating expense ratio* ***(OPE_EXP):*** This ratio is calculated as discretionary operating expenses divided by total sales. It reflects the effectiveness in controlling operating costs, including excessive consumption of indirect benefits and other agency costs. According to *Singh and Davidson (2003),* a relatively high ratio of operating expenses may indicate excessive spending on non-sales activities. This could be a signal that shareholders wealth is expropriated by the mangers through diverting corporate resources, by increasing operational costs or investing in negative NPV projects. As a result, this ratio should be positively linked to agency costs (*Ang et al. (2000)*).
- *Administrative expenses* ***(ADM_EXP):*** This ratio is calculated as administrative expenses divided by total sales (Singh and Davidson (2003)). It includes salaries, managerial commission to facilitate transactions, travelling expenses, advertising and marketing costs, rent and some public services. In addition, administrative and other costs include the postage, Telegraph and telephone costs, transport and movement costs and the depreciation expense. This measure should reflect significantly, the managerial discretion in spending the company's resources since it follows from overspending on the indirect benefits. In other words, firms with higher administrative expenses are associated with higher agency costs of equity.

The Independent Variables: Based on the literature review, managerial entrenchment degree was operationalized by using specific indicators able to explain the management opportunistic behavior. In this study, we adopt five measures, namely: the CEO age, his tenure, the CEO duality, the higher managerial ownership as well as the separation between ownership and control.

- *The managerial age* ***(CEO_AGE):*** several empirical studies have shown that CEO age is a determinant of his entrenchment (Shleifer and Vishny (1989), Paquerot (1996) and Mtanios (1997)). However, the hypothesis of the specificity of human capital hypothesis predicted that the managerial expertise compensates this effect. According to *Cline and Yore (2016),* the acquisition of knowledge tools enables a considerable improvement in firm performance. We measure CEO age by means of a continuous variable (in numbers of years). This measure was adopted by previous studies (Rose and Shepard (1997), Barker and Mueller (2002) and Ghosh and al (2007)).

H_1*:* There is a positive relationship between CEO age and agency costs.

- *The CEO tenure* ***(CEO_TENURE):*** According to previous research, CEO tenure enables managers to form coalitions with principal shareholders, to accumulate power and forge relationships with different partners. Managers tend to have more control over the internal control mechanisms and are more likely, therefore, to pursue their own interests rather than shareholders' interests (*Brockman and Thistle (2009), Chen et al. (2012) and Hermalin and Weisbach (2003)*). Similarly, CEO tenure will be measured by years the CEO has held this position. This measure has been adopted by several previous studies (*Hill and Phan (1991), Berger et al. (1997), Rose and Shepard (1997), Ryan and Wiggins (2002) and Barker and Mueller (2002)*).

H_2: There is a positive relationship between CEO tenure and agency costs.

•*Management duality* ***(DUAL):*** Fama and Jensen (1983), Jensen (1993) and Rashid (2012) found that the accumulation of functions reduces the ability of the board of directors to monitor managers and has a positive impact on agency conflicts between managers and shareholders. On the other hand, many researchers consider duality as an important tool of reducing the costs of sharing information, business planning and management (*Brickley and al (1994) and Florackis and Özkan (2004)*). We measure duality by a binary variable, which takes the value of 1 if the CEO is the Chairman of the board and 0 otherwise.

H_3: Agency costs will be stronger when the CEO is the Chairman of the board.

•*Managerial ownership* ***($MOWN_{(50,100)}$):*** According to Mörck and al (1988), the managerial entrenchment effects prevail if management ownership is between 5% and 25%. However, this result is valid in the American context. Taking into account the distribution of the capital of French companies, we retain the measurement of *Charreaux (1991)*. The author found that when it is over 50%, the effects of managerial entrenchment is observed. In order to assess the validity of their conclusions to our sample, we consider the following measure: $MOWN_{(50,100)}$**:** a dummy Variable equal to 1 if MOWN≥50% and 0 otherwise.

H_4: There is a positive relationship between the higher levels of managerial ownership and agency conflicts.

