

Institutional Investors and Corporate Governance

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Abstract

This study aims to explore the role of institutional investors in the improvement of corporate governance within the companies in which they invest (investee companies). This aim is accomplished by analysing evidence concerning the characteristics of numerous companies' boards of directors, and of their key subcommittees, listed across the globe. These characteristics are related to board attributes (composition, activity, entrenchment and busyness) and board diversity (gender, age, nationality and education). Furthermore, this study also seeks to investigate the behaviour of institutional investors in improving corporate governance by considering different settings, including various economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures.

Using a sample collected from 15 countries for the period of 2006 to 2012, this study finds that institutional investors promote more favourable corporate governance outcomes, with foreign institutional investors playing a lead role in the improvement and convergence of corporate governance practices around the world. This study provides evidence that institutional investors promote the enhanced composition of boards and of their audit and compensation committees, though not of nomination committees. Furthermore, institutional investors are positively associated with the activity of audit committees but not with the activity of boards nor of compensation and nomination committees. The results also demonstrate that institutional investors reduce board entrenchment though no evidence is found that institutional investors reduce board busyness. The findings also suggest that the role of institutional investors in corporate governance is determined by a company's institutional environment including the prevalent economic condition, the legal system and the ownership structure of the country in which it operates. In particular, the findings show that institutional investors play a stronger role in the improvement of governance structures during crisis and post-crisis periods than they do during pre-crisis times. This result is also applicable to individual board attributes, such as

the independence of audit committees. Additionally, institutional investors improve the independence of boards and of their key subcommittees (with the exception of nomination committees) in civil law countries and reduce board busyness in common law countries. However, there is no evidence that institutional investors reduce board entrenchment in either legal system. Furthermore, the results indicate that they improve governance outcomes in non-family-owned firms but not in family-owned firms.

Moreover, this study presents no evidence that institutional investors promote board diversity; in fact, this study generally finds no association between institutional ownership and various board diversity attributes such as gender, age, nationality and education. However, the findings do show that institutional investors are positively associated with the education diversity of boards during times of crisis and are negatively associated with board age diversity during pre-crisis and post-crisis periods. Furthermore, while in common law countries institutional investors are found to be negatively associated with board age diversity, they have no influence over board diversity attributes (i.e., gender, age, nationality and education) in civil law countries. The results also suggest that the associations between institutional investors and board diversity are mixed and insignificant within different ownership structures, i.e. in family- and non-family-owned firms.

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Dedication

‘This thesis is dedicated to my family.’

Presented Papers

Parts of this thesis were presented at the following conferences and colloquiums:

Institutional Investors and Corporate Governance (with C. Mallin and F. Cuomo). Paper presented at the Second Annual International Corporate Governance Society Conference; Boston, US, October 2016.

Institutional Investors and Corporate Governance (with C. Mallin and F. Cuomo). Paper presented at the Portsmouth-Fordham Conference on Banking & Finance; Portsmouth, UK, September 2016.

Institutional Investors and Corporate Governance. Paper presented at the Doctoral Colloquium of the European Academy of Management; Warsaw, Poland, June 2015.

Institutional Investors and Corporate Governance. Paper presented at the Second Young Finance Scholars Conference; Sussex, UK, June 2015.

Institutional Investors and Corporate Governance. Paper presented at the Doctoral Colloquium of the British Accounting and Finance Association; Manchester, UK, March 2015.

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List of Abbreviations

AFEP	Association Française des Entreprises Privées
AGM	Annual General Meeting
ASX	Australian Stock Exchange
CEO	Chief Executive Officer
CNMV	Comisión Nacional del Mercado de Valores
FE	Fixed Effect
FRC	Financial Reporting Council
GMI	Governance Metrics International
GMM	Generalised Methods of Moments
IAIM	Irish Association of Investment Managers
ICGN	International Corporate Governance Network
INED	Independent Non-Executive Director
ISC	Institutional Shareholders Committee
MEDEF	Mouvement des Entreprises de France
NCGB	Norwegian Corporate Governance Board
OECD	The Organisation for Economic Co-operation and Development
OLS	Ordinary Least Squares
RE	Random Effect
SEC	Securities and Exchange Commission
S&P	Standard and Poor's
TSX	Toronto Stock Exchange
VIF	Variance Inflation Factor

Chapter 1

1.0 Overview of the Research

1.1. Research Background and Motivation

Institutional investors maintain a notable presence in, and exercise growing influence over, global capital markets. The increasing growth of their worldwide investments affords them the opportunity to influence the behaviour of investee firms through their monitoring activities (Gillan and Starks, 2003; Mallin, 2016). Generally, institutional investors who are dissatisfied with company performance or with the governance structure of a company may choose to sell their company shares ('exit') or opt to engage with their investee firms ('voice') (Martin et al., 2007; Ferreira and Matos, 2008). Since the 'exit' option is considered costly, mostly large and active institutional investors choose to engage with their investee firms in order to alter unfavourable governance structures and to correct undesirable performance (Jin, 2006; McCahery et al., 2016). This engagement between institutional investors and their investee firms can assume many forms, such as one-to-one meetings, voting, shareholder proposals and resolutions, focus lists and corporate governance rating systems (Martin et al., 2007; Mallin, 2016). More recently, studies show that one-to-one meetings held behind-the-scenes are considered an effective approach that is regularly used by institutional investors to enhance the governance structures of their investee firms (see for example; McCahery et al., 2016). Moreover, the stewardship codes and guidelines issued by several institutions in various countries represent a significant move towards improved interactions between institutional investors and their investee firms, as they aim to promote positive governance structures (Haxhi et al., 2013; McNulty and Nordberg, 2016).

A corporate board is considered to be the main governing mechanism that mitigates the agency costs that arise from the separation of ownership and control (Fama and Jensen, 1983). Given that boards exist as the centre of decision-making policy, much attention has been paid to their

attributes (Solomon, 2013; Mallin, 2016). For instance, Useem et al. (1993) provided evidence that the composition and functionality of a company's board are crucial considerations for US-based institutional investors. Furthermore, following the completion of a global survey of 200 institutional investors, Coombes and Watson (2000) found that most institutional investors consider the attributes of a corporate board to be as important as a company's financial performance. Furthermore, Chung and Zhang (2011) also found that institutional investors favour firms with higher board independence, as these firms are associated with lower monitoring costs. Accordingly, this study posits that institutional investors will improve board characteristics by establishing various engagement channels with their investee firms. These characteristics are related to the attributes (composition, activity, entrenchment and busyness) and diversity qualities (gender, age, nationality and education) of corporate boards and their key subcommittees.

Several corporate governance studies have highlighted the importance of national institutional factors in explaining corporate governance phenomena (Aguilera et al., 2008; Aguilera et al., 2012; Aslan and Kumar, 2014; Kim and Ozdemir, 2014; Iannotta et al., 2015). One such institutional factor is the economic condition of a country (Essen et al., 2013; McNulty et al., 2013). Interestingly, the weakness of corporate governance in many countries is largely considered to have been a main contributor to the onset of the recent financial crisis (Akbar et al., 2017). Several studies have suggested that both institutional investors and corporate boards are to blame for their inability to prevent that crisis from occurring (Conyon et al., 2011; Reisberg, 2015). In response to such a devastating crisis, several countries introduced or revised their corporate governance codes in an attempt to strengthen their governance practices (Adams; 2012; Cuomo et al., 2016). Moreover, in the wake of the recent financial crisis, several countries issued stewardship codes and guidelines (beginning with the UK in 2010) in an effort to encourage and enhance engagement between institutional investors and their investee firms

(ICGN, 2017). However, we still know little about the role played by institutional investors in efforts to improve corporate governance with respect to the recent financial crisis. Therefore, this study also aims to examine the role of institutional investors in the improvement of corporate board characteristics in light of various economic conditions (pre-crisis, crisis and post-crisis periods).

Additionally, the bundle perspective of comparative corporate governance (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014) argues that differences between board attributes across countries cannot be studied without also considering at least two other governance characteristics—legal system and ownership structure—as each of these characteristics is contingent upon the strength and prevalence of the other. Previous studies have shown that the legal system of a country (i.e., common or civil law) affects its accepted levels of investor protection (strong versus weak) (La Porta et al., 1998; La Porta et al., 2000). To this end, La Porta et al. (1998) argued that in countries where investor protection rights are weak, investors may seek other means of protection. As a board of directors is entrusted with the protection of shareholder interests, institutional investors can improve corporate board characteristics to a greater degree in countries where shareholder protections are weak. Thus, this study complements previous empirical findings (Aggarwal et al., 2011) by investigating the capacity of institutional investors to improve a wide range of board characteristics within various legal systems (common versus civil law systems).

Moreover, previous studies on this topic (see, for example, Aggarwal et al., 2011; Ferreira and Matos, 2008) have failed to consider a firm's controlling shareholders when examining the role of institutional investors in the improvement of corporate governance. However, ownership structures are an important component of the bundle perspective of global corporate governance practices (Aguilera et al. 2012). Corporate governance practices and outcomes cannot be properly investigated without also considering the pivotal function of a firm's

ownership structure (Aguilera and Crespi-Cladera, 2016; Desender et al., 2013; Judge, 2011; Judge, 2012; Sure et al., 2013). Indeed, ownership structures vary across countries; widely-held firms are more common in the US and the UK, while firms with concentrated ownership structures are more common in continental European countries (La Porta et al., 1999). On the one hand, the presence of controlling shareholders might be beneficial; this might be because they have the incentive to better monitor managers' actions due to their ownership interests. On the other hand, controlling shareholders might expropriate the interests of minority shareholders in favour of their own (Shleifer and Vishny, 1997). In such a context, this research aims to examine the role of institutional investors in improving the governance structures of companies with various ownership structures (concentrated or dispersed ownership systems).

1.2. Research Objectives and Questions

In light of the above discussion, this research aims to examine the role of institutional investors in the improvement of corporate governance via the use of an international sample of corporate boards and their key subcommittees. In so doing, this study will examine various characteristics related to both board attributes (composition, activity, entrenchment and busyness) and board diversity (gender, age, nationality and education). This research also aims to investigate institutional investors' role in improving corporate governance in companies across different settings, including a variety of economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. In order to achieve these objectives, this study seeks to answer the following six questions:

1. Do institutional investors influence corporate board attributes?
2. Do institutional investors influence the characteristics of a board's key subcommittees?
3. Do institutional investors influence board diversity?

4. Do institutional investors play different roles within different economic environments (pre-crisis, crisis and post-crisis periods)?
5. Do institutional investors play different roles within different legal systems?
6. Do institutional investors play different roles according to whether they operate within concentrated or dispersed ownership structures?

1.3. Scope of the Study

The research scope of this study is limited by three specific parameters: (i) location, (ii) unit of analysis and (iii) investigation period. First, this research has an international scope and therefore considers an international sample. This sample includes firms listed on the major stock exchanges of 15 countries, namely Australia, Belgium, Canada, Denmark, Finland, France, India, Ireland, Italy, Netherlands, Norway, Spain, Sweden, Switzerland and the UK. Second, the unit of analysis is related to two particular components: institutional investors from around the world and boards of directors in the sample countries. Third, this study covers the years between 2006 and 2012; this period was chosen in order to fully capture the role of institutional investors in improving corporate governance within various economic environments (pre-crisis, crisis and post-crisis periods).

1.4. Structure of the Study

This thesis consists of nine chapters, which are described as follows. *Chapter 1* provides a brief overview of the research background and motivation; additionally, this chapter highlights the research objectives, questions and scope. *Chapter 2* reviews the theoretical aspects of this study, beginning with a review of agency theory, which is considered to be the predominant theory in the field of corporate governance. Chapter 2 also reviews several other relevant theories, such as the stewardship, resource dependence, institutional and stakeholder theories. Finally, chapter 2 discusses the multiple theoretical frameworks of the study. *Chapter 3*

discusses the features of international corporate governance, in the process describing the importance of a corporate board and its key subcommittees and explaining the various corporate board structures that are used around the world. This chapter also highlights the role of financial crises, legal systems and ownership structures in corporate governance and illustrates the different approaches that are most often adopted, such as insider versus outsider structures and hard versus soft law systems. Finally, Chapter 3 highlights the development history and main features of corporate governance for each country included in the sample.

Chapter 4 reviews existing literature on the role of institutional investors in the improvement of corporate governance. The chapter begins with a definition of the various types of institutional investors and then moves on to an illustration of the tools used by institutional investors to influence the governance structures of their investee firms. This chapter also discusses the various national and transnational stewardship codes and guidelines that have been established across the globe. Finally, Chapter 4 concludes with a review of the major empirical studies that have been published on this topic.

Chapter 5 presents the hypothesis development; notably, this discussion is divided into two sections. The first section reviews the hypotheses that concern the role of institutional investors in improving various attributes related to a corporate board and its key subcommittees (composition, activity, entrenchment and busyness). The second section reviews the hypotheses that involve institutional investors' influence over board diversity (gender, age, nationality and education).

Chapter 6 describes the methodology that was adopted in order to test the hypotheses that were developed for this research study. The chapter begins by clarifying the research philosophy and approach. Then, the sample selection, period and data sources are explained. Additionally, Chapter 6 outlines the variables used in this study and describes and justifies the selection of firm fixed effect panels as the primary estimation technique. This chapter also illustrates the

main models used in the study and concludes with a description of the various robustness checks utilised to verify the main results.

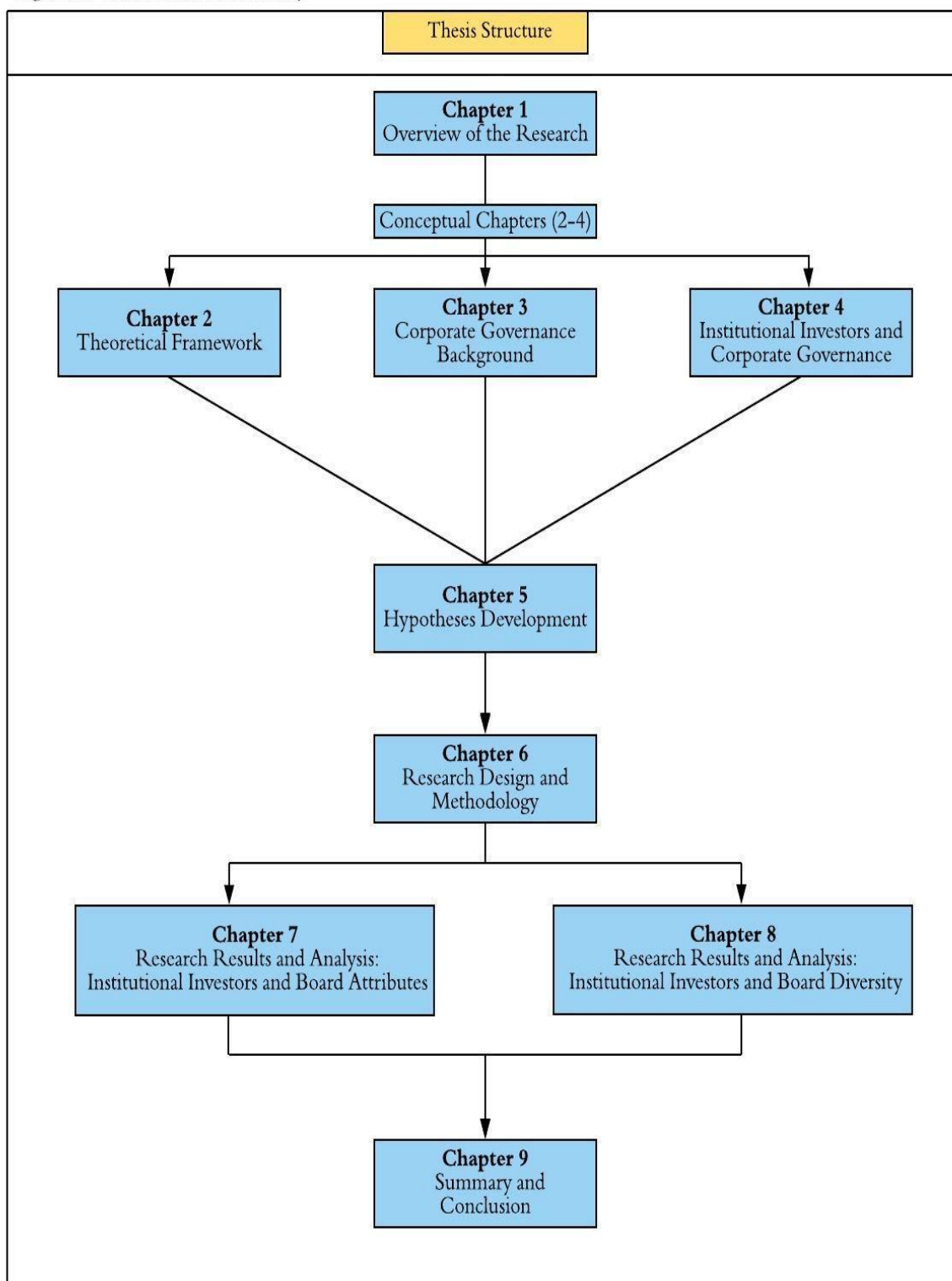
Chapter 7 presents the results of the role of institutional investors in improving board attributes. It illustrates the results of the descriptive statistics and of the correlation matrix and describes the empirical analysis, study findings, and robustness test results.

Chapter 8 presents the results of the role of institutional investors in improving board diversity. It provides the results of the descriptive statistics and of the correlation matrix and describes the empirical analysis, study findings, and robustness test results.

Finally, *Chapter 9* summarises this study by first restating the research questions and objectives. This chapter then explains the main findings and research implications which can be directed towards policy-makers and regulators who seek to enhance the role of institutional investors in the improvement of global corporate governance. This chapter also clarifies and justifies this study's contribution to the field. Ultimately, Chapter 9 concludes by identifying the research limitations and discussing potential directions for further research.

The structure of this thesis is illustrated below in Figure 1.1.

Figure 1.1 The structure of the study



Chapter 2

2.0 Theoretical Framework

2.1. Introduction

This chapter presents the theoretical framework of this research; to that end, five main theories are considered, each of which is well-known within the corporate governance discipline. These theories include agency theory, stewardship theory, resource dependence theory, institutional theory and stakeholder theory¹. This chapter is outlined as follows: section 2.2 discusses agency theory, section 2.3 covers stewardship theory, section 2.4 reviews resource dependence theory, section 2.5 explains institutional theory, section 2.6 examines stakeholder theory, section 2.7 discusses the multiple theoretical frameworks of the study and section 2.8 provides a chapter summary.

2.2. Agency Theory

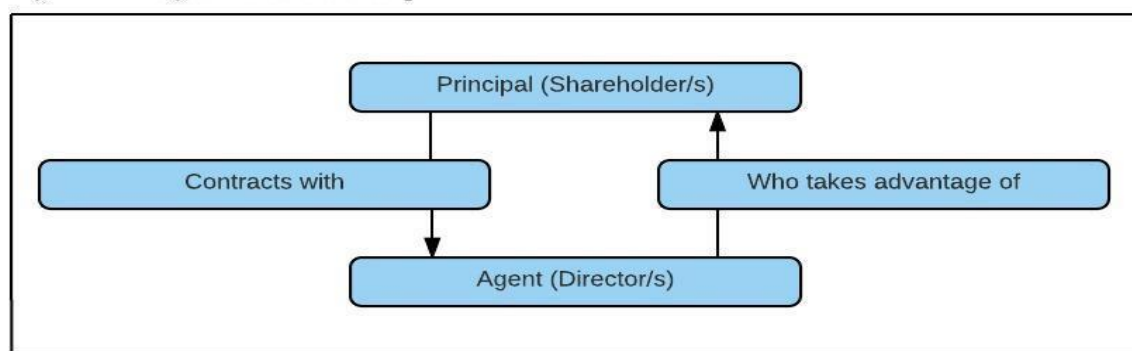
Agency theory helps us to understand the relationship that exists between two or more parties in situations wherein one party tackles the role of the principal and the other takes on the role of the agent (Eisenhardt, 1989). According to Jensen and Meckling (1976), ‘most organisations are simply legal fictions that serve as [a] nexus for a set of contracting relationships among individuals’ (p. 310). The basic implication of this theory is that ‘if both parties to the relationship are utility maximisers, there is a good reason to believe that the agent will not always act in the best interest of the principal’ (Jensen and Meckling, 1976, p. 308).

Agency theory is derived from the disciplines of finance and economics, and its main aim is to alleviate conflicts between a firm’s management and its shareholders (Mallin, 2016; Solomon, 2013). In their work on this issue, Berle and Means (1932) suggested that the separation of

¹ More recent corporate governance studies considered several theories, to include contingency theory and strategic leadership theory (see Durisin and Durisin, 2009). However, those were deemed inappropriate for use in this study.

ownership and control creates an ‘agency problem’; such a separation enables corporate directors to act in their own interests rather than in the interests of shareholders. Similarly, Tricker (2015) argued that on occasion, corporate directors make decisions that lead to the maximisation of their own benefits, even if the repercussions of those decisions are disadvantageous to shareholders. This is not an easy problem to solve, as these two parties often have differing interests. Figure 2.1 illustrates the governance relationship between principals (shareholders) and agents (directors).

Figure 2.1 The governance relationship.



Source: Tricker (2015).

Interestingly, there are two facets of agency theory that have the power to adversely affect a principal. First, Mallin (2016) argued that an agent might choose to act, at least in part, in the best interests of the principal. For example, directors might dedicate corporate funds to risky projects that are neither desired nor expected by the shareholders (Tricker, 2015). However, potential investors are able to judge and evaluate the quality of directors’ decisions by screening various reports published by the company. Second, information asymmetry is another issue that can arise from the agency problem. This situation occurs when an agent and a principal have varying levels of information about a company (Gillan and Starks, 2003). In reality, an agent typically has more information than does a principal, as that agent is responsible for the daily functions of the firm. This creates a situation wherein an agent might exploit private information in order to meet their personal goals (Gomez and Wiseman, 2007).

The more information the managers possess as compared to their shareholders, the more difficult it becomes to solve the agency problem.

According to Grossman and Hart (1983) and Mintz (2005), managing the agency costs that arise between managers and shareholders is the key to ensuring that a firm is operating efficiently and increasing shareholder value. Scholars have suggested various mechanisms and actions that can be implemented during efforts to reduce potential agency problems between managers and investors. According to Shleifer and Vishny (1997), one feasible means of alleviating agency costs is to concentrate a firm's shareholdings. It is also important to note that an examination of the role of blockholders in corporate governance systems has attracted academic attention for two reasons. First, large-block shareholders have the ability to resolve the free riding problem (Grossman and Hart, 1983). Second, large-block shareholders are more strongly motivated to monitor the actions of management due to the power and volume of their votes (Demsetz, 1983). However, Shleifer and Vishny (1997) argued that the presence of larger shareholders may not always efficiently alleviate the agency problem, as such parties might expropriate private benefits at the expense of minority investors. If large-block shareholders maintain their interests to the detriment of minority shareholders, additional conflicts between shareholders may arise (e.g., the Principal-Principal conflict).

