

Park, Bum-Jin

Article

What triggers firms to appoint outside directors beyond the legal minimum requirement?

South African Journal of Business Management

Provided in Cooperation with:

University of Stellenbosch Business School (USB), Bellville, South Africa

Suggested Citation: Park, Bum-Jin (2018) : What triggers firms to appoint outside directors beyond the legal minimum requirement?, South African Journal of Business Management, ISSN 2078-5976, African Online Scientific Information Systems (AOSIS), Cape Town, Vol. 49, Iss. 1, pp. 1-12, <https://doi.org/10.4102/sajbm.v49i1.319>

This Version is available at:

<https://hdl.handle.net/10419/218687>

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.


You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.



<https://creativecommons.org/licenses/by/4.0/>

What triggers firms to appoint outside directors beyond the legal minimum requirement?

**Author:**Bum-Jin Park¹ **Affiliation:**

¹Department of
Business Administration,
Soonchunhyang University,
Republic of Korea

Corresponding author:

Bum-Jin Park,
sunguja@sch.ac.kr

Dates:

Received: 26 Oct. 2017

Accepted: 01 June 2018

Published: 14 Nov. 2018

How to cite this article:

Park, B.-J., 2018, 'What
triggers firms to appoint
outside directors beyond the
legal minimum requirement?',
*South African Journal of
Business Management* 49(1),
a319. [https://doi.org/
10.4102/sajbm.v49i1.319](https://doi.org/10.4102/sajbm.v49i1.319)

Copyright:

© 2018. The Authors.
Licensee: AOSIS. This work
is licensed under the
Creative Commons
Attribution License.

Background: Although previous studies provide important insights on how firms respond to institutional pressure, they fail to acknowledge the salience of globalisation that results in institutional pressures diffusing across countries.

Objectives: Drawing on a selective adaptation model, this article examines whether firms comply with reforms to board structures beyond the minimum legal requirement.

Method: It investigates the determinants of appointing outside directors beyond the minimum legal requirement by analysing the relationship between four main variables and minimum compliance.

Results: Using a sample of Korean listed firms during 2002–2014, this study found that the salient organisational conditions (firm complexity and firm performance) and key organisational actors (controlling shareholders and foreign investors) determine the extent to which firms appoint outside directors on their boards.

Conclusion: This study contributes to the strategy literature that examines organisational response to institutional pressure, furthering the understanding of why there is heterogeneity in firm decisions even from firms in the same institutional environment that face similar institutional pressures. Moreover, it makes a contribution to corporate governance literature, in particular to the adoption of governance mechanisms that originate from foreign models.

Introduction

Why, among firms in similar institutional environments, do some adopt and implement governance practices that go well beyond regulatory compliance requirements while others pursue merely symbolic compliance? At the heart of this question is the probability that the effects of institutional pressures may be moderated by organisational attributes such as financial characteristics and key actors (Okhmatovskiy & David 2012; Short & Toffel 2010). In attempting to understand this theme, some researchers have begun to integrate theories of institutional and organisational dynamics. They explain how differences can persist even among organisations that face comparable institutional pressures (Greenwood et al. 2011; Pache & Santos 2010).

Although these studies provide important insights on how firms respond to institutional pressure, helping us to understand the relationship between the external environment and internal organisational dynamics, their approach and scope neglect other aspects that are necessary to understand organisational responses. Firstly, they explore conditions under which organisations are more likely to resist institutional pressure, but do not consider cases where organisations actually welcome institutional pressure by being proactive and doing more than what is expected. Secondly, these studies fail to acknowledge the salience of globalisation that results in institutional pressures diffusing across countries. Indeed, the pressure to adopt locally derived practices should be expected to be different from that which drives acceptance of imported practices. The contest and resistance that result from the latter are more complex, drawing on notions of normative and cultural differences. Consequently, theoretical lenses applied to imported management practices should reflect the cross-national diversity of corporate governance systems (Beuselinck et al. 2017; Biukovic 2008; Böhren & Siv Staubo 2016; Buck & Shahrim 2005; Gregorič et al. 2017; He & Lu 2018; Jin 2017; Petry 2018; Testa et al. 2018).

Given these omissions, this article examines the adoption of the concept of the outside director in Korea, a practice derived from the Anglo-American model of governance (Reed 2002). Specifically, I seek to understand why, in the face of legal reforms in South Korea (hereafter Korea), some firms

Read online:

Scan this QR
code with your
smart phone or
mobile device
to read online.

complied with the minimum requirement of appointing 25% of the board with outside directors, while others went well beyond this prescribed minimum.¹

Two points are worth noting from this development. The first one is about the adoption of outside directors by Korean firms from a different corporate governance model. While the Anglo-American model is arguably considered to carry standard and recommended governance practices (Witt 2004), in the context of Korean firms it is naturally foreign and inevitably contestable (Chizema & Kim 2010; Min 2016; Min & Smyth 2014). Consequently, management practices imported from alternative governance models should be adaptations that are acceptable, useful and complementary to local practices. Studies of adoption, diffusion and implementation of innovation and management practices have observed that any original template is usually altered or adapted when implemented in a different context (Buck & Shahrim 2005; Greenwood et al. 2011; Pache & Santos 2010). The second issue is about the embodiment of both mandatory and voluntary aspects of compliance in the use of outside directors by firms. Korean listed firms are expected to constitute their boards with at least 25% of outside directors, hence the mandatory part. However, firms could voluntarily choose to appoint more than the stipulated percentage. It could, therefore, be argued that minimum compliance by Korean firms is mandated by the institutional environment, that is, government regulation, but any further appointment of outside directors beyond the 25% mark is organisationally driven.

The choice made by Korean firms between complying with the minimum requirement or going beyond the 25% rule can be described as selective adaptation. Here, selective adaptation is defined as the process of adopting and implementing international management or foreign norms in the context of local cultural and firm-specific management traditions (Biukovic 2008; Potter 2004; Schwindt & McDaniels 2008). Selective adaptation, thus, helps explain how compliance with international governance practices remains contextualised to the local firm's conditions, imperatives and capabilities.

Drawing on the selective adaptation paradigm, in the context of corporate governance changes in Korea, this study seeks to provide answers to the research questions proposed earlier, hoping especially to establish whether there are any differences in organisational attributes between firms that comply with the minimum requirement and firms that go beyond this legal expectation. I refer to a firm that complies with the minimum requirement, as 'passively adaptive' and to one that goes beyond the minimum as 'actively adaptive'.

Using a comprehensive data set for an emerging market, this study makes a number of contributions to the theory of corporate governance. Firstly, it examines, for the first time, the appointment of outside directors beyond the minimum

regulatory requirement, at least in the context of Korea. Previous studies have not gone this far (Chizema & Kim 2010; Min & Smyth 2014). Secondly, it extends the application of the selective adaptation paradigm to the study of corporate governance changes and more importantly to firm-level analysis. Despite its potential explanatory power of the challenges faced by organisations in the diffusion of international management and governance practices and its extensive application in other disciplines such as law (Biukovic 2008; Potter 2004; Schwindt & McDaniels 2008), the use of selective adaptation as an analytical lens in corporate governance is almost non-existent (see Nakamura 2011 as an exception). Thirdly, it presents the selective adaptation model that may be applicable to countries in which there are mandatory requirements for companies to form boards or mandatory standards relating to the composition. For example, since 2006, the Norwegian government has required listed companies to meet minimum 40% representation of women on the board. Other European countries (e.g. France, Germany, Holland, Spain, Belgium and the Netherlands) also follow Norway's way (Bøhren & Siv Staubo 2016; Gregorič et al. 2017). South Africa also has legislation which obligates listed companies to promote broad-based black economic empowerment (BBBEE). The *BBBEE Act of 2003* aims to address the socio-economic injustices of the past between white South Africans and non-white South Africans and particularly includes mandatory requirements of 50% (25) black South Africans (black female) representation on the boards (Ntim 2013; Ntim & Soobaroyen 2013).