•*Discrepancy between the ownership and control* ***(SEP_MOW):*** *Bebchuk et al. (2000)* and *Claessens et al. (2002)* found that when the voting rights exceed the property rights of the largest shareholders, this intensifies significantly the agency costs since their decisions will not be in favour of maximizing the wealth of the company. Like *Faccio and Lang (2002), Bigelli and Mengoli (2004)* and *Ben-Amar and Ahmad (2006)*, We estimate this variable using a binary measure that takes value 1 when the voting rights are greater than the property rights and the CEO is the majority shareholder in the company, 0 otherwise.

H_5: agency costs are positively related to the discrepancy between voting rights and property rights when the CEO is blockholder in the company.

•*The Free cash flow* ***(FCF)*** (note 3): Most academic research assumes that free cash flow is a source of conflicts between managers and shareholders (*Jensen (1986), Masulis and al (2007)* and *Titman et al. (2004)*). Shareholders wish that these funds should be distributed, as dividends while manager's aims to increase their compensation in the form of imputed income through unprofitable investments and ignoring the negative current value of invested projects. As a result, shareholder value will be reduced (*Gul (2001) and Br-Bukit and Iskandar (2009)*).

H_6: free cash flows (FCF) have a positive impact on agency costs.

•*Intangible assets* ***(INTANG):*** Agency costs are expected to be great for firms with higher intangible asset (note 4). The discretionary power and the likelihood of opportunistic behavior by the CEO are more verified when firm's intangible assets are important. In this context, managers may improve their bargaining power by developing specific investments (Holmström (1989)). According to *Choi et al. (2000)* and *Turki et al. (2006),* this ratio is calculated as intangible assets divided by total assets.

H_7: Intangible assets have a positive impact on agency costs.

The Control Variables: Multivariate control variables are specific to the company and commonly used in previous studies and included in our analysis as an attempt to alleviate the problem of the omitted variables, capture different characteristics of the company and the factors that potentially affect agency costs. Our control variables consists of return on capital invested, the firm size and the firm age.

•*The return on capital invested* ***(ROIC):*** performance of the invested capital is a financial measure of profitability. A business that generates a higher return than the cost of capital indicates generally that managers have deployed intelligently the company's resources. Therefore, this measure is used to assess the performance of executives and to select investment projects when it is greater than the cost of capital (*Brewer et al. (1999)*).

H_8: There is a negative relationship between the return on capital invested and agency costs.

•*The firm size* ***(SIZE):*** the firm size can have both positive and negative effects on agency costs. In fact, *Wang (2003)* showed that large companies can take advantage of economies of scale, yet they may be less effective due to managers losing control of the strategic and operational activities. In this line of thinking, *Watts and Zimmerman (1986)* suggest that firm size may be used as an indicator of a political cost since large companies can get more attention from the Government, and thus to alleviate the agency problems to a certain extent. However, Fama and Jensen (1983) have shown that agency conflicts rise progressively with an increase in firm size.

H_9: There is a (negative) positive relationship between the firm size and agency costs.

•*The firm age* ***(AGE):*** This variable measures the degree of maturity. Older firms can be more effective than younger firms and the fact that they have survived since their incorporation shows that agency costs for these companies are smaller. However, the oldest firms may reflect situations where investment opportunities that have been largely exhausted and the excess cash allows a greater misuse of resources.

H_{10}: There is a positive (negative) relationship between firm age and agency costs.

3.2. Model specification and estimation methodology

The econometric formulation proposed in this study examines the determinant of agency cost of equity.

The empirical model to be tested is presented in the following form:

$$Agency\,\text{Cos}ts_{it} = \alpha_0 + \alpha_1\, Entrenchment_{it} + \alpha_2\, FCF_{it} + \alpha_3\, INTANG_{it} + \alpha_5\, CV_{it} + \varepsilon_{it} \quad (1)$$

Where:

•Agency cost as measured by asset utilization ratio (AUR) , Discretionary operating expense ratio (OPE_EXP) and Selling, general and administrative expenses (ADM_EXP) for 120 French firms (i = 1,..., 15) and over the period 2000-2014.