Importantly, institutional investors have the potential to reduce agency costs in the firms in which they invest. Given the recent growth of institutional investor activity across the globe, such investors have the ability to be good monitors of their investee firms—and they can do so at a lower cost as compared to other investors (Gillan and Starks, 2003). Furthermore, institutional investors face continuous pressure to improve governance practices from several sources, including government agencies, stock markets and a firm's ultimate beneficiaries (Mallin, 2016). Additionally, the stewardship codes and guidelines published by several countries are seen as effective tools that institutional investors can use to engage with their

investee firms during efforts to discuss corporate governance-related issues (Haxhi et al., 2013; McNulty and Nordberg, 2016). This engagement can assume various forms, such as one-to-one meetings, voting, shareholder proposals and resolutions, focus lists and corporate governance rating systems (Martin et al., 2007; Goranova and Ryan, 2014; Mallin, 2016). Indeed, institutional investors have regularly been found to engage in behind-the-scenes discussions of corporate governance issues (Holland, 1998; McCahery et al., 2016).

An efficient means of reducing information asymmetry concerns is to allow outsiders to collect information about a firm (Huddart and Ke, 2010). In comparison to individual investors, institutional investors are often in a more suitable position to collect and analyse information due to the scope of their holdings and the skills that they possess (Ayers and Freeman, 2003; El-Gazzar, 1997). Because of the high monitoring costs associated with the collection and analysis of information, as well as the costs associated with acting on the resultant findings (Fich et al., 2015), institutional investors are better able to provide active monitoring of investee firms than are their smaller-investing counterparts. This is due to the fact that large-portion owners can bear the high costs of monitoring, as the potential returns associated with monitoring often exceed the attendant costs (Gillan and Starks, 2000).

A well-structured corporate board is seen as an important mechanism that can be used to reduce agency costs and improve corporate governance systems (Davies and Hopt, 2013; Mallin, 2016). Solomon (2013) argued that a corporate board is responsible for leading a firm and that an effective board leads to firm success. Furthermore, Bertoni et al. (2014) contended that an effective corporate board can contribute to firm value in two ways. First, a board of directors can protect suppliers of finance from managerial misbehaviour, thus reducing the cost of capital. Second, a board of directors can afford a company a competitive advantage by enhancing its good reputation, helping it to establish a network of contacts and rendering strategic decisions. Moreover, the effectiveness of a corporate board can be measured with

regard to several factors; these factors include the ability to attract additional funds, enhance firm value, augment share prices and provide consistent returns for shareholders (see Carlsson, 2001).

Some empirical research has suggested that board composition must be considered when attempting to reduce agency costs. For example, the hiring of additional non-executive directors who are independent of firm management can play an important role in balancing the interests of managers and shareholders (Rosenstein and Wyatt, 1990). Furthermore, outside directors can play a key role in alleviating the agency problem, as such parties have the ability to monitor a firm's management and defend shareholders' interests. Moreover, many academicians have emphasised the role of outside directors in lessening information asymmetry, which in turn enhances firm value (see, for example, Lim et al., 2007; Baysinger and Butler, 1985). In order to protect their own reputations, independent directors are often inclined to voluntarily disclose additional information about the firm (Lim et al., 2007). In so doing, these independent directors safeguard their public standing and are thus shielded in the event of future firm failure. Other scholars have indicated that a board's size can play a role in improving the agency problem (see Lipton and Lorsch, 1992; Yermack, 1996). The directors of smaller boards often have simpler systems of communication and coordination; thus, they are often better able to scrutinise the actions of management.

Also, the establishment of key sub-committees (audit, remuneration and nomination) is considered to be an effective means of reducing the agency problem. Such committees play an important role in the monitoring of a board, as their monitoring power is derived from the authority delegated to them by the corporate board (see Beasley, 1996; Carcello and Neal, 2000; Kaczmarek et al., 2012). Forming such committees can also increase directors' commitment to a company, as each director is allocated specific tasks that they are required to fulfil. Harrison (1987) argued that board sub-committees can also be used to mitigate the issue

of poor board attendance; to this end, directors are assigned specific responsibilities and tasks that are delegated to them during committee meetings. Furthermore, Lipton and Lorsch (1992) noted that as a board's size increases, the efficiency of its directors is expected to decrease. This issue can be addressed by allocating specific responsibilities to each committee, which in turn increases the efficiency and accountability of each director. Given the importance of board sub-committees in monitoring a firm's management and in increasing board efficiency, institutional investors are expected to improve the structure of key sub-committees.

According to Vafeas (1999b), board activity, as measured by the number and frequency of meetings, is an important aspect of the agency cost issue. He argued that boards respond to poor performance by holding more meetings, which enhances the monitoring role of the corporate board. The author also emphasised that board monitoring contributes to the identification of valuable projects, which in turn improves shareholder value (Vafeas, 1999b). Furthermore, Brick and Chidambaran (2010) argued that regulatory institutions play a role in increasing the pressure placed upon firms to establish more independent and active boards. For example, in recent years, the level of board activity has increased significantly, especially following the issuance of Sarbanes-Oxley, which called for greater board monitoring of management's actions.

Another issue that is often discussed in the relevant literature is board busyness. For example, Ferris et al. (2003) argued that the possession of multiple directorships can bring about favourable outcomes. An individual director who holds a high number of posts is often viewed as having a positive reputation, which often contributes to improved firm performance. This contention is consistent with the findings of Fama and Jensen (1983), who argued that a director's good reputation is linked to a positive effect in the marketplace. Conversely, Fich and Shivdasani (2006) maintained that if the majority of outside directors are busy, firm performance is adversely affected. This argument suggests that a busy board will lead to a more

significant agency cost problem, as a busy board does not have the ability to efficiently monitor firm management.

According to Davies and Hopt (2013), ownership structure is a major factor that impacts the role of corporate boards in publicly traded firms. The ownership structure of a firm can influence what the board does and to whom it is accountable. In firms where the ownership structure is dispersed, the corporate board plays an active role in the decision-making process. Conversely, in firms where the ownership structure is concentrated, large-block shareholders are in a better position to affect the decisions made by the corporate board. In this context, the second agency problem (Principal-Principal conflicts)—which occurs between controlling shareholders and minority shareholders—can arise, as large-block shareholders are more likely to advocate for their own interests over the interests of minority shareholders. Thus, this finding may inspire institutional investors to establish mechanisms whereby the influence of shareholders can be reduced; these mechanisms may include efforts to establish lobby groups that work to protect the interests of minority shareholders (Davies and Hopt, 2013).

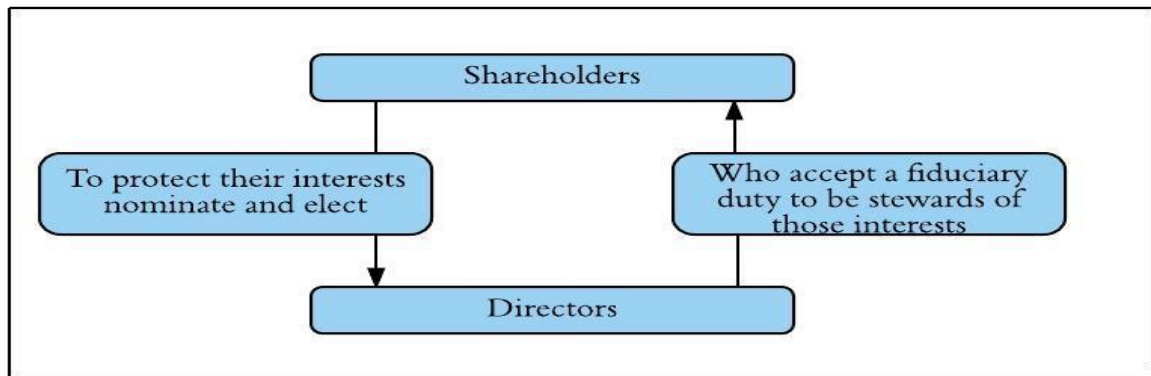
Considering the implications of agency theory as discussed above, it is clear that there are various limitations associated with this concept. One ongoing concern in corporate governance is the potential for ‘Principal-Principal’ conflicts between controlling shareholders and minority shareholders. Young et al. (2008) argued that Principal-Principal conflicts may arise as a result of many factors, including concentrated ownership and weak legal protections for minority shareholders. Furthermore, agency theory fails to consider the various other stakeholders of a company (see Hill and Jones, 1992), including suppliers, customers, creditors and employees. For instance, employees play an important role in corporate governance reform in countries such as Germany and Japan (see Jackson, 2005). Moreover, Donaldson and Davis (1991) determined that the Model of Man is a significant limitation; this model suggests that self-interested actors will rationally maximise their own personal economic gain. Notably, this

model is individualistic and addresses conflict between managers and owners. However, Davis et al. (1997) also argued that the utilisation of self-benefits may not be applicable to all managers. They therefore introduced the stewardship theory, which suggests that managers do not work to achieve their own goals—rather, they attempt to meet the needs of shareholders. The following section explains this theory.

2.3. Stewardship Theory

Stewardship theory was derived from the disciplines of sociology and psychology and was introduced by Donaldson and Davis in 1991. The stewardship theory focuses on the behaviour of a firm and its management, to include corporate boards of directors in Anglo-Saxon countries and supervisory boards in Germany. This concept is considered to be an alternative to agency theory; according to stewardship theory, directors are elected by shareholders and are believed to be self-motivated to meet shareholders' needs and interests (see Figure 2.2) (Davis et al., 1997). Such directors should be eager to perform well and be seen as good stewards of a firms' assets. If true, the efforts of directors will lead to positive outcomes that benefit all shareholders. Furthermore, as per stewardship theory, the behaviour of stewards is collective; a steward aims to achieve the objectives laid out by the firm, which in turn leads to potential benefits for shareholders as profits, dividends and share prices are positively affected (Davis et al., 1997).

Figure 2.2 : The shareholder/director relationship.



Source: Tricker (2015).

According to stewardship theory, conflicts of interest between management and shareholders do not exist, and there is no inherent potential problem associated with executives' motivation (Donaldson and Davis, 1991). Therefore, shareholders can expect higher returns, as senior management is able to exercise effective control over the company (Muth and Donaldson, 1998). However, this explanation does not mean that a steward does not consider his own survival needs; indeed, a steward should realise that his personal needs can be met by achieving organisational objectives and goals. Hence, a proper steward will recognise that the benefits to be gained by attaining company goals are greater than the benefits that might be obtained through individualistic behaviours (Davis et al., 1997).

There are various dimensions to consider when analysing the differences between agency theory and stewardship theory. For example, the aim of stewardship theory is to empower the upper managers of a firm rather than to monitor and control them (see Donaldson and Davis, 1991; Fox and Hamilton, 1994). For instance, the actions of CEOs who are considered to be stewards are best facilitated when the governance structure of a firm provides them with greater levels of authority, especially if those CEOs also serve as board chairs (Donaldson and Davis, 1991). This structure is deemed functional under stewardship theory, as CEOs are viewed as utility maximisers who serve organisational goals rather than their own ends. However, such a

structure is not preferred under the agency theory's Model of Man; according to this theory, CEOs are in danger of becoming entrenched. This can affect the decisions made by the board, potentially leading them to pursue such tactics as corporate policy pay-out schemes (see Hu and Kumar, 2004).

According to Muth and Donaldson (1998), directors are more committed to firm performance and success than are shareholders who may simply be seeking short-term benefits. Furthermore, the researchers argued that executives who run the daily operations of a firm have a wider knowledge of the firm's goals than do outside directors. From the stewardship perspective, higher levels of interest alignment between managers and shareholders lead to superior firm performance.

However, there are various limitations associated with stewardship theory. For example, Davis et al. (1997) argued that stewardship theory is affected by the cultural environment in which a company operates. For instance, if a firm exists within an individualistic culture, its directors may look after their own interests rather than the interests of shareholders. Furthermore, the theory fails to consider the varied interests of various stakeholders within a company. For example, some institutional investors (i.e., investment fund managers) may seek short-term returns, while others (i.e., pension funds) may favour long-term results (see Johnson and Greening, 1999). Given the implications of stewardship theory, a corporate board is expected to adopt strategies to improve a firm's governance structure; importantly, these steps must align with shareholder interests.

2.4. Resource Dependence Theory

This theory was initially introduced by Salancik and Pfeffer (1978), who emphasised that a company's survival is dependent on its ability to secure resources that are necessary for the enhancement of shareholder wealth. According to Tricker (2016), these resources might include potential customers, competitors, access to capital and other sources of financing,

relationships with other businesses and political or social networks. For a firm to achieve success, its corporate board must build connections with other external companies in order to reduce dependency and obtain needed resources (Hillman et al., 2007).

According to Bazerman and Schoorman (1983), there are four benefits to be gained by linking a firm to its external environment: network connections between directors, horizontal coordination, vertical coordination and expertise and reputation. Muth and Donaldson (1998) further argued that horizontal links between directors can increase communication opportunities, which contributes to the efficient exchange of information regarding topics of concern. Furthermore, vertical links between directors and a firm's customers and suppliers play an important role in increasing awareness of the external environment. Such information can be employed by a firm's directors, thus allowing them to make appropriate decisions that will lead to the firm's success. This concept is consistent with the work of Pfeffer (1972), who argued that control over external stakeholders can be achieved by utilising the network of board members.

Furthermore, Hillman and Dalziel (2003) maintained that board capital (a combination of directors' human capital and social capital) is a valuable resource that enables a board to more effectively monitor management's actions. These board resources provide a firm with the ability to understand the environment in which it operates. Additionally, directors with diverse characteristics (in terms of gender, age, nationality, ethnicity and education) can facilitate various functions of the corporate board; indeed, the presence of diverse directors can enhance decision-making practices (Hillman et al., 2000; Anderson et al., 2011), improve managerial monitoring (Kim et al., 2013), satisfy the needs of stakeholders (Harjoto et al., 2015) and draw additional attention to the ethical aspects of firm activities (Hafsi and Turgut, 2013).

Taking into account the implications of resource dependence theory, Salancik and Pfeffer (1978) argued that success depends on proper coordination between all involved organisations.

Any failure to coordinate while attempting to acquire needed resources can limit the amount of resources obtained from the surrounding environment. In the context of this study, institutional investors are expected to utilise the resources available to a firm by striving to improve diversity attributes within the boards of their investee firms (including gender, age, nationality and educational diversity).

2.5. Institutional Theory

The institutional theory was drawn from the fields of economics and sociology and refers to the process by which structures—such as norms, rules and routines—are established as authoritative guidelines for social activities (Scott, 2004). This theory also describes how these elements are issued and adopted over time. In other words, institutionalisation refers to those repeated processes that have acquired similar meanings over a given period of time (Bondy et al., 2008). According to Selznick (1957), an organisation is an adaptive entity that is shaped by participants' characteristics, influences, constraints and commitments. Furthermore, Scott (2004) noted that an organisation's processes are shaped by its external environment. According to institutional theory, companies seek legitimacy and pursue their ultimate survival by adapting their structure to institutional norms (Li and Harrison, 2008). Moreover, companies are influenced by the social norms that exist within their external social environment (Granovetter, 1985). In the context of corporate governance practices, several scholars have argued that corporate governance structures are shaped by their institutional environments; thus, companies are influenced by the legal systems (Kim and Ozdemir, 2014), ownership structures (Aguilera and Crespi-Cladera, 2016; Desender et al., 2013; Judge, 2011; Judge, 2012; Sure et al., 2013), economic conditions (Essen et al., 2013) and national cultures (Li and Harrison, 2008; Grosvold and Brammer, 2011; Volonte, 2015) of the countries in which they operate.

Furthermore, DiMaggio and Powell (1983) argued that a firm's institutional environment can lead to the development of formal structures within the company. Furthermore, pressure from various institutions can, in turn, lead to the homogeneity of organisational structures. Therefore, in the context of this research, institutional investors are in a solid position to exert pressure over their investee firms to adopt healthy governance structures. This position is supported by national corporate governance and stewardship codes, which are often developed and revised over time. From an international perspective, several corporate governance codes and guidelines have been published in an attempt to motivate firms to develop and implement effective governance structures. For example, the OECD issued a set of corporate governance principles in 1999, which were later revised in 2004. The OECD Principles of Corporate Governance provide guidance for policy-makers, regulators and market participants who seek to enhance the legal, institutional and regulatory frameworks that underpin corporate governance practices across the globe (Jesover and Kirkpatrick, 2005). These OECD principles have served as guidelines for companies seeking to establish corporate governance codes in some countries (Mallin, 2016). Indeed, Jesover and Kirkpatrick (2005) contended that international principles govern the relationships that exist between managers and shareholders as well as those that occur among stakeholders who serve as employees and creditors; ultimately, healthy relationships drive economic efficiency and contribute substantially to market confidence.

The International Corporate Governance Network (ICGN) was founded in 1995 and is comprised of members who hail from every region across the world; as such, the ICGN covers major institutional investors, investor representative groups, companies, financial intermediaries, academics and others (Mallin, 2016). The main objective of the ICGN is to facilitate an international dialogue on matters related to corporate governance. To this end, the ICGN issued its Statement on Global Corporate Governance Principles in 1999, which were

revised and updated in 2009 (Mallin, 2016). These revised principles addressed various governance issues, including corporate board practices, corporate culture, risk management policies, remuneration plans, audit systems, disclosure and transparency procedures, shareholder rights and shareholder responsibilities. More recently, the ICGN published its first stewardship code in 2016; this code aims to offer a global framework regarding good practices as they relate to the stewardship of institutional investors.

Additionally, Kostova et al. (2008) maintained that multinational companies are able to operate within wider institutional landscapes, as exposure to diverse practices allows them to pursue appropriate patterns and practices. Therefore, the corporate governance and stewardship codes that are issued at the national and international levels can place additional pressure on companies to adopt the best possible governance practices. Furthermore, institutional investors are expected to play a significant role in efforts to motivate their investee firms to implement favourable governance structures.

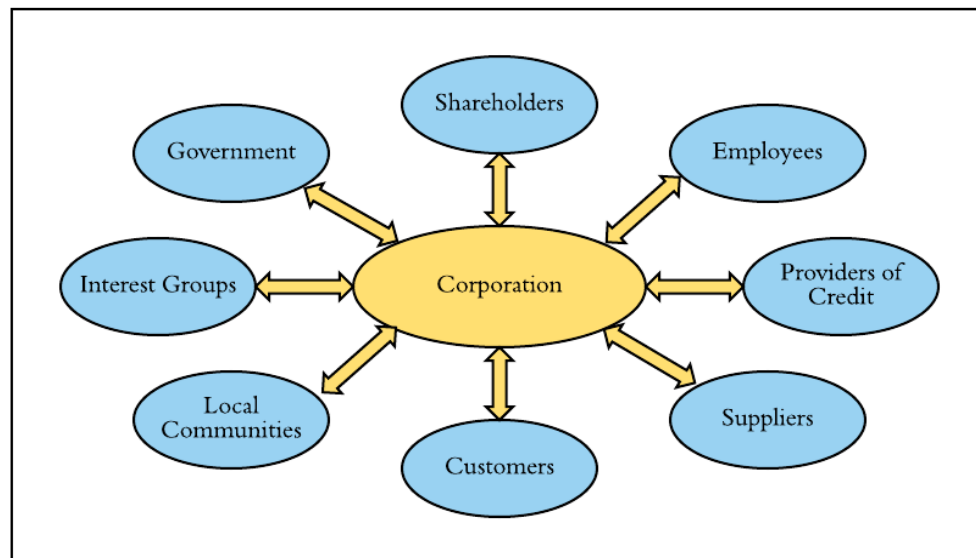
2.6. Stakeholder Theory

Freeman's (1984) seminal book on stakeholder theory suggested that efficient managers must consider the interests of a firm's various stakeholders. As such, stakeholder theory goes beyond the relationships between agents and principals and includes other parties within the corporation as well (Freeman, 1984). Furthermore, this theory challenges the notion that the primary goal of a firm is the maximisation of shareholder wealth; rather, stakeholder theory argues that a company's main objective is to satisfy all stakeholders who are associated with the firm (Wall et al., 2009). This belief is consistent with the work of Hasnas (1998), who argued that the fundamental obligation of a firm's management is to consider the claims of various stakeholders in order to ensure the company's survival.

According to Mallin (2016), stakeholders are classified according to their relationship to the company; stakeholders have either direct relationships (e.g., employees, providers of credit,

suppliers and customers) or indirect relationships (e.g., local communities, environmental groups and governmental bodies) (see Figure 2.3). For example, a firm has a fiduciary responsibility to its providers of credit to be solvent and to repay debts (Boatright, 1994). It is in the company's interest to pay off its debts on time in order to build stable relationships with financial providers. Furthermore, suppliers provide a firm with unique goods and services; if a company lacks cash, suppliers can be adversely affected (Mallin, 2016). Similarly, employees have a vested interest in their company as well, as it is the source of their income. Moreover, employees may be particularly concerned with a company's pension fund scheme, which they will need to access in the future and which is dependent on the company's sustainability and success within the marketplace. With regard to the corporate governance systems of German and French companies, for instance, employees take part in electing representatives to corporate boards. Furthermore, banks (the providers of credit) may also place directors who represent their interests on such supervisory boards (see Mallin, 2016).

Figure 2.3 The corporation and its stakeholders.



Source: Mallin (2013).

There are numerous codes and guidelines that highlight the roles of shareholders and stakeholders and that explain how the interests of these parties can be accommodated within a

company's corporate governance structure. For example, in the OECD's Principles of Corporate Governance (2004) one tenet is dedicated to an explanation of the role of stakeholders in corporate governance. According to this principle, 'the corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises' (OECD, 2004). As per Mallin (2016), this principle emphasised two issues: first, stakeholder rights are dependent on the legal provisions concerning stakeholders that exist within a particular country; and second, stakeholders do not play a role in corporate governance unless they have access to relevant information that will allow them to participate effectively in the process.

According to Johnson and Greening (1999), institutional investors are considered to be major stakeholders of countless firms; indeed, their holdings have increased dramatically in recent years. Gilson and Kraakman (1991) argued that institutional investors do not only consider the financial performance of their firms, they are also interested in various other aspects of organisational life, including the corporate governance structure of their firms. As such, investee firms are expected to consider the views of institutional investors with regard to corporate governance structure.

In light of this stakeholder theory, Mallin (2016) argued that the involvement of shareholders and stakeholders is dependent on national laws and customs and on the individual approach adopted by a particular company. Furthermore, boards are confronted with the significant challenge of considering a diverse set of stakeholder interests. For example, the presence of employee representatives on a supervisory board might affect decision-making, potentially leading to outcomes that are favourable for employees but not for the firm as a whole.

2.7. Multiple Theoretical Frameworks

According to Kumar and Zattoni (2015), the need to consider multiple theoretical frameworks in corporate governance research has become essential. Adopting multiple theories enables scholars to broaden the understanding of global governance phenomena, and also interpret the findings from different lenses (Zattoni and Van Ees, 2012). Zattoni and Van Ees (2012) reviewed the papers published in the *Corporate Governance: An International Review* journal between 2008 and 2010; one of their main findings was that most of the corporate governance studies are derived from the theoretical framework of the agency theory. Therefore, they encourage scholars to broaden the theoretical scope of corporate governance research by adopting alternative theories to the agency theory. Hence, in this research, five main theories were utilised: agency theory, stewardship theory, resource dependence theory, institutional theory and stakeholder theory. These theories were integrated into a model to capture the role of institutional investors in improving corporate governance in their investee firms and to ascertain whether institutional settings (economic conditions, legal system and ownership structure) determine the association between institutional investors and corporate governance structure.