Theory and research hypotheses

Korean institution and globalisation

While companies in the United States and the United Kingdom have a unitary board structure in which the outside director system is active, those in Germany and Japan have a dual-board structure in which the outside directors system is relatively less active. Since the Watergate scandal of 1974, the United States has implemented reforms to improve board function. In 1978, the American Bar Association proposed that the board be composed of a majority of outside directors and that an audit committee consisting exclusively of outside directors be established. The New York Stock Exchange also required all listed companies to establish an audit committee composed of three or more outside directors. The *Sarbanes-Oxley Act of 2002* stipulates that audit committees are responsible for the oversight of boards and the external auditors. In 1998, the UK's Hampel Report also stipulated that a majority of the board of directors should comprise outside directors, which was included in the Combined Code on Corporate Governance in 2006.

Following the Asian financial crisis in 1997, Korea undertook broad institutional reforms that significantly changed the corporate governance landscape (Chizema & Kim 2010; Min 2016). One such governance mechanism is the appointment of outside directors on the board. Similar to other emerging markets (e.g. India, Brazil, Mexico, Nigeria), Korea, where companies have a unitary board structure, decided to follow

1. Korean Commercial Code stipulated the appointment of outside directors as requirement of all listed firms.

Anglo-Saxon models of corporate governance (Reed 2002). Here, major features of the reforms included an amendment of the *Listing Act* in February 1998 that mandated the appointment of outside directors for publicly traded firms. Specifically, boards were required to be constituted by outside directors, with the minimum number set at 25% of the total number of directors. To ensure the independence of outside directors, the *Act* clarified the definition of an outside director by excluding current and former employees of the company, the controlling shareholders' family and friends, and anyone who has a business relationship with the firm or business group. Further to the amended *Listing Act of 1998*, the Korean government introduced a regulation in 2001 for large firms (i.e. asset size is equal to or greater than 2 trillion won, where 1,000 won = 1 USD) to appoint outside directors as at least 50% of board members. The listed companies are subject to a fine of up to 50 million won when failing to comply with the requirement of outside directors (Commercial Code 635.3). However, the greater punishment than this fine would be the reputational damage that companies suffer when not complying with this requirement (Gregorič et al. 2017). Against the background that Korean firms are adopting the use of outside directors in response to legal requirements, this is a clear case of organisational adaptation. Given further that changes in Korean corporate law is in turn a response to the pressures of globalisation and that the use of outside directors is an Anglo-American practice, certain characteristics of the firm and key actors within the firm are likely to influence this process in a manner that is consistent with a specific type of organisational adaptation, that is, selective adaptation.

Another change is the introduction of regulations to alleviate the concentration of economic power of large business groups called *chaebol*, which are controlled by a large shareholder who holds more than 30% of the outstanding shares or has a substantial influence on the management (Korea Fair Trade Commission [KFTC]). The controlling shareholders of such groups tend to engage in tunneling activities that transfer the wealth of external stakeholders to their wealth through cross-shareholding among affiliates (Bae et al. 2002; Baek et al. 2004). This corporate governance system in Korea was identified as one of the causes of the 1997 financial crisis (OECD 2001). Having noticed the criticism of *chaebol's* debt-ridden strategy before the crisis, Korean government initiated a strong *chaebol* reform following the crisis. That is, the government banned cross-shareholding and mutual guarantee for debt payment among affiliates, which facilitated affiliates to access loan markets. Since 2002, the KFTC has been announcing the business groups that are prohibited from cross-shareholding and mutual debt guarantee among their affiliates every April. The history of controlling shareholder's powers in Korea has been deeply rooted, which, coupled with *chaebol* problems to fair competition, motivated to the establishment of the KFTC.

Organisational adaption

Organisational adaptation refers to modifications in the organisation or its components in order to adjust to changes

in the external environment (Levinthal 1991). Adaptation generally refers to a process, not an event, whereby changes are instituted in organisations. As such, previous research has examined organisational adaptation to changing institutional environments, documenting the spread and persistence of discrete practices and structures across organisational fields. These practices and structures include the multidivisional form (Natividad 2013), corporate diversification (Del Brio et al. 2011; Goranova et al. 2007), accounting standards (Brown et al. 2014) and corporate governance affirmative action (Ntim 2013; Ntim & Soobaroyen 2013).

Recent changes to organisations' institutional environments have been triggered by pressures of globalisation, with the effect that practices and structures have been spreading not only across organisational fields but also across national boundaries. For example, Testa et al. (2018) examined the adoption of Eco-Management and Audit Scheme, which is considered as common practice for corporate greening in worldwide. Bøhren and Siv Staubo (2016), Gregorič et al. (2017) and Petry (2018) studied organisational responses to mandatory board diversity (e.g. 40% representation of women on the board in Norway, 50% worker representation on boards in Germany) in international trends. Research on accounting uses the mandatory adoption of International Financial Reporting Standards as pressures of globalisation (Beuselinck et al. 2017; He & Lu 2018; Jin 2017).

Selective adaptation addresses the adoption and implementation of international management models 'to fit the demands of domestic markets and institutions' (Zeitlin & Herrigel 2000:5). Underlying selective adaptation is a belief that compliance with internationally accepted practices, including corporate governance mechanisms, is dependent *inter alia* on three key factors. Firstly, local actors should have appreciation of international governance practices as well as good understanding of local norms and practices (Potter 2004). Such an appreciation enables local actors or adopters to make judgements about or a better perception of the relevance of foreign management practices in their local context. Secondly, compliance with internationally accepted practices depends on the degree of support that local actors welcome international practices. This support is a function of the *legitimacy* that international practices have in the eyes of local actors (Berrone & Gómez-mejía 2009).² Thirdly, selective adaptation depends on the extent to which international practices and local norms are complimentary or capable of co-existing and operating in effective ways despite the fact that they might substantively contradict each other (Biukovic 2008). There is a dearth of empirical studies in corporate governance in general that employ the selective adaptation theoretical lens (Biukovic 2008; Potter 2004; Schwindt & McDaniels 2008).

While I acknowledge the possibility of numerous intervening firm-level characteristics over a course of action, four factors

2. Legitimacy can be thought of as an assumption that a practice meets some minimum constraint.

are considered as key determinants to selective adaptation of the concept of outside directors in Korea. These factors are classified under two groups, namely salient organisational conditions (*firm complexity* and *firm performance*) and key organisational actors (*controlling shareholders* and *foreign investors*). Considering organisational conditions, firm complexity may suggest diversity of numerous tasks that require a larger board, composed of directors with diverse backgrounds and experience. Previous research has shown firm performance as an important moderator of an organisation's responsiveness to environmental change (Boeker & Goodstein 1991; Böhren & Siv Staubo 2016; Chizema & Kim 2010; Hermalin & Weisbach 1988; Orlitzky et al. 2003). With respect to organisational actors, controlling shareholders are common in Korea and hold a great deal of power and influence over key corporate decisions (Bae et al. 2002; Baek et al. 2004; Young et al. 2008). Foreign ownership could, as opposed to controlling shareholder power, be viewed as an important actor to motivate organisational adaptation (Greenwood et al. 2011; Kim et al. 2010; Young et al. 2008).

Firm complexity

The organisational impacts and consequences of complexity have long been part of the research tradition (Herbst & Prüfer 2016; Rawley 2010). An organisation is complex if change in one unit, either in its internal or external environment, requires change in many other units. This suggests that firms that are complex are better able to deal with the changing external environment. Applying this reasoning to the composition of the board suggests that beyond top executives, boards should also be constituted by sophisticated actors drawn from the wider institutional environment, hence the appointment of outside directors.

The board of directors makes the firm's complex strategic decisions such as the selection of the CEO (Khurana 2001), business diversifications (Kroll et al. 2005), resolving conflict of interest inherited in all contractual arrangements involving principles and agents (Tuggle et al. 2010) and takeover defences (Sundaramurthy 1996).

