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ABSTRACT

This paper examines the incentives of controlling shareholders in the market for corporate control. We investigate the takeover premiums paid by a sample of European acquiring firms with concentrated voting rights structures. The results show a positive relationship between takeover premiums and the bidder's concentration of both voting rights and excess voting rights over cash-flow rights. With higher levels of bidder entrenchment, the valuation of a takeover target increasingly reflects the private benefits of control which bidders seek to extract from a deal**.**

Keywords: Controlling shareholders, separation between the ownership and the control, takeover premiums, private benefits

JEL Classifications: **G32, G34**

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I Introduction

Mergers and Acquisitions (M&A) represent distinct managerial initiatives with measurable consequences for corporate performance. A vast and growing literature on the performance implications of M&A finds that many deals lead to disappointing post-M&A performance. As a result, M&A are widely viewed through the prism of an agency cost framework (Shleifer et Vishny (1997); Erickson and Wang (1999). For instance, management may seek acquisitions not to create value for shareholders, but instead in an attempt to diversify their employment risk (by smoothing corporate earnings over time). Alternatively, managers may seek acquisitions in order to increase company size. This would allow managers to consume perquisites such as increased prestige and executive remuneration in the post-M&A period. However, when ownership structure in bidding firms is concentrated, the main merger-related conflict of interest between managers and dispersed shareholders is replaced by concerns over how large shareholders may use M&A to expropriate minority shareholders (La Porta, 2002).

Controlling shareholders may expropriate other shareholders by investing the firm's resources such that to maximize their personal interests especially when investor protection is weak (Bae et all (2002)) or when voting rights exceed broadly cash-flow rights (Claessens et al. (2002); Cronqvist and Nilsson (2003)). When controlling a large share of the voting rights, shareholders are able to make strategic decisions such as acquisitions without significant opposition from minority shareholders. Controlling shareholders are, hence, likely to pay more for deals which satisfy their personal interests. Therefore, higher takeover premiums may be an indicator of the various private benefits which a controlling shareholder intends to extract from a deal. Private benefits of control represent the resources extracted by the control coalition which are not shared with minority shareholders. Such benefits are often pecuniary and involved opportunities for insider trading or inflated salaries where the controlling shareholder holds a position in the firm. However, the private benefits of control which controlling shareholders seek to extract from a deal may also be non-pecuniary such as enhanced prestige and reputation.

As pointed out by Dyck and Zingales (2004), private benefits of control are difficult to observe and even more difficult to quantify in a reliable way. In this study, we employ the acquisition premiums paid by a sample of bidding firms with controlling shareholders as an indicator of the private benefits which bidders link to control.

We base our study in Europe for a variety of reasons. First, concentrated ownership is the norm in most European countries. Faccio and Lang (2002) report that 63% of publicly-traded firms in Europe have a shareholder which controls more than 20% of the voting rights. In the US, 28%

of listed firms have a large shareholder who controls 20% or more of its votes (Gadhoum, Lang and Young (2005)). Second, most European firms suffer from relatively weak investor protection regimes. This leaves controlling shareholders with fewer constraints when pursuing their private objectives. Finally, most European public firms are affiliated within a business group (Faccio, Lang and Young (2001)). Bae et al (2002) show that within diversified business groups, controlling shareholders may exert power over subordinated firms which is in excess of the cash-flow rights. The devices enabling a shareholder to control a firm while retaining only a small fraction of the cash-flow are pyramidal groups, cross-holding and dual or multiples class share structures. Generally, these mechanisms allow controlling shareholders to entrench themselves within the firm and to circumvent monitoring mechanisms put in place by minority shareholders.

Previous empirical studies which highlight the relationship between ownership structure and M&A offer mitigated results. Most of these studies attempt to explain the merger motives of controlling shareholders. Johnson and al (2000) show that controlling shareholders use M&A to create groups of firms which transfer resources for their own benefit. Bigelli and Mengoli (2004) study acquisitions by listed Italian firms and find that when acquisitions occur within a pyramidal group, the price may be set so as to transfer wealth from those companies located in the bottom of the pyramidal chain to companies situated at the upper levels. Holmen and Knopmf (2004) find that in Swedish mergers with dual owners (who control both the bidder and the target), there is a transfer of wealth from bidders to target shareholders. Dual owners are more likely to initiate diversifying mergers and they overpay for targets with higher ROA in order to overcome capital constraints within their pyramids.

However, controlling shareholdings may not necessarily extract private benefits. Instead, controlling shareholders may play an active governance role and monitor management activities. Shleifer and Vishny (1986) were among the first to discuss the role of the large shareholder as a monitor who and creates shared benefits for all equity holders. Kaplan and Minton (1994) and Kang and Shivdasani (1995) show that firms characterized by the presence of large shareholders are more likely to replace managers due to their poor performance. La Porta et al. (2002) find higher valuations of firms with more concentrated cash-flow rights held by the controlling shareholder.

Consistent with this view, some studies reject the hypothesis that controlling shareholders expropriate minority shareholders in the market for corporate control. Buysschaert, Deloof and Jergers (2004) find positive and significant cumulative abnormal returns for Belgium firms up and down pyramidal groups. The authors suggest that controlling shareholders use equity stake

sales to create more transparent firm groups. Ben Ammar and André (2006) and Faccio and Stolin (2006) do not confirm that controlling shareholders use M&A to extract private profits. These authors suggest that good legal and extra legal institutions can make such expropriation too costly for the controlling shareholders.

To examine whether a bidder's controlling shareholder experiences private wealth from M&A transactions, previous studies focus on the performance around the announcement date using event study methodology (Bae et al (2002); Holmen and Knopmf (2004); Buysschaert, Deloof and Jergers (2004); Ben Ammar and André (2006) and Faccio and Stolin (2006)) or the operational performance (Tze Yu Yen and André (2007)) or the return differentials of equity with different voting rights at the announcement date (Bigelli and Megnoli (2004)). In this study, we examine the expropriation of private wealth by bidders by analyzing the premium offered in a deal. Studies which focus on control block transactions have considered the premium as a measure of private benefits of control. Arguably, it may be misleading to use acquisition premiums as a measure of private benefits in general samples of M&A because premiums also reflect the expected deal synergies for which an acquirer is prepared to pay. However, our study focuses on the special case of M&A initiated by bidders with concentrated voting rights. In this case, the major corporate decisions are made by the controlling shareholder. We may therefore assume that the controlling shareholder is willing to overpay for deals which satisfy his or her personal interests. Higher takeover premiums can then be interpreted as a proxy of the private benefits which the bidder's controlling shareholder intends to extract from an acquisition.