In the context of this study, the agency theory (Jensen and Meckling, 1976) was used to explain the extent to which the characteristics of a corporate board can mitigate the agency costs that exist between the principal (shareholders) and the agent (managers). In addition, the theory was used to investigate to what extent institutional investors can enhance the corporate governance structure in their investee firms, which contributes to the reduction of agency costs (Gillan and Starks, 2003). This can be achieved by adopting several engagement tools, such as one-to-one meetings, voting, shareholder proposals, shareholder resolutions, focus lists and corporate governance-rating systems (Martin et al., 2007; Goranova and Ryan, 2014; Mallin, 2016). In addition, the stewardship theory (Donaldson and Davis, 1991) was also considered to provide

the theoretical framework of the institutional investors acting as stewards and maintaining the interest of their beneficiaries. Therefore, the monitoring role of institutional investors was expected to enhance the governance structure in their investee firms. Given their presence globally, the institutional investors were considered as key stakeholders of the company in light of the stakeholder theory (Freeman, 1984). Therefore, their views regarding the corporate governance structure was expected to be recognised and taken into account. The resource dependence theory (Salancik and Pfeffer, 1978) was utilised in this research to explain the tendency of the firm to secure resources by building connections with other companies. In particular, this theory was employed to investigate to what extent the company adopts a diverse board under the monitoring role of the institutional investors. Finally, the institutional theory was also employed in this research to explain whether institutional settings, such as economic conditions, legal systems and ownership structure, can influence the role of institutional investors in improving corporate governance structure in their investee firms. Several studies argue that it is essential to consider the institutional settings when studying the global phenomena of corporate governance (see Aguilera et al., 2008; Aguilera et al., 2012; Desender et al., 2013, Kim and Ozdemir, 2014).

Table 2.1 provides a summary of the theories discussed in this chapter. This summary highlights several aspects of each of the discussed theories, to include their main principles, predominant perspectives, prevailing perceptions of corporate management, established discipline practices, emergence histories and relevant criticisms.

Table 2.1. Summary of Corporate Governance Theories

Issues	Agency Theory	Stewardship Theory	Resource Dependence Theory	Institutional Theory	Stakeholder Theory
Principles	Describes a relationship wherein one party delegates work to another party. In terms of a corporation, owners are the principals and directors are the agents.	Directors are regarded as the stewards of a company's assets and are expected to act in the best interests of shareholders.	Directors are able to connect the company with the resources required to achieve corporate objectives.	The institutional environment influences those social beliefs and practices that impact various actors within a society.	Takes into account a wide range of constituents rather than placing all focus on the shareholders.
Perspective	Outside	Inside	Outside	Outside	Outside
Perception of Corporate Management	Managers are self-interested.	Corporate managers are loyal and work towards the best interests of shareholders.	Corporate managers seek to secure valuable resources.	Corporate managers are influenced by external norms and regulations.	Corporate managers have a different view of each stakeholder.
Discipline	Finance and Economics	Sociology and Psychology	Sociology	Economics and Sociology	Economics and Organisational Theory
Emergence	1970s	1990s	1980s	1980s	1980s
Critics	- Principal-Principal conflict. - Other stakeholders are not considered - The Model of Man.	- Dependent on cultural norms. - Achieving balance between the various stakeholders' interests is not explored.	- A lack of coordination between firms, which can limit an organisation's ability to acquire needed resources.	- Some institutional practices are mandatory.	- The involvement of stakeholders is dependent on national laws and customs. - Achieving balance between the interests of all stakeholders seems unfeasible.
Authors	Jensen and Meckling (1976); Fama and Jensen (1983)	Donaldson and Davis (1991); Donaldson and Davis (1994)	Pfeffer (1972); Salancik and Pfeffer (1978)	Scott (2004); DiMaggio and Powell (1983)	Freeman (1984)

2.8. Chapter Summary

This chapter illustrates the theoretical framework associated with the role of institutional investors in corporate governance. The theories discussed in this chapter include agency theory, stewardship theory, resource dependence theory, institutional theory and stakeholder theory. Each of these theories provides a set of concepts and principles that together serve to shape this work's research questions and hypotheses. The chapter also provides a discussion of the multiple theoretical frameworks.

Chapter 3

3.0 Corporate Governance Background

3.1. Introduction

This chapter discusses the primary features of global corporate governance. First, the importance of corporate boards is highlighted, and the various potential board structures are illustrated; this is followed by an illustration of the significance of key subcommittees (audit, compensation and nomination). Then, this chapter discusses the role that the institutional setting—whether a financial crisis exists, what legal system is in place and which ownership structure has been adopted—plays in corporate governance. The comparative features of corporate governance are then discussed, to include insider versus outsider systems and hard versus soft law systems. Finally, the chapter examines the main features of corporate governance in the sample countries (Australia, Belgium, Canada, Denmark, Finland, France, India, Ireland, Italy, Netherlands, Norway, Spain, Sweden, Switzerland and the UK), and relates the history of corporate governance development to date. The countries under study are classified as having adopted either an Anglo-Saxon model, a Germanic model, a Latin countries system or a Nordic governance system.

Accordingly, the chapter is organised as follows: section 3.2 illustrates the importance of corporate boards and their key subcommittees and highlights the various board structures (unitary versus dual boards, for example) in place around the world. Section 3.3 highlights the importance of financial crises in corporate governance, while section 3.4 examines the significance of legal systems in corporate governance. Section 3.5 discusses the issue and import of ownership structure; more specifically, section 3.6 further examines insider versus outsider systems, while section 3.7 discusses hard versus soft law models. Section 3.8 considers the Anglo-Saxon corporate governance system (in place in Australia, Canada, Ireland, India, the UK and the US), section 3.9 illustrates the Germanic model (at play in Switzerland), section

3.10 describes the Latin countries system (adopted by companies in Belgium, France, Italy, the Netherlands and Spain) and section 3.11 discusses the Nordic model (embraced in Denmark, Finland, Norway and Sweden). Finally, section 3.12 concludes the chapter.

3.2. The Importance of the Board of Directors

Given the direct link it enjoys with two important participants—managers and shareholders—the corporate board is considered to be the main internal governance mechanism that determines and shapes the governance practices of a particular firm (Aguilera et al., 2012; Mallin, 2016). According to Zahra and Pearce (1989), a corporate board has two main roles, to control and to advise. The controlling role is primarily related to the responsibility of directors to monitor and oversee management’s behaviour and to ensure that management and shareholder interests align. This responsibility is rooted in agency theory, according to which the main objective of a corporate board is to eliminate the self-serving behaviours of top managers who may not always be working in the best interests of shareholders (Jensen and Meckling, 1976). The advising role describes a corporate board’s potential to provide executive members with valuable advice, knowledge and insight regarding the firm’s external environment. This role is rooted in the resource dependence theory, which submits that corporate boards should provide top managers with needed guidance and support by linking a firm to its external environment (Pfeffer and Salancik, 1978).

3.2.1. Unitary Boards versus Dual Boards

One of the most significant corporate governance differences that exists among countries is board structure, which can be classified into two types: unitary (one-tier) boards and dual (two-tiered) boards. The unitary board structure is the most common form in countries such as the UK, the US and EU member states. However, in countries like Austria, Germany, the Netherlands and Denmark, the dual board structure is predominant (Mallin, 2016). In some

countries (such as France) both corporate board systems are common. The implications of each corporate board structure are explained below.

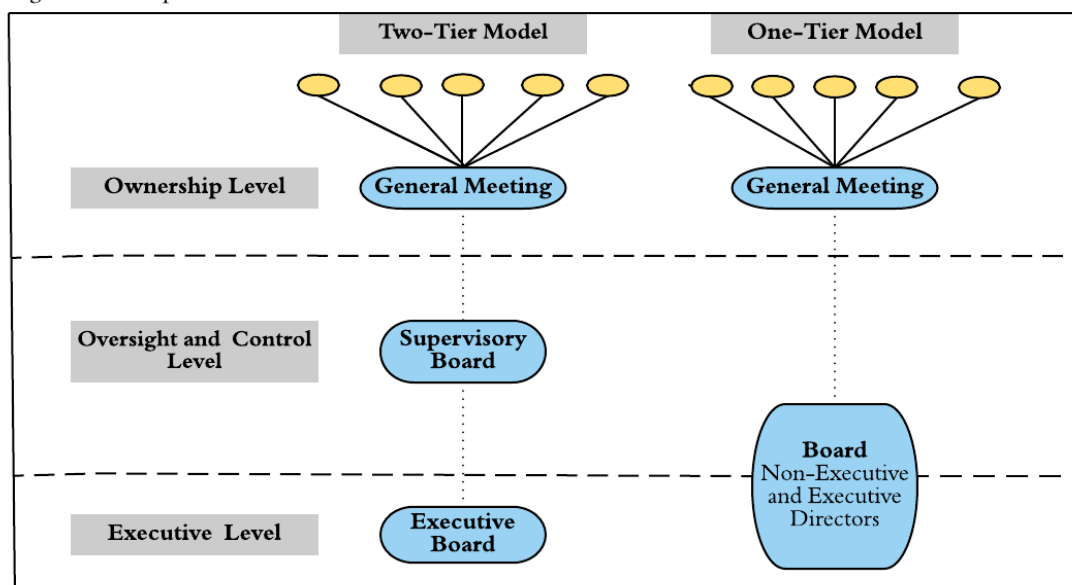
Unitary boards are characterised as single boards that include both executive and non-executive directors who tend to make decisions as a unified group. According to this structure, a board is responsible for all aspects of company affairs, and all directors are responsible for achieving company goals. Directors are nominated by shareholders during a company's annual general meeting (see Mallin, 2016; Solomon, 2013). In countries where unitary boards are predominant, importance is attached to independent directors who are responsible for monitoring the actions of management (Conyon and Peck, 1998).

In a dual board system, a company has two distinct boards: a supervisory board and a management board. The supervisory board supervises, directs and monitors the management board, while the management board runs the business's day-to-day activities (Mallin, 2016). Importantly, individuals cannot be members of both boards. In dual board systems, supervisory board members are elected by the shareholders, with the exception of employee representative members; these individuals are elected by the employees themselves. The management board is, in turn, elected by the supervisory board.

Despite the structural differences that exist between the unitary and dual board systems, both share some common approaches (see Krivogorsky, 2006). For example, both systems recognise that boards should adopt a supervisory function and a managerial function. However, the dual board system, wherein a separate executive body is appointed, is more formal. Additionally, in both systems, a managerial body is appointed, either by the unitary board itself or by the supervisory board; this group of executive directors is delegated authority by the single board in a unitary system or by the management board in a dual system (Mallin, 2016). Furthermore, shareholders elect the unitary board and the dual system's supervisory board. However, in countries where a dual system is predominant, such as Germany, employees are given the right

to elect certain board members. Moreover, the unitary board and the supervisory board are responsible for ensuring the implementation of financial reporting standards as per the regulations and laws of the country in which they operate. According to Mallin (2016), regardless of a board's structure, global corporate governance codes seem to offer similar recommendations regarding board functions, key subcommittees and shareholder rights. Figure 3.1 compares the one-tier and two-tiered systems.

Figure 3.1 Comparison between one and two-tier board structures.



Source: Adapted from Lekvall (2014)

3.2.2. Board Key Subcommittees

Corporate boards typically delegate some key tasks to subcommittees (i.e., audit, compensation and nomination committees). The delegation of particular tasks to key committees provides for better monitoring and allows skilled directors to assess specific organisational needs. Hence, the composition of these committees is essential, as it determines their contribution to companies' governance systems (Brennan and McDermott, 2004). These committees should regularly report their work to the board to enhance decision-making processes (Mallin, 2016). Lorsch and MacIver (1989) argued that although boards of directors meet regularly to discuss and vote on key issues, the majority of decisions are made by board subcommittees. Tricker

(2015) found that corporate boards typically establish subcommittees for two reasons: (i) to enable independent directors to meet separately from the board so that they may be able to fulfil their oversight duties and (ii) to reduce the burden placed on the board by delegating specific duties to subcommittees. Essentially, almost all corporate governance codes for listed firms recommend that a board create audit, compensation and nomination committees. For instance, the Cadbury Report recommends the formation of an audit committee and a remuneration committee, as well as a nomination committee to ensure that the nomination process is transparent and reliable (Cadbury Report, 1992). In addition to these three main committees, other subcommittees, such as risk and ethics committees, may be formed to deal with specific issues (Mallin, 2016). The importance and role of the most common types of subcommittees are discussed below.

Audit committees are considered the most important form of subcommittee, as their role is to review audit scopes and outcomes (Mallin, 2016). Furthermore, their duties involve reviewing the audit fees and the independence of companies' external auditors. An audit committee is considered a bridge between the internal and external auditors and the corporate board (Mallin, 2016). Furthermore, Du Plessis (2015) stated that the audit committee plays a central financial reporting role, as it monitors the top management's and the auditors' participation in the financial reporting process. The audit committee also selects the financial reporting standards. This can be done in coordination with the internal and external company auditors and can thus influence companies' financial reporting credibility. Given the importance of the audit committee, corporate governance codes in many countries recommend that it be comprised only of independent directors. For example, the UK Corporate Governance Code (2012) states that a board should establish an audit committee of at least three independent directors (two independent directors in the case of smaller companies).

Remuneration committees, or compensation committees as they are known in the US, determine board member compensation packages. The financial crises and the continuing financial scandals that have occurred across the globe have cast a spotlight on the remuneration packages of top executives and board members (Tricker, 2015). Mallin (2016) stated that the remuneration committee process should provide formal and transparent procedures to determine compensation schemes for executive directors. Given the level of shareholder attention towards excessive executive director remuneration, policy-makers have continually revised corporate governance codes to align manager and shareholder interests. For instance, the UK Corporate Governance Code was revised in 2014 to highlight changes related to remuneration recommendations (Mallin, 2016). The revision contained alterations to the design of remuneration packages intended to promote firms' long-term success. Furthermore, the UK government, represented by the Department for Business, Energy and Industrial Strategy, recently published the *Green Paper*, which considers the appropriate changes that must be addressed with regard to three main issues: executive pay; enhancing stakeholder voices, including those of employees, customers and suppliers; and corporate governance practices in large, privately-held businesses (Green Paper, 2016).

Lastly, **nomination committees** are responsible for selecting appropriate directors to sit on a board. According to Vafeas (1999a), the existence of nomination committees can enhance a board's effectiveness in many ways. First, the appointment of quality directors can enhance the monitoring role of outside directors. Second, the formation of a nomination committee can reduce individual bias in firms where the nomination process is delegated to individual board members. Third, a nomination committee can prevent CEO intervention in the nomination process, as it is more likely to make decisions that are consistent with the interests of shareholders. It follows that since it plays an integral part in board composition and succession planning, a nomination committee will ensure that a board is appropriately composed in order

to effectively fulfil its duties and functions (Kaczmarek et al., 2012). Given their importance with regard to board success, Mallin (2016) stated that nomination committees should evaluate a board's existing skills, knowledge and experience, focusing on filling gaps when selecting new candidates. Furthermore, nomination committees should be involved in firms' succession planning so that they may identify what skills and knowledge should be considered when identifying potential board candidates.

3.3. Financial Crises and Corporate Governance

Considered the worst period of economic distress since the Great Depression, the recent financial crisis of 2008–2009 resulted in enormous costs to several economies (Conyon et al., 2011; Adams, 2012). The crisis began in the US and spread to other countries, resulting in the freezing of the global credit market, which required global governmental intervention (Erkens et al., 2012). For instance, the US and UK governments spent \$700 billion and £500 billion, respectively, on rescue packages aimed at supporting financial markets (Akbar et al., 2017).

It has been argued that the weakness of corporate governance practices is one factor that contributed to the onset of this recent financial crisis (Strouhal et al., 2012). Several scholars have argued that both institutional investors and firms' corporate boards are also to blame for their inability to mitigate the crisis (Conyon et al., 2011; Reisberg, 2015). Erkens et al. (2012) studied a sample taken from financial firms in 30 countries around the world and found that firms with greater levels of institutional investment demonstrated poorer stock returns during the crisis; this may be due to the fact that institutional investors took on more risk prior to the financial crisis of 2007–2008 than did other investors. The authors also discovered that boards with higher numbers of independent directors were more heavily criticised, as they raised more equity capital during the crisis in an effort to ensure that their investee firms would have adequate capital and in an attempt to minimise the risk of bankruptcy (Erkens et al., 2012). However, this action was not seen as benefitting firms in the long run. Additionally, in

examining a sample drawn from southern Europe (Spain, Portugal, Italy and Greece), Díez-Esteban et al. (2016) demonstrated that the financial deregulation processes that were in place in those countries prior to the recent financial crisis provided an incentive for institutional investors to be proactive in their monitoring; this then encouraged firms to overinvest in risky projects. In such a context, our study attempts to investigate the role of institutional investors in the improvement of corporate governance practices when various economic conditions are at play (pre-crisis, crisis and post-crisis periods).

Several studies have documented that corporate board characteristics are contingent on the economic condition of a country. For instance, using a sample taken from 26 European countries, Essen et al. (2013) found that the prescription of good governance practices—including the independence of a board, the separation of CEO and chairmanship positions, and incentive-based compensation packages—were considered harmful to firm performance during times of crisis (Essen et al., 2013). However, some governance prescriptions at the country level—including the equality of cash flow, creditor protections, voting rights and the rule of law—were found to benefit firms during crisis periods (Essen et al., 2013). These results imply that governance policies should be loosened during times of crisis so that a corporate board can allow the management team the opportunity to respond effectively. Sun et al. (2015) found that the corporate boards of Chinese-listed firms were more likely to appoint women to sit on their corporate boards during times of crisis than they were during periods of economic prosperity. The authors also found that the presence of women in Chinese-listed firms led to improved performance during periods of market stress, thus indicating that a higher presence of female directors on a board results in the support of strict and appropriate investment decisions during difficult economic cycles.

3.4. Legal Systems and Corporate Governance

The bundle perspective of comparative corporate governance argues that differences in the attributes of board members across countries cannot be studied without also considering the legal systems of the country in question (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014). A country's legal system is considered a crucial determinant of the corporate governance efficacy of that country (La Porta et al., 1998). One legal approach to corporate governance holds that enacting and enforcing laws is essential to the protection of minority shareholders and creditors. In countries where shareholders enjoy strong protections, investors are more likely to hold minority positions rather than to serve as the dominant shareholder of a firm. However, in countries where shareholder protections are weak, investors are more likely to be controlling shareholders so as to compensate for deficiencies in legal protections (Shleifer and Vishny, 1997).

La Porta et al. (1998) compared the external financial environments of roughly 49 countries by considering the functions and origins of their laws, the quality of legal investor protections and the quality of legal enforcement measures. They found that those countries that have common law systems in place provided greater protection from the expropriation of insiders for both shareholders and creditors; this protection, however, was found to be low in French civil law countries, while German and Scandinavian civil law countries typically resided in the middle of the spectrum. As a result, the protection of minority shareholders has played a relatively more significant role in expanding and developing capital markets in common law countries than in those countries with civil law systems. In a subsequent paper, La Porta et al. (2000) showed that, on average, there was a greater tendency for firms to be widely held in countries with common law systems than in those with civil law systems. A third paper by La Porta et al. (2002) provided evidence of a positive association between firm valuation and a country's

legal system, finding that company performance was higher in common law countries than in civil law countries.

A country's legal system has also been found to influence investors' portfolio allocation. For instance, Leuz et al. (2009) conducted an international study in an effort to determine what factors influence the portfolio allocation of US-based institutional investors who do business around the globe. Their results emphasised that American institutional investors invested less in countries that lacked investor protection rights and disclosure rules and in countries where insider controls were high (Leuz et al., 2009). Their results were particularly applicable to firms with higher earnings management, given that the monitoring costs and information asymmetry faced by US-based institutional investors are the main drivers of results. This view is consistent with the work of Giofr  (2013), who also demonstrated that investor protections were the main determinants of foreign investment activity around the world; in particular, they chose to invest in countries with strong legal systems in order to eliminate the riskiness of projects. Importantly, several researches have drawn similar conclusions (see Fox and Weber, 2002; Giannetti and Koskinen, 2010).

Additionally, many scholars have argued that the composition and characteristics of a corporate board can be attributed to the legal system of the country in which it operates. For instance, using data from 23 countries around the world, Kim and Ozdemir (2014) investigated which national institutional characteristics influenced a corporate board's role as monitor (boards as wealth protectors) or advisor (boards as wealth creators)². Their results demonstrated that in countries with higher investor protections, stronger rules of law and open market institutions, corporate boards were structured to serve as monitors rather than advisors, which indicates that these national characteristics and the monitoring role of corporate boards are complementary

² Two different scores have been used to proxy the structure of a board (monitoring versus advising structure). The monitoring score involves three items: the independence of the board, CEO duality and the ratio of outsider director tenure to CEO tenure in the firm. The advising score also involves three items: gender diversity, nationality diversity and whether the firm has a strategy-related committee (see Kim and Ozdemir, 2014).

mechanisms of corporate governance (Kim and Ozdemir, 2014). This view is consistent with the findings of Grosvold and Brammer (2011), who examined how national institutional settings shaped the gender diversity of corporate boards in 38 countries between 2001 and 2007. According to their results, legal and cultural institutions appeared to play a significant role in the prevalence of female directors on corporate boards across the globe.

To alleviate the effects of weak investor protection rights, several scholars have suggested that the existence of multiple large shareholders may increase shareholder protection efforts. Among them, Casado et al. (2016) examined the listed firms of Switzerland and found that the existence of multiple large shareholders enhanced the shareholder protections of a firm. Their results emphasised that conflict between several large shareholders ('Principal-Principal conflicts') helped to monitor not only the actions of a firm's managers, but also the behaviour of large shareholders who might have otherwise tried to obtain rent at the expense of other shareholders. Moreover, the results of this study implied that the weakness of corporate governance (protection rights) can be reconciled by having multiple shareholders invest in a firm.

3.5. Ownership Structure and Corporate Governance

Ownership structure is generally viewed as a major component of corporate governance bundles (Aguilera et al., 2012; Desender et al., 2013; Judge, 2011; Judge, 2012; Sure et al., 2013). Ownership structures vary across countries; widely-held firms are more common in the US and the UK, while firms with concentrated ownership structures are the norm in continental European countries (La Porta et al., 1999). Notably, Berle and Mean (1932) argued that modern corporations were becoming diffused in their ownership; in their seminal study, they maintained that modern corporations were rapidly adopting dispersed ownership schemes. However, more recent empirical studies conducted around the world have revealed little evidence supporting this contention. For instance, La Porta et al. (1999) found that most

corporations around the world, with the exception of those in the US and the UK, are controlled by families or by the state, which is categorised as concentrated ownership. This finding was also supported by their prior study, in which they examined up to 10 of the largest companies (by market capitalisation) in 49 countries across the globe. They collected data on each company's top three shareholders by combining their ownership stakes and found that, on average, their shareholdings represented roughly 46% of a firm's holdings (see La Porta et al., 1998).