Firm complexity would increase the difficulty of the board's role in Korea for the following reasons. Firstly, the simple number of activities to manage and supervise, as a result of firm complexity, multiplies. Following the Asian financial crisis of 1997, Korean corporate boards were heavily criticised for having failed on a number of corporate governance duties. This meant that top management had to adjust or take control of multiple activities in their organisations. Moreover, given the rise of foreign ownership and globalisation of businesses in Korean firms (Chizema & Kim 2010; Kim et al. 2010; Min 2016; Min & Smyth 2014), the scope of managerial activities has expanded beyond traditional business to cope with requests from multiple stakeholders, including foreign investors. Thus, while traditionally Korean firms did not engage with or appreciate the role of outside directors, increased firm complexity may force them to seek expertise

that complement their existing capabilities on how to deal with new pressures, hence the need for more outside directors. Secondly, the knowledge and techniques needed to understand and manage these activities, respectively, increases substantially. In the context of Korea, Min and Chizema (2015) reported that executive board members of firms took the largest portion (32.9%) of the appointed outside directors, followed by university professors (21.6%), ex-government officer (5.2%) and accountant (4.1%). Thus, in the context of firm complexity, there is likely to be a strong perception of the usefulness of outside directors who provide managers with helpful advice based on their own experience and social networks (Durbach & Parker 2009; Haynes & Hillman 2010). Thirdly, complex organisations are usually characterised by higher levels of information asymmetry (Sanders & Carpenter 2003). In particular, larger firms have more significant agency problems (Boone et al. 2007) and their boards of directors must work harder to monitor management, assessing whether the decisions taken by top management are aligned with shareholders' interests (Dalton et al. 2007; Linck et al. 2008). The complexity of the firm means that insiders rely more on external 'human capital' for effective decision makings. Thus, *ceteris paribus*, more outside directors are required as a firm's complexity increases. I hypothesise that:

Hypothesis 1: Firm complexity is positively associated with the appointment of outside directors beyond the minimum legal requirement.

Controlling shareholders

In the Anglo-American corporate governance model, outside directors are meant to protect the interests of (minority) shareholders from self-serving management. Scholars argue that this approach is appropriate given the lack of alignment between executives' interests with those of dispersed shareholders (Dalton et al. 2007; Jensen & Meckling 1976; Zardkoohi et al. 2017). In contrast to the *principal-agent* problem, the challenge in Asian economies such as Korea, where family businesses are prevalent, is the *principal-principal* conflict between a controlling shareholder and minority shareholders (Bae et al. 2002; Baek et al. 2004; Sun et al. 2017; Young et al. 2008). The contrast in the corporate governance models questions the wisdom of Asian firms in importing the concept of outside directors from the Anglo-American system without simultaneous adjustments to ownership structure and the generality of other institutions. Outside directors are expected to monitor and prevent expropriations by the controlling shareholder (Dalton et al. 2007; Linck et al. 2008). Indeed, research that draws on agency theory recommends the appointment of outside directors to the board.

Based on this *ex ante* equilibrium requirement of agency theory (Jensen & Meckling 1976), firms with more controlling shareholders' interests are more likely to appoint more outside directors than firms with less controlling shareholders' interests. However, given the contrast between the Korean

corporate governance environment and the Anglo-American variety, the position of this study is not influenced by agency theory. This study offers an alternative explanation rooted in the paradigm of selective adaptation. In particular, the selective adaptation proposition is about process (or even *ex post* and not *ex ante*) of an organisation's response.

Consistent with the principle of selective adaptation, the controlling shareholder may not welcome the concept of the outside director for the following reason (Dalton et al. 2007; Linck et al. 2008; Pache & Santos 2010; Young et al. 2008). The controlling shareholders may hold the *perception* that the introduction of the outside director system following the 1997 crisis are mainly for monitoring themselves though scholars propose outside directors are useful for both strategy formulation and resource provision. Given the background of the reform of governance system, they would consider outside directors as a threat as long as the principal-principal problems remain as an issue in Korea. To the extent that the outside director's role does substantively include the protection of minority shareholders, controlling shareholders are more likely to reject the appointment of outside directors. This argument suggests that the controlling shareholder and outside directors are considered incompatible. I, therefore, hypothesise that:

Hypothesis 2: Controlling shareholders' power is negatively related to the appointment of more outside directors.

Foreign investors

As discussed earlier, compliance with internationally accepted practices depends on the degree of support that local actors welcome international practices. This support is a function of the *legitimacy* and perceived value that international practices have in the eyes of local actors. International investors tend to value international practices more than domestic investors and have led to stronger board independence (Chizema & Kim 2010; Kim et al. 2010; Min & Smyth 2014; Okhmatovskiy & David 2012). International investors could perceive that value of outside directors is high to an economy with relation-based crony capitalism, which indeed caused the 1997 Asian crisis. This perception will be even more so when power of controlling shareholder prohibits active adaptation of the new system in a family-controlled economy (Greenwood et al. 2011; Kim et al. 2010; Young et al. 2008).

International investors may also think outside director system could be a complementary to local norm. Many institutional investors including California State Teachers' Retirement System in America have publicly announced that corporate governance is an important factor to be considered for their investment decisions. This movement illustrates that firms invested by foreigners should consider these investors' demand. I, therefore, hypothesise:

Hypothesis 3: An increase in foreign ownership increases outside directors.

Firm performance

Literature in the area of organisational performance has tended to be ideologically split concerning the effects of performance on organisational response to institutional pressure. Here, arguments have been made for the effects of both poor and successful performance. Starting with poor performance, firm performance could exacerbate conservatism and inertia because organisations with performance problems may restrict the numbers of sources of information consulted and alternatives considered when developing potential solutions, consequently developing inertial tendencies (Cameron et al. 1987; Gómez-Mejía et al. 2011). Contrary to the point made earlier, poor performance could act as a catalyst to organisational adaptation because it may signify the ineffectiveness of existing practices and thus provides strong and legitimate reasons for firms to reform their administrative systems (Boeker & Goodstein 1991; Chatterji & Toffel 2010). In the context of corporate governance, previous studies show that firms appoint more outside directors during or following periods of poor performance (Bøhren & Siv Staubo 2016; Hermalin & Weisbach 1988). In the context of Korea, Chizema and Kim (2010) found the positive relationship between weak financial performance and the appointment of outside directors.

However, arguments for good firm performance have also been made. Firstly, success could breed inertia and apathy (Boeker & Goodstein 1991), because organisational success promotes the development of internal forces for stability and inertia, potentially leading to resistance to organisational changes (Gómez-Mejía et al. 2010). Secondly, and contrary to the point made earlier, it is the view that success encourages adaptation because the excess resources that successful organisations generate allow 'an organization to compete in its environment more boldly' (Bourgeois 1981:35). This view has received support from research on the introduction and diffusion of innovation that has provided empirical evidence that successful organisations are more likely to both introduce innovations and be early adopters of innovations deriving from elsewhere (Christensen & Van Bever 2014; Orlitzky et al. 2003). Given these diversified views, I hypothesise that:

Hypothesis 4: Firm financial performance is related to the appointment of outside directors beyond the minimum requirement.

Data and model

Data

Data on outside directorships are crucial in this study. To ensure reliability of data, I manually collected all these board-related information from the official website provided by Data Analysis, Retrieval and Transfer (DART) system. This is the Financial Supervisory Service's (FSS) electronic corporate disclosure system. The FSS is South Korea's integrated financial regulator. Other annual data on non-financial listed firms were obtained from the Korea Information Service (KIS)

database, which is one of the most comprehensive data set for corporations in Korea. The classifications of chaebol affiliates were sourced from the KFTC.

The basic data sources for the KIS database are business (semi-annual) reports, quarterly reports and consolidated auditing reports, which are prepared and submitted by all listed corporations according to the Commercial Code and stock exchange laws. This database provides a wide range of corporate information, including balance sheets, income statements, stock prices, auditors' opinions and general information about stock exchange-listed and Korean Securities Dealers Automated Quotations (KOSDAQ)-listed corporations. The data set excluded KOSDAQ-listed firms and financial institutions in order to increase the comparability between firms. The data set ranged from 2002 when the DART system began to publicise the information about appointed outside directors, to 2014.