Our approach to approximate the private benefits by using acquisition premiums follows Barclay and Holderness (1989), Barclay and Holderness (1991), Bebchuk (1994), Burkart et al (2000), Nicodano and Sembenelli (2004), Dyck and Zingales (2004), Atanasov (2005) and others. These studies analyze the premium linked to private block sales of voting shares. In public transactions, there are usually legal rules that require the equal treatment of all target shareholders. However, in our case, we are interested basically in the expropriation of the minority shareholders in the bidder. We conceptualize the overpayment for targets as an agency problem between controlling shareholder and minority shareholders within the bidder. Therefore, by analyzing bidder ownership structure, our contribution is to show that takeover premiums reflect the private benefits in public takeover transactions as well.

Our findings can be summarized as follows. The main finding reveals a positive relationship between takeover premium and the entrenchment instruments of the bidder's controlling shareholder. In our case, the entrenchment is indicated by the high level of voting rights and the

level of separation between the ownership and the control when the cash-flow rights are low or when the bidder is controlled through other corporations. Within these ownership structures, we interpret our result as evidence that acquisition premiums reflect the private interests of the controlling shareholder. We also find that bid premium in a concentrated voting rights setting are positively affected by the activity relatedness of bidder and targets and negatively affected by the bidder's leverage as well as a number of other bidding firm characteristics.

The rest of the paper is organized as follows. Section II describes the methodology including the data sample and the variables. In section III, we report our analysis. Section IV summarizes and concludes.

II. Data and Methodology

II.1. Sample

We obtain our sample from Thomson Financial's Mergers and Acquisition Database (SDC). We collect data for deals which were announced by bidding firms located in Austria, Belgium, Finland, France, Germany, Ireland, Italy, Norway, Portugal, Spain, Sweden, Switzerland, and the UK between 1994 and 2001. We excluded exchange offers, repurchases, recapitalizations, self-tender offers, spin-offs, acquisitions of minority interests (less than 10%). Further, we restricted to transactions deals where there was a reported transaction value or price per share. Both bidders and targets are publicly traded firms.

We merge merger data with ownership data from Faccio and Lang (2002). Faccio and Lang (2002) provide ownership and group affiliation data for 5,232 firms from 13 European countries. The ownership data are collected from various sources between 1996 and 1998. Barclay and Holderness (1989) find that once a firm has a large block shareholder (independent of whether the blockholder or a representative sits on the board of directors), the firm usually has a blockholder five years later. Hence, we choose our sample period as 1994 - 2001.

Following Cronqvist and Nilson (2003), we define a shareholding as controlling if a single shareholder controls more than 25% of the voting rights. Cronqvist and Nilson (2003) note that shareholdings of 25% of voting rights tend to be sufficient to control a firm's main corporate decisions.

Finally, we verified various deal characteristics (announcement date, deal value, etc.) against news sources on LexisNexis. We excluded deals due to inconsistencies between the data

supplied by Thomson Financial and the information provided by the press coverage. Further, we exclude deals which are linked to the exercise of a call option on the target's shares. In these cases, the takeover premium is likely to have been determined by factors prevailing at the time period the option was underwritten. Finally, bidders must have financial and accounting data on the Datastream / Worldscope database. This leaves us with a final sample of 231 deals by bidders with concentrated voting rights structure.

II.2 Acquisition Premiums

As standard in the literature, we define the premium as the excess of the price paid for the target above its pre-acquisition market value four weeks (28 days) before the announcement date supplied by Thomson Financial (e.g., Jarrell et al (1988); Jarrell and Poulsen (1989); Sharma et al (1991); Cotter and Zenner (1994)). Four weeks allows for adequate time to avoid information leakage (Nathan and O'Keefe (1989)) and it is short enough to avoid contamination effects from other events (Flanagan and O'Shaughnessy (2003)). Premiums are computed using market data from Datastream in the following manner:

$$\text{Premium} = \frac{\text{Price per share} \ - \ \text{Target stock price 4 weeks before the announcement date}}{\text{Target stock price 4 weeks before the announcement date}}$$

II.3 The Model

In our study, we establish several models according to the following format:

$$\text{Premium} = \alpha + \sum_{i=1}^{n} \beta_i \, \text{OWNERSHIP} + \sum_{j=1}^{m} \beta_j \, \text{control} + \text{O}_i \qquad (2)$$

OWNERSHIP is a vector of ownership variables that includes the percentage of voting rights held by the bidder controlling shareholder (votes); the percentage of cash-flow rights held by the bidder controlling shareholder (own) ; a dummy variable equals one when there is a separation between ownership and voting rights (sepa); the excess of this separation as the percentage difference between ownership and voting rights (excess); a dummy variable equals one when the firm has outstanding non-voting, limited voting or multiple voting shares (dual); a dummy variable which equals one if the controlling shareholder controls the bidder through other firms (indirect) and a dummy variable which is equal one when there is one other owner that controls at least 10% of voting rights (other).

The vector of control variables include the relative size of the target compared to the bidder measured by target total assets divided by bidder total assets (Rsize). This variable helps us understand if bidders value the opportunity to grow fast via M&A. Then, we include three bidder specific variables. Since we focus on agency conflicts between controlling shareholders and minority shareholders, we use the dividend payout ratio (DPR) measured as the ratio of dividends to net income (in the last twelve months). Firms that use to pay higher dividends are constrained not to waste funds; therefore, we expect that the dividend payout ratio will be negatively related with takeover premiums. Second, we include the ratio of cash flows to net sales (CFS). We assume that bidders with high cash flows are in a better position to overbid. Third, we include bidder leverage as measured by the ratio of total debt to total assets one year prior to the acquisition (leverage). We assume that highly leveraged bidders are less likely to engage in negative net present value projects and will, hence, be less likely to overpay in acquisitions. Consequently, we expect a negative association between leverage and takeover premiums.