To alleviate agency costs in widely-held firms, Shleifer and Vishny (1986) suggested that shareholders concentrate their shareholdings in order to better shoulder the costs of monitoring. According to Aguilera et al. (2012), ownership concentration might be beneficial, as controlling shareholders have more power and incentive to monitor the actions of managers than do minority shareholders; thus, the 'Principal-Agent' problem may be eliminated (Yoshikawa et al., 2014). However, ownership concentration might lead to 'Principal-Principal conflicts' if controlling shareholders take advantage of minority shareholders. Such expropriation is likely to occur when the 'one share-one vote' system is breached by dominant shareholders who strive to employ instruments of control, such as pyramidal ownership or the collection of dual-class shares; in such cases, their voting rights might exceed their cash flow rights (Faccio and Lang, 2002).

Several scholars have argued that corporate board characteristics are contingent on the ownership structure of a firm. Among them, Desender et al. (2013) analysed French- and Spanish-listed firms in 2007 and reported that different ownership structures influenced the monitoring level of a corporate board in different ways. Their results showed that board independence in widely-held firms was more likely to result in additional audit services, thus indicating that board independence and external audit fees are complementary in such firms (Desender et al., 2013). However, this result did not hold for firms with concentrated ownership

systems, which suggests that board independence and ownership concentration becomes substituted when monitoring the management of a firm (Desender et al., 2013). Their results also indicated that the association between board composition and audit fees was contingent on the controlling shareholders' type (i.e., whether firms were controlled by families, corporations, banks or whether they were widely held). Examining the listed firms of 12 Sub-Saharan African countries from 2006 to 2009, Munisi et al., (2014) found that firms with concentrated ownership systems and firms with foreign and managerial ownership structures were negatively associated with board size. The study also showed that state ownership was positively associated with the proportion of outside directors; however, the relationship was found to be negative in firms with concentrated ownership structures, thus indicating that board composition and ownership structure are used as substitutes in mitigating agency costs (Munisi et al., 2014).

Several scholars have called for a distinction to be made between the various types of controlling shareholders when discussing the ownership structure of a firm (Aguilera et al., 2012; Mallin; 2016). Different types of investors aim to achieve different objectives and pursue various strategies when investing in their investee firms; furthermore, they might demand different governance environments. Therefore, the following forms of controlling shareholders will be identified and distinguished: institutional investors, family owners and state owners.

Institutional Investors and Corporate Governance

As international capital markets continue to liberalise, the growth of institutional investments across the globe is becoming a key factor in the world economy (Ferreira and Matos, 2008; Aggarwal et al., 2011). According to the International Monetary Fund (IMF), the value of worldwide assets managed via institutional investments has risen to approximately \$100 trillion, a sevenfold increase over 1990 levels (Kim et al., 2016). Given their global investment footprint, institutional investors face increasing pressure from policymakers and governments

to play a meaningful role in the enhancement of governance structures within their investee firms (Mallin, 2016). Institutional investors' duties in monitoring their investee firms extend beyond their financial incentives to include stewardship responsibilities, which leads to the maximisation of beneficiaries' interests (see Mallin, 2016; Solomon, 2013).

Institutional investors can adopt several channels of engagement with their investee firms in order to improve a firm's corporate governance structure. These channels include one-to-one meetings, voting, shareholder proposals and resolutions, focus lists and corporate governance rating systems (Martin et al., 2007; Mallin, 2016). In addition to these methods, private negotiation is another effective approach that is regularly used by institutional investors to enhance the governance structure of their investee firms (Holland, 1998; McCahery et al., 2016). The stewardship codes and guidelines that have been published by several countries are also considered to be essential tools that may be used to enhance the dialogue between institutional investors and their investee firms (Haxhi et al., 2013; McNulty and Nordberg, 2016). The next chapter will further elaborate on the role of institutional investors in corporate governance.

Family-Owned Firms and Corporate Governance

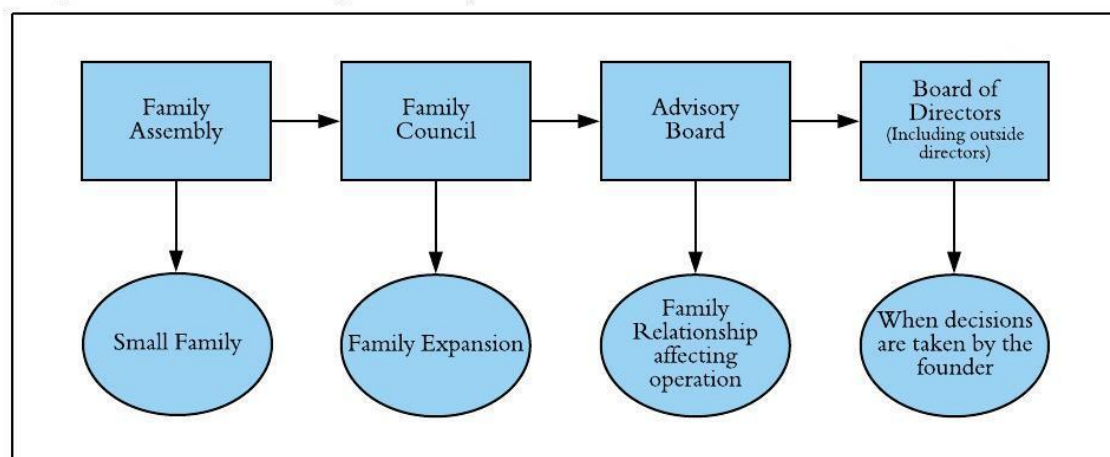
Nordqvist (2012) argued that members of a company-controlling family play an important role in improving the strategies adopted by their businesses. This is likely due to the nature of the interaction that occurs between family members, which often results in the development of unique and united skills that are used to push a business forward (Chrisman et al., 2003). Eddleston et al. (2008) claimed that an increased level of participation by family members in decision-making processes can eliminate conflict and improve a company's productivity. Furthermore, Mallin (2016) pointed out that the main advantage of a family business is the disappearance of the agency problem, as control and ownership are exercised by the same parties. Therefore, less monitoring of management's actions within the company is required.

According to Bammens et al. (2011), however, family control can increase the danger of four main hazards that are known to contribute to the agency problem. First, the controlling family might expropriate the economic wealth of their investee firms, which can harm the interests of minority shareholders (Bammens et al., 2011). The second hazard refers to situations wherein a controlling family pursues non-economic objectives to the detriment of minority shareholders (Bammens et al., 2011). The third threat is related to the interpersonal relationships that may be damaged when a certain job is secured for close relatives of the controlling family (Bammens et al., 2011). The fourth criticism involves a possible divergence of objectives between the members of a family that controls a firm (Bammens et al., 2011). All of these attitudes might affect a company's efficiency and lead to poor performance. This theory is consistent with the work of Sorenson (1999), who claimed that one of the undesirable outcomes of the presence of a controlling family within a firm is their neglect of the company's performance in favour of the maintenance of their own interests. Furthermore, Herrero (2011) argued that an agency conflict can exist when a firm is widely owned by many families. He added that the likelihood of such a conflict is increased when each family has its own interests, objectives and involvement plan (Herrero, 2011).

Mallin (2016) described different mechanisms whereby conflicts within family businesses may be solved. Each of these mechanisms is advisable in certain situations. For example, at the earliest stage of a family business, it is advisable that the family organise regular meetings or assemblies in order to facilitate the expression and exchange of family members' views (Mallin, 2016). Later, when the family has expanded due to marriage, the establishment of a family council is advisable (Mallin, 2016). This is consistent with the findings of Neubauer and Lank (1998), who suggested that the formation of a family council is suitable if the number of family members exceeds 30 or 40. When and if the relationships between family members begin to affect the operation and efficiency of the business, it is desirable that the family be

advised and directed by an advisory board that is tasked with helping the family to establish a more formal governance structure (Neubauer and Lank, 1998). However, such an advisory board may not provide the same advantage to a family firm as would a defined board that is dominated by independent non-executive directors. To this end, Bammens et al. (2011) argued that independent board members have the ability to question and challenge managers and thus protect not only the interests of lenders and investors but also those of the controlling family itself. Figure 3.2 outlines the possible stages of a family firm's governance.

Figure 3.2 The Possible Stages of Family Firms' Governance.



Source: Adapted from Mallin (2016)

State-Owned Firms and Corporate Governance

It is believed that governments and institutional investors have similar features in terms of their significant resources and the power they can wield over their investee firms (Borisova et al., 2012). However, governments and institutions might have different objectives when it comes to the implementation of corporate governance. Governments are much wealthier than are institutional investors, and thus they have the ability to leverage themselves by adopting various strategies (such as securing debt financing for the firms under their control). However, these kinds of facilities might hinder their ability to monitor the management of their investee firms, which may cause the agency problem to inflate. Furthermore, governments have the

ability and the power to craft regulations that may positively or negatively affect a company—some regulations may even force their investee firms to shut down. With regard to information gathering, governments have their own means of extracting required information about their investee firms—for example, they can utilise regulations or employ other legal means. However, this information may not always be used to improve the governance structures of their investee firms, particularly if this goal contradicts a superior objective, such as unemployment reduction or the increase of tax collection, that might lead to the stability of the financial system as a whole (see Borisova et al., 2012).

To encourage state-owned firms to enhance their corporate governance structures, the OECD issued its first set of guidelines regarding the corporate governance of state-owned enterprises in 2005. These guidelines highlight many aspects of governance, such as developing an effective legal and regulatory framework, acting as owner, treating shareholders equitably, developing positive relations with stakeholders, pursuing transparency and disclosure and taking responsibility of the boards of state-owned companies (OECD, 2005).

3.6. Outsider versus Insider Systems

Comparative corporate governance research has identified two contrasting models of corporate governance; outsider and insider systems (Franks and Mayer, 1994). The term ‘outsider system’ (or ‘shareholder-oriented system’) refers to a corporate governance system in which a company is controlled by a management team but is owned by outside shareholders (Solomon, 2013). The concept of an outsider-dominated system of corporate governance was first suggested by Berle and Means in 1932. Under this system, the ownership structure is dispersed, and agency costs are significant due to the separation of ownership and control (Solomon, 2013). However, institutional investors (such as those in the UK and the US) have gained influence over the management of many companies, which reduces the severity of agency costs. This is consistent with the findings of Mallin (2016), who pointed out that the growth of

institutional investors indicates that they hold an important and increasingly significant role in the affairs of companies wherein they act as owners rather than merely as shareholders. Additionally, under this system of corporate governance, hostile takeovers are frequent and are typically used to discipline the management of a firm for not achieving shareholders' objectives (Solomon, 2013).

Conversely, 'insider systems' (or 'stakeholder-oriented systems') are corporate governance systems in which most listed firms are controlled and owned by a small number of shareholders (Solomon, 2013). Franks and Mayer (2001) indicated that companies in Germany and Japan are good examples of such a system. In Germany, for instance, roughly 85% of the largest listed companies have a single shareholder who owns more than 25% of the voting shares (Franks and Mayer, 2001). The same pattern of ownership is found in the firms of East Asia (Hong Kong, Indonesia, Japan, South Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand); in fact, Claessens et al. (2000) reported that more than two-thirds of the firms in this region are basically owned by a single shareholder. Moreover, insider-dominated systems may suffer from a lack of transparency, which may adversely affect minority shareholders, as such shareholders may not be able to gain access to essential information regarding company functions; additionally, minority shareholders may have a reduced incentive to provide a firm with equity finance if the law fails to offer them sufficient protection (Solomon, 2013). Compared to outsider systems, insider systems are characterised as having little separation between ownership and control; therefore, the agency problem is rare. However, a second type of agency conflict (the 'Principal-Principal conflict') may arise if controlling shareholders expropriate private benefits at the expense of minority shareholders (Shleifer and Vishny, 1997).

3.7. Hard Law versus Soft Law Systems

An important aspect of global corporate governance involves whether a country abides by a hard law system, such as the Sarbanes-Oxley Act (SOX) of 2002, or a soft code approach, such as the principles of ‘good governance’. In hard law systems, the code of corporate governance is implemented via legislation. In the US, the federal SOX resulted in mandatory rules to which companies are required to adhere (Aguilera and Cuervo-Cazurra, 2009). Soft law systems, however, are represented by codes of corporate governance and largely utilise a ‘comply or explain’ approach; this approach requires firms to either comply with code recommendations or explain and justify their noncompliance (Luo and Salterio, 2014). These codes of corporate governance contain recommendations for best practices and mainly concern the function and composition of corporate boards; they also tend to touch on other governance practices (Zattoni and Cuomo, 2008).

The voluntary ‘comply or explain’ approach to UK corporate governance is generally considered to be a benchmark for other countries (Arcot et al., 2010). According to a recent international review of corporate governance codes conducted by Cuomo et al. (2016), figures show that since the publication of the Cadbury Report, a total of 354 corporate governance codes³ had been issued by 91 countries around the world by the end of 2014. There are various factors at play behind the development of corporate governance codes in a particular country. Aguilera and Cuervo-Cazurra (2004) argued that these factors include weak shareholder protections, elevated levels of government liberalisation and the increased presence of institutional investors. They also added that institutional and market pressures are the two main drivers behind the global spread of ‘good corporate governance’ codes. Furthermore, they

³ The development of corporate governance codes in the sample countries is discussed later in this chapter.

argued that the need for corporate governance codes arose from an increase in the number of public firms and from the ensuing agency problems that began to appear between dispersed owners and managers or between minority and majority shareholders (Aguilera and Cuervo-Cazurra, 2009). According to Cuomo et al. (2016), the financial crisis and the various high profile corporate collapses that have occurred around the world over the past two decades led to the diffusion of corporate governance codes. The first wave of corporate governance codes began in the late 1990s in parallel with the Asian and Russian stock crises—and with the collapses of high-profile firms such as Enron, Worldcom and Parmalat (Cuomo et al., 2016). The second wave, however, started after the recent financial crisis of 2007–2008 (Cuomo et al., 2016). Furthermore, international organisations such as OECD, Pan-European and ICGN have played their part in encouraging the global diffusion of national codes (Aguilera and Cuervo-Cazurra, 2009; Cuomo et al., 2016). These institutions have actively promoted governance practices and have provided guidance to developing countries regarding how best to cultivate corporate governance practices within their borders. Zattoni and Cuomo (2008) argued that legal systems (common versus civil) influence the diffusion of corporate governance codes. Their study aimed to examine whether the proliferation of corporate governance codes in civil law countries is driven by legitimization reasoning (without an eye towards improving governance practices) or by determination reasoning (to enhance governance practices). With respect to the determination aspect, their results showed that civil law countries were more likely to extend code recommendations to non-listed firms than were their common law counterparts (Zattoni and Cuomo, 2008). Regarding the legitimacy facet, however, their findings showed that civil law countries adopted governance codes later, issued fewer codes and included more ambiguous and lenient recommendations as compared to common law countries (Zattoni and Cuomo, 2008).

This voluntary approach to corporate governance has some proven advantages over the adoption of a hard set of regulations. For instance, Arcot et al. (2010) conducted a study to examine the effectiveness of the ‘comply or explain’ approach in non-financial UK companies between 1998 and 2004; their results revealed that the introduction of a voluntary code accelerated compliance, especially regarding those practices that were not covered by a forerunner (i.e., the Cadbury Report). Their results also revealed that, on average, for each particular provision, only 10% of the total sample was noncompliant (Arcot et al., 2010). More recently, using a sample of Canadian-listed firms in operation in 2006, Lou and Salterio (2014) found that a voluntary governance disclosure approach allowed companies to choose those governance practices that best suited their unique circumstances and settings; on average, these practices were found to be positively associated with firm performance.

3.8. The Anglo-Saxon Model

Followed by countries such as Australia, Canada, India, the US and the UK, the Anglo-Saxon model of corporate governance is based on the fiduciary relationship that exists between shareholders and management. Listed firms in these countries are expected to maximise the wealth of their shareholders; thus, there is need for a robust system whereby shareholder interests may be maintained (Franks and Mayer, 1990). Weimer and Pape (1999) stated that companies in Anglo-Saxon countries are generally controlled by a single board of directors that is comprised of insider and outsider directors. The outside directors are responsible for advising and monitoring the management team, and they are expected to be loyal, honest and to act in the best interests of the shareholders (Lorsch and MacIver, 1989). In these countries, boards of directors are supported by three key subcommittees: the audit, remuneration and nomination committees. In addition to these key subcommittees, other committees might be formed to deal with certain issues (such as risk and ethics).

3.8.1. Corporate Governance in Australia

The Australian system of corporate governance is traditionally described as employing an outsider approach, though it does share some basic similarities with the UK model (Stapledon, 1996). While the two systems are generally similar, differences exist with regard to ownership structures and the extent to which shareholders are involved in their companies (Solomon, 2013). Australian-listed firms have mixed structures in terms of ownership; companies range from widely-held firms to firms with controlling shareholders (normally-founded firms or those retaining intercompany ownership) (Mallin, 2016; Solomon, 2013). Given that block holders enjoy significant levels of ownership, the Australian corporate governance system can also be characterised as an insider system (Mallin, 2016). This point is emphasised by Stapledon (2006), who argued that one of the main features that distinguishes the Australian system of corporate governance from other Anglo-Saxon models is the existence of large blockholders in some of the listed firms. Furthermore, until the mid-1990s, the activism of institutional investors in Australia was less evident as compared to the activism of UK investors (Stapledon, 1996). In fact, the activism of shareholders in Australia increased following the introduction of the Australian Investment Managers' Group in the early 1990s, which introduced mechanisms to regulate the collective actions of shareholders (Solomon, 2013).

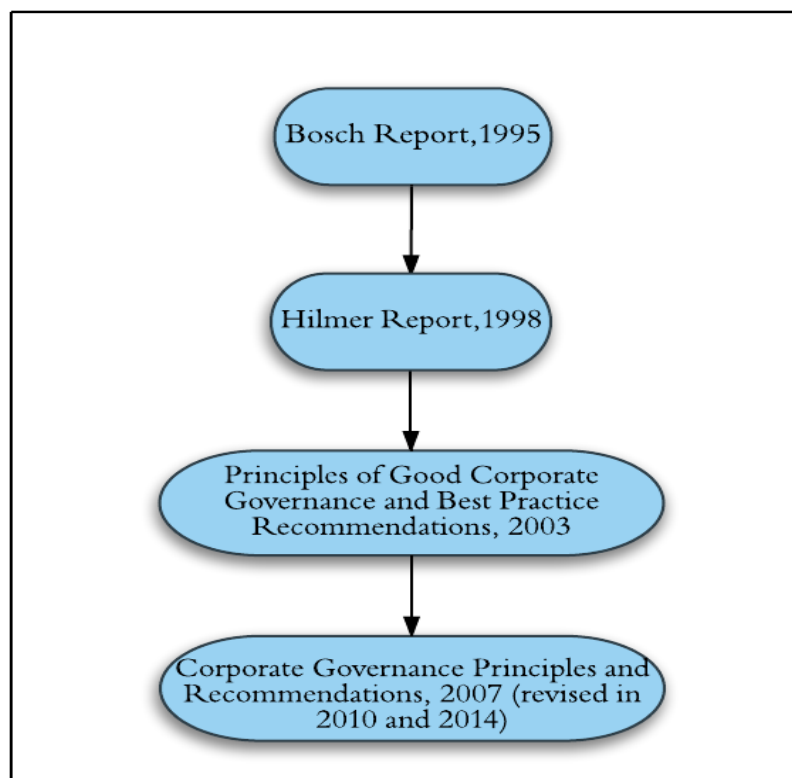
Paving the way for the development of corporate governance in Australia, dishonesty and abuse on the part of the directors of Australian firms caused the collapse of many companies in the 1980s. This led some leading business organisations⁴ to form a working group in 1991; this group was tasked with developing Australia's first corporate governance code (Bosch, 2002). This working group published its first report, *The Bosch Report on Corporate Practice and Conduct*, in 1991; additional issues were published in 1993 and 1995 (Mallin, 2016). This

⁴ Such organisations included the Business Council, the Australian Stock Exchange, the Australian Institute of Company Directors and various professional accounting bodies (Bosch, 2002).

report highlighted a wide range of corporate governance issues, such as corporate board structuring, the appointment of non-executive directors, directors' compensation, risk management, auditing and financial reporting, conflicts of interests and the role of the company secretary (Mallin, 2016). Several codes and guidelines on corporate governance practices have been issued since the formation of this working group; for example, 1998's *Hilmer Report* highlighted several issues, including board composition, the remuneration of the executive team and matters relating to the quality of disclosures (Mallin, 2016). In 2003, The Australian Stock Exchange (ASX) issued the first edition of its *Principles of Good Corporate Governance and Best Practices Recommendations*, which outlined ten principles according to a 'comply or explain' model (Tricker, 2015). These ten core principles collectively highlighted the importance of a board's structure and identified the board's responsibility to, along with the management team, promote ethical decision-making, maintain proper financial reporting, instantly disclose company-related matters, respect shareholders' rights, identify risk, properly manage that risk, consider the interests of the firm's stakeholders and encourage the enhanced performance of the board and management team, with an emphasis on fair compensation (ASX Corporate Governance Council, 2003). This code further recommended that the majority of the corporate board be comprised of independent directors. The code also proposed that corporate boards establish audit, compensation and nomination committees, the majority of whose members should be independent. In 2007, the ASX revised these principles for the first time, renaming the result the *Corporate Governance Principles and Recommendations*. Though this revision included some changes to wording, the ten principles remained essentially the same (Mallin, 2016). Following that revision, the ASX published its second modification to these principles in 2010, this time including various recommendations concerning the promotion of gender diversity; this revision described a measurable objective and outlined a clear policy on gender diversity. Furthermore, this revision pronounced that firms listed in the ASX should be

required to establish a compensation committee comprised of a majority of independent directors. However, this proposal was presented as guidance rather than as a recommendation, as was the case with the previous version (Mallin, 2016). Additionally, this revision required that ASX-listed firms adopt and disclose an organisational trading policy. Finally, in order to enhance shareholders' rights, this code called on ASX-listed firms to arrange for widely-accessible shareholder briefings; this accessibility could be accomplished by utilising communication technologies such as web-casts and conference calls (Mallin, 2016). The ASX further updated its principles and recommendations in 2014. According to Mallin (2016), this revision reflected the global developments in corporate governance that were made following the issuance of the ASX's second revision in 2007. Furthermore, this revision granted companies more flexibility in terms of disclosure. Figure 3.3 demonstrates the development of Australia's major corporate governance codes and guidelines.

Figure 3.3 The development of major corporate governance codes in Australia.