•*Entrenchment is measured by five possible proxies as the managerial age* ***(CEO_AGE),*** *the CEO tenure* ***(CEO_TENURE),*** Management duality ***(DUAL),*** *Managerial ownership* ***($MOWN_{(50,100)}$)*** *, Discrepancy between the ownership and control (****SEP_MOW).***

•*FCF is free cash flow variable, INTANG is Intangible assets.*

•*CV is control variables as measured by (i) the return on capital invested* ***(ROIC),*** *the firm size* ***(SIZE),*** *the firm age* ***(AGE).***

The model will be estimated by using the panel method. Our estimation is conducted in three regressions where the difference lies only in the measurement of the dependent variable. The estimate of the three models will be processed by 'STATA software. To this end, we test homogeneity of our sample, i.e. to check for specific individual effects.

4. THE RESULTS AND DISCUSSIONS

In order to examine the determinants of agency costs of French firms, we estimate three regressions related each measure of the dependent variable. Table 6 shows the PCSE estimators for our regression models.

•Regression 1: the dependent variable is measured by *The asset utilization ratio (AUR):*

•Regression 2: the dependent variable is measured by *Discretionary operating expense ratio (OPE_EXP):*

•Regression 3: the dependent variable is measured by *Administrative expenses (ADM_EXP):*

Table 1. Results of the regression of the equation (1), (2) and (3)

Prais-Winsten regression, Correlated panels corrected standard errors (PCSEs)			
Variables	Reg(1) (AUR)	Reg(2) (OPE_EXP)	Regression (3) (ADM_EXP)
	Coef	***Coef***	***Coef***
CEO_AGE	0.00099	**-0.00674**[a]	**0.00430**[a]
CEO_TENURE	**0.00779**[a]	**0.00230**[a]	**0.00155**[a]
DUAL	**-0.06914**[a]	**0.05414**[b]	**-0.05385**[a]
MOWN(50,100)	**0.21494**[a]	**-0.05819**[a]	0.01458
SEP_MOWN	**-0.09258**[a]	0.01623	0.01499
FCF	0.06705	**-0.15926**[a]	**-0.11042**[b]
INTANG	**-0.63507**[a]	-0.04733	**0.22399**[a]
ROIC	**0.00234**[a]	**-0.00349**[a]	**-0.00090**[a]
SIZE	**-0.03177**[a]	**-0.01449**[a]	**-0.02095**[a]
AGE	**-0.02549**[b]	**-0.08487**[a]	**-0.05539**[a]
Constant	1.75694	1.88232	**0.68012**[a]
R2 overall	0.2030	0.2115	0.1459
Wald chi2(10)	4391.48	648.21	2040.09
Prob > chi2	0.0000	0.0000	0.0000
Nbr. Obs	1800	1800	1800

Notes: AUR is the asset utilization ratio. OPE_EXP is the ratio of the discretionary operating expenses ratio. ADM_EXP is the ratio of administrative expenses ratio. . CEO_AGE denotes the age of the Chief Executive Officer. CEO_TENURE is measured by years the CEO has held this position. DUAL is a dummy variable that takes 1 if the CEO is Chairman of the Board and 0 otherwise. $MOWN_{(50,100)}$ is a binary variable that takes 1 if MOWN ≥50% and 0 otherwise. SEP_MOWN is a binary variable that takes 1 when the CEO's voting rights are greater than the property rights and he is the majority shareholder in the company, 0 otherwise. FCF represents free cash flow. INTANG is a ratio that indicates the proportion of company's intangible assets to its total assets. ROIC is the return on capital invested. SIZE is the log of the total asset of the firm. AGE is the age of the firm (in logarithm). c, b and a indicate statistical significance at the 10%, 5%, and 1% levels. Estimates were obtained using panels corrected standard errors (PCSEs).