We also include a number of deal control variables. First, we include the number of bidders that bid for a target (Nbidders). We expect that a high number of bidders stimulates the target's bargaining power and, thus, increases the takeover premium. Second, we control for if a bidder has previously held a toehold in a target (toehold). We use a dummy variable which is equal to one when the bidder has held shares in the target before the announcement. If the bidder holds a significant part of the target's equity before the offer, it may implement a pressure on target managers. We expect large toeholds to be negatively related to bid premiums. Third, we control for the industrial relatedness between bidder and target (relatedness). We include a dummy variable which is equal to one if the acquiring and target firms share the same 2-digit SIC code. We expect that controlling shareholders will be paying higher premiums for unrelated deals, because, this type of deal is more likely to serve their private interests. Fourth, we include the method of acquisition payment through a dummy variable which is equal to one when the payment is 100% cash (payment). Through cash payment, the controlling shareholder is more likely to keep its control. Moreover, stock payment may be linked to higher acquisition premiums if bidders believe their equity is overvalued. Finally, we control respectively for the value of the transaction (size_tr), whether or not a deal is hostile (hostility) (control contests are likely to drive up premiums), and whether or not the deals takes the form of a tender offer (tender). Tender offer are market offers which require all shareholders to be treated equally. We expect that controlling shareholders in the target are unable to fetch a higher takeover price in privately-negotiated transactions. Therefore, tender offer should be positively related to acquisition premiums.

Country control variables include first real GDP growth (GDPG) measured to proxies for changes in economic conditions. Second, we include the ratio of the number of domestic firms listed in a given country to its population (in millions) (market) as a proxy for the liquidity of local stock markets. Stock markets with a higher number of traded firms tend to be more liquid and as a result the informational efficiency of assets traded on these exchanges will be different from that of country with few listed firms. We hold no a prior expectations as regards the impact of this variable on merger premiums. Finally, we include government effectiveness (govern) which combines various indicators of the ability of the government to formulate and implement sound policies. We find in unreported correlation tests, that the two last variables are highly correlated, we include only one of them depending in each model.

II.4 Descriptive statistics

Panels A, B and C of Table 1 report respectively the number of premiums by year, by country and by industry. Table 2 reports the descriptive statistics for all variables. The mean of our dependant variable, the PREMIUM is 44.39%. This does not indicate particular overpayment behavior by firms with concentrated voting rights. Laamanen (2007) finds that the average premium paid in acquisitions has been between 40% and 50% over the past 20 years. The separation between ownership and control and its devices do not seem to be the rule in our sample. Only one-third of the bidders have ownership structures where voting rights exceed cash-flow rights. Roughly, one in four bidders have dual-class share structures and 20% have of a controlling shareholder monitoring bidders indirectly. The mean of the variable of other blockholders (33.76%) is similar to that in Laeven and Levine (2008) who find that over one-third of listed firms in Europe have more than one large owner.

One the other hand, the mean of industrial relatedness (54.11%) does not show a particular preference for unrelated deals. However, pure cash payment represents more than 65% of our sample. In studies which examine general merger samples which do not require ownership criteria, the pure cash payment is less than 50% (38.7% in Betton et al (2009); 40.4% in Moeller et al. (2004); 37.6% in Dumontier and Petitt (2002); 35.4% in Andrade et al (2001)). So, we suggest that bidders with concentrated voting rights prefer to finance acquisitions via cash payments. This is because controlling shareholders intend to maintain their position of control and stock payments may dilute this position. Consistent with this, Faccio and Masulis (2005) find that incentives to choose cash are particularly strong in bidding firms with relatively concentrated ownership structures. Eckbo (2009) argues that bidding firm managers opt for cash over stock to avoid diluting the private benefits of control.

[Insert about here Tables 1 & 2]

III ANANLYSIS

In order to determine how the incentives of bidder controlling shareholder are reflected in takeover premiums, we examine, in a multivariate setting, the relationship between takeover premiums and the extent to which bidding firm shareholders exert control as well as the arrangement which underlie this. The following sections examine the effects of voting rights, cash flow rights and excess voting rights, respectively.

III.1 Voting Rights and Premiums

Claessens et al (2002) indicate that the positive incentive effect relates to the share of cash-flow rights held by large shareholders and the negative entrenchment effect relates to the share of control held by large shareholders. The concentration of voting rights in the hands of a single controlling shareholder may reduce the effectiveness of governance mechanisms within a company and weaken its disciplinary. The controlling shareholder may easily divert corporate wealth and expropriate minority shareholders. Holderness (2003) argues that blockholders have the incentive to use their voting power to consume corporate resources or to enjoy corporate benefits that are not shared with minority shareholders. Burkart, Gromb, and Panunzi (1997) provide a theoretical model which suggests that tight control of large shareholders constitutes an ex ante expropriation threat that reduces managerial initiative and non-contractible investments. Holmen and Knopmf (2004) find that dual owners improve their control in the bidder by acquiring more voting rights when other shareholders are likely to oppose an acquisition. Therefore, if the premium reflects the private benefits of control, it should be positively associated with the voting rights held by the bidder controlling shareholder.

[Insert about here Table 3]

Table 3 presents the results of our linear regressions of premiums on voting rights. After controlling for variables, such as relative size of target, bidder financial ratios, deal

characteristics and country indicators, we conclude from the first model that voting rights affect significantly and positively the premium. Moreover, we use the square (as in McConnel and Servaes (1990) and (Faccio and Lasfer (1999)) and the cube (Short and Keasey (1999) and Tze Yu Yen and André (2007)) of the percentage of voting rights held by the controlling shareholder in order to capture the impact of high levels of ownership. The three first models show that as voting rights increase, the impact on the premium becomes more significant. Model 4 shows that at lower level of voting rights, the impact becomes negative but insignificant and significantly positive at higher levels. Using this last model, we found that the inflexion point, i.e., the level where the voting rights start to have a positive impact on premiums is 41.70% which is close to the voting rights median (42.5%). Bozec and Laurin (2008) note that dominant shareholders can still use the control granted by high levels of voting rights to expropriate minority shareholders.

In order to confirm the last result of Table 3, in Table 4 we split our main explanatory variable 'votes' into four levels: below and above the median sample (42.5%), below the first quartile (30%) and above the third quartile (54.5%).