3.8.2. Corporate Governance in Canada

Broadly speaking, corporate governance in Canada is based on a voluntary adoption approach and is similar to the systems of the UK and Australia (Du Plessis et al., 2015). In general, Canada, Australia and the United Kingdom have similar guidelines for board composition, disclosure requirements and the establishment of key subcommittees (audit, remuneration and nomination) (Du Plessis et al., 2015). In contrast to the makeup of firms in other countries (such as the US and the UK), the ownership structures of Canadian-listed firms are more concentrated, and companies are controlled by wealthy families, firms and institutional investors (Du Plessis et al., 2015). Focusing on the Canadian securities regulatory framework, it is worth noting that Canada is the only developed country without a national securities regulator. Rather than establishing a national regulator, such as the one in operation in the US, each of Canada's 13 provinces has its own securities regulator that is in charge of formulating its own regulation policies. However, the Canadian Securities Administrator (CSA) does attempt to harmonise and coordinate the regulation of the various provinces (Du Plessis et al., 2015).

An examination of Canada's corporate governance development reveals that the first corporate governance guideline issued in Canada was *Where Were the Directors? Guidelines for Improved Corporate Governance in Canada*, which was popularly known as the *Dey Report* (Solomon, 2013). This report was published by the Committee on Corporate Governance, which was established by the Toronto Stock Exchange (TSX) in 1993 (Kleffner et al., 2003). The Dey Report outlined the 14 principles that were considered to encompass the best corporate governance practices of the time. The report described the ideal composition of a corporate board and its key subcommittees and emphasised the stewardship responsibility of a corporate board, describing its role in long-term planning, internal control and risk management (TSX, 1994). Five years later in 1999, a follow-up survey was conducted in an attempt to evaluate the

overall development of corporate governance in Canada; the resulting document was cleverly titled *Five Years to the Dey* (Kleffner et al., 2003). This report revealed that the guidelines published in the Dey Report were taken into wide consideration by Canadian-listed firms. However, the report also highlighted various concerns in terms of the stewardship role of a corporate board; such concerns related to board evaluation, risk management, the disclosure of corporate governance practices and the training of new directors (Rousseau, 2003). In response, the TSX formed the Saucier Committee in 2000 in an effort to review the process of decision-making as it related to corporate boards. After one year of deliberation, the committee proposed a total of 15 recommendations aimed at enhancing the stewardship role of corporate boards; this document is commonly known as the *Saucier Report* (Rousseau, 2003).

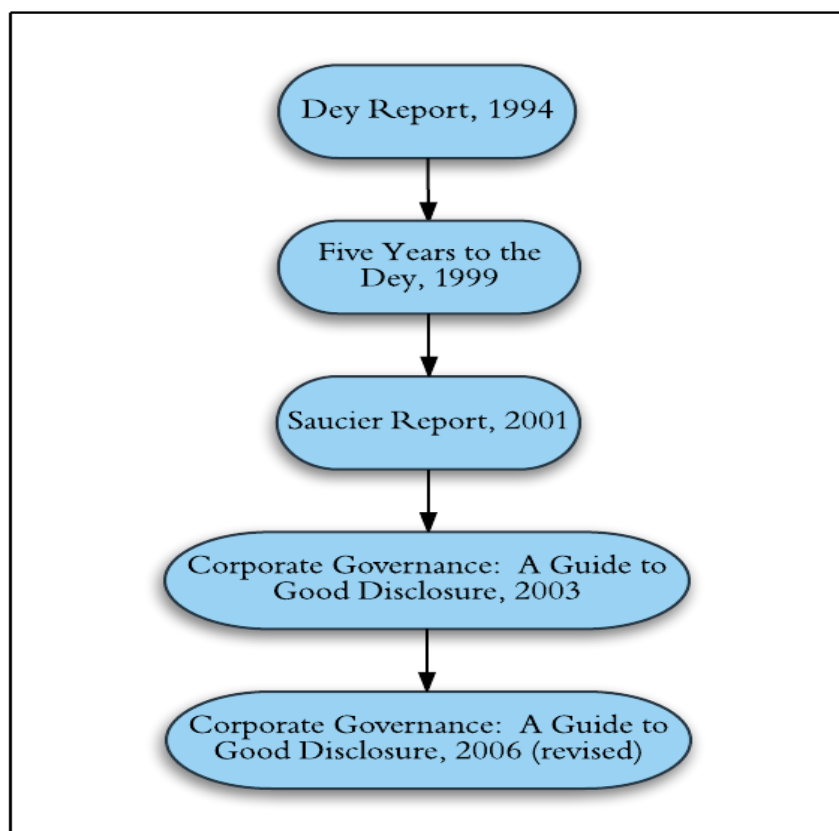
Due to the US passage of the SOX in 2002 and a financial scandal involving several Canadian corporations⁵, the TSX developed guidelines for better disclosure in 2003. The resulting publication, entitled *Corporate Governance: A Guide to Good Disclosure*, was issued in order to enhance the level and quality of the country's disclosure policies (Du Plessis et al., 2015). According to this guide, firms were required to disclose their governance practices and explain their level of compliance with the recommendations outlined in the report; if a company chose not to conform to a specific guideline, they were required to clearly state the reason for such noncompliance. Furthermore, the guide also provided an example of disclosure for each of the 14 guidelines (TSX, 2003). In 2006, the TSX elaborated on the previously-issued disclosure code by including a number of templates to be used as examples of good disclosure. These templates required listed firms to disclose their governance aspects according to subject (TSX, 2006). Figure 3.4 illustrates the development of Canada's major corporate governance codes and guidelines.

⁵ Such companies included Nortel, Livent and the Cinar Corporation (Du Plessis et al., 2015).

In an attempt to promote gender diversity in Canada, the province of Quebec prescribed that 50% of a firm's board seats should be occupied by female directors (Deloitte, 2015); this quota applied to state-owned firms, and full compliance was achieved in 2011. Additionally, in 2014, the Senate of Canada proposed a gender quota of 40% for listed firms, financial institutions and state-owned firms. Boards with eight or fewer members were required to have a maximum two-member gender differential. Following the passage of this quota, each gender was required to have at least 20% representation on a firm's board after three shareholder meetings and 40% representation after the sixth shareholder meeting (Deloitte, 2015).

It is also worth noting that in 2014, the Canadian Securities Administrator began to require firms to disclose several aspects related to gender diversity. For example, firms were expected to release policy information concerning the representation of female directors and the appointment of women to executive positions; firms were also required to disclose the number of female board directors and the number of women in executive positions. Furthermore, firms were obliged to establish targets with regard to the appointment of women to their boards and to executive positions (see Deloitte, 2015).

Figure 3.4 The development of major corporate governance codes in Canada.



3.8.3. Corporate Governance in India

As a former colony of Britain, India has the same legal system as the UK; as such, India offers a considerable level of protection to minority shareholders as compared to other East Asian countries (Solomon, 2013). Equity shares in India are traded in two stock exchanges—the Bombay Stock Exchange and the National Stock Exchange of India. To a certain extent, the ownership structures of most Indian firms are characterised as widely-held; however, in certain cases, firms are controlled by families or by the state⁶ (Chakrabarti et al., 2008).

⁶ Roughly 60% of the 500 largest listed firms are controlled by families, and 11% are controlled by the state of India (Chakrabarti et al., 2008).

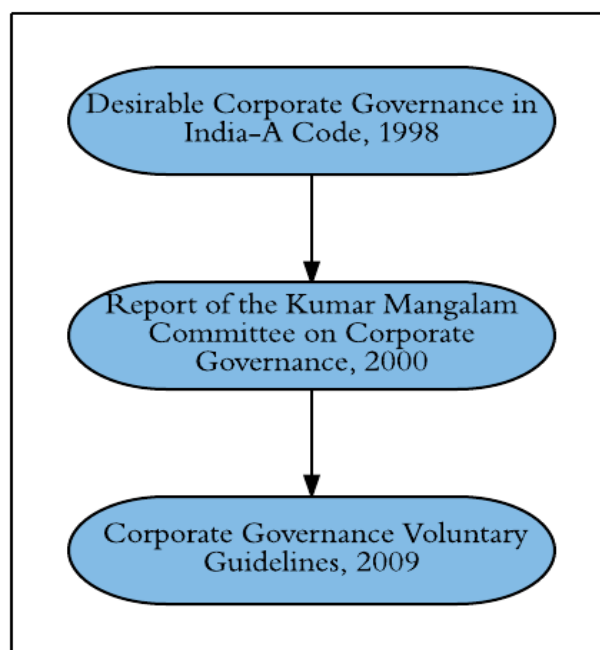
To facilitate the reform of corporate governance practices in India⁷, the Confederation of Indian Industry published its first code in 1998, entitled the *Desirable Corporate Governance in India: A Code*, which was based upon the voluntary compliance system (Mallin, 2016; Solomon, 2013). This code presented 17 recommendations and covered several governance areas, including board composition, external directorship limits, the responsibilities of non-executive directors, the recording of attendance during board meetings and disclosure enhancements (Confederation of Indian Industry, 1999). The code further decreed that at least 30% of a corporate board's seats should be occupied by non-executive directors, provided that the board chair was also considered a non-executive director; if a firm's CEO maintained a duality position on the board, however, the proportion of required non-executive directors rose to 50% (Dahiya and Rathee, 2001). Following the publication of this code, another initiative was undertaken by the Securities and Exchange Board of India in 1999; to accomplish its goals, the board formed a committee chaired by Shri Kumar Mangalam Birla. The aim of this committee was to design a corporate governance code that took into consideration the views of those who invested in the listed firms of India (Dahiya and Rathee, 2001). One year later, the committee published its report under the title *The Report of the Kumar Mangalam Birla on Corporate Governance* (Mallin, 2016). Additionally, the Ministry of Corporate Affairs introduced *The Corporate Governance Voluntary Guidelines* in 2009 in an attempt to further enhance and improve India's corporate governance practices (Ministry of Corporate Affairs, 2009). These guidelines were divided into six main topics: boards of directors, the responsibility of a board, the responsibility of a board's audit committee, the establishment of auditors, the rules of the secretarial audit and the institution of mechanisms regarding whistleblowing (Mallin, 2016).

⁷ This initiative was developed in response to public concerns regarding investor protections, the legal level of disclosure for listed firms and the need to adopt international governance standards (Dahiya and Rathee, 2001).

Figure 3.5 demonstrates the development of India's major corporate governance codes and guidelines.

In an attempt to promote the diversity of the country's corporate boards, India's Institute of Company Secretaries took the initiative to bring female representation on corporate boards more in line with the levels of other countries. To this end, *The Companies Act of 2013* required that Indian firms have at least one woman on their corporate boards (Deloitte, 2015). This requirement was mandatory for all listed firms, public firms with a paid-up share capital of 1 billion Indian Rupee (INR) and firms with a turnover of 3 billion INR or more (Deloitte, 2015).

Figure 3.5 The development of major corporate governance codes in India.



3.8.4. Corporate Governance in Ireland

The Irish corporate governance system is a special case; while Ireland's legal and institutional environment mirrors that of the UK, the Irish business environment is considerably influenced by the US (Donnelly and Mulcahy, 2008; Solomon, 2013). According to Donnelly and Mulcahy (2008), due to the historical links between the UK and Ireland, the Irish corporate governance system parallels the approach established by the UK. For instance, the Irish Stock

Exchange requires that public and limited firms operating in Ireland comply with the corporate governance codes published by the UK; thus, firms must explain how they comply with the codes' principles or otherwise provide justification for their noncompliance. However, Ireland is also tightly linked to the US due to the direct investment of US companies in Ireland, a practice that has influenced the country's institutional and managerial practices (Donnelly and Mulcahy, 2008). It is important to note that Ireland has a relatively small stock exchange as compared to those of the US and the UK⁸ (O'Connell and Carmer, 2010). With a one-tier board structure, the corporate governance system in Ireland follows the Anglo-Saxon style.

Given the historical links and the similarities of accounting practices and ownership structures within companies in the UK and Ireland, it is not surprising that Ireland mirrors the corporate governance practices followed in the UK (Donnelly and Mulcahy, 2008; Ward et al., 2013). In 1973, the Irish Stock Exchange merged with the British Stock Exchange, forming the International Stock Exchange of Great Britain and Ireland (currently known as London Stock Exchange). However, the Irish Stock Exchange became independent in 1995, and annexed the provisions of the Combined Code in the UK to its listing requirements in 1999 (Ward et al., 2013).

In addition to this, investors' associations and the central bank in Ireland published several governance guidelines in an effort to promote the practices in some specific areas. Among them, the Irish Association of Investment Managers (IAIM) issued one such set of recommendations, *Corporate Governance, Share Option and Other Incentive Schemes*, in 1999. This document recommended that listed firms offer their directors share options and other incentive schemes as part of a remuneration package in order to increase a director's

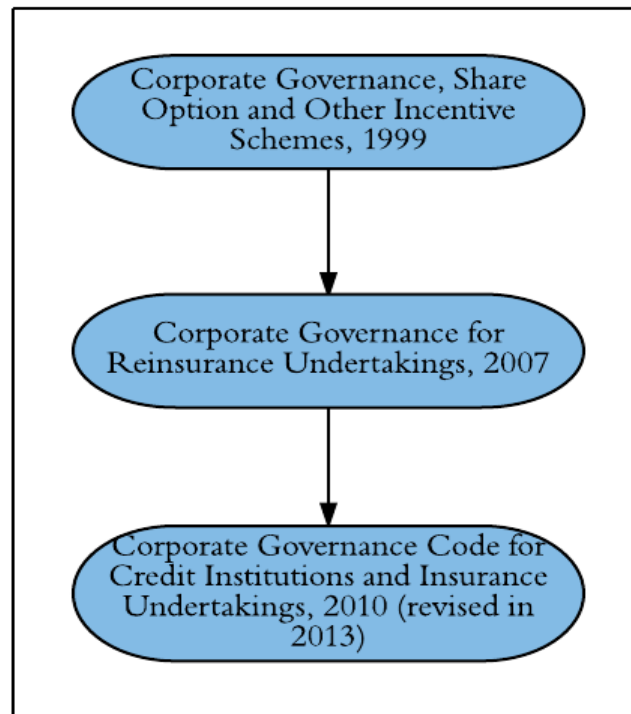
⁸ In 2008, the market capitalisation of the Irish stock exchange represented only 3.2% of the market capitalisation of the UK (O'Connell and Carmer, 2010).

commitment to the firm and align the interests of a particular firm's shareholders and management teams (IAIM, 1999).

In 2007, the Central Bank of Ireland published a set of corporate governance guidelines pertaining to insurance companies in response to the publication of Council Directive 2005/68/EC. The document was titled the 'Corporate Governance for Reinsurance Undertakings' and covered six main recommendations for Irish insurance companies, namely involving corporate boards and their key subcommittees, internal controls, audit functions, compliance and the roles of INEDs and senior management officials (Central Bank of Ireland, 2007). Another code, this time targeting credit institutions as well as insurance companies, was issued by the Central Bank of Ireland in 2010. This particular code was titled the 'Corporate Governance Code for Credit Institutions and Insurance Undertakings' and aimed to ensure that corporate governance frameworks be established to reflect the nature of these institutions as well as their associated risks (Central Bank of Ireland, 2010). A subsequent revision of the code was issued in 2013; this revision included additional recommendations related to the number of directorships that should be held by members of the corporate boards of credit and insurance firms and suggestions regarding the composition of risk, compensation and nomination committees (Central Bank of Ireland, 2013). Figure 3.6 demonstrates the development of Ireland's major corporate governance codes and guidelines.

As in the UK, Ireland has no mandatory quota to promote gender diversity on corporate boards; however, an initiative has been introduced that would require firms owned by the state to have 40% female representation on their boards and committees (European Commission, 2016).

Figure 3.6 The development of major corporate governance codes in Ireland



3.8.5. Corporate Governance in the United Kingdom

The UK has a well-developed market, and companies in the UK are listed in the London Stock Exchange. In the UK, ownership structures are based on a system of diversified shareholders and include institutional investors, financial institutions and individuals; importantly, the various institutional investors (pension funds, insurance companies and mutual funds) have become much more influential over the last few decades (Mallin, 2016). The most noteworthy point about UK ownership structures involves the increased expansion of foreign investors in the listed firms of the UK⁹ (Fleckner and Hopt, 2013). The UK has a unitary board structure, and corporate governance codes require that at least half of a company's board members, excluding the chairman, be non-executive directors who have been determined to be independent (Fleckner and Hopt, 2013).

⁹ Recent statistics show that roughly 53.8% of UK-listed firms are owned by overseas investors (Office for National Statistics, 2015).

As in other countries, financial scandals and the collapse of various firms were the main drivers of corporate governance development in the UK. According to Mallin (2011), the failure of Coloroll and Polly Peck led to the establishment of the Committee on the Financial Aspects of Corporate Governance in May of 1991. After the committee was formed, scandals involving Maxwell and the Bank of Credit and Commerce International occurred, which led the committee to look beyond financial aspects and consider corporate governance issues as a whole (Mallin, 2016). The committee published its findings in 1992; the resulting report is commonly known as the *Cadbury Report* in honour of Sir Adrian Cadbury, the committee chair (Mallin, 2016). While the Cadbury Report was not considered a compulsory set of rules to be adopted by public companies quoted in the stock exchange (Solomon, 2013), such companies were required to conform to the report's guidelines or provide justification for their noncompliance. The recommendations of this report focused on three main areas: boards of directors, auditing practices and shareholder responsibilities (Cadbury Report, 1992). The Cadbury Report considered boards of directors to be important governance mechanisms that should constantly monitor and assess the management of their firms. Thus, the report called for the wider use of independent non-executive directors and recommended that boards establish three key subcommittees (audit, remuneration and nomination) comprised wholly or mainly of non-executive directors. The report also endorsed a division of responsibility between the chairman of the board and the chief executive (these two positions are sometimes held by the same figure). Furthermore, auditing functions were seen as essential procedures that possessed the ability to enhance corporate governance by emphasising the importance of transparency in all firm activities. Lastly, the Cadbury Report highlighted the vital role of institutional investors, the largest and most influential group of shareholders, in enhancing the corporate governance of their investee firms. In particular, the report recommended that institutional investors regularly engage with their investee firms concerning firm performance, strategies,

board composition and management quality. Additionally, the report also encouraged institutional investors to engage with their firms, to use their voting power to ensure that an appropriate governance structure be established and to fulfil their fiduciary responsibility towards their ultimate beneficiaries. The report inspired institutional investors to focus on board composition and to promote the recruitment of experienced non-executive directors who were independent of the management team. To date, there have been numerous revisions to and developments on various aspects of the Cadbury Report. These revisions and amendments are discussed below.

Following the publication of the Cadbury Report, another committee (led by Sir Richard Greenbury) was formed in 1995 in an attempt to address shareholders' concerns regarding directors' remuneration packages and the lack of disclosure regarding such matters in firms' annual reports (Solomon, 2013). The ensuing *Greenbury Report* was published in 1995, and it provided a means of establishing a balance between directors' compensation schemes and firm performance (Solomon, 2013). According to Mallin (2016), the Greenbury Report aimed to enhance the accountability and performance of firms' directors by (i) requiring firms to provide detailed annual reports of directors' compensation packages, to be prepared by a remuneration committee comprised of independent non-executive directors and (ii) linking compensation packages to the performance of both the firm and individual directors, thus aligning the interests of directors and shareholders (see Mallin, 2016).

The Hampel Committee was formed in 1995, and the resulting *Hampel Report* was published in 1998. The main role of this committee was to review the implementation of both Cadbury and Greenbury Report recommendations (Solomon, 2013). Per Mallin (2016), much of the Hampel Report focused on the extent to which firms maintained good relationships with their stakeholders (employees, customers, suppliers and providers of credit) and protected the interests of their shareholders. Furthermore, the report highlighted the important role of

institutional investors in their investee firms. To this end, the Hampel Report highly recommended that rather than engaging in ‘box ticking’, institutional investors should enter into a dialogue with their investee firms in an effort to discuss issues of concern (Hampel, 1998).

Following the issuance of these three reports, the *Combined Code* was published in 1998; this code aimed to merge the recommendations of the previous reports (Cadbury, Greenbury and Hampel), thus consolidating the main points and presenting the basic principles (Ward et al., 2013). According to Mallin (2016), this code was divided into two main parts. The first section dealt with companies and covered the following topics: (i) directors, (ii) directors’ remuneration, (iii) relations with shareholders and (iv) accountability and auditing. The second section discussed institutional investors and discussed the following three issues: (i) shareholder voting, (ii) dialogue with companies and (iii) the evaluation of governance disclosures.

Following the publication of the Combined Code, the Turnbull Committee was formed by the Institute of Chartered Accountants in England and Wales (ICAEW) in 1999 and chaired by Nigel Turnbull (Mallin, 2016). The main aim of the resulting *Turnbull Report* was to provide guidance on the implementation of the internal control provisions put forth in the Combined Code (Turnbull, 1999). The report provided clear recommendations for the enhancement of internal control systems in UK companies (Solomon, 2013). The report also highlighted the significance the corporate board’s role in ensuring that a company possesses a reliable internal control system (Mallin, 2016).

Another committee chaired by Derek Higgs was formed, and the subsequent *Higgs Report* was published in January of 2003. According to Ward et al. (2013), the collapse of Enron led most countries, including the UK, to assess their corporate governance codes, particularly those concerning the role and effectiveness of non-executive directors. This report focused on the

role and responsibility of non-executive directors and recommended that annual reports should disclose the number of meetings held at the board and subcommittee levels as well as the attendance records of each board member (Higgs, 2003). The report also highlighted the importance of succession planning, arguing that the chairman and CEO should implement executive development programmes to prepare individuals within the firm to take on directorship roles in the future. The review further stated that the performance of a board, its subcommittees and its members should be evaluated at least once per year, the outcome of which should appear in the annual report. Concerning the practice of holding directorships in multiple firms, the review recommended that full-time executive directors hold no more than one additional directorship in another firm, provided that the second position is not the chairmanship of another major company; furthermore, the report stated that a non-executive director cannot sit on all key subcommittees of a board (audit, remuneration and nomination) (see Higgs, 2003).

Another committee was formed following the publication of the Higgs Report in an effort to address the role of audit committees in the wake of the Enron collapse. Thus, the Smith Committee was appointed by the Financial Reporting Council (FRC) in January of 2003 (Smith, 2003). The main issues raised in the *Smith Report* concerned the relationship between external auditors and the firms they were auditing as well as the duties of the audit committee within a company (Solomon, 2013). The report also recommended that the audit committee be tasked with ensuring that an appropriate system of control take effect, though it would not monitor the process itself (Mallin, 2016).

A revised Combined Code was published in July of 2003 and included the recommendations highlighted in both the Higgs and Smith reviews. This code emphasised the role of the chairperson and the senior independent director; according to this code, a chairperson is responsible for providing leadership to non-executive directors, communicating shareholders'

views to the corporate board, highlighting the annual evaluation for the board and its subcommittees and calling attention to the performance of each individual director. Furthermore, the Combined Code called for the independence of the board, arguing that in larger firms, half of the board should be comprised of independent non-executive directors (FRC, 2003).

In June of 2006, the FRC published a new edition of the Combined Code that highlighted three major changes. As per Mallin (2016), these changes were made (i) to allow the chairman of a firm to serve as a member of the remuneration committee, where he would be considered an independent chairman on appointment, (ii) to provide a ‘vote withheld’ option on proxy appointment forms, which would allow shareholders to withhold their votes and (iii) to encourage firms to disclose on their websites all details concerning general meeting proxies, where votes would be taken via a show of hands.