Model

Given the goal of the research and restricted dependent variable at low level of 25% (i.e. ratio of outsider to board is 0.25), the Tobit model was employed to test the hypotheses in Equation 1.

$$Y_{it} = \text{const} + \theta_i + \psi_j + \beta_1 \text{Complexity}_{it} + \beta_2 \text{CS-owner}_{it} + \beta_3 \text{Foreign-owner}_{it} + \beta_4 \text{Performance}_{it} + \text{Others}_{it} + \varepsilon_{it} \quad [\text{Eqn } 1]$$

where Y_{it} is the dependent variable which is the restricted ratio of outsiders to board members at lower level of 0.25 (*Od2board_Tobit*). That is, the ratio of outsider to board members was replaced with zero if the ratio failed to be beyond the legal requirement (i.e. 0.25). Summary statistics in Table 1 report that the mean (median) value of dependent variable (*Od2board_Tobit*) over sample period was 0.303 (0.286) which indicates that skewness was not a major problem. As expected, this mean value was approximately

3.3% lower than the mean value (0.336) of unrestricted ratio of outsider to board (*Od2board*). The Korean government introduced a further regulation in 2001 for large firms (i.e. asset size is equal to or greater than 2 trillion won, where 1,000 won = 1 USD) to appoint outside directors as at least 50% of board members. This study focuses on the 25% regulation and this 50% regulation is examined as further analysis. θ_i captures time effects and ψ_j is to control for industry-level (Korea Standard Industry Classification [KSIC] two-digit) clustering effects. Others are control variables described below. ε_{it} is a time-varying residual and follows the unit normal distribution.

To investigate the effect of complexity on board structure, two different proxy variables were used. Firstly, this hypothesis was examined by using *Intangibleasset* variable which is calculated by intangible asset divided by total assets. This *Intangibleasset* is expected to proxy technology-related complexity (Maria 2016; Saunders & Brynjolfsson 2016). Following Gregorič et al. (2017) and Russell (2017), the log of the number of employees (*Lnemployee*) also was used to proxy size-related complexity. Mean (median) values of these variables in Table 1 were 0.49 (0.39) and 6.13 (6.01), respectively.

To investigate the effect of controlling shareholder's powers, shareholder's equity ownership (*CS-owner*) was used. *CS-owner* is taken as the percentage of outstanding stock owned by dominant or controlling shareholders. Both mean and median values of controlling shareholder were 0.41. For hypothesis 3, foreign investor's ownership was employed (*Foreign-owner*) which has a mean (median) value of 9 (2) percentages and is calculated by the number of shares owned by foreign investors divided by the total number of ordinary shares.

Two sets of variables were used to capture firm performance. One was share return (*Sharereturn*) which is calculated by

TABLE 1: Variable definitions and summary statistics.

Variable	Definition	Mean	Median	Max	Min	Standard deviation	N
Outside director							
Od2board	The ratio of outside directors to board members	0.336	0.286	1	0	0.150	6970
Od2board_Tobit	Replaced <i>Od2board</i> with zero if <i>Od2board</i> < 0.25	0.303	0.286	1	0	0.192	6970
Firm characteristic							
Intangible asset	Intangible asset divided by asset	0.488	0.390	1	0	0.428	8031
Lnemployee	Natural logarithm of number of employees	6.129	6.006	11.532	0	1.434	7503
CS-owner	Controlling shareholder equity ownership	0.412	0.411	1	0	0.172	6982
Foreign-owner	Equity owned by foreign investors	0.090	0.020	0.929	0	0.142	8020
Share return	Continuously compounded rate of return	0.004	0.037	3.283	-7.249	0.536	7215
ROA	3-year average of net income divided by asset	0.036	0.039	5.262	-1.673	0.132	6084
FCF	Cash and cash equivalent divided by asset	0.058	0.039	0.795	0	0.064	8012
Man-owner	Executive board member's equity ownership	0.127	0.067	0.600	0	0.146	6536
Leverage	Total debt divided by equity	66.871	39.46	968.56	0	92.628	7930
Dividend	Dividend per share in 1,000 KRW	0.696	0.350	20	0	1.254	5419
TobinQ	Book value of debt plus market value of equity divided by book value of asset	0.977	0.799	53.751	-3.247	1.022	4654
Boardsize	Number of board members	6.240	6	15	0	3.387	6981
Chaebol	Unity if a firm belongs to a chaebol and zero otherwise	0.157	0	1	0	0.364	8411

Note: Variables except outside director are winsorised at upper and lower 5% each.

ROA, return on assets; FCF, free cash flow; Min, Minimum value; Max, Maximum value; N, Number.

constantly compounded rate of return. The other variable was return on assets (ROA) which is calculated by the net income divided by assets. Instead of a single year's ROA, 3-year averaged one was used to account for the fluctuations of ROA, which could be affected by noise factors other than real performance. Mean (median) values of *Sharereturn* and ROA were 0.4% (4) and 3.6% (3.9), respectively.

Following Jensen (1986) and Min and Chizema (2018), it was controlled for free cash flow (FCF), calculated by cash and its equivalents and scaled by asset value. The expected sign of the FCF is positive. This is because the more FCF, the more monitoring is required. It was controlled for the effect of the firm's capital structure using leverage (*Leverage*), calculated by book values of debt scaled by equity. A debt-ridden growth strategy without profitability was regarded as one of the causes of the 1997 crisis (Joh 2003; Min & Smyth 2014). As such, high leverage is expected to require more monitoring by outsiders during the sample periods. Executive managers' ownership (*Man-owner*) was also included. A common view in corporate governance literature is that managerial ownership mitigates contractual conflicts, which are generated by the separation of ownership between control and ownership (Cheng & Warfield 2005; Goranova et al. 2007; Jensen & Meckling 1976). Managerial ownership could, therefore, be viewed as a corporate governance mechanism that potentially complements or substitutes other governance tools in minimising agency problems.

While empirical evidence has revealed equivocal findings (Dalton et al. 2007), increased managerial ownership may increase executives' incentive to increase shareholder wealth, hence less need for added monitoring (Goranova et al. 2007). Increased interests and power through managerial ownership by insiders may lead to a reduced need for outsiders, who may be seen as an unnecessary cost. *TobinQ* was included to control for firm's investment opportunity (Gregorič et al. 2017). *TobinQ* is calculated by book value of debt plus market value of equity divided by book value of assets, where market value of equity is calculated by share price times number of issued ordinary shares. The sign of the estimated coefficient of this *TobinQ* is positive. *Boardsize* refers to total number of board members. *Dividend* is calculated by cash dividend

divided by share price in 1,000 Korean Won. In some of estimation models, a dummy variable was included for Korean business conglomerate (*Chaebol*) to examine any differences between affiliates to chaebols and non-chaebol firms. It was also controlled for industry and year fixed effects. Industry fixed effect was based on two-digit level of the KSIC.

Results

The descriptive statistics of all the variables are presented in Tables 1 and 2. Specifically, Table 1 presents the mean, median, standard deviation as well as minimum and maximum values, while Table 2 presents Pearson's pairwise correlations.

Figure 1 shows compliance patterns by listed firms. Results from this table show that listed firms' compliance strategies to the legal requirement are not homogeneous. For example, the upper panel of the table (i.e. point frequency) indicates that average 2.12% of the total listed firms did not appoint outside directors. More non-chaebol firms (2.48%) did not appoint outsider than chaebol affiliates (0.54%).

Second column of the upper panel shows 25.67% of the listed firms complied with 'just' the 25% rule. Interval frequency indicates 19.01% of total firms failed to meet the 25% rule. This figure, combined with the 25.67% of firms which just met the 25% rule, indicate that 55.32% (=100-25.67-19.01) of firms appointed outside director beyond the minimum legal requirement. As discussed earlier, these 55.32% firms are active adapters.

Interval frequency also shows that almost 49.05% of firms appointed outsiders between 25 and 33% of board members, followed by 19.01% of firms between 0 and 24% of board. Cumulative interval frequency at lower panel describes more than two thirds of firms appointed one outside director in three board members.

Turning to independent variables in Table 3, hypothesis 1 posits that firm complexity is positively associated with the appointment of outside directors beyond the minimum requirement. This hypothesis was examined by using

TABLE 2: Correlation matrix.