Results of the asset utilization ratio (regression 1):

The first regression connects the asset utilization ratio (AUR) to managerial entrenchment and the control variables. The results indicate that CEO tenure seems to have a significant and a positive impact on the effectiveness of the use of assets use. Knowing that the average of CEO tenure of our sample is 12 years old, this result corroborates with the assertion of *Daily and Johnson (1997)* that the CEO's professional experience, as well as their expertise allows for resisting the challenges of the business environment that they manage. The CEO duality seems to have a significant and a negative impact on assets utilization ratio of the French companies, which is in line with the view that duality, will increase agency costs. Knowing that this variable is 70.72% of our sample, it is inconsistent with the findings of *Rashid (2012)* who showed that the accumulation of functions allows managers to have enormous power by reducing the monitoring ability of the board of directors. Contrary to the results found by *Charreaux (1997)*, we found that high managerial ownership has a positive association with asset utilization ratio. We can conclude that managers try to maintain a good reputation of their businesses by minimizing agency conflicts.

These results support predictions put forth by the theories of *Jensen and Meckling (1976)* who

predicted that that agency costs vary inversely with the managerial ownership. It seems that when CEO's voting rights are greater than property rights and he is the majority shareholder in the French company, the entrenchment effect is observed. Accordingly, the CEO can manage the company in his own interests rather than the shareholders' interests. Regarding the impact of the Free cash flow (FCF) on assets utilization ratio, the results show that the sign of the coefficient of this variable is positive but not significant. We conclude that in the presence of a strong managerial ownership, monitoring assets utilization among companies with higher free cash flow is more efficient than companies with a poor free cash flow. In addition, French companies in our sample are characterized by a high ownership concentration; therefore, we can predict the role of large shareholders in monitoring managers on the use of free cash flow.

By estimating the control variables, the empirical test results show that the coefficients of performance of the invested capital, size, and age of the French company are negative and statistically significant at the 1 % significance level. These results are consistent with the findings of Fama and Jensen (1983a, b) which showed that agency conflicts increase gradually with increasing size of companies. Likewise, the oldest firms may reflect situations where investment opportunities have been largely exhausted and the cash surplus allows for greater misuse of resources.

Results of the operating expense ratio (regression 2):

Regression 2 estimating the impact of the different strategies of managerial entrenchment on agency costs as measured by the ratio of operating expenses to annual sales ratio. The results indicate that CEO AGE seems to have a significant and a negative impact on the operating expenses ratio. Our result is consistent with the findings of *Cline and Yore (2016)*; which indicated that managerial experience, as well as the acquisition of knowledge of the company, allows him to improve the company's performance and shareholders value. This result also joined empirical work from *Klein (1998) and Dowen (1995),* who suggest that long time spent as a manager within the company allows him to know the different technical specificities of the business sector. Therefore, the manager will benefit from mature business skills and this allows him to control expenses (*Finkelstein and Hambrick (1990) and Zan (2002*)). On the other hand, CEO tenure seems to have a significant and a positive impact on the operating expenses ratio, which is in line with the view that higher CEO tenure will increase agency costs.

The coefficient of the variable (DUAL) is significant and positive which confirms the predictions of agency theory, which assumes that duality is a potential source of conflicts between managers and shareholders (*Shleifer and Vishny (1986)*). Therefore, the accumulation of functions reduces the ability of the board of directors to monitor managerial decisions. Our results also indicate that the negative sign of the coefficient on high managerial ownership ($MOWN_{(50,100)}$) is not consistent with that found by *Charreaux (1997)* in his study of French companies. Indeed, with a high level of detention, managerial ownership is an excellent incentive to manage the business taking into account shareholders' interests. The results in table 6 also show a significant negative relationship between FCF and the operating expenses ratio, which means that FCF will decrease agency costs.

Results of Administrative expenses (regression 3):

Regression 3 estimating the impact of the different strategies of managerial entrenchment on agency costs as measured by the administrative expenses divided by total sales. The results indicate that CEO age and tenure seem to have a significant and a positive impact on agency costs. Given that the average age of managers in our sample is 54-year-old with a maximum value of 81 years. We can deduce that the older the CEO is; the easier to deal with governance mechanisms, in a way he can make specific decisions that other managers will be unable to implement correctly (*Shleifer and Vishny (1989)*). In addition, experience accumulated through managers seniority allows them to build relationships with various partners, thus consolidating their negotiating power, extending their dominance and influence, as a result, maintaining the decision-making process in their favor (*Hermalin and Weisbach (1998, 2003)*).