In June of 2008, the FRC issued another new edition of the Combined Code, this time highlighting two main changes. These changes would (i) permit an individual to chair more than one firm operating in the FTSE 100 and (ii) allow the chairperson of a company to sit on the audit committee, if on appointment he or she was considered to be independent (this applied to all firms listed outside the FTSE 350) (Mallin, 2016).

In response to the financial crisis of 2007–2008, Sir David Walker carried out an independent review of the governance practices of the banks and other financial institutions of the UK (Walker, 2009). The ensuing *Walker Review* was published in November of 2009 and contained 39 recommendations concerning various aspects of corporate governance, including the composition and qualifications of corporate board members, the functioning and performance assessment of the board, communication with institutional investors and their engagement with investee firms, the governance of risk, recommendations related to the role of the remuneration

committee and the disclosure of the remuneration packages of executive directors (Mallin, 2016).

In 2010, the FRC published the *UK Corporate Governance Code* (formerly known as the Combined Code). This updated code demonstrated a wider understanding of the UK's corporate governance evolution and incorporated some of the recommendations made by the Walker Review (Mallin, 2016). According to Mallin (2016), the UK Corporate Governance Code retained the 'comply or explain' approach and comprised the following six changes. (i) In an effort to enhance a firm's risk management practices, a company's business model should be explained, and a corporate board should be held responsible for any risk it is willing to undertake. (ii) Performance-related pay should be aligned with the long-term interests of a firm and with its risk system. (iii) To increase the accountability of the directors sitting on the boards of FTSE 350 firms, such directors should be re-elected each year. (iv) New principles related to the leadership of the chairman of a board should be established, and the responsibility of non-executive directors to provide constructive debate in the boardroom should be defined. (v) New principles related to the composition and appointment of board directors should be created, and firms should consider appointing directors with diverse characteristics (for example, members of both genders). And finally, (vi) a chairman should hold regular development reviews for each director, and firms listed in the FTSE 350 should conduct external evaluations every three years in an effort to enhance board performance and to identify a board's strengths and weaknesses.

It is important to note that this code included one schedule to explain various principles related to the engagement of institutional investors within their investee firms (see FRC, 2012a). This schedule has since been deleted and incorporated into the *UK Stewardship Code*, which was published in 2010. The Stewardship Code aimed to enhance engagement between institutional investors and their investee firms and attempted to explain the best methods of engagement.

The FRC revised the Stewardship Code in 2012, the result of which is discussed in detail in the following chapter.

The FRC published a revised version of the UK Corporate Governance Code in 2012; among the included changes were the recommendations that (i) firms listed in the FTSE 350 should put out external audits for tender at least once every ten years in an effort to ensure high quality standards, (ii) audit committees must disclose to shareholders how they have fulfilled their responsibilities and must release their assessments of external audits, (iii) boards must ensure that annual reports and accounts are understandable and reflective of the company's performance, (iv) companies must disclose their policies regarding board diversity and (v) companies are required to disclose the reason for any noncompliance with certain provisions of the code (see Mallin, 2016). In 2014, the FRC issued further revisions to the UK Corporate Governance Code; such changes were related to the three main topics of risk management, remuneration and shareholder engagement (see Mallin, 2016).

Due to the lack of representation of female directors in UK-listed firms, the UK's Coalition Government invited Lord Davies to assess the situation, calling on him to identify the barriers that prevented female directors from joining UK-listed firms and to issue recommendations aimed at enhancing the representation of women on corporate boards (Mallin, 2016). The ensuing *Women on Boards* report, also known as the *Davies Report*, was published in February of 2011 and provided several recommendations. The report called on the chairmen of FTSE 350 companies to disclose how many women would be targeted to join their boards in 2013 and 2015. Furthermore, the Davies Report argued that the boards of FTSE 100 companies should aim for a board composition that was, at a minimum, 25% female. The quoted companies were also requested to disclose in their annual reports the percentage of females sitting on their boards, the number of females holding senior executive positions and the number of female employees serving within the company (Davies, 2011). Following the

publication of the original report's recommendations in 2011, an annual review was conducted to assess the compliance of UK-listed firms. The latest review was completed in 2015 and showed that the number of female directors in FTSE 350 companies has almost doubled over the figure that was recorded when the report was initially issued in 2011 (Davies, 2015). This new figure of 23.5% is considered to mark good progress towards the recommended target of 25% female representation by 2015 (Mallin, 2016).

It is also worth noting that in order to increase the representation of women in UK-listed firms, the government appointed Sir Philip Hampton (chairman of GlaxoSmithKline plc) to lead an independent review in February of 2016; this review aimed to promote greater female representation among the executive positions of FTSE 350 companies (see GlaxoSmithKline, 2016). Figure 3.7 illustrates the development of corporate governance in the UK.

Figure 3.7 The development of major corporate governance codes in the UK.



3.8.6. Corporate Governance in the US

In the US, the development of a corporate governance system has included reforms that are different from those pursued by other countries. As per Mallin (2016), in contrast to the national codes of many other countries, the US lacks a definitive set of corporate governance codes, as each state has the authority to establish its own laws and regulations. Additionally, the corporate governance regime is oriented towards a hard law system that is regulated by inflexible legal statutes and mandatory regulations; this system stands in contrast to the voluntary British approach (Tricker, 2015). As a common law country, the US federal government¹⁰ is responsible for issuing corporate laws regarding auditing and disclosure requirements as they apply to public firms (Fleckner and Hopt 2013; Tricker, 2015). The US corporate governance system subscribes to a unitary board structure that is subject to the dominance of independent outside directors. Furthermore, the listing requirements of the US Stock Exchange also mandate the establishment of audit, remuneration and nomination subcommittees of a corporate board (Tricker, 2015).

The US has a well-developed market with a diversified shareholder base that includes institutional investors, financial institutions and individuals (Mallin, 2016). Due to the large number of publicly traded firms and the widely-held ownership structures of many US companies, the American financing system has been described as outside- or market-based (Fleckner and Hopt, 2013). Furthermore, many sources of private and public financing are available in the US for both debt and equity purposes, and public markets drive many of the regulations concerning corporate governance issues. According to Fleckner and Hopt (2013), US firms have significant influence over the corporate governance system of the country, which can be summarised as encompassing the following three features: the separation of

¹⁰ In the US, such matters are predominantly the responsibility of the Securities and Exchange Commission (SEC) (see Tricker, 2015).

ownership and control, the heightened role of institutional investors and the political significance of ownership structures (Fleckner and Hopt, 2013). First, in firms wherein the ownership structure is dispersed, there is no large shareholder population to monitor the actions of management. In these cases, if managers misuse a firm's resources, shareholders may suffer losses and receive insufficient gains. Therefore, many of the US's corporate governance regulations are formatted in such a way that balances the costs and benefits of such a system, and monitoring techniques are developed to protect shareholders from this separation (Fleckner and Hopt, 2013). The second aspect of the US corporate governance system involves the ownership structures of US-based public firms. As per Fleckner and Hopt (2013), for most of the twentieth century, the ownership of listed firms was dominated by individuals. However, in the last few decades, such ownership has shifted, with more firms being controlled by institutional investors such as pension funds, insurance companies, private equity firms and hedge funds (Fleckner and Hopt, 2013). In the past, shareholders preferred to sell their shares rather than attempt to influence their investee firms, thus exercising the exit option rather than the voice option. However, due to the advent of larger institutional investors (especially pension and hedge funds), the voice option has become preferred and is more often exercised by modern shareholders (Fleckner and Hopt, 2013). The third facet of the US system concerns the political voice of shareholders, in particular following the corporate scandals of 2001. In response to these scandals, a quick federal response was issued in the form of the *Sarbanes-Oxley Act of 2002*. This swift response also highlighted the importance of shareholder protections.

As mentioned above, the US has no definitive corporate governance code like those issued by various other countries. However, prior to the issuance of the Sarbanes-Oxley Act of 2002, the

Business Round Table¹¹ introduced several corporate governance codes beginning in the 1970s. According to Aguilera and Cuervo-Cazurra (2004), the US's first corporate governance code was published in 1978 by this organisation. This code was named *The Role and Composition of the Board of Directors of the Large Publicly Owned Corporation* and was based on the voluntary approach (The Business Round Table, 1997). Following the publication of this code, the Business Round Table published several other protocols, including the 'Statement on Corporate Responsibility' in 1981, the 'Statement on Corporate Governance and American Competitiveness' in 1990, and the 'Statement on Corporate Governance' in 1997 (The Business Round Table, 1997). The latter statement highlighted three main topics: the function of a board, the structure and operation of a board and stockholder meetings (The Business Round Table, 1997).

The passage of both the Sarbanes-Oxley Act (2002) and the New York Stock Exchange's (NYSE) *Corporate Governance Rules* (2003) served to improve the structure of national corporate governance in the US (Mallin, 2016). In response to the financial scandals of Enron, Worldcom and Global Crossing—which occurred due to the existence of close relationships between companies and their external auditors (Mallin, 2016)—the US Congress agreed to amend some of the NYSE Listing Rules in what became known as the Sarbanes-Oxley Act. This act described many practices that US-listed companies should be compelled to implement. Importantly, the act required that chief executive officers and chief financial officers certify that quarterly and annual reports, which are filed using the 10-Q, 10-K and 20-F forms, are (i) in compliance with securities law and (ii) present a clear picture of a firm's financial position. Furthermore, the Sarbanes-Oxley Act aimed to strengthen the independence of auditors and of a corporate board's audit subcommittee. To this end, the act stated that listed companies must

¹¹ The Business Round Table is a national organisation that expresses its authoritative voice on matters related to large corporations in the US; this group is keenly interested in increasing awareness of corporate governance practices (The Business Round Table, 1997).

establish audit committees comprised solely of independent directors; additionally, the act required that at least one member be a financial expert. The act also decreed that all relevant information must be disclosed. Additionally, the act requested that all auditors of both US-based and overseas firms register with the appropriate regulatory body, the Public Company Accounting Oversight Board (PCAOB) (Mallin, 2016).

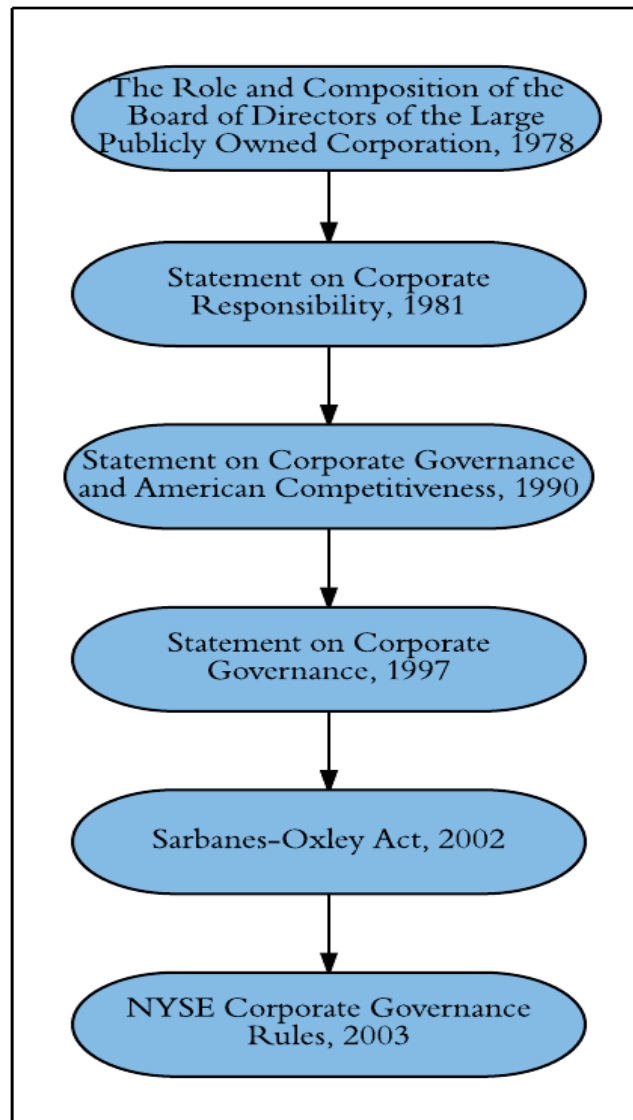
In November of 2003, the Securities and Exchange Commission (SEC) agreed to approve new rules on corporate governance. These new rules aimed to strengthen corporate governance standards for listed firms and were intended to enable directors, officers and employees to operate more effectively (Mallin, 2016). Moreover, the new rules enabled shareholders to monitor their companies' performance and alleviate any incidences of corporate collapse. The NYSE rules further required that a majority of directors be independent and provided details regarding the type of figure that could be considered as such. Non-management directors were required to meet regularly and without the executive directors being present. Furthermore, the rules mandated the formation of the three key subcommittees and stated that each should be comprised only of independent directors. Additionally, the SEC recommended that the purpose and annual evaluations of each committee be disclosed. According to these new rules, companies should implement these corporate governance guidelines and disclose their practices on the company website, along with the makeup of each committee (Mallin, 2016).

Furthermore, the US system boasts various distinctive features, including the *Delaware General Corporation Law*, which provides companies incorporated in Delaware with various benefits, and the *Employee Retirement Income Security Act of 1974* (ERISA), which mandates the activism of pension funds to vote their shares (see Mallin, 2016; Solomon, 2013). Over the years, the Delaware Law has become the most predominant system in the US. Mallin (2016) stated that the Delaware approach is considered to be 'company friendly'; thus, the majority of companies listed in the NYSE are enticed to register in Delaware in order to take advantage of

the state's flexible approach. The main goal of the Delaware Law was to provide boards of directors with the authority to establish corporate policies and objectives whilst operating within the context of fiduciary duty (Mallin, 2016). Furthermore, this law demanded that various requirements be abided, to include the protection of minority interests. Because the Delaware Law has fewer procedural requirements as compared to other state laws on the books in the US, the state attracts many US-listed companies (Mallin, 2016). Another notable facet of the US corporate governance system involves the ERISA. According to this act, private pension funds are compelled to vote the shares that they hold domestically as well as those that they hold internationally. Furthermore, this act decreed that if a pension fund intends to purchase overseas shares, a cost-benefit analysis must be conducted in order to assess the viability of voting those shares (see Mallin, 2016). Figure 3.8 demonstrates the development of US's major corporate governance codes and acts guidelines.

Regarding the gender diversity of corporate boards, the US—like the UK—has no mandatory quota system. However, several organisations across the country have established various targets regarding the representation of females on corporate boards. For example, the Thirty Percent Coalition recommended that by 2015, 30% of corporate board directors should be female. Furthermore, The 30% Club has advocated that 30% of corporate board seats should be held by female directors (Deloitte, 2015). Additionally, the Organisation of 2020 Women has focused on achieving a target of 20% female representation on the boards of US-listed firms (see Deloitte, 2015).

Figure 3.8 The development of major corporate governance codes/Acts in United States



3.9. The Germanic Corporate Governance System

The German model is characterised by the involvement of numerous participants, including shareholders, management teams, banks, employees, suppliers of goods and customers (Moerland, 1995). Most of the countries that employ this model—including Germany, the Netherlands, Switzerland and Austria—have adopted a two-tiered system comprised of a supervisory and a management board (Weimer and Pape, 1999). The role of the supervisory board is to advise and direct the management board, though it also has the authority to appoint

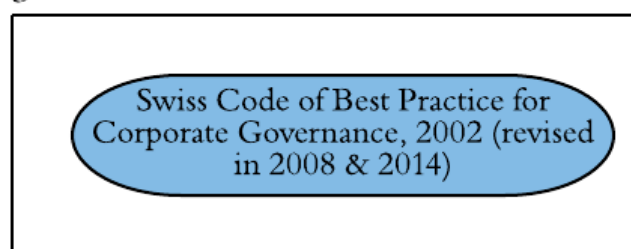
and dismiss members of that board. According to the German model, employees are allocated seats on the supervisory board; companies with more than a certain number of employees (typically 500 or 2000) are recommended to allocate one-third or one-half of the supervisory board seats to representatives of the employees.

3.9.1. Corporate Governance in Switzerland

Swiss firms generally follow a unitary board model. However, due to the flexibility of Swiss corporate law, companies also have the right to adopt a two-tiered board structure (Fleckner and Hopt, 2013). According to Ruigrok et al. (2007), a large number of Swiss-listed firms are owned and controlled by their founders or their founders' family members. Similar to the models adopted by other European countries, the transparency level of Switzerland's corporate governance system is relatively low. Prior to 2003, Swiss-listed firms were not required to publicly disclose their corporate governance practices, with the exception of those companies owned by parties whose ownership levels exceeded 5%; in such instances, the names and details of the company's officers had to be released (Ruigrok et al., 2006). Ruigrok et al. (2006) also argued that despite Switzerland's higher market capitalisation, the market has little influence over firms' management systems, which could be justified as follows. First, most Swiss-listed firms are, on average, under the control of family owners (Ruigrok et al., 2006). Second, Swiss firms have the flexibility to pursue one of several means of achieving anti-takeover objectives, such as the issuance of different types of shares (Ruigrok et al., 2006). Third, as large creditors, Swiss banks can influence firms in various ways; for example, they can promote their own representation on corporate boards or utilise the voting rights associated with depositary shares (Ruigrok et al., 2006). Fourth, the passivity of Swiss pension funds allows them to own small amounts of shares; this is due to their minor levels of ownership within individual firms (Ruigrok et al., 2006).

Switzerland's first corporate governance code, the *Swiss Code of Best Practice for Corporate Governance*, was initiated by economiesuisse¹² in 2002 in collaboration with the Swiss Stock Exchange (Economiesuisse, 2002). The code was based on a system of voluntary compliance and was designed specifically for Swiss-listed firms. This Swiss code provided several recommendations with regard to shareholders, boards of directors, executive management teams, auditing practices and disclosure requirements (Economiesuisse, 2002). Five years later, in response to further discussion about the remuneration of directors and executive team members, economiesuisse decided to revise the previous code and publish ten recommendations related to the remuneration of directors and senior managers (Economiesuisse, 2008). The most recent version of this code was published in 2014 and incorporated changes to the guidelines with regard to risk management and the social responsibility of firms. This revised code also recommended various changes to the composition of corporate boards, suggesting, for example, that both genders be represented on such boards (Economiesuisse, 2014). It is worth noting that the corporate governance code of Switzerland has retained the same name since its 2004 initiation. Figure 3.9 demonstrates the development of Switzerland's major corporate governance codes guidelines.

Figure 3.9 The development of major corporate governance codes in Switzerland



¹² The Swiss Business Federation.

3.10. The Latin Countries Model

Predominantly practiced in France and Italy, the Latin governance model lies somewhere between the Anglo-Saxon and Germanic systems (Weimer and Pape, 1999). Shareholders in Latin systems are much more influential than are those in German systems, but not as powerful as those operating in Anglo-Saxon countries. With regard to ownership structure, Latin countries typically embrace financial holding, cross shareholding, and governmental and family control (Moerland, 1995). As compared to Italy, France enjoys somewhat diverse schemes in terms of ownership; for instance, Italian banks are not allowed to hold securities on behalf of a business, while in France, corporations and their subsidiaries may hold one another's voting rights (De Jong, 1989). France's banking system was initialised in 1981, which resulted in the government taking ownership of a majority of shares in a variety of corporations; however, the privatisation measures implemented in France since that time have served to reduce government ownership in many companies (Weimer and Pape, 1999).

3.10.1. Corporate Governance in Belgium

Belgian firms traditionally adopt a unitary board structure, though a two-tiered system is also allowed (Fleckner and Hopt, 2013; Mallin, 2016). According to Fleckner and Hopt (2013), the ownership structures of Belgian-listed firms are characterised as concentrated in comparison to those of US firms. Belgium's ownership concentration is a result of the presence of individual shareholders and holding companies who hold a large number of shares in various companies; this enables these players to influence management's strategic decisions in the firms that they own. Moreover, family ownership is also present and is often exercised via holding companies. Furthermore, institutional investors have recently cut their investments in Belgian firms; thus, the state exercises ownership only in the short-term and rarely holds equity for long periods (Fleckner and Hopt, 2013).

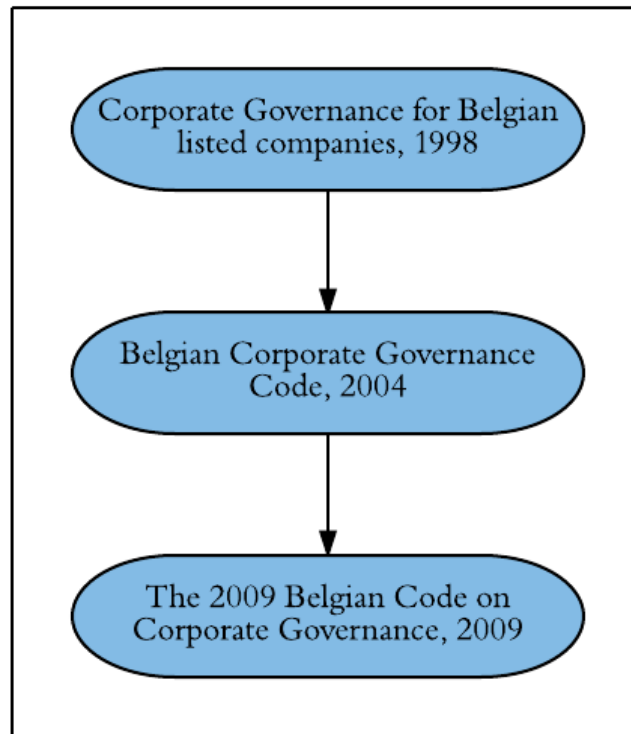
Belgium's first corporate governance code was issued in 1998; this code, entitled *Corporate Governance for Belgian-Listed Companies* (Solomon, 2013), was established by the Belgian Commission on Corporate Governance under the chairmanship of Daniel Cordon¹³. The code contained two sets of recommendations for Belgian-listed firms, though it did not discuss the enforcement of these rules. These recommendations highlighted the role of the corporate board and its key subcommittees and discussed their responsibilities and desired composition. This code further recommended that companies provide information about their members, activities and relationships with dominant shareholders. Moreover, this code suggested that companies should disclose information regarding the subcommittees that were formed to assist the board in fulfilling its duties; additionally, companies should release materials concerning the duties and composition of these committees (Commission on Corporate Governance, 1998). Due to demand for the development of governance guidelines that aligned with European and international recommendations, the Banking, Finance and Insurance Commission, Euronext Brussels and the Federation of Belgian Enterprises formed a committee—the 'Belgian Corporate Governance Committee'—to accomplish this task. The committee developed a new version of the code, titled the *Belgian Corporate Governance Code*, which was published in 2004. As with other issued codes, these guidelines were flexible and applied a voluntary compliance approach. This updated code outlined nine main principles and included recommendations on the adoption of clear governance structures, the function and responsibility of the corporate board, the formation of specialised committees and the disclosure of corporate governance practices (Belgian Corporate Governance Committee, 2004). Following the publication of this update, the Corporate Governance Committee received suggestions and comments from several individuals and institutions in light of the recent financial crisis; therefore, in 2009, the Committee published a new version of the code, entitled

¹³ This code is well known as the Cardon Report (Solomon, 2013).