Variables	1	2	3	4	5	6	7	8	9	10	11
1. Od2board_Tobit	1	-	-	-	-	-	-	-	-	-	-
2. Intangibleasset	0.25*	1	-	-	-	-	-	-	-	-	-
3. Lnemployee	0.29*	0.19*	1	-	-	-	-	-	-	-	-
4. CS-owner	-0.05*	-0.07*	-0.14*	1	-	-	-	-	-	-	-
5. Foreign-owner	0.21*	0.07*	0.39*	-0.10*	1	-	-	-	-	-	-
6. ROA	-0.01*	-0.03*	0.08*	0.07*	0.13*	1	-	-	-	-	-
7. FCF	0.03*	0.05*	-0.04*	-0.05*	0.12	0.03*	1	-	-	-	-
8. Man-owner	-0.05*	-0.01	-0.08*	0.05*	-0.06	-0.05*	0.02	1	-	-	-
9. Leverage	0.09*	0.04*	0.08*	-0.05*	-0.15*	-0.02	-0.17*	-0.04*	1	-	-
10. Dividend	0.18*	0.04*	0.25*	-0.05*	0.36*	0.08*	0.04*	-0.15*	-0.09*	1	-
11. TobinQ	0.21*	0.09*	0.14*	-0.12*	0.16*	0.09*	0.07*	-0.04*	0.08*	0.18*	1
12. Boardsize	-0.01	-0.01	0.35*	-0.10*	0.23*	0.03*	-0.02	-0.02	0.04*	0.15*	0.00

Note: The table presents Pearson's pairwise correlations.

ROA, return on assets; FCF, free cash flow; *, Indicates significance at $p < 0.05$ level.

Firms	Point frequency						Total firms
	0.00	0.25	0.33	0.50	0.67	1.00	
Non-chaebol firms	141 2.48%	1606 28.26%	923 16.24%	379 6.67%	53 0.93%	27 0.47%	5682
Business group affiliates	7 0.54%	183 14.21%	102 7.92%	195 15.14%	44 3.42%	6 0.47%	1288
Total firms	148 2.12%	1789 25.67%	1025 14.71%	574 8.24%	97 1.39%	33 0.47%	6970
Interval frequency	-	(0.00,0.24)	(0.25,0.33)	(0.34,0.50)	(0.51,0.67)	(0.68,1.00)	-
Non-chaebol firms		20.80%	54.47%	17.67%	5.74%	1.32%	100.00%
Business group affiliates		11.10%	25.00%	24.69%	35.56%	3.65%	100.00%
Total		19.01%	49.05%	18.94%	11.25%	1.75%	100.00%
Cumulative interval frequency		19.01%	68.06%	87.00%	98.25%	100.00%	

Note: This table reports point frequency (upper panel), interval frequency (middle panel) and cumulative interval frequency (lower panel) of board structure, defined as the ratio of outside directors to board members. Figures in the upper and lower parts indicate observed numbers and percentages in total observations, respectively. Total number of firms in column 7 in upper panel (6,970) is greater than the sum of the numbers of each column (148+1,789+...) because these numbers of each column (148, 1,789...) represent numbers for only certain point of the ratio (i.e. 0.0, 0.25...). Cumulative interval frequency is calculated based on the interval frequency.

FIGURE 1: Distribution of board structure (ratio of outside directors to board) (number, %).

TABLE 3: Benchmark estimation results of excessive appointment of outside directors.

Variable	Tobit model					OLS	
	1	2	3	4	5	6	7
Intangibleasset	0.08*** (11.78)	0.06*** (6.25)	0.06*** (6.29)	0.04*** (4.49)	0.04*** (4.29)	0.06*** (6.66)	0.04*** (4.97)
CS-owner	-0.13*** (8.40)	-0.07*** (2.83)	-0.07*** (3.00)	-0.06** (2.55)	-0.06** (2.50)	-0.06*** (2.77)	-0.05** (2.44)
Foreign-owner	0.003*** (18.06)	0.00*** (6.93)	0.00*** (7.78)	0.00*** (4.64)	0.00*** (5.12)	0.00*** (6.53)	0.00*** (4.62)
Sharereturn	-0.001 (0.14)	-0.02** (2.32)	-0.02** (2.07)	-0.02*** (2.67)	-0.02** (2.54)	-0.01* (1.75)	-0.01** (1.90)
FCF	-	0.14* (1.74)	0.11 (1.39)	0.18** (2.41)	0.15** (1.97)	0.18*** (2.95)	0.23*** (3.87)
Leverage	-	0.00*** (7.12)	0.00*** (7.39)	0.00*** (5.32)	0.00*** (5.28)	0.00*** (6.92)	0.00*** (5.37)
Man-owner	-	-0.04 (1.48)	-0.08*** (3.11)	0.02 (0.99)	-0.01 (0.35)	-0.03 (1.39)	0.02 (1.14)
TobinQ	-	0.04*** (6.17)	0.03*** (5.32)	0.04*** (6.19)	0.03*** (5.38)	0.03*** (4.61)	0.03*** (4.62)
Boardsize	-	0.02*** (10.12)	0.02*** (10.91)	0.01*** (9.66)	0.02*** (10.38)	0.01*** (5.10)	0.01*** (4.77)
Dividend	-	0.01*** (4.36)	0.01*** (3.86)	0.01*** (2.85)	0.01*** (2.62)	0.01*** (4.88)	0.01*** (2.87)
Chaebol	-	-	-	0.13*** (13.95)	0.13*** (14.43)	-	0.12*** (13.79)
Year effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry effect	Yes	Yes	No	Yes	No	Yes	No
Intercept	0.21*** (3.97)	0.15** (2.09)	0.13*** (6.13)	0.33*** (4.68)	0.13*** (6.12)	0.18*** (3.82)	0.21*** (4.10)
Adjusted R^2	n.a.	n.a.	n.a.	n.a.	n.a.	0.36	0.41
N	6,727	2,831	2,831	2,831	2,831	2,831	2,831
Pseudo R^2	0.37	0.70	0.62	0.83	0.76	n.a.	n.a.

Note: Dependent variable is *Od2board_Tobit*. Numbers in parentheses are *t*-values.

FCF, free cash flow.

*, ** and *** indicate significance at 10%, 5% and 1% levels, respectively.

technology-related (*Intangibleasset*) complexity. This study found strong support for hypothesis 1, as the variable on firm complexity is positive and significant. Estimated coefficient of the *Intangibleasset* using Tobit model (Models 1–5) in Table 3 ranged between 0.04 and 0.08. *T*-statistics in brackets indicates that all these estimated coefficients are statistically significant with $p < 0.001$. This finding illustrates that the evidence for hypothesis 1 is robust irrespective of model specifications. Results in Models (6) and (7), based on OLS for comparison purpose,

also imply that this finding is robust even when a different estimation method is used.

Hypothesis 2 argues that controlling shareholders' power is negatively related to the appointment of outside directors beyond the minimum requirement, thus in line with passive adapters. Using controlling shareholder's ownership as proxy for the controlling shareholder's power, this study found supportive evidence for this hypothesis. As shown in Table 3 the coefficients are negative and significant at 1% in

TABLE 4: Estimation of excessive appointment of outside directors: a further restriction for large firms.

