

# Family Governance is Not the Problem: Evidence from Dual-Class Shares

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# Family Firms Face a Persistent Critique

## What governance reformers say

- Concentrated ownership creates entrenchment
- Dual-class shares harm minority investors
- Family succession destroys value
- Dispersed ownership is the governance ideal
- Index providers should exclude dual-class firms

These criticisms are taken seriously by regulators and governance rating agencies.

## What the evidence shows

Family firms **persist and outperform** across generations and countries.

Sophisticated institutional investors **hold more**, not less, of dual-class shares.

Minority investors in family-controlled firms **earn a positive risk premium**.

Something important is being missed.

# Two Puzzles the Standard View Cannot Explain

## The diversification puzzle

Standard portfolio theory says diversification is valuable. Yet founding families hold **concentrated, illiquid, undiversified** positions in a single firm, often across generations.

If family control is purely extractive, the private benefits would need to be implausibly large to justify forgoing diversification.

Why do families stay?

## The dual-class puzzle

Dual-class shares are associated with valuation discounts of 15–20% and are widely criticized as harmful to minority investors.

Yet these structures are even more common and popular over the last 2 decades.

And investors continue to demand **more** of these shares, not less.

Why do investors keep buying them?

# A High-Stakes Test

## The conventional narrative on dual-class shares

- Insiders retain disproportionate voting power
- Significant valuation discounts of 15–20%
- Calls to ban or restrict these structures
- Index providers excluding dual-class firms

## These structures have surged

1% of IPOs in 1980 to nearly 49% today

## The predictions to test

If minority shareholders are harmed

Sophisticated investors avoid these firms

Outside investors earn **negative** abnormal returns

If the market compensates for commitment risk

Sophisticated investors hold more  
Outside investors earn **positive** risk-adjusted returns

# The Missing Variable. 89% Are Family Firms

## Russell 3000 industrial firms, 2001–2017

(Anderson et al., 2025)

- **89%** of dual-class firms are family-controlled
- Families hold the super-voting class almost exclusively
- Average family holds 29.8% of cash flow rights and 57.9% of votes
- Prior literature compares dual-class to all single-class firms

Dual-class firms should be compared to **single-class family firms**, failing to do so conflates the effects.

## Russell 3000 composition

Group	Share
Single-class nonfamily	65.8%
Single-class family	24.9%
<b>Dual-class family</b>	<b>8.3%</b>
Dual-class nonfamily	1.0%

*Dual-class is not primarily a share structure story. It is a **controlling shareholder** story.*

# Who Actually Holds These Shares

## Institutional ownership of freely floated shares (OLS, Russell 3000)

	Coefficient	t-statistic
All dual-class firms	+2.9%***	(3.94)
Dual-class <i>family</i> firms	+3.9%***	(4.94)
Dual-class <i>nonfamily</i> firms	-3.1%	(-1.70)
Single-class family firms	+0.2%	(0.51)

Controls include size, age, leverage, ROA, volatility, R&D/sales, year and industry FE

Institutions hold **more**, not less, of these shares. Confirmed for both index and non-index funds, robust to 13F data.

The effect is **entirely driven by family firms**. Dual-class nonfamily firms show the reverse pattern.

*Sophisticated investors are not fleeing these structures. The harm narrative does not survive this test.*

# The Control Risk Premium

Annual abnormal returns, 2001–2017 (single-class nonfamily as benchmark)

Group	Ind.-adj.	Mkt.-adj.	FF-adj.
All dual-class	+250 bps**	+230 bps**	+220 bps**
Dual-class <b>family</b>	+340 bps***	+320 bps***	+250 bps**
Dual-class <b>nonfamily</b>	+80 bps	+60 bps	+300 bps
Single-class <b>family</b>	+190 bps***	+170 bps**	+110 bps
Single-class nonfamily	0	0	0

## The central finding

The premium follows **family control**, not share structure. Single-class family firms earn it. Dual-class nonfamily firms do not. The wedge between votes and cash-flow rights is not what is being priced. The controlling family is.

# The Premium Is Systematic. It Reverses in Bad Times

## Family firms underperform in adverse industry conditions

Adverse shock measure	Extra return for family firms	t-statistic
Negative sales growth shock	-440 bps	(-2.41)
Negative employment growth shock	-350 bps	(-2.07)
Negative net income shock	-380 bps	(-2.27)
Negative ROA shock	-280 bps	(-1.73)

Family firm returns **co-move more** with each other than with nonfamily firms. A shared systematic risk factor.

Controlling shareholders protect their own interests in downturns. Precisely what the commitment mechanism predicts.

*Outperform in good times, underperform in bad times. This is what a genuine risk premium looks like.*

# The Neglected Governance Problem

## So why do family firms earn this premium?

Many firms depend on parties who make investments **specific to the relationship** and difficult to redeploy

- Suppliers retool production for a buyer
- Employees accumulate firm-specific capital
- Communities that bend local resources

These investments only create value if the firm **does not exploit them afterward**. But courts cannot enforce the things that matter most in long-run relationships.

## The commitment problem

Stakeholders already know the firm promised to behave well. Firms always say that.