[Insert about here Table 4]

Model 1 of Table 4 shows that below the first quartile, the voting rights do no affect the premium. This result continues to hold even when we drop financial control variables to have more observations (Model 2), when we focus only on ownership variables (Model 3), or when the voting rights are below the median (Model 4). However, when the voting rights are greater than the median (Model 5), the coefficient of voting rights becomes positive and significant at 10% threshold. More than the third quartile, the coefficient remains significant at 10% threshold (Model 6) and becomes highly significant at 5% threshold when we drop financial control variables to have more observations (Model 7) and highly significant at the 1% threshold when we focus only on ownership variables (Model 8).

These results show that, at higher levels of voting rights, the premium reflect the incentives of controlling shareholders looking for M&A. As the entrenchment effect becomes dominant at those levels, higher premium signal increasing benefits of private benefits of control for bidding shareholders.

III.2 Cash Flow Rights and Premiums

La Porta et al (2002) find that higher cash-flow ownership is associated with less expropriation of minority shareholders. Therefore, higher cash-flow rights of the controlling shareholder may act as an important incentive in acquisitions. Furthermore, in managerial ownership cases, as the stake held by managers increases, they are less inclined to make decisions that against the interests of minority shareholders. La Porta et al (1998) show that the ownership concentration can be a substitute for low investor protection. Shleifer and Vishny (1997) suggest that the benefits from concentrated ownership may be relatively larger in countries that are generally less developed and where property rights are not well enforced by judicial systems. Hence, more concentrated ownership can consequently lead to less private benefits of control. In those cases, the acquisition decision can be undertaken in order to promote the general wealth of the firm. However, we should mention that previous studies offer equivocal results as results the effects of ownership effects on firm performance. Stulz (1988) finds a concave relationship between firm value and managerial ownership. Morck et al (1988) find a non-linear relationship between firm value and managerial ownership with the positive effect of ownership beyond 25%. Moreover, Himmelberg, Hubbard, and Palia (1999) argue that unobserved firm heterogeneity complicates the estimation of the ownership performance relationship.

[Insert about here Table 5]

Model 1 in Table 5 shows that the cash-flow rights have no impact on premiums. This result continues to hold when cash-flow rights are greater than the median (38.6%) (Model 2) and greater than the third quartile (51.4%) (Models 3 and 4) or when we use the square of cash-flow rights (Model 5). Previously, we expected to find a negative effect because the increase of cash-flow rights aligns the incentives of controlling shareholders with the interests of other investors; hence, controlling shareholders are less inclined to make sub-optimal decisions, such as, target overpayment. But, we mention also that the real effect of higher ownership can not be clearly expected due to the possibility of entrenchment effect. Our result can be due to the number of firms having no separation between ownership and control: almost of the controlling shareholders in our sample have cash-flow rights that equal voting rights and, as far as, voting rights have a positive and significant effect, the cash-flow rights could not have a negative effect. As a robustness test, in Model 6, we regress the premium on cash-flow rights only for firms having separation between ownership and control. In consistence with our expectations,

the coefficient of cash-flow rights becomes negative; however, it is still insignificantly different from 0.

III.3 Separation, Excess of separation, Means of Separation and Premiums

The concept of separation between ownership and control closely linked to expropriation by minority shareholders and negative effects on firm value. Claessens (2002) notes that in non-US firms the largest shareholder often establishes control despite having low cash-flow rights. This in turn could involve potential agency problems between controlling and minority shareholders. Bigelli and Mengoli (2004) find that bidder announcement returns are significantly lower when the separation of ownership and control in the bidder is high. Therefore, if the premium reflects the private benefits of control, we assume that the premium is positively related to the separation, the excess of separation and the different means of separation. However, according to the Model 1 of Table 6, the coefficient of separation between the ownership and the control is insignificantly different from 0.

[Insert about here Table 6]

Moreover and in consistence with previous studies, the behaviour of expropriation is accentuated when the separation between the ownership and the control is high and the cash-flow rights held by the controlling shareholder are basically low. Faccio and Stolin (2006) admit that the expropriation takes place when the controlling shareholder's ownership is low. Bozec and Laurin (2008) add that the incentives to extract private benefits of control are even stronger when the cash-flow rights of the dominant shareholder are low.

Thus, if the premium reflects the private benefit of control, it should be highly related with the degree of separation when the cash-flow rights are low. In order to check for this assumption, first, in unreported test of equality, we use a t-test for the level of separation by the median of cash-flow rights. Obviously, we find that the coefficient of the separation is quite higher (t-stat = 4.90) for the lower cash-flow rights subsample (less than the median (38.6%)).

Second, we run a regression of the premium on the main separation variable focusing on this part of low ownership. The finding of this specification is consistent with our assumption, Model 2 of Table 6 shows that the coefficient of separation becomes positively significant at 5% threshold. Therefore, we can admit that the premium reflects the private benefits of control in case of separation between the ownership and control when the cash-flow rights are low.

As noted by Faccio and Lang (2002), in western European corporations, the separation between the ownership and the control comes from different mechanisms including dual class shares, pyramids, cross holding, multiple control chain. These mechanisms allow the controlling shareholder to maintain grip on control while holding only a small fraction of cash-flow rights.

Furthermore, we use other measures of separation, the excess of separation and the main means of separation basically the dual class shares and the indirect control using mostly pyramids. In Model 3 of Table 6, the coefficient of the excess of separation is also insignificant. In Model 4, dual class shares do not seem to have an impact on premiums; however, in both Models 4 and 5, the coefficient of indirect control is positive and statistically significant at 5% threshold. This result is quite conform with the assumption which implies that when the controlling shareholder monitor the firm through pyramids or multiple chain of control, he can make decisions that don't coincide with the interests of the firm but rather with the interests of other companies that are closely controlled by him. Many studies document that pyramiding is the main device allowing the entrenchment of large controlling shareholders. In this area, Bertrand et al (2002) show that there is more expropriation of firms further down pyramids. Furthermore, Bigelli and Mignoli (2004) argue that the high separation of ownership from control achieved through the concurrent use of stock pyramiding could favor acquisitions made to increase private benefits of the controlling shareholders rather than all shareholders' wealth. Wolfenzon (1999); Bebchuk et al (2000) and Claessens et al (2002) report that the expropriation arise when the corporation is affiliated to a large group of corporations, all controlled by the same shareholder. Faccio and Stolin (2006) note that group structures allow controlling shareholders to divert the resources of a company further down the pyramid by transferring assets, by lending or borrowing at nonmarket rates, by guaranteeing other companies borrowing or, generally, by "unfairly" pricing transactions with other corporations higher in the pyramid in which the controlling shareholder has a larger ownership stake.