The 2009 Belgian Code on Corporate Governance. This revision retained the same nine principles, though it included various changes pertaining to the separation of the roles of the CEO, the board chairperson and the corporate board; furthermore, this revision emphasised executive remuneration. It is also important to note that this code provided recommendations regarding female representation on Belgium's corporate boards; while it was recommended that companies consider women when nominating members to their corporate boards, specific targets were not established (Belgian Corporate Governance Committee, 2009). Notably, the chairman of the Belgian Corporate Governance Committee recently announced that another revision of the code will be published in 2017 in order to accommodate new regulations that have been issued since 2009 at the national and European levels (Belgian Corporate Governance Committee, 2017). Figure 3.10 demonstrates the development of Belgium's major corporate governance codes and guidelines.

With regard to gender quota recommendations, Belgium passed legislation in 2011 that was aimed at promoting the increased representation of women on the corporate boards of firms regulated by the capital market. According to this quota legislation, one-third of a firm's board members must be of a gender that is different from that of the other two-thirds; large firms must reach this quota by 2017, while medium and small firms have until 2019 to accomplish this goal (Deloitte, 2015).

Figure 3.10 The development of major corporate governance codes in Belgium.



3.10.2. Corporate Governance in France

The French legal system is based on a model of civil law and provides relatively low levels of protection to minority shareholders (Mallin, 2016). France's corporate governance system adopts an approach that may be best characterised as being closer to the insider than the outsider, as the ownership structures of French firms are controlled by the state, institutional investors and individuals (Mallin, 2016; Solomon, 2013). As far as board structure is concerned, French companies typically utilise a unitary board system, although some may choose to adopt a two-tiered system (Mallin, 2016).

The most important corporate governance codes in France were issued by two French business organisations, the *Association Française des Entreprises Privées* (AFEP) and the *Mouvement des Entreprises de France* (MEDEF). France initially issued two corporate codes of best practice in order to promote the country's corporate governance system: the *Vienot Report I*,

issued in 1995, and the *Vienot Report II*, published in 1999 (see Mallin, 2016; Fleckner and Hopt, 2013).

Following the Enron collapse, another corporate governance code was issued: the *Bouton Report*, named after the chair of the working group, Daniel Bouton, president of the *Société Générale*. The report was published in October of 2002 and consisted of three parts (Mallin, 2016). The first part outlined further improvements to corporate governance practices and highlighted the desired role and characteristics of a corporate board; the second part presented various recommendations aimed at strengthening the independence of statutory auditors; and the third part was allocated to a discussion of financial standards, accounting standards, practices and the means of achieving these benchmarks (Mallin, 2016).

The first segment of the *Bouton Report* advocated that in widely-held companies with no controlling shareholders, half of all corporate board seats should be held by independent directors. The report also recommended that companies establish three key subcommittees: audit, compensation and nomination. The report also maintained that two-thirds of an audit committee's members ought to be independent directors, while the majority of a compensation committee's members should be independent directors; furthermore, the nomination committee should include the chair of the board as a member. The report also highlighted the importance of board evaluation and recommended that a board's independent directors undertake an assessment of its operations, with the assistance of experienced consultants (Bouton, 2002). The report also suggested that such evaluation be performed at least once every three years; additionally, shareholders should be notified of the evaluation outcomes via the company's annual report (Bouton, 2002).

In October of 2003, all three previous reports (*Vienot I*, *Vienot II* and *Bouton*) were consolidated by the AFEP and the MEDEF into a single report, *The Corporate Governance Code of Listed Corporations*. Providing a set of principles of corporate governance based on

the three previous reports, this combined report came to be deemed the most significant set of recommendations concerning corporate governance in France (Fleckner and Hopt, 2013). This code covered many features related to boards of directors, independent directors, board evaluation, meetings of the board and of key subcommittees, director compensation and the formation and actions of key board subcommittees (audit, compensation and nomination) (Fleckner and Hopt, 2013). This code was formulated according to a ‘comply or explain’ approach and thus recommended that companies clarify which recommendations have been adopted. Following the publication of this combined report, the AFEP and the MEDEF issued two reports in 2007 and 2008 concerning the compensation of the executive directors of listed companies.

In December of 2010, the AFEP and the MEDEF published another joint recommendation, *The Corporate Governance Code of Listed Corporations*, concerning women’s representation on corporate boards. This recommendation suggested that French-listed companies attain a specified quota in the subsequent years; for instance, companies were required to achieve a 20% female presence on their boards within three years, with a target of at least 40% female representation within a period of six years either from the date of the recommendation’s issuance or from the first trading date on the regulated market, whichever was later (AFEP and MEDEF, 2010).

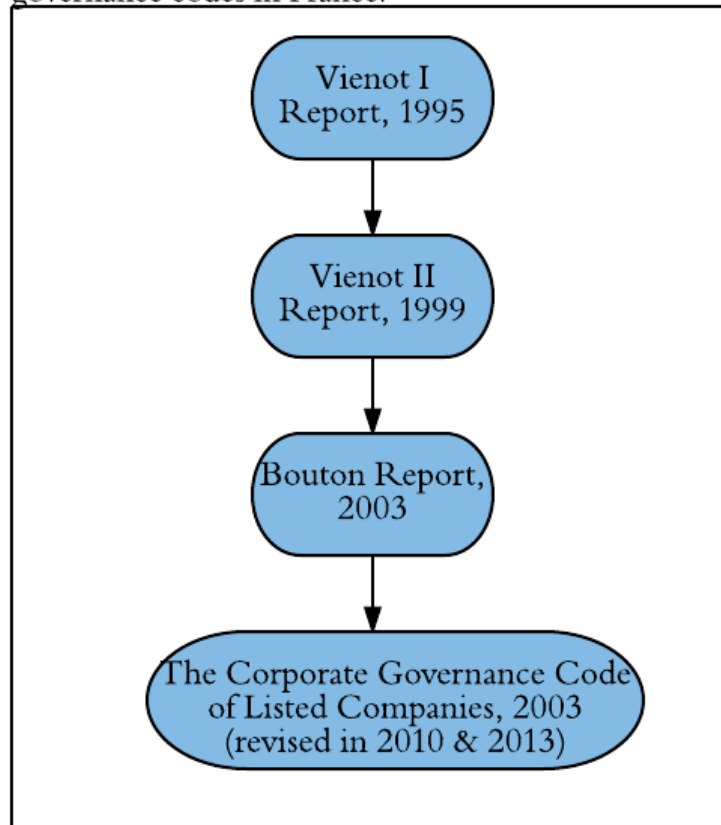
The final amendment of *The Corporate Governance Code of Listed Corporation* was issued in June of 2013. This revised code recommended that companies establish a ‘high committee’ of up to seven members. The main responsibility of this committee would be to coordinate with a board in order to monitor and assess its compliance with the principles put forth in the code. If a company were to fail to adhere to any specific recommendation of the code without providing adequate justification, such action—and an explanation—should be disclosed in the annual report. The amendment also included a strict recommendation regarding the

remuneration of executive directors; the remuneration packages of executive directors were to be presented at the shareholders' annual general meeting (AGM) (AFEP and MEDEF, 2013). Furthermore, the code embraced a reinforced 'comply and explain' approach, thus requesting that companies provide a detailed explanation in the case of noncompliance with the code's recommendations (AFEP and MEDEF, 2013). Figure 3.11 illustrates the development of France's major corporate governance codes and guidelines.

It is also worth noting that France has issued quota legislation regarding gender diversity in an effort to enhance women's representation on French corporate boards. Issued in 2011 and reinforced in 2014, this law stated that both genders must have 40% representation by the beginning of 2017. This quota legislation was applicable to (i) listed firms whose shares are traded in regulated markets and (ii) listed and unlisted companies whose revenues or total assets exceed €50 million and who have retained at least 500 employees for three consecutive years (Deloitte, 2015)¹⁴.

¹⁴ Starting in 2020, this legislation will also apply to firms whose total number of employees exceeds 250 (Deloitte, 2015).

Figure 3.11 The major development of corporate governance codes in France.



3.10.3. Corporate Governance in Italy

Italian firms traditionally adopt a one-tier board structure, although a two-tiered arrangement is also possible. The Italian governance system is distinctive, insofar as it requires the formation of a board of auditors (Mallin, 2016). Italy's corporate governance system falls into the insider system category, as widespread family or cross-company ownership is prevalent (Solomon, 2013)¹⁵. In contrast to other insider corporate governance models—such as that of Germany, for example—banks have no major influence over Italy's non-financial listed firms (Melis and Gaia, 2011). In fact, one of the main concerns in Italy involves the power of blockholders. These blockholders are able to extract the benefits of their control at the expense of small

¹⁵ Roughly two-thirds of Italian-listed firms are family-owned (Bianco et al., 2015).

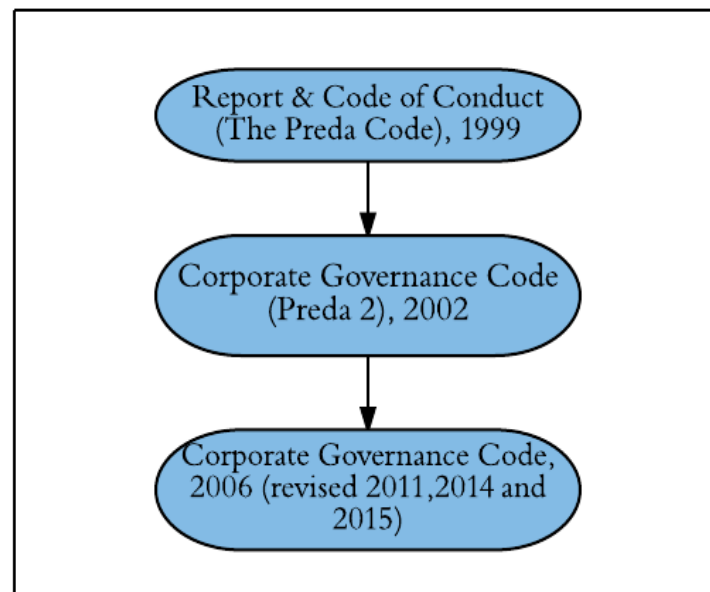
investors, who in Italy enjoy relatively poor protections as compared to those afforded by other Anglo-Saxon governance systems (Mengoli et al., 2009).

Italy's first corporate governance code was initiated by *Borsa Italia* and published in 1999 as the *Preda Code of Conduct*. This code provided recommendations concerning several aspects of governance, including the composition of corporate boards, the establishment of key subcommittees, the independence of board members and the role of the CEO and board chair (Mallin, 2016). This report presented a voluntary approach and required listed firms to disclose their degree of compliance. In 2002, a second edition of the code was issued. *Preda 2* covered a wide range of corporate governance issues, including the role and composition of corporate boards, the independence of directors and the chairman of the board, the information to be provided to the corporate board, the release of confidential information, the remuneration of directors, internal controls, transactions with other parties, relations between institutional investors and other shareholders, shareholder meetings and the membership of boards of auditors (Mallin, 2016).

In 2006, aiming to take into account changes to international corporate governance practices, *Borsa Italiana* published a new corporate governance code to replace those that were issued in 1999 and 2002 (Borsa Italia, 2006). According to Mallin (2016), this version contained content that was similar to that of the previous codes, though it highlighted new recommendations related to external directorship limits, a board's annual evaluation practices, the introduction of a lead independent director, internal control of the firm and the promotion of shareholder activism via the exercise of shareholder rights. Various revisions to this code were made in 2011, 2014 and 2015, with a particular emphasis placed on remuneration policies (Mallin, 2016). Figure 3.12 demonstrates the development of Italy's major corporate governance codes and guidelines.

As far as gender diversity is concerned, Italy mandated a gender quota for listed firms in 2011. The regulation, which came into effect in 2012, required that one-third (or one-fifth during the first term) of board seats be held by the less represented gender (Bianco et al., 2015).

Figure 3.12 The Major development of corporate governance codes in Italy.



3.10.4. Corporate Governance in the Netherlands

In the Netherlands, the corporate governance system adopts a two-tiered board system (Mallin, 2016). The corporate governance system of this country allows employees, through the works of a council, to be involved in the appointment processes of the supervisory board (Fleckner and Hopt, 2013). As compared to that of other European countries, ownership concentration is considered to be the lowest, as more than 70% of the country's total market capital was owned by overseas investors in 2007 (Fleckner and Hopt 2013).

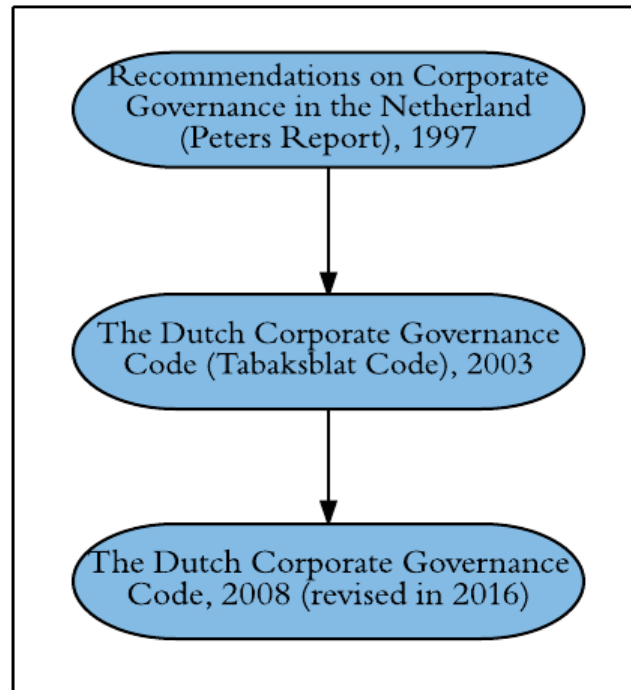
The first report on corporate governance in the Netherlands was published in 1997 by the Committee on Corporate Governance. This report, the *Recommendations on Corporate Governance in the Netherlands*, was also known as the Peters Report (Solomon, 2013). The

Peters Report included some 40 recommendations that highlighted several main areas of Dutch corporate governance, including the composition, duties and remuneration of both the supervisory and management boards (Corporate Governance Committee, 1997). Following this code, and in an attempt to enhance and inspire transparency and to increase the accountability of listed firms in the Netherlands (Akkermans et al., 2007), the Corporate Governance Committee, which was drawn from several organisations in the Netherlands,¹⁶ developed another code in 2003 entitled the *Dutch Corporate Governance Code*, commonly referred to as the Tabaksblat Code. This code was divided into five sections, which concerned (i) compliance with and enforcement of the code, (ii) management boards, (iii) supervisory boards, (iv) shareholders and the general meeting of shareholders and (v) the auditing of financial reporting (Corporate Governance Committee, 2003). In 2008, the code was revised by the Corporate Governance Committee based on numerous recommendations (this revision utilised the same name, *The Dutch Corporate Governance Code*). It is important to note that this revision called on companies to consider board members with respect to age and gender diversity when making new appointments to supervisory boards (Corporate Governance Committee, 2008). Another revision to this code was conducted in 2016 in an effort to reflect legislative changes made since 2008. Figure 3.13 demonstrates the development of the major corporate governance codes and guidelines of the Netherlands.

With regard to quotas for female representation, the Dutch Management and Supervision Act provided a non-mandatory gender diversity quota in 2013, which applied to both listed and non-listed firms. According to this act, supervisory and management boards were expected to be comprised of a minimum of 30% of each gender by 2016, with the outstanding 40% to be determined by the company (Deloitte, 2015).

¹⁶ Including Euronext Amsterdam, the Netherlands Centre of Executive and Supervisory Directors, the Foundation for Corporate Governance Research for Pension Funds, the Association of Stockholders, the Association of Securities-Issuing Companies and the Confederation of Netherlands Industry and Employers.

Figure 3.13 The development of major corporate governance codes in Netherlands.



3.10.5. Corporate Governance in Spain

The legal system of Spain is based on civil law, and the country has a relatively small number of firms as compared to the US and the UK (Fleckner and Hopt 2013). Additionally, the Spanish governance system adopts a unitary board structure (Mallin, 2016). According to Fleckner and Hopt (2013), the ownership structure of Spanish-listed firms is highly concentrated and controlled by non-financial companies, financial institutions and family owners.

The first self-regulation recommendation on corporate governance in Spain was published in 1996 by the Managers' Circle of Madrid and the Association of Spanish Businessmen. This report, *The Report of the Managers' Circle of Madrid*, recommended that several ideas and proposals be adopted in order to allow corporate boards to function more effectively (Lopez-Iturriaga and Tejerina-Gaite 2014). In 1997, the Ministers Council of the Spanish government established another commission in order to develop an ethical code that the corporate boards

of listed firms were to voluntarily follow (Lopez-Iturriaga and Tejerina-Gaite 2014). In 1998, the commission issued its report, known as the *Olivencia Report*; this report considered the ownership structure of Spanish firms and presented various recommendations concerning the protection of minority shareholders. Overall, the recommendations of the Olivencia Report appeared similar to those of the Cadbury Report published in the UK (Lopez-Iturriaga and Tejerina-Gaite 2014).

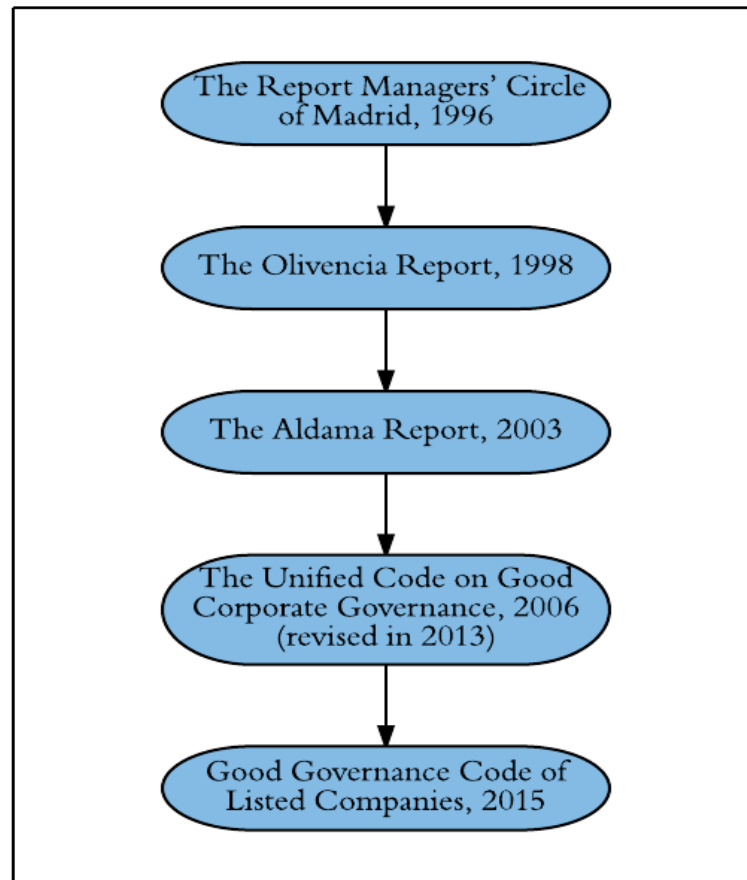
With 23 recommendations in total, the Olivencia Report highlighted the importance of corporate board composition (arguing that non-executive directors should be in the majority) and the establishment of key subcommittees (such as audit, compensation and nomination committees) to assist the board in fulfilling its duties. The report also stated that a board should include between five and fifteen directors; it further suggested an age limit with regard to corporate board directors (Lopez-Iturriaga and Tejerina-Gaite 2014). Roughly two years after the publication of the *Olivencia Report*, the Council of Ministers approved the establishment of another commission, formed to focus specifically on the enhancement of transparency and security in Spanish capital markets (Lopez-Iturriaga and Tejerina-Gaite 2014). Issued in 2003, the resulting *Aldama Report* was largely in line with its predecessor, though it placed a particular emphasis on the obligation of companies to provide full records of their corporate governance systems, which were to be disclosed annually. Furthermore, as indicated by Lopez-Iturriaga and Tejerina-Gaite (2014), both reports reflected certain issues that were of concern to the Spanish legislature at the time of their issuance. Following the publication of the Aldama Report, the Ministry of Economics called on the National Securities Market Commission (CNMV) to form a template that listed firms could use as a benchmark when reporting compliance with corporate governance recommendations (up to 2003). To this end, the government established another group to assist the CNMV and also to consider the principles issued by the Organisation for Economic Cooperation and Development (OECD), the

recommendations of the European Commission and the Recommendations on Corporate Governance for Banking Organisations, which were approved by the Basel Committee on Banking Supervision.

The group completed its work in May of 2006 and published a report entitled *The Unified Code on Good Corporate Governance*, which consisted of 58 voluntary recommendations for Spanish-listed firms. This code primarily focused on the composition of corporate boards (size and directors' independence), annual disclosures of board remuneration policies and the auditing of financial statements. The code also considered various new topics, such as the promotion of gender diversity on corporate boards and their key subcommittees and the promotion of transparency with respect to board compensation. Furthermore, the code recommended that firms justify their level of compliance within their annual reports (Lopez-Iturriaga and Tejerina-Gaite 2014). The code was later amended in 2013, though Spain's most recent corporate governance code, issued in 2015, contained several changes to the updated (2013) Unified Code, including recommendations concerning corporate social responsibility (CNMV, 2015). Figure 3.14 illustrates the development of Spain's major corporate governance codes and guidelines.

Moreover, in 2007, Spain passed a voluntary law related to the representation of women on the corporate boards of its listed firms. This regulation required that each gender enjoy at least 40% representation by 2015 (Deloitte, 2015).

Figure 3.14 The major development of corporate governance codes in Spain.



3.11. The Nordic Governance Model

Distinct from the Anglo-Saxon and continental (German and Latin) models in various ways, the Nordic corporate governance system is essentially regarded as a modified version of the German model, with a strong emphasis placed on aligning the interests of the management team and the owners of a firm (Piekkari et al., 2015). Fleckner and Hopt (2013) argued that Nordic (Scandinavian) countries have two special aspects that should be highlighted. First, Nordic firms all regularly update company statutes to include modern corporate governance practices, which are regulated via ‘comply or explain’ codes in other countries. Second, Nordic capital markets have become increasingly integrated. A high number of cross-border mergers in Nordic countries have led several companies to be listed in multiple stock exchanges. This also leads to a kind of harmonisation with the various rules and requirements of stock exchange

listing practices in these countries. Additionally, as in the German model, the corporate governance systems of Nordic countries (excluding Finland) allow employees to be represented on corporate boards. This implies that these countries also consider it important to protect the rights of other stakeholders of a company.