Variable	1	2	3	4	5	6
Intangibleasset	0.04*** (2.75)	0.05*** (2.91)	0.04** (2.55)	0.04** (2.55)	0.04** (2.56)	0.05*** (2.91)
CS-owner	-0.09** (2.40)	-0.09** (2.55)	-0.07* (1.64)	-0.09*** (2.58)	-0.09** (2.52)	-0.07* (1.65)
Foreign-owner	0.00* (1.81)	0.00** (2.51)	0.00** (2.31)	0.00** (2.20)	0.00** (2.55)	0.00** (2.31)
Sharereturn	-0.03** (2.42)	-0.03** (2.33)	-0.03** (2.34)	-0.03** (2.37)	-0.03** (2.14)	-0.03** (2.22)
Largefirm	0.20*** (12.77)	0.23*** (10.19)	0.23*** (7.03)	0.22*** (10.86)	0.21*** (13.06)	0.27*** (6.38)
Chaebol	0.03** (2.15)	0.02* (1.83)	0.02* (1.83)	0.02* (1.87)	0.02* (1.91)	0.02* (1.67)
FCF	0.15 (1.39)	0.08 (0.79)	0.09 (0.83)	0.08 (0.80)	0.09 (0.83)	0.07 (0.70)
Leverage	0.00** (2.36)	0.00*** (2.63)	0.00*** (2.59)	0.00** (2.50)	0.00** (2.56)	0.00** (2.51)
Man-owner	0.02 (0.64)	0.02 (0.54)	0.02 (0.53)	0.02 (0.66)	0.02 (0.60)	0.02 (0.47)
TobinQ	0.02** (2.28)	0.01* (1.86)	0.01** (1.99)	0.01** (1.98)	0.01** (1.97)	0.01* (1.87)
Boardsize	0.00 (1.63)	0.00* (1.68)	0.00 (1.64)	0.00 (1.61)	0.00* (1.66)	0.00 (1.59)
Dividend	0.00 (0.49)	0.00 (0.67)	0.00 (0.59)	0.00 (0.70)	0.00 (0.62)	0.00 (0.75)
Largefirm × Intangibleasset	- -	-0.04 (1.48)	- -	- -	- -	-0.04 (1.53)
Largefirm × CS-owner	- -	- -	-0.05 (0.74)	- -	- -	-0.07 (0.97)
Largefirm × Foreign-owner	- -	- -	- -	0.00 (0.59)	- -	0.00 (0.97)
Largefirm × Sharereturn	- -	- -	- -	- -	0.00 (0.15)	0.01 (0.34)
Year effect	Yes	Yes	Yes	Yes	Yes	Yes
Industry effect	Yes	No	No	No	No	No
Intercept	0.45*** (6.18)	0.23*** (7.17)	0.23*** (6.95)	0.24*** (7.55)	0.24*** (7.57)	0.22*** (6.42)
N	2,831	2,831	2,831	2,831	2,831	2,831
Pseudo R ²	0.77	0.73	0.73	0.73	0.73	0.73

Note: Dependent variable is *Od2board_Large*. This variable is replaced *Od2board* with zero if *Od2board* < 0.5. Numbers in parentheses are *t*-values.

FCF, free cash flow.

*, ** and *** indicate significance at 10%, 5% and 1% levels, respectively.

Models (1) through (3) without *Chaebol* and at 5% level in Models (4) and (5) with *Chaebol*. Again, these estimates using OLS in Models (6) and (7) are similar to the results using Tobit estimator.

Hypothesis 3 states that foreign ownership will be positively related to the appointment of outside directors beyond the minimum requirement, thus in line with active adapters. Estimated coefficients of foreign ownership (*Foreign-owner*) are positive and statistically significant at 1% level in Models (1) through (7), implying that increase in foreign ownership can attenuate the resistance by controlling shareholder's power.

Hypothesis 4 posits that firm financial performance will be associated with the appointment of outside directors beyond the minimum requirement. The estimated signs of the *Sharereturn* variable in Table 3 are consistent. *Sharereturn* as a proxy for the financial performance is negative but not significant in Model (1) without control variables.

However, *Sharereturn* with control variables became statistically significant at 5% level irrespective of model specifications (i.e. Models 2–5) and estimation methods (Models 6–7). This finding suggests that while firms with poor performance seek to improve their performance by seeking out alternative methods of governance, good firm performance can lead to resistance to organisational changes.

Estimates of most included control variables in Table 3 are as expected. Ownership by executive board member (*Man-owner*) is negative though statistical significance was observed only in Model (2). The coefficient of *Leverage* was positive and significant at 1% level irrespective of model specifications and estimation methods. This finding suggests that Korean listed companies were sensitive to risks associated with capital structure following the 1997 crisis. *TobinQ* was also positive and significant at 1% level throughout the models and different estimation methods.

Researchers often interpret Tobin Q as an indicator of a firm's investment opportunities. Similar to *Leverage*, this finding suggests changing behaviours of corporate strategies following the crisis. In other words, increasing investment opportunities invited more outsiders' monitoring rather than the traditional debt-ridden growth strategy. The positive sign of *Boardsize* is somewhat counter-intuitive. The positive sign might have captured some aspects of size-related complexity of the firm. *Dividend* was positively significant and this could have required a strengthened monitoring for controlling shareholders' tunneling behaviours (Bae et al. 2002; Chen et al. 2009). The positive sign of *FCF* is as expected because more free cash on hand requires more monitoring. However, statistical significance of *FCF* is not consistently found. Interestingly, the coefficient of *Chaebol* is positive and significant at 1% level. Chaebols have been popular places in job markets. Job experience with chaebol may improve the career opportunities of an outside director in the market. As such, chaebol could have appointed outside directors by having less transaction costs than non-chaebols. The results in Table 3 illustrate chaebols have appointed outside directors more actively than non-chaebol firms.

As described earlier, the Korean government requires large firms to appoint outside directors as at least 50% of board members. As such, one may be concerned that this strengthened regulation may cause a bias to the estimation. To address this issue, I defined dependent variables differently with modifications of model specifications. Firstly, the dependent variable is defined the same way as in Table 3 except the lower restriction point is 0.5. That is, the ratio of outsiders to board members was replaced with zero if the ratio is equal to or less than 0.5 which is a minimum requirement of large firm. Secondly, I generated a binary variable for large firm (*Largefirm*) which is equal to 1 if a firm belongs to the large firm and zero otherwise. Results of the four main independent variables in Table 4 are qualitatively similar to the ones in Table 3 irrespective of model specifications. As expected, *Largefirm* was positive and significant through Models 1–6. This finding indicates that the appointment of outsiders beyond the 50% mark was more evident than by smaller firms.

In contrast to the results in Table 3, variables of *Boardsize* and *Dividend* were not significant though the signs are consistent. Results in Models 2–6 indicate that none of the interaction variables between *Largefirm* and the four main independent variables was significant, suggesting no moderation effect by large firm.

For further robustness checks, the models using different proxy variables were rerun (not reported). To account for the difficulty of finding a good proxy for the complexity, natural logarithm of number of employees (*Lemployee*) was used. Considering the inconsistency of the statistical significance of *Sharereturn* to proxy performance, 3-year average of rate of return (ROA) also was used. Results illustrate that the main findings are robust against using different proxies.

Conclusions

Drawing on arguments grounded in the selective adaptation model, this article has examined an important issue involving the appointment of outside directors in a context not traditionally associated with this governance mechanism. Specifically, it was investigated why some firms go beyond the minimum requirement of appointing a specified proportion of outside directors on the board while others do not. This was carried out by studying the behaviour of listed Korean firms under two different classifications: actively adaptive firms and passively adaptive firms.

While many studies have studied organisational responses to institutional pressure, some important aspects have been missed in this endeavour. For example, these studies have not distinguished the origin of institutional pressures. Specifically, they have not considered institutional pressures that originate from a foreign or alternative corporate governance model. Moreover, they have not considered a situation where firms adopt a practice beyond the legal minimum requirement, at least in the context of corporate governance practices in Korea.

As such, the study provides evidence of the utility of the selective adaptation perspective to explain corporate governance reforms and subsequent adoption of practices in Korea. Selective adaptation helps to understand the origins and implications of local interpretation of imported governance practices, thus illuminating distinctions between local contextualisation of familiar institutional arrangements and truly innovative local approaches that depart from the confines of imported governance forms.

Firstly, it was observed that firm complexity is positively associated with the appointment of outside directors. Owing to the range of functions and activities that complex firms have to handle, such firms understand the need for more and varied expertise. While this practice is foreign to Korean firms, the positive perception that results from the need is likely to mean the appointment of more outside directors.

Findings from the second hypothesis suggest that controlling shareholders' power is negatively associated with the appointment of outside directors. This finding supports controlling shareholders' perception that the introduction of outside director system is mainly to monitor controlling shareholders. The selective adaptation theory implies that a controlling shareholder would refuse monitoring even if it is legitimate.

The third hypothesis shows that foreign ownership is positively associated with the excessive appointment of outside directors. The confirmation of this hypothesis in the case of Korean firms suggests foreign investors could have influenced organisations to be proactive directly or indirectly.

Finally, the fourth hypothesis suggests that performance is negatively associated with the appointment of outside directors. This finding supports perceptions that poor performance pushes firms to improve their performance by seeking out alternative methods of governance, but good performance leads to resistance to organisational changes. That is, organisational decision-makers will adopt imported practices when they perceive them to be potentially beneficial to the organisation (Chatterji & Toffel 2010).