III.4 Other implications

Outside the US, controlling shareholders are seldom surrounded by only atomic shareholders. Over one-third of publicly listed firms in Europe have more than one large owner. Those blockholders play an active governance role in reducing the magnitude of control of the ultimate shareholder and disapproving harmful business decisions. Lehman and Weigand (2000), Maury and Pajuste (2005) and Laeven and Levine (2008) show that firm valuations decrease when the difference between the two stakes held by the largest and the second shareholder intensifies. Bloch and Hege (2001) argue that when control is more contestable there are less private

benefits of control. Therefore, we assume that in the presence of other blockholders, the controlling shareholder is more constrained to pay less for targets and we expect that the premium will be negatively associated with the presence of other blockholders. However, all regression tables show that the presence of other blockholders does not affect the premium amount. In spite of their governance role, blockholders do not seem to have an influence on the magnitude of the premium paid. Other studies (Bolton and von Thadden (1998); Zwiebel (1995)) show also that the presence of other blockholders might not be sufficient to contrary controlling shareholders decisions or to reduce expropriation of minority shareholders. Moreover, those shareholders can sign agreements or concerted actions with the controlling shareholder and create together a coalition of control allowing them to make common decisions at the expense of minority shareholders. Faccio et al (2001) find evidence that the blockholders collude in expropriating outside shareholders in Eastern Asia.

In our study, all models in which we do not use any specification[1], show that the coefficient of industry relatedness is significantly positive and the coefficients of bidder's toehold, leverage and the ratio of cash flow / sales are significantly negative. Our finding for the industrial relatedness is similar to Bae et al (2002) that argue that, usually, synergies are more pronounced for related acquisitions. However, in unreported univariate analyses, we find that more concentrated voting rights are associated with unrelated deals. Amihud and Lev (1981), Shleifer and Vishny (1990), Lins and Servaes (2002) and Pecherot-Petitt and Dumontier (2002) suggest that unrelated acquisitions, which diversify the firms' holdings, are not mainly aimed at common interests of bidder shareholders. They serve first to improve the acquiring firm manager's job security by diversifying the risk of their human capital that cannot otherwise be properly diversified.

When the bidder has a previous toehold in the target, this is associated with lower premiums. Bidding toehold reducing the offer premium was discovered at first by Betton and Eckbo (2000). Kisgen et al (2009), Betton et al (2009) among others find a similar result. According to agency theory, higher level of debts or leverage reduces the incentives of managers towards wasteful projects, thus, they are less inclined to overpay targets. This assumption is also confirmed through our findings for concentrated voting rights bidders. Schwert (2000) don't find significant result. Besides, in Table 4, we observe that at low level of voting rights that are normally associated with lower premiums, the coefficient of leverage is insignificant but becomes significantly negative at high level of voting rights.

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[1] All models in Table 3, Models 1 and 5 in Table 5 and Models 1, 2 and 3 in Table 6

Our unusual result is the coefficient of the ratio of cash flow/sales which is quite significantly negative. In consistence with our perspective, the cash flow, as a generator of free cash flow and agency costs, is more likely to be correlated with the amount of the premium. In unreported analysis, we swap this ratio by the ratio of cash flow/total assets, the coefficient becomes positive. Thus, our first negative coefficient can be due to the weight of sales. Moreover, Table 4 shows this coefficient moves from highly negative when the voting rights are low to insignificant when the voting rights become higher, therefore, we assume that the cash flow increase with the voting rights held by the controlling shareholder.

Concerning the relative size of the target, in consistence with Slusky and Caves (1991), we find also no statistical significant effect on the premium. Gondholekar, Sant and Ferris (2004) use target market equity scaled by bidder market equity, they find a negative impact at 1% threshold, we find also no statistical significant effect.

The dividend payout ratio does not affect negatively the premium as we expected previously. The role of dividend policy as a disciplining mechanism can be reduced when the controlling shareholder hold an internal position within the firm. Moreover, Holderness and Sheehan (2000) find that the dividend payout ratio is lower in individual majority-shareholder firms. Gugler and Yurtoglu (2003) show that large blockholdings, is related to a significantly lower payout ratios.

The payment method does not seem to have an impact on premiums; Kisgen et al (2009) also do not find that the payment method affect the premium. Gondholekar, Sant and Ferris (2004) use target market equity scaled by bidder market equity, they find a negative impact at 1% threshold.
According to Eckbo (2009), we did not find a significant effect of multiple bidders on the premium. Slusky and Caves (1991), Schwert (2000) and Flanagan and O'Shaughnessy (2003) find a positive effect on premiums at 1% threshold. Also, according to Eckbo (2009), the hostility of the deal does not seem to affect the premium. Rossi and Volpin (2004) find a positive effect on premiums at 1% threshold. Schwert (2000) create several variables to measure hostility and find a negative effect on the premium of the principal component of variables with complete data.

Usually, tender offers are costly than mergers or other types of acquisitions (Easterbrook and Fischel (1996)). Schwert (2000) and Rossi and Volpin (2004) find a positive effect on premiums at 1% threshold for tender offers. However, Eckbo (2009) find a significant and negative effect.

Our analyses do not reveal a significant result. Finally, none of the control country variables has an impact on the premium.

IV Conclusion

In this paper, we find strong evidence that the premium offered in M&A can be affected by the entrenchment of controlling shareholders. Therefore, we argue that the premium is an indicator for the private benefits of control. Our results show that target overpayment is positively and significantly associated with higher level of voting rights, as well as, the level of separation between the ownership and the control when cash-flow rights are low. Furthermore, when controlling shareholders exert control via other corporations, takeover premiums increase as well. Previous papers show that the premium reflects the private benefits in privately negotiated transactions (mainly block transactions). In the present study, we show that the premium can also reflect private benefits in public transactions.

European firms are characterized by a strong legal environment and broad extralegal institutions which make the issue of expropriation by majority shareholders less prevalent. Our results show that controlling shareholders are able to further their private objectives even if these objectives do not overlap with the interests of the non-controlling shareholders. These results provide an empirical support for previous studies that suggest that the expropriation of minority shareholders is an important principal agent problem in European acquisitions.