What they want to know is whether anyone will actually **keep those promises** once their investment is sunk.

If they doubt it, they under-invest or avoid the relationship entirely. Value is destroyed before expropriation even occurs.

# Why Family Ownership Solves It

## The mechanism

Commitment is credible when the owner's personal cost of defection outweighs the gain from exploitation. **Family ownership creates three channels of exposure**

- 1 **Financial lock-in.** Concentrated, illiquid stake. Costly to exit before reputational damage arrives.
- 2 **Reputational bundling.** Family name and personal standing suffer even after selling.
- 3 **Control-rights visibility.** Stakeholders can verify who decides.

## Dispersed vs. family ownership

Dispersed owners can sell before reputational consequences arrive. Damage does not land personally.

Family owners cannot easily exit. The family name survives any financial restructuring. Damage is personal and lasting.

**The firm's governance structure determines whether its promises are worth making.**

# Succession as a Commitment Problem

## The standard question

Why do families choose heirs over better outside managers?

## The standard answers

- Altruism (Bertrand et al., 2008)
- Private benefits and socioemotional wealth (Gómez-Mejía et al., 2007)
- Tacit knowledge transmission (Burkart et al., 2003)

## The commitment answer

Families are preserving **exposure**, not talent or preferences. What transfers at succession is the bundle of channels for credibility.

## The discriminating prediction

The effect of succession type on performance should be near zero in **low-relational-intensity** industries and large in **high-relational-intensity** industries.

A continuous interaction could follow from many theories. A **threshold** where succession type is completely irrelevant requires a commitment story.

*Reeb and Zaldokas (2026, WIP), Inherited Credibility*

# The Organizing Framework of Corporate Governance

## The dominant view

- Governance means disciplining insiders
- Boards protect shareholders from managerial opportunism (Fama and Jensen, 1983)
- Independent directors, dispersed ownership, and contestability are the instruments
- Family control means entrenchment, extraction, and governance failure

**This framework has real content.**

It is well-suited for widely-held firms.

## The problem

Family firms are the dominant organizational form globally (La Porta et al., 1999; Faccio and Lang, 2002).

In family firms, ownership and control are **not separated**. The framework's central assumption does not hold.

Applying it anyway may produce the wrong diagnosis and the wrong prescriptions.

# Policy. The Wrong Diagnosis Produces the Wrong Cure

## The current regulatory impulse

- Exclude dual-class firms from indices
- Mandate independent board majorities
- Impose sunset provisions on super-voting shares
- Treat dispersed ownership as the governance ideal

## What the evidence says

- Markets already price expropriation risk at 250 bps per year
- No net harm to minority investors

## The deeper cost

Governance reforms that force dispersed ownership destroy commitment capacity.

The cost falls on **employees, suppliers, and communities** in relationship-intensive industries, not on minority shareholders.

Estate taxes that force asset sales at succession impose the same cost.

# Conclusions

- ① **The monitoring framework is the wrong lens for family firms.** The binding governance problem is making credible promises to stakeholders, not disciplining insiders.
- ② **Family ownership is a commitment technology.** Concentrated, illiquid stakes bundle family wealth and reputation with firm behavior in ways dispersed ownership cannot replicate.
- ③ **Dual-class share evidence confirms this.** Sophisticated investors hold more of these shares. Minority investors earn 250 bps per year. The premium follows family control, not share structure.
- ④ **Policy aimed at dispersed ownership as the governance ideal may destroy more value than it protects,** for stakeholders, not just shareholders.
- ⑤ **Family governance structures are not obstacles to purpose.** They are a solution to a credibility problem.

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# The Commitment View Inverts the Standard Predictions

<b>Feature</b>	<b>Monitoring view</b>	<b>Commitment view</b>
Concentrated ownership	Entrenchment risk	Raises owner exposure, sustains relational contracts
Family control	Extraction of private benefits	Bundles reputation with firm behavior
Long-tenured directors	Captured board, weak oversight	Deepens reputational stakes, raises cost of defection
Family governance persistence	Resistance to reform	Rational response to contractual incompleteness
Minority investor returns	Should be low (harmed)	Should be positive (compensated for systematic risk)

# Calendar-Time Portfolios. The Premium Is Robust

## Long portfolio of family firms vs. nonfamily benchmark

Asset pricing model	Annual $\alpha$ (OLS)	Annual $\alpha$ (WLS)
Market model	+5.5%**	+9.8%***
FF three-factor	+3.0%**	+4.1%***
FF five-factor	+4.6%***	+6.6%***
FF five-factor plus momentum	+4.3%***	+5.6%***
Long-short portfolio	+1.9% to +2.7%	+2.2% to +2.9%

WLS weights by number of firms in portfolio each period

*The premium is not an artifact of buy-and-hold methodology.  
It survives every asset pricing model we apply.*

# Boards as Commitment Infrastructure

## Family-friendly directors in the monitoring view

- Long tenure means a captured board
- Family ties mean weak independence
- Embeddedness means governance failure

## Family-friendly directors in the commitment view

- Long tenure deepens reputational attachment
- Personal standing is non-portable across firms
- If the firm defects, damage falls on

*Credibility benefits rise with relational reliance*

