Control Motivations and Capital Structure Decisions  
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Abstract  

This paper investigates the impact of corporate control motives on the firm’s capital structure decision. Blockholders with high control motivations face a trade-off between getting external finance and losing or diluting their control over the firm’s decisions. Debt offers a solution to this dilemma while external equity does not. We hypothesize that firms with blockholders that value control should have higher debt-equity ratios. Furthermore, we also hypothesize that debt is used more where control is valued most: in countries where minority shareholders rights are not well-protected and where losing control would cost the most. Risk-reduction motivations provide the competing hypothesis to control. In such a case, undiversified blockholders would want to decrease leverage to reduce firm specific risk in their undiversified portfolios. We investigate the impact of family blockholders because these are the best example of shareholders who, on one hand, value corporate control most and, on the other, have undiversified portfolios. We use 3,608 firms from 36 different countries and find that, after controlling for all variables identified by the existing literature, control motives influence capital structure decisions significantly. Family firms have higher leverage relative to nonfamily firms and they have even higher leverage in countries where minority shareholders are least protected. Families are found to use leverage in a strategic way. They use it less when (a) they possess control-enhancing mechanisms, and (b) when their stake is high enough that can allow them to have control anyway.

Keywords: Ownership Structure; Corporate Control; Capital Structure; Family Firms; International