Nevertheless, even if the private benefits are consumed by bidding firm shareholders, we should not forget the important role of controlling shareholders in the organization. For example, Holmen and Knompf (2004) suggest that some of the mergers are motivated by dual owners' desire to provide additional equity funds to capital constrained firms within their pyramids. Furthermore, we should also mention that private benefits and shared benefits are not mutually exclusive (Holderness (2003)). Thus, the incentives of controlling shareholders can coincide with those of the other shareholders. Further studies should pursue these issues in order to develop appropriate governance tools to constrain detrimental takeovers made by bidder controlling shareholders.

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Table 1

Descriptive Statistics

Panel A: number of premiums per year

Year	1994	1995	1996	1997	1998	1999	2000	2001	Total
N	8	14	9	26	29	56	66	23	231

Panel B: number of premiums per country

Acquiror Nation	Austria	Belgium	Finland	France	Germany	Ireland	Italy	
N	7	18	4	43	30	4	16	Total
Acquiror Nation	Norway	Portugal	Spain	Sweden	Switzerland	United Kingdom		
N	8	8	13	16	15	49		231

Panel C: Number of premiums per Industry

Industry	Consumer Product	Consumer Staples	Energy and Power	Financials	Health care	High Technology	
N	22	18	18	41	5	9	Total
Industry	Industrials	Materials	Media and Entertainment	Real Estate	Retail	Telecommunication	
N	25	40	16	11	14	12	231

Table 2: Descriptive statistics

variable	N	Mean	Median	St.Dev	p5	p95
	231	44.39343	35.5205	40.22453	-1.00672	132.2438
VOTES	231	45.91333	42.5	17.35326	25	81.7
OWN	231	40.1081	38.6241	19.70879	10	75
SEPA	231	.3376623	0	.4739397	0	1
EXCESS	231	5.805229	0	10.74953	0	30.7184
OTHER	231	.3376623	0	.4739397	0	1
DUAL	226	.2477876	0	.4326862	0	1
INDIRECT	231	.1991342	0	.4002164	0	1
RSIZE	189	.3394636	.1785646	.4180676	.0025561	1.063065
LEVERAGE	225	.2944751	.267641	.2314022	.0021955	.7771733
DPR	211	.370734	.317746	.3431514	0	1.053874
CFS	192	.1453302	.1047032	.1725854	.0000506	.4492536
NBIDDERS	231	1.047619	1	.2834277	1	1
TOEHOLD	231	.4545455	0	.4990109	0	1
RELATEDNESS	231	.5411255	1	.4993879	0	1
PAYMENT	231	.6536797	1	.47683	0	1
SIZE_TR	231	1060.268	180.968	4553.113	6.635	3599.748
HOSTILITY	231	.030303	0	.1717921	0	0
TENDER	231	.5757576	1	.4953007	0	1
GDPG	231	1.204934	1.223197	2.222847	-1.23281	3.673023
MARKET	231	16.94	12.66	12.00796	3.91	35.68
GOVERN	231	92.62294	93.4	4.626929	80.6	100

See Appendix for variable definitions.

Table 3
Voting Rights And Premiums

	Model 1	Model 2	Model 3	Model 4
VOTES	0.375**			-1.477
	(0.0367)			(0.117)
VOTES2		0.00406**		0.0176**
		(0.0151)		(0.0459)
VOTES3			4.96e-05***	
			(0.00722)	
OTHER	3.716	3.260	2.673	0.582
	(0.551)	(0.597)	(0.662)	(0.927)
RSIZE	-11.40	-10.92	-10.31	-8.635
	(0.141)	(0.155)	(0.177)	(0.266)
DPR	-0.947	-1.159	-1.278	-2.141
	(0.920)	(0.901)	(0.891)	(0.818)
CFS	-53.16***	-52.61***	-51.84***	-49.56***
	(0.00570)	(0.00591)	(0.00639)	(0.00942)
LEVERAGE	-28.44**	-27.84**	-27.03**	-25.34*
	(0.0383)	(0.0413)	(0.0465)	(0.0635)
NBIDDERS	19.21	19.21	19.14	18.84
	(0.135)	(0.132)	(0.132)	(0.138)
TOEHOLD	-16.52***	-16.39***	-16.33***	-16.52***
	(0.00710)	(0.00721)	(0.00717)	(0.00653)
RELATEDNESS	13.46**	13.69**	13.85**	13.51**
	(0.0302)	(0.0267)	(0.0243)	(0.0280)
PAYMENT	-9.120	-8.964	-8.757	-8.445
	(0.162)	(0.167)	(0.175)	(0.191)
SIZE_TR	-0.000148	-0.000145	-0.000142	-0.000143
	(0.796)	(0.800)	(0.803)	(0.802)
HOSTILITY	-8.338	-7.476	-6.269	-2.410
	(0.671)	(0.702)	(0.747)	(0.902)
TENDER	-6.291	-6.345	-6.507	-6.679
	(0.307)	(0.300)	(0.286)	(0.273)
GDPG	-1.314	-1.402	-1.468	-1.569
	(0.266)	(0.234)	(0.211)	(0.183)
GOVERN	0.560	0.548	0.540	0.477
	(0.394)	(0.401)	(0.406)	(0.464)
Constant	-13.58	-5.303	-2.089	36.44
	(0.837)	(0.935)	(0.974)	(0.603)
Observations	159	159	159	159
R-squared	0.256	0.264	0.270	0.276
F	3.272	3.411	3.531	3.387

Note. - The dependant variable is the premium computed as the difference between the price per share offered and the target stock price four weeks before the deal announcement, divided by the target stock price four weeks before the announcement. Our sample period is from 1994 to 2001. All models comprise 159 deals with complete values for all variables. For the OLS regressions estimates, p-values are in parentheses *** $p<0.01$, ** $p<0.05$, * $p<0.1$. See Appendix for variable definitions.