With regard to management duality, our third hypothesis is not confirmed. The coefficient of the variable (DUAL) is significant and negative. We can deduce that the duality acts as an internal governance mechanism controlling the administrative expenses. This result shows that duality allows the CEO to have a good knowledge of the companies they manage. We find that high levels of managerial ownership have a positive coefficient but not statistically significant. This result means that managers, with this the level of detention, are passive with respect to controlling administrative expenses. We can also see that their managerial discretion may result from specific investments related to intangible assets (INTANG). In addition, the positive sign of this variable suggests that managers take advantage of their expertise as well as information asymmetry with shareholders and creditors by increasing their spending via indirect benefits.

This result confirms the work of *Holmström, (1989)* pointing to the importance of intangible assets in the explaining managerial discretionary behavior. Considering that free cash flow is an important determinant of agency conflicts including administrative expenditure, the empirical results show the inverse relationship, which is consistent with the findings of *Wang (2010).* This author has observed that the free cash flow can be generated thanks to mangers' prudent spending in order to avoid negative consequences on their careers. Finally, in accordance with regression 1 and 2, the control variables regression (SIZE) and (AGE) have a significant and negative impact (at the 1 % level) on the administrative expenditure, which also shows that agency conflicts related to these expenses decrease gradually with the increasing size and age of companies.

5. CONCLUDING REMARKS

The aim of this study was to identify the different determinants of agency conflicts between managers and shareholders in the French context. We have

presented the contributions of agency theory in establishing a framework of corporate governance. This theory has given particular attention to two principal partners, who are managers and shareholders. Each of them has interests that differ from the other groups. Using data on 120 listed French companies for the years 2000-2014, we integrated different managerial entrenchment measures in order to study their impact on agency conflicts. We have used three measures of conflicts namely asset utilization ratio, discretionary operating expense ratio and selling, general and administrative expenses ratio. After having checked the multicollinearity and the correlation, eight variables have been selected in the model.

We have also introduced the control variables of firm size and age. Our results show that all managerial entrenchment strategies seem to have contradictory effects. Indeed, the CEO age with a negative sign appears to be a governance mechanism for French companies of assets utilization and operating expenses level. However, this variable positively relates to administrative expenses and thus plays in favor of managerial opportunism. We found also that CEO tenure allows him to master the management of his business by improving the efficiency of its assets. However, the latter took advantage of its effect on administrative expenditure. The results also show that the CEO's discrepancy between voting rights and the property rights is a primary determinant of entrenchment, especially when the CEO is the majority shareholder in the company.

NOTES

1. The prefrontal cortex is the anterior cortex of the frontal lobe of the brain, located in front of the premotor areas. This region is the headquarters of different higher, so-called cognitive functions (including language, working memory, reasoning, and more generally the executive functions). It is also the region of taste and smell. It is one of the areas of the brain, which underwent the largest expansion in the evolution of primates to hominids.

2. Hippocampus is one of the first structures affected by Alzheimer's disease, which explains the memory and disorientation problems that characterize the appearance of this neurodegenerative pathology. Hypoxia (oxygen deprivation), encephalitis, and temporal lobe epilepsies are also the conditions with lesions to the hippocampus. People undergoing severe damage to the hippocampus are likely to suffer from different types of amnesia.

3. Jensen (1986) defined free cash flow as the set of positive net funds available after all projects to current value. We calculate free cash flow, referring to Thomson one banker, as follows: FCF = cash flow from operational activities - cash dividends paid to shareholders - capital expenditures)

4. The intangible assets included trademarks, patents, licenses, copyrights, patents, franchises and trademarks.

5. Statistically, the linearity occurs when some of the columns of the matrix X (matrix of values corresponding to the independent variables) are almost linearly dependent. In this case, the matrix X'X is quite reversible but the regression results are very unstable and therefore hardly interpretable.

6. Typically, bright is acceptable threshold advocated by *Emanuel et al. (2003)* is 4. For his part, Hamilton (1992) to shown that greater than 0.2 and a tolerance bright 4 below allow the lack of multicollinearity.

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