The findings contribute to the growing stream of literature on the adoption of corporate governance elements across governance models (Okhmatovskiy & David 2012; Short & Toffel 2010). Such a contribution has implications for the long-standing discussion on the convergence or divergence from the Anglo-American model of corporate governance model. A conclusion, and of course a managerial implication, from this article would be that individual firms make choices from a variety of mechanisms contingent on their circumstances including ownership structure, performance and level of complexity. This study also extends the application of the selective adaptation model, beyond legal studies, to strategic management. This way, the possibility of heterogeneity is demonstrated in firm decisions towards the adoption of a foreign and contestable aspect of management. There is an active debate on the level of board independence in many countries. This study thus provides interesting insights that may be applicable to countries in which there are mandatory requirements for the board composition (e.g. mandatory board gender diversity in Norway [40% female directors], BBBEE in South Africa, etc.).

Acknowledgements

The author would like to thank the Soonchunhyang University for funding this study.

This work was supported by the Soonchunhyang University Research Fund.

Competing interests

The author declares that he has no financial or personal relationships which may have inappropriately influenced him in writing this article.

References

- Bae, K.H., Kang, J.K. & Kim, J.M., 2002, 'Tunneling or value added? Evidence from mergers by Korean business groups', *Journal of Finance* 57(6), 2695–2740. <https://doi.org/10.1111/1540-6261.00510>
- Baek, J.S., Kang, J.K. & Park, K.S., 2004, 'Corporate governance and firm value: Evidence from the Korean financial crisis', *Journal of Financial Economics* 71, 265–313. [https://doi.org/10.1016/S0304-405X\(03\)00167-3](https://doi.org/10.1016/S0304-405X(03)00167-3)
- Berrone, P. & Gomez-Mejia, L.R., 2009, 'Environmental performance and executive compensation: An integrated agency-institutional perspective', *Academy of Management Journal* 52, 103–126. <https://doi.org/10.5465/amj.2009.36461950>
- Beuselinck, C., Joos, P.P.M., Khurana, I.K. & Meulen, S., 2017, 'Which analysts benefited most from mandatory IFRS adoption in Europe?', *Journal of International Accounting Research* 16(3), 171–190. <https://doi.org/10.2308/jiar-51918>
- Biukovic, L., 2008, 'Selective adaptation of WTO transparency norms and local practices in China and Japan', *Journal of International Economic Law* 11(4), 803–825. <https://doi.org/10.1093/jiel/jgn028>
- Boeker, W. & Goodstein, J., 1991, 'Organizational performance and adaption: Effects of environment and performance on change in board composition', *Academy of Management Journal* 34(4), 805–826.
- Bøhren, Ø. & Siv Staubo, S., 2016, 'Mandatory gender balance and board independence', *European Financial Management* 22(1), 3–30. <https://doi.org/10.1111/eufm.12060>
- Boone, A.L., Field, L.C., Karpoff, J.M. & Raheja, C.G., 2007, 'The determinants of corporate board size and composition: An empirical analysis', *Journal of Financial Economics* 85(1), 66–101. <https://doi.org/10.1016/j.jfineco.2006.05.004>
- Bourgeois, L.J., 1981, 'On the measurement of organizational slack', *Academy of Management Journal* 6(1), 29–39.
- Brown, P., Preiato, J. & Tarca, A., 2014, 'Measuring country differences in enforcement of accounting standards: An audit and enforcement proxy', *Journal of Business Finance & Accounting* 41(1) & (2), 1–52.
- Buck, T. & Shahrim, A., 2005, 'The translation of corporate governance changes across national cultures: The case of Germany', *Journal of International Business Studies* 36(1), 42–61. <https://doi.org/10.1057/palgrave.jibs.8400109>
- Cameron, K., Kim, M. & Whetten, D., 1987, 'Organizational effects of decline and turbulence', *Administrative Science Quarterly* 32(2), 222–240. <https://doi.org/10.2307/2393127>
- Chatterji, A.K. & Toffel, M.W., 2010, 'How firms respond to being rated', *Strategic Management Journal* 31(9), 917–945. <https://doi.org/10.1002/smj.840>
- Chen, D., Jian, M. & Xu, M., 2009, 'Dividends for tunneling in a regulated economy: The case of China', *Pacific-Basin Finance Journal* 17, 209–223. <https://doi.org/10.1016/j.pacfin.2008.05.002>
- Cheng, Q. & Warfield, T.D., 2005, 'Equity incentives and earnings management', *Accounting Review* 80, 441–476. <https://doi.org/10.2308/accr.2005.80.2.441>
- Chizema, A. & Kim, J., 2010, 'Outside directors on Korean boards: Governance and institutions', *Journal of Management Studies* 47(1), 109–129. <https://doi.org/10.1111/j.1467-6486.2009.00868.x>
- Christensen, C.M. & Van Bever, D., 2014, 'The capitalist's dilemma', *Harvard Business Review* 92(6), 60–68.
- Dalton, D.R., Hitt, M.A., Certo, S.T. & Dalton, C.M., 2007, 'The fundamental agency problem and its mitigation: Independence, equity and the market for corporate control', *Academy of Management Annals* 1(1), 1–64. <https://doi.org/10.5465/078559806>
- Del Brio, E.B., Maia-Ramires, E.L. & Miguel, A.D., 2011, 'Ownership structure and diversification in a scenario of weak shareholder protection', *Applied Economics* 43, 4537–4547. <https://doi.org/10.1080/00036846.2010.491472>
- Durbach, I.N. & Parker, H., 2009, 'An analysis of corporate board networks in South Africa', *South African Journal of Business Management* 40(2), 15–26.
- Gómez-Mejia, L.R., Cruz, C., Berrone, P. & De Castro, J., 2011, 'The bind that ties: Socioemotional wealth preservation in family firms', *Academy of Management Annals* 5(1), 653–707. <https://doi.org/10.5465/19416520.2011.593320>
- Gómez-Mejia, L.R., Makri, M. & Larraza-Kintana, M., 2010, 'Diversification decisions in family-controlled firms', *Journal of Management Studies* 47(2), 223–252. <https://doi.org/10.1111/j.1467-6486.2009.00889.x>
- Goranova, M., Alessandri, T.M., Brandes, P. & Ravi, R., 2007, 'Managerial ownership and corporate diversification: A longitudinal view', *Strategic Management Journal* 28(3), 211–225. <https://doi.org/10.1002/smj.570>
- Greenwood, R., Raynard, M., Kodeih, F., Micelotta, E.R. & Loundsbury, M., 2011, 'Institutional complexity and organizational responses', *The Academy of Management Annals* 5, 317–371. <https://doi.org/10.5465/19416520.2011.590299>
- Gregorič, A., Oxlheim, L., Randøy, T. & Thomsen, S., 2017, 'Resistance to change in the corporate elite: Female directors' appointments onto Nordic boards', *Journal of Business Ethics* 141, 267–287. <https://doi.org/10.1007/s10551-015-2703-4>
- Haynes, K.T. & Hillman, A., 2010, 'The effect of board capital and CEO power on strategic change', *Strategic Management Journal* 31(11), 1145–1163. <https://doi.org/10.1002/smj.859>
- He, W. & Lu, C., 2018, 'Why do analysts issue sales forecasts? Evidence from mandatory IFRS adoption', *Accounting Horizons* 32(1), 121–141. <https://doi.org/10.2308/acch-51941>
- Herbst, P. & Prüfer, J., 2016, 'Firms, nonprofits, and cooperatives: A theory of organizational choice', *Annals of Public & Cooperative Economics* 87(3), 315–343. <https://doi.org/10.1111/apce.12130>
- Hermalin, B.E. & Weisbach, M.S., 1998, 'Endogenously chosen boards of directors and their monitoring of the CEO', *American Economic Review* 88(1), 96–118.
- Jensen, M.C., 1986, 'The agency costs of free cash flow: Corporate finance and takeovers', *American Economic Review* 76(2), 323–329.
- Jensen, M. & Meckling, W.H., 1976, 'Theory of the firm: Managerial behaviour, agency costs and capital structure', *Journal of Financial Economics* 3(4), 305–360. [https://doi.org/10.1016/0304-405X\(76\)90026-X](https://doi.org/10.1016/0304-405X(76)90026-X)
- Jin, Y., 2017, 'DuPont analysis, earnings persistence, and return on equity: Evidence from mandatory IFRS adoption in Canada', *Accounting Perspectives* 16(3), 205–235. <https://doi.org/10.1111/1911-3838.12142>
- Joh, S.W., 2003, 'Corporate governance and firm profitability: Evidence from Korea before the economic crisis', *Journal of Financial Economics* 68(2), 287–322. [https://doi.org/10.1016/S0304-405X\(03\)00068-0](https://doi.org/10.1016/S0304-405X(03)00068-0)
- Khurana, R., 2001, 'Finding the right CEO: Why boards often make poor choice', *MIT Sloan Management Review* 43(1), 91–95.
- Kim, I.J., Eppler-kim, J., Kim, W. & Byun, S.J., 2010, 'Foreign investors and corporate governance in Korea', *Pacific-Basin Finance Journal* 18(4), 390–402. <https://doi.org/10.1016/j.pacfin.2010.04.002>