Table 4

Level of Voting Rights And Premiums

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
	Low levels of voting rights				**High levels of voting rights**			
	<1st quartile	<1st quartile	<1st quartile	<median	>median	>3rd quartile	>3rd quartile	>3rd quartile
	25% - 30%	25% - 30%	25% - 30%	25%-42.5%	42.5%-100%	54.5%-100%	54.5%-100%	54.5%-100%
VOTES	-1.522	1.797	1.397	-0.305	0.511*	1.380*	1.222**	1.260***
	(0.694)	(0.520)	(0.584)	(0.629)	(0.0973)	(0.0575)	(0.0261)	(0.00829)
OTHER	-7.596	-3.520	-4.370	-3.893	-3.953	14.52	0.869	-6.610
	(0.594)	(0.730)	(0.667)	(0.616)	(0.684)	(0.391)	(0.955)	(0.610)
RSIZE	-8.149					-18.43		
	(0.757)					(0.304)		
DPR	-13.86					35.19		
	(0.500)					(0.221)		
CFS	-125.3***					-16.78		
	(0.00594)					(0.671)		
LEVERAGE	-18.04					-63.17**		
	(0.664)					(0.0293)		
NBIDDERS	0	-12.71		-21.52	12.21		-40.15	
	()	(0.538)		(0.263)	(0.352)		(0.415)	
TOEHOLD	-6.689	1.050		-13.13*	-13.82		-19.77	
	(0.695)	(0.924)		(0.0720)	(0.114)		(0.212)	
RELATEDNESS	-5.669	13.68		10.26	4.449	22.96	-0.158	
	(0.691)	(0.177)		(0.154)	(0.601)	(0.157)	(0.990)	
PAYMENT	-8.970	7.312		0.892	-2.164	-8.670	13.56	
	(0.595)	(0.544)		(0.905)	(0.813)	(0.666)	(0.346)	
SIZE_TR	0.00539	0.00625		0.000818	-0.00143	-0.00212	-0.000180	
	(0.365)	(0.237)		(0.242)	(0.310)	(0.245)	(0.916)	
HOSTILITY	0	0		0	-2.186	-23.36	-7.165	
	()	()		()	(0.908)	(0.604)	(0.798)	
TENDER	-9.058	-18.23*		-1.687	2.714	10.15	23.77	
	(0.526)	(0.0817)		(0.821)	(0.757)	(0.527)	(0.125)	
GDPG	2.515	1.990		-1.228	-3.316*	4.682	-1.379	
	(0.493)	(0.459)		(0.459)	(0.0729)	(0.496)	(0.800)	
MARKET	-0.403	0.692		0.00426	-0.257	-0.560	-0.689	
	(0.603)	(0.158)		(0.989)	(0.475)	(0.450)	(0.351)	
Constant	134.6	-8.338	10.34	78.98**	15.58	-43.11	-2.533	-43.44
	(0.273)	(0.922)	(0.884)	(0.0231)	(0.563)	(0.484)	(0.966)	(0.179)
Observations	43	62	62	117	120	36	59	59
R-squared	0.386	0.179	0.010	0.077	0.099	0.456	0.198	0.118
F	1.404	1.115	0.309	0.879	1.085	1.418	1.056	3.747

Note. - The dependant variable is the premium computed as the difference between the price per share offered and the target stock price four weeks before the deal announcement, divided by the target stock price four weeks before the announcement. Our sample period is from 1994 to 2001. Models 1 and 6 comprise deals with complete values for all variables. Models 1, 2 and 3 include 62 deals in which the bidder's controlling shareholder has voting rights less than the first quartile (30%). Model 4 includes deals in which the bidder's controlling shareholder has voting rights less than the median (42.5%). Model 5 includes deals in which the bidder's controlling shareholder has voting rights greater than the median (42.5%). Models 6, 7 and 8 include 59 deals in which the bidder's controlling shareholder has voting rights greater than the third quartile (54.5%). For the OLS regressions estimates, p-values are in parentheses *** p<0.01, ** p<0.05, * p<0.1. See Appendix for variable definitions.

Table 5

Cash flow Rights And Premiums

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
OWN	0.170	0.366	0.662	0.770		-0.0160
	(0.282)	(0.195)	(0.217)	(0.227)		(0.954)
OWN2					0.00304	
					(0.194)	
OTHER	2.612	-12.08	2.931	-0.541	2.803	2.304
	(0.679)	(0.228)	(0.857)	(0.969)	(0.655)	(0.851)
RSIZE	-10.57				-10.44	-19.34
	(0.176)				(0.232)	(0.277)
DPR	-5.561				-5.711	12.23
	(0.556)				(0.508)	(0.524)
CFS	-56.42***				-56.27***	-90.35*
	(0.00317)				(0.00207)	(0.0866)
LEVERAGE	-28.45**				-28.26**	-46.31*
	(0.0397)				(0.0247)	(0.0680)
NBIDDERS	17.82	13.67	36.57		17.66	2.028
	(0.169)	(0.321)	(0.186)		(0.182)	(0.905)
TOEHOLD	-18.76***	-14.54	-16.35		-18.35***	-27.12**
	(0.00338)	(0.109)	(0.356)		(0.00323)	(0.0209)
RELATEDNESS	11.24*	-0.756	-4.690		11.59**	17.60
	(0.0682)	(0.930)	(0.740)		(0.0434)	(0.116)
PAYMENT	-9.870	-1.129	2.525		-9.618	-7.723
	(0.146)	(0.899)	(0.863)		(0.175)	(0.578)
SIZE_TR	-0.000117	-0.00172	-0.000986		-0.000114	-0.00116
	(0.840)	(0.223)	(0.591)		(0.809)	(0.763)
HOSTILITY	-6.109	-4.131	-12.44		-5.165	1.532
	(0.758)	(0.856)	(0.732)		(0.600)	(0.955)
TENDER	-4.974	7.486	22.52		-5.248	0.0359
	(0.435)	(0.383)	(0.182)		(0.402)	(0.998)
GDPG	-1.495	-0.313	2.728		-1.587	-2.053
	(0.219)	(0.888)	(0.639)		(0.274)	(0.249)
MARKET	-0.233	-0.250	-0.400		-0.196	0.219
	(0.374)	(0.526)	(0.602)		(0.420)	(0.662)
Constant	58.20***	21.31	-40.75	-6.454	58.24***	80.10***
	(0.00411)	(0.403)	(0.481)	(0.871)	(0.00296)	(0.00967)
Observations	159	117	58	58	159	63
R-squared	0.241	0.083	0.143	0.044	0.251	0.339
F	3.032	0.864	0.698	0.749	3.513	1.607

Note.- The dependant variable is the premium computed as the difference between the price per share offered and the target stock price four weeks before the deal announcement, divided by the target stock price four weeks before the announcement. Our sample period is from 1994 to 2001. Models 1 and 5 comprise 159 deals with complete values for all variables. Model 2 comprises 117 deals in which the bidder's controlling shareholder has cash-flow rights greater than the median (38.6%). Model 3 and 4 comprise 58 deals in which the bidder's controlling shareholder has cash-flow rights greater than third quartile (51.4%). Model 6 comprises 63 deals with complete values for all variables and in which the variable of separation equal 1. For OLS regressions estimates, p-values are in parentheses *** p<0.01, ** p<0.05, * p<0.1. See Appendix for variable definitions.

Table 6

Separation, Excess of Separation, Means of Separation And Premiums

	Model 1	Model 2	Model 3	Model 4	Model 5
SEPA	5.220	16.36**			
	(0.405)	(0.0421)			
EXCESS			0.237		
			(0.366)		
INDIRECT				15.85**	16.72**
				(0.0375)	(0.0279)
DUAL				-2.811	
				(0.665)	
OTHER	0.985	6.098	1.601	-1.730	-2.544
	(0.876)	(0.436)	(0.798)	(0.790)	(0.694)
RSIZE	-10.26	-4.279	-10.33	-8.524	-10.26
	(0.189)	(0.757)	(0.186)	(0.271)	(0.182)
DPR	-2.402	5.853	-0.705	-1.677	-4.175
	(0.795)	(0.636)	(0.941)	(0.856)	(0.646)
CFS	-54.65***	-86.52***	-52.25***	-60.95***	-65.03***
	(0.00411)	(0.00508)	(0.00728)	(0.00198)	(0.000856)
LEVERAGE	-29.33**	-14.25	-28.11**	-20.08	-28.86**
	(0.0352)	(0.491)	(0.0431)	(0.159)	(0.0347)
NBIDDERS	17.87	-244.8	19.54	20.54	20.21
	(0.169)	(0.270)	(0.134)	(0.110)	(0.115)
TOEHOLD	-17.70***	-15.78*	-17.82***	-19.79***	-17.73***
	(0.00407)	(0.0524)	(0.00420)	(0.00142)	(0.00348)
RELATEDNESS	11.58*	16.55**	12.58**	13.84**	12.42**
	(0.0612)	(0.0443)	(0.0453)	(0.0253)	(0.0422)
PAYMENT	-9.640	-9.030	-9.969	-9.277	-10.79*
	(0.145)	(0.326)	(0.135)	(0.163)	(0.0996)
SIZE_TR	-0.000120	0.00478	-0.000169	-0.000139	-9.85e-05
	(0.837)	(0.196)	(0.772)	(0.808)	(0.863)
HOSTILITY	-6.147	-7.795	-6.693	-8.258	-8.917
	(0.758)	(0.758)	(0.737)	(0.673)	(0.650)
TENDER	-5.989	-6.903	-6.206	-5.186	-6.865
	(0.335)	(0.387)	(0.320)	(0.405)	(0.263)
GDPG	-0.943	-2.588*	-0.851	-0.0947	-0.635
	(0.438)	(0.0804)	(0.487)	(0.943)	(0.595)
Constant	57.13***	299.1	10.68	49.46***	56.72***
	(0.00145)	(0.175)	(0.872)	(0.00583)	(0.00130)
Observations	159	86	159	156	159
R-squared	0.233	0.372	0.237	0.242	0.255
F	3.124	3.001	2.957	2.980	3.516

Note.- The dependant variable is the premium computed as The difference between the price per share offered and the target stock price four weeks before the deal announcement, divided by the target stock price four weeks before the announcement. Our sample period is from 1994 to 2001. Models 1, 3 and 5 comprise 159 deals with complete values for all variables. Model 4 comprises 156 deals with complete values for all variables. Model 2 comprises 86 deals with complete values for all variables and in which the bidder's controlling shareholder has cash-flow rights less than the median (38.6%). For the OLS regressions estimates, p-values are in parentheses *** $p<0.01$, ** $p<0.05$, * $p<0.1$. See Appendix for variable definitions.

Appendix:

Variables description

Name	Description	Source
premium	The difference between the price per share offered and the target stock price four weeks before the announcement date, divided by the price four weeks before the announcement date.	Thomson Financial & Datastream
own	The percentage of cash-flow rights held by the bidder's controlling shareholder	JFE website: Faccio Lang Data
own2	The square of the percentage of cash-flow rights held by the bidder 's controlling shareholder	
votes	The percentage of voting rights held by the bidder's controlling shareholder	
votes2	The square of the percentage of voting rights held by the bidder's controlling shareholder	
votes3	The cube of the percentage of voting rights held by the bidder's controlling shareholder	
sepa	One if the percentage of cash-flow rights and the percentage of voting rights held by the bidder's controlling shareholder differ and zero otherwise	
excess	The difference between the percentage of voting rights and the percentage of cash-flow rights held by the bidder's controlling shareholder	
indirect	One if the bidder's controlling shareholder controls the firm through other firms and 0 otherwise	
dual	One if the bidder has outstanding non-voting, limited voting or multiple voting shares and 0 otherwise	
other	One if there is one other owner that controls at least 10% of voting rights and 0 otherwise	
Rsize	Target total assets last twelve months divided by bidder total assets last twelve months	Thomson Financial & Datastream
DPR	Common dividend last twelve months divided by net income last twelve months	
CFS	Total cash flow last twelve months divided by net sales last twelve months	
leverage	Ratio of total debt to total assets one year prior to the acquisition	
Nbidders	The number of entities (including the acquirer) bidding for a target.	Thomson Financial
toehold	One if the bidder has a previous participation in the target prior to the offer	
relatedness	One if the acquiring and target firms had equivalent 2-digit primary SIC code and zero otherwise	

payment	One if the acquisition is entirely paid in cash and zero otherwise	
size_tr	Deal size is defined as the total value of consideration paid by the acquirer (in million USD), excluding fees and expenses.	
hostility	One if the bid is classified as unsolicited and zero otherwise	
tender	One if the acquisition technique is a tender offer and zero otherwise	
GDPG	Real GDP growth equal to nominal GDP growth minus inflation.	Worldbank
govern	Measures the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.	
market	Ratio of the number of domestic firms listed in a given country to its population (in millions).	La Porta et al (1998)