- Kroll, M., Walters, B.A. & Wright, P., 2005, 'Board vigilance, director experience and corporate outcomes', *Strategic Management Journal* 29(4), 363–382. <https://doi.org/10.1002/smj.649>
- Levinthal, D.A., 1991, 'Organizational adaptation and environmental selection: Interrelated processes of change', *Organization Science* 2(1), 140–145. <https://doi.org/10.1287/orsc.2.1.140>
- Linck, J.S., Netter, J.M. & Yang, T., 2008, 'The determinants of board structure', *Journal of Financial Economics* 87(2), 308–328. <https://doi.org/10.1016/j.jfineco.2007.03.004>
- Maria, D.A., 2016, 'Intangible assets as a source of competitiveness in the post-crisis economy. The role of brands', *Theoretical & Applied Economics* 20(12), 127–138.
- Min, B.S., 2016, 'Reform of corporate governance: The case of Korea', *Asian Journal of Political Science* 24, 21–41. <https://doi.org/10.1080/02185377.2015.1106956>
- Min, B.S. & Smyth, R., 2014, 'Corporate governance, globalization and firm productivity', *Journal of World Business* 49(3), 372–385. <https://doi.org/10.1016/j.jwb.2013.07.004>
- Min, B.S. & Chizema, A., 2015, 'Outside director's board meeting attendance', *Journal of Business Ethics* 13, 187–214.
- Min, B.S. & Chizema, A., 2018, 'Board meeting attendance by outside directors', *Journal of Business Ethics* 147(4), 901–917. <https://doi.org/10.1007/s10551-015-2990-9>
- Nakamura, M., 2011, 'Adoption and policy implications of Japan's new corporate governance practices after the reform', *Asia Pacific Journal of Management* 28(1), 187–213. <https://doi.org/10.1007/s10490-010-9230-8>
- Natividad, G., 2013, 'Multidivisional strategy and investment returns', *Journal of Economics & Management Strategy* 22(3), 594–616. <https://doi.org/10.1111/jems.12018>
- Ntim, C.G., 2013, 'Corporate governance, affirmative action and firm value in Post-apartheid South Africa: A simultaneous equation approach', *African Development Review* 25(2), 148–172. <https://doi.org/10.1111/j.1467-8268.2013.12021.x>
- Ntim, C.G. & Soobaroyen, T., 2013, 'Black economic empowerment disclosures by South African listed corporations: The influence of ownership and board characteristics', *Journal of Business Ethics* 116, 121–138. <https://doi.org/10.1007/s10551-012-1446-8>
- Okhmatovskiy, I. & David, R.J., 2012, 'Setting your own standards: Internal corporate governance codes as a response to institutional pressure', *Organization Science* 23(1), 155–176. <https://doi.org/10.1287/orsc.1100.0642>
- Organisation for Economic Co-operation and Development (OECD), 2001, *Corporate governance in Asia: A comparative perspective*, OECD, Paris.
- Orlitzky, M., Schmidt, F.L. & Rynes, S.L., 2003, 'Corporate social and financial performance, A meta-analysis', *Organization Studies* 24(3), 403–441. <https://doi.org/10.1177/0170840603024003910>
- Pache, A.C. & Santos, F., 2010, 'When worlds collide: The internal dynamics of organizational responses to conflicting institutional demands', *Academy of Management Review* 35, 455–476.
- Petry, S., 2018, 'Mandatory worker representation on the board and its effect on shareholder wealth', *Financial Management* 47(1), 25–54. <https://doi.org/10.1111/fima.12181>
- Potter, P.B., 2004, 'Legal reform in China: Institutions, culture and selective adaptation', *Law and Social Inquiry* 29(2), 465–495. <https://doi.org/10.1111/j.1747-4469.2004.tb00343.x>
- Rawley, E., 2010, 'Diversification, coordination costs and organizational rigidity: Evidence from microdata', *Strategic Management Journal* 31(8), 873–891. <https://doi.org/10.1002/smj.838>
- Reed, D., 2002, 'Corporate governance reforms in developing countries', *Journal of Business Ethics* 37, 223–247. <https://doi.org/10.1023/A:1015239924475>
- Russell, M., 2017, 'Management incentives to recognise intangible assets', *Accounting and Finance* 57, 211–234. <https://doi.org/10.1111/acfi.12154>
- Sanders, W. & Carpenter, M.A., 2003, 'Strategic satisfying? A behavioral-agency theory perspective on stock repurchase program announcements', *Academy of Management Journal* 46(2), 160–178.
- Saunders, A. & Brynjolfsson, E., 2016, 'Valuing information technology related intangible assets', *MIS Quarterly* 40(1), 83–110. <https://doi.org/10.25300/MISQ/2016/40.1.04>
- Schwindt, R. & McDaniels, D., 2008, 'Competition policy, capacity building, and selective adaptation: Lessons from Japan's experience', *Washington University Global Studies Law Review* 7, 35–86.
- Short, J.L. & Toffel, M.W., 2010, 'Making self-regulation more than merely symbolic: The critical role of the legal environment', *Administrative Science Quarterly* 55(3), 361–396. <https://doi.org/10.2189/asqu.2010.55.3.361>
- Sun, J., Yuan, R. Cao, F. & Wang, B., 2017, 'Principal–principal agency problems and stock price crash risk: Evidence from the split-share structure reform in China', *Corporate Governance: An International Review* 25(3), 186–199. <https://doi.org/10.1111/corg.12202>
- Sundaramurthy, C., 1996, 'Corporate governance within the context of antitakeover provisions', *Strategic Management Journal* 17(5), 377–394. [https://doi.org/10.1002/\(SICI\)1097-0266\(199605\)17:5<377::AID-SMJ816>3.0.CO;2-B](https://doi.org/10.1002/(SICI)1097-0266(199605)17:5<377::AID-SMJ816>3.0.CO;2-B)
- Testa, F., Boiral, O. & Iraldo, F., 2018, 'Internalization of environmental practices and institutional complexity: Can stakeholders pressures encourage greenwashing?', *Journal of Business Ethics* 147, 287–307. <https://doi.org/10.1007/s10551-015-2960-2>
- Tuggle, C.S., Sirmon, D.G., Reutzel, C.R. & Bierman, L., 2010, 'Commanding board of director attention: Investigating how organizational performance and CEO duality affect board members' attention to monitoring', *Strategic Management Journal* 31(9), 946–968. <https://doi.org/10.1002/smj.847>
- Young, M.N., Peng, M.W., Ahlstrom, D., Bruton, G.D. & Jiang, Y., 2008, 'Corporate governance in emerging economies: A review of principal–principal perspective', *Journal of Management Studies* 45(1), 196–220. <https://doi.org/10.1111/j.1467-6486.2007.00752.x>
- Witt, P., 2004, 'The competition of international corporate governance systems-A German perspective', *Management International Review* 44(3), 309–333.
- Zardkoobi, A., Harrison, J. & Josefy, M.A., 2017, 'Conflict and confluence: The multidimensionality of opportunism in principal–agent relationships', *Journal of Business Ethics* 146, 405–417.
- Zeitlin, J. & Herrigel, G., 2000, *Americanization and its limits: Reworking US technology and management in post-war Europe and Japan*, Oxford University Press, Oxford.