3.11.1. Corporate Governance in Denmark

The corporate governance system in Denmark falls somewhere between an insider and an outsider system; controlling shareholders exist to some extent, and shareholder protections are enshrined in law via the presence of varying degrees of voting rights for different classes of shares (Solomon, 2013). Denmark's ownership structure is quite different from that of the US and the UK, as foundation ownership structures are common¹⁷ (Mallin, 2016). In fact, roughly 19 of the largest 100 firms in Denmark enjoy foundation ownership and control (Solomon, 2013). Additionally, there is a substantial amount of ownership by institutional investors in Denmark; such systems represent approximately 35% of the Danish market capitalisation, thus indicating a significant level of corporate governance for institutional investors (Mallin, 2016). Moreover, the dual board structure is dominant and, as provided for in the Danish Companies Act, the majority of supervisory board members are elected by company shareholders during the AGM (Fleckner and Hopt, 2013). Furthermore, the employees of a company also have the opportunity to elect supervisory board members; this practice applies to all companies whose number of employees exceeds 35. This implies that Denmark's corporate governance system was originally created to protect a wide base of stakeholders, to include employees, society, and creditors who are not shareholders (Rose and Mejer, 2003). Moreover, due to the predominance of foundation ownership, companies in the Danish system are not subject to hostile takeover activities, as are firms located in countries that employ the Anglo-Saxon model

¹⁷ A foundation is a legal entity wherein no owners have been established to control a large number of shares in a particular company; shares are often donated by the company or family founder (Mallin, 2016; Solomon, 2013).

(Solomon, 2013). However, the combination of recent attempts to improve corporate governance practices in Denmark and the integration of global capital markets has pushed the country's corporate governance system towards a more outside-oriented model (Solomon, 2013).

Turning to an examination of the evolution of corporate governance in Denmark, the Nørby Committee (established by the Copenhagen Stock Exchange) published its first guidelines on corporate governance, *The Nørby Committee's Report on Corporate Governance in Denmark*, in 2001 (Mallin, 2016). These voluntary recommendations were divided into seven main sections, which concerned: the role of shareholders and the importance of their engagement with the managers of a firm, the importance and role of stakeholders within a company, openness and transparency, the responsibilities and tasks of a corporate board, the composition of a corporate board, the compensation of directors and managers of a company and risk management procedures (Mallin, 2016). The publication of these guidelines in 2001 created the basis for further development in Danish corporate governance. In 2002, an independent corporate governance committee¹⁸ was created by the Copenhagen Stock Exchange to further develop corporate governance guidelines for Danish-listed firms and to consider any needed revisions. According to Mallin (2016), this committee was formed because of the influence of international initiatives such as the US Sarbanes-Oxley Act (2002), the UK Combined Code (2003) and the EU Action Plan (2003), which called for the development of company laws and corporate governance in EU countries. In December of 2003, the committee issued its report, known as the Nørby Report (Mallin, 2016). A subsequent review of the code was conducted by the Copenhagen Stock Exchange Committee on Corporate Governance, which resulted in the issuance of the *Revised Recommendations for Corporate Governance in Denmark*. This revision primarily focused on recommendations related to disclosure requirements and

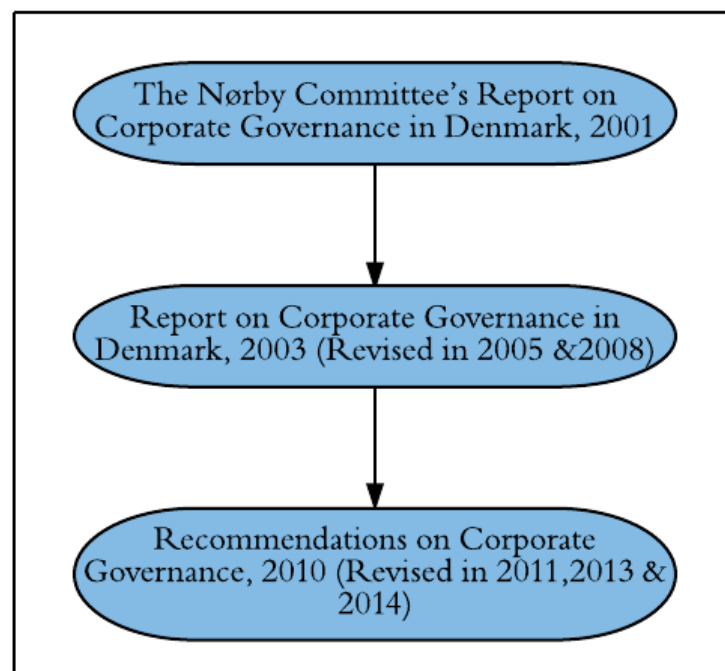
¹⁸ Known as the Copenhagen Stock Exchange Committee on Corporate Governance.

compelled listed firms in Denmark to voluntarily disclose in their annual reports how they had addressed these recommendations (Mallin, 2016). Following this update, two revisions were published in 2008. The first revision was issued in February and concerned the remuneration of supervisory and executive directors, requiring that the remuneration policy of a firm be disclosed on the company website and in its annual report. The second revision was released in December and amended two aspects of its predecessor. First, attempting to address issues of transparency, the revision called on firms to disclose the details of their non-financial information, including the gender and age of members who held positions on a company's supervisory and management boards (Mallin, 2016). Second, in an effort to tackle the composition of supervisory boards, the revision recommended that the diversity (in terms of gender and age) of a board should be reviewed regularly (Mallin, 2016).

According to Mallin (2016), the Committee on Corporate Governance revised its recommendations on corporate governance in 2010; these revisions were made in light of the Companies Act of 2009, new rules established by the Financial Statements Act and the Act on Approved Auditors and Audit Firms and because of various EU Commission recommendations. The Code was titled the *Recommendations on Corporate Governance*, and included amendments related to the remuneration of directors sitting on supervisory and management boards; it also included recommendations aimed at motivating firms to become more engaged with their social responsibilities. This same code was revised in 2011, 2013, and 2014, with the last revision including 47 recommendations that highlighted five main governance topics, which were: a company's communication and interaction with its investors and other stakeholders, the tasks and responsibilities of a board of directors, the composition and organisation of a board of directors, the remuneration of management, and financial reporting, risk management and auditing (see Mallin, 2016). Figure 3.15 demonstrates the development of Denmark's major corporate governance codes and guidelines.

In 2013, Denmark issued legislation requiring firms to promote gender equality within their corporate boards (Deloitte, 2015). According to this legislation, equality goals can be achieved if every company sets its own target and works to ensure that gender equality is taken into consideration. This legislation was applicable to all listed companies, large non-listed companies and state-owned companies (Deloitte, 2015).

Figure 3.15 The development of major corporate governance codes in Denmark.



3.11.2. Corporate Governance in Finland

Finish-listed firms mainly adopt a one-tier board system, as per Finish governance recommendations; however, two-tiered boards also exist and accounted for roughly 22.5% of all listed firms in Finland in 2000 (see Liljeblom and Löflund, 2006). The ownership structure of Finish firms is concentrated, with state ownership being a significant factor (Liljeblom and Löflund, 2006).

With regard to the corporate governance history of Finland, the first corporate governance code was issued in 2003 as a collaboration between the Central Chamber of Commerce, Hex Plc

(currently NASDAQ OMX Helsinki Ltd) and the Confederation of Finnish Industry and Employers (currently the Confederation of Finnish Industries) (see Solomon, 2013). This code, titled the *Corporate Governance Recommendations for Listed Companies*, consisted of 57 voluntary recommendations that covered 12 aspects of governance, including the role and composition of corporate boards, communication and disclosure practices, the compensation of directors and external auditing systems. Five years later¹⁹, the Securities Market Association²⁰ was formed in an effort to update the existing code; the resulting *Finnish Corporate Governance Code* was published in 2008 and consisted of 52 voluntary recommendations that were largely similar to those published in 2003 (The Securities Market Association, 2008). Furthermore, it is worth noting that this version of the code called for board diversity in terms of gender, arguing that in listed firms, both genders should be represented on corporate boards.

In 2009, due to the freshness of the recent financial crisis as well as a need to develop regulations related to the compensation of corporate board members, the Securities Market Association appointed a committee to revise Finnish corporate governance recommendations (The Securities Market Association, 2010). The committee issued its revised code in 2010, which retained many of the same recommendations that were issued in 2008. The main aim of this code was to meet international governance recommendations in order to attract foreign investors to the Finnish market (The Securities Market Association, 2010). Following this revision, the Finnish code was again revised in 2015 in order to accommodate national and international regulatory frameworks that had been developed over the previous five years. This code included 28 recommendations that covered several issues related to corporate governance

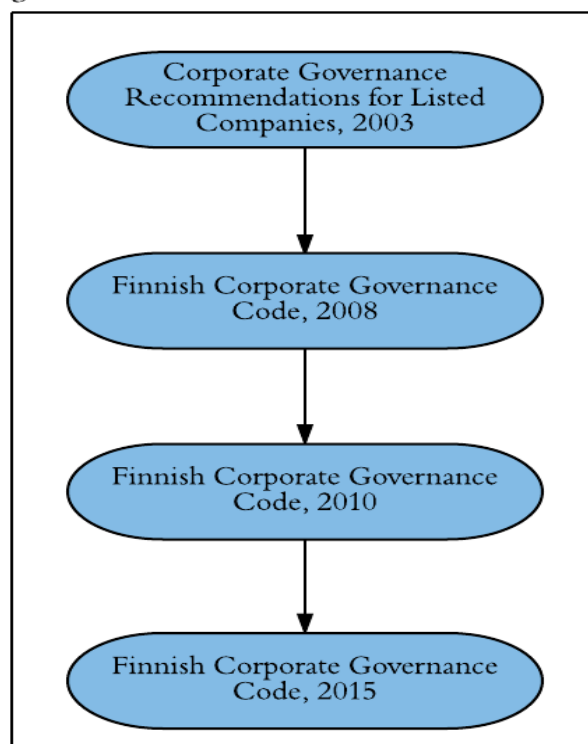
¹⁹ Another code was issued in 2006 for non-listed firms. That code was issued by a working group that was formed by the Central Chamber of Commerce of Finland (Finland Central Chamber of Commerce, 2006).

²⁰ Established by the Confederation of Finnish Industries EK, the Central Chamber of Commerce of Finland and NASDAQ OMX Helsinki Ltd.

(The Securities Market Association, 2015). Figure 3.16 demonstrates the development of the major corporate governance codes and guidelines of Finland.

In Finland, state-owned firms are required by law to consider gender equality when comprising their corporate boards, unless there are adequate reasons for acting otherwise (Deloitte, 2015).

Figure 3.16 The development of major corporate governance codes in Finland



3.11.3. Corporate Governance in Norway

With regard to an examination of Norway's corporate governance system, Rasmussen and Huse (2011) argued that several important aspects must be understood, such as the history of the country and its major players. This mainly refers to the fact that Norway has relatively few large companies that represent a large percentage of the country's market capitalisation; similarly, Norway has relatively few very wealthy people. Furthermore, the government and public organisations are seen as important actors in the development of the country's corporate governance system. The government of Norway is considered the largest single shareholder,

as it holds roughly 40% of the total number of shares that are traded in the country (Rasmussen and Huse, 2011).

Norway also follows a codetermination tradition in corporate governance whereby employees are allowed to elect representatives to serve on corporate boards (Rasmussen and Huse, 2011). These employee-elected directors do not represent workers' unions and are not elected by such unions. Thus, the Norwegian governance system differs from the Swedish model, wherein employee representative directors are elected by unions, and the German model, whereby unions can elect board members who are not employees (Rasmussen and Huse, 2011).

Turning to the development of corporate governance in Norway, the first corporate governance code, the *Norwegian Code of Practice for Corporate Governance*, was published in 2004 by the Norwegian Corporate Governance Board (NCGB)²¹. This code was based on a provisional code that was published in 2003 and was issued following consultation and suggestions from various companies and interested parties in Norway (NCGB, 2004). Containing 14 voluntary recommendations regarding several aspects of governance, this code aimed to ensure that all listed firms in Norway implement healthy governance practices by outlining the potential roles of shareholders, corporate boards and executive teams (NCGB, 2004). Additionally, the code sought to guarantee that companies continue to create value for all stakeholders (NCGB, 2004). These recommendations were largely related to the implementation and reporting of governance practices, the role and composition of corporate boards, nomination processes, directors' compensation packages and general meetings. Since the publication of the first Norwegian code in 2004, there have been eight additional publications concerning corporate governance best practices, the most recent of which was issued in 2014 (NCGB, 2014).

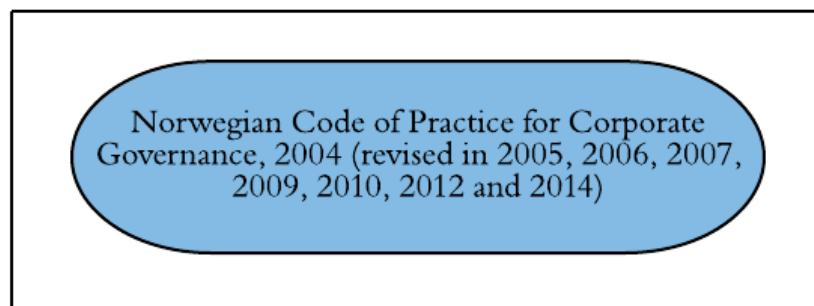
²¹ The Norwegian Corporate Governance Board consists of nine organisations: the Norwegian Shareholders Association, the Norwegian Institute of Public Accountants, the Institutional Investor Forum, the Norwegian Financial Services Association, the Norwegian Society of Financial Analysts, the Confederation of Norwegian Business and Industry, the Norwegian Association of Private Pension Funds, the Oslo Børs and the Norwegian Mutual Fund Association (Fleckner and Hopt, 2013).

Following the issuance of the first code, the NCGB published revisions in 2005 to accommodate recommendations made by the EU to enhance the quality of director remuneration schemes (NCGB, 2005). Further revision of the code took place in 2006 when the NCGB introduced a number of changes to various recommendations related to risk management and internal controls, take-over procedures, director nomination policies and external auditor selection practices (NCGB, 2006). In the following year, the NCGB again updated the code to bring it in line with recent legislation and regulations. These changes contained various clarifications related to specific recommendations and dealt with the implementation and reporting of governance practices, general meetings, the composition of a corporate board and its key subcommittees and shareholder communications (NCGB, 2007). The NCGB revised the code again in 2009 in light of consultations conducted in 2008 and changes to Norwegian legislation made earlier that year. The resulting code retained the same name and included various changes related to voting policies and the composition of audit committees (NCGB, 2009). The NCGB circulated another proposal in mid-2010 aimed at altering various aspects of the code. Subsequently, a new revision was published; this revision recommended that companies provide guidelines concerning the duties of a nomination committee and concerning a company's corporate social responsibilities and also suggested that an absolute limit be identified with respect to the performance-related remuneration of corporate directors (NCGB, 2010). In 2011, the NCGB was compelled to make minor adjustments to the code, and thus another edition was issued in 2012. This version included various new rules regarding the independence of corporate boards and emphasised the creation of audit committees in firms that are not Norwegian-listed public companies; this revision also underscored the importance of reporting on governance practices in a company's annual reports (NCGB, 2012). The most recent revision to this code was conducted in 2014; major changes included new procedures of dividend payment approval and calls for shareholder engagement

with the nomination committee in the selection of new candidates to a corporate board (NCGB, 2014). It is worth noting that the name of Norway's corporate governance code has remained the same since its first publication until its latest revision. Figure 3.17 demonstrates the development of Norway's major corporate governance codes guidelines.

Notably, in 2005, Norway became the first country to legally require the presence of female directors on corporate boards. The legislation mandating this action specified that 40% of a company's board members should be female. Listed firms were given until the beginning of 2008 to comply with this legislation; if a company did not comply, it would be subject to dissolution by court order (Deloitte, 2015). By the end of 2015, all Norwegian-listed firms were in compliance with this requirement (Deloitte, 2015).

Figure 3.17 The development of major corporate governance codes in Norway



3.11.4. Corporate Governance in Sweden

Sweden's corporate governance system somewhat resembles the Anglo-Saxon model in terms of its transparency requirements (Poulsen et al., 2010); nevertheless, Solomon (2013) argued that Sweden has a corporate governance system that is best characterised as an insider-oriented model. In Sweden, corporations are traditionally under the control of a small group of shareholders; this is achieved via pyramidal ownership and dual-class ownership (in fact, family ownership is common). Furthermore, the Swedish system also employs a unitary system of board structuring and is considered to be stakeholder-oriented (Mallin, 2016; Solomon,

2013). Thus, employee representation at the board level is highly encouraged. As mentioned in the previous section, in Sweden—unlike in Norway—employee representatives are elected by unions (Rasmussen and Huse, 2011).

Regarding the development of Sweden's system of corporate governance, it was in 2001 that the Swedish Shareholders Association published its first set of corporate governance guidelines, titled the 'Corporate Governance Policy'. This code featured eight guidelines that were related to various aspects of governance; the code aimed to enhance confidence among investors in the Swedish stock market, improve transparency and increase confidence in the corporate boards and management teams of nationally listed companies (The Swedish Shareholders Association, 2001). Three years later, the Swedish government established a committee called the Code Group²² that was tasked with proposing corporate governance codes to be circulated to Sweden's various organisations for their feedback and suggestions. The proposed code was circulated in April 2004 after taking into consideration the opinions and comments of several concerned organisations; the final version of the code, the *Swedish Code of Corporate Governance: A Proposal by the Code Group*, was published in December of 2004. This code was based on the 'comply or explain' approach and discussed several issues relating to corporate boards and the responsibilities of shareholders (The Swedish Code Group, 2004). Following the issuance of this code in 2004, which was applicable to Sweden's largest listed firms²³, the code was revised so that it could be applied to all Swedish-listed firms. The new code was revised by the Swedish Corporate Governance Board²⁴ and published in 2008 (Swedish Corporate Governance Board, 2008). In 2010, the Swedish Corporate Governance

²² The Code Group is comprised of three members from the Commission on Business Confidence and six members from the corporate sector; it is currently chaired by Erik Åsbrink, a former Finance Minister and present chair of the Commission on Business Confidence.

²³ Whose capital exceeds 3 billion Sweden Krona.

²⁴ This board consists of a chair, a deputy chair and a maximum of 12 members who represent the following three categories: (i) institutional, private and state ownership, (ii) the Swedish and international capital markets and (iii) executive management and directorship (Swedish Corporate Governance Board, 2017).

Code was again modified to include new recommendations regarding management compensation (based on suggestions from the EU), board independence, audit committees and the release of required information (Swedish Corporate Governance Board, 2010). The latest version of the code was published in 2015 following comprehensive revisions by the Swedish Corporate Governance Board in 2013. The purpose of this revision was to accommodate recent recommendations made by the European Commissions concerning corporate governance reporting, shareholder rights, non-financial information release and regulations related to auditors and auditing procedures (Swedish Corporate Governance Board, 2015). Figure 3.18 illustrates the development of Sweden's major corporate governance codes and guidelines.

With regard to the promotion of gender diversity on the boards of listed firms in Finland, Finnish legislation recommends that both genders be equally represented on the boards of state-owned firms (Deloitte, 2015).

Figure 3.18 The development of major corporate governance codes in Sweden

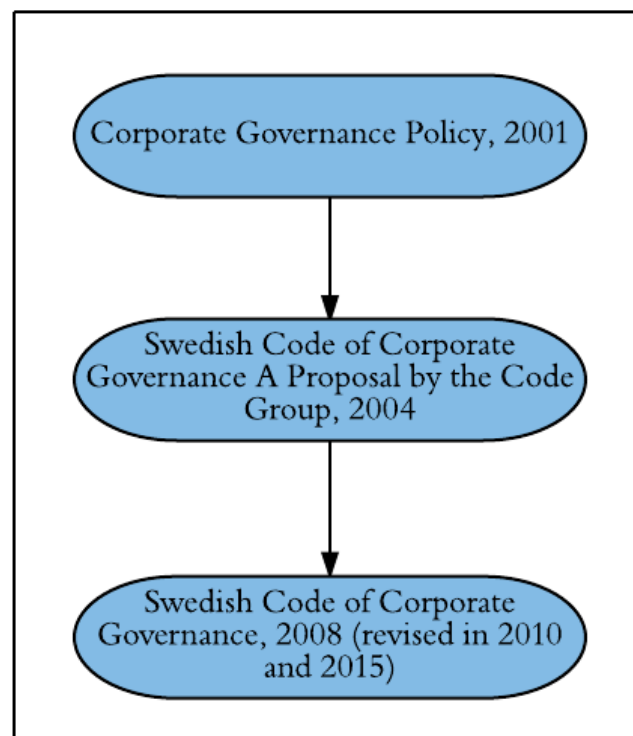


Table 3.1 below provides a summary of the main corporate governance features of each country included in the sample. The table mainly highlights several aspects of corporate governance features in the sample countries, including the first corporate governance code issued in each country, the issuer name, the year of issuance, and board structure (unitary or two-tier). As far as the corporate governance codes are concerned, it is clear that the financial scandals and financial crisis were the causes underlying corporate governance diffusion in many countries. As described by Cuomo et al. (2016), two main waves of corporate governance codes diffusion occurred throughout the world. The first wave began in the late 1990s in parallel with the Asian and Russian stock crises and with the collapse of high-profile firms, such as Enron, WorldCom, and Parmalat (Cuomo et al., 2016). The second wave of corporate governance codes diffusion began after the financial crisis of 2007–2008 (Cuomo et al., 2016). Table 3.1 also illustrates the issuer of the first corporate governance code in each country. According to Aguilera and Cuervo-Cazurra (2004), the issuers of corporate governance codes across the globe included the stock exchange, governments, directors' associations, managers' associations, professional associations, and investors' associations.

Further, Table 3.1 reveals that common law countries issued their corporate governance codes earlier than their civil law counterparts. This finding is consistent with Zattoni and Cuomo (2008), who reported that civil law countries adopted codes later, issued fewer codes, and involved more ambiguous and lenient recommendations as compared to common law countries. Finally, Table 3.1 reports the structure of the corporate boards (unitary or two-tier) in the sample countries. It is apparent that the unitary board structure is dominant in Australia, Canada, India, Ireland, the UK, and the US, whereas the two-tier board structure is dominant in countries including Denmark and the Netherlands. In addition, both structures are common in other countries: Belgium, Finland, France, Italy, and Switzerland (Mallin, 2016). Despite the structural differences between the two structures (unitary and two-tier), they both share

some common aspects (Krivogorsky, 2016). For instance, both the unitary board and the dual board (two-tier structure) are both responsible for appointing the members of the managerial body, with the unitary board delegating authority to the group of managers and the dual board delegating authority to the board of management (Mallin, 2016). In addition, both structures are also responsible for maintaining financial reporting, maintaining control systems and ensuring that the control systems are operating properly, as well as ensuring the compliance with the law (Mallin, 2016). While the shareholders typically elect the members of both the unitary board and the supervisory board (in the two-tier structure), employees may also elect members of the supervisory board in some countries, such as Germany (Mallin, 2016).

Table 3.2 summarises the various national statistics and regulations regarding gender diversity. The table shows the share of women sitting on boards as of 2015 in the sample countries, the quota regulation in place (hard law), and the self-regulation gender quota in place (soft law). In terms of the share of women on corporate boards, Table 3.2 shows that countries with the highest share of women serving on corporate boards are Norway (36.7%), France (29.9%), Sweden (24.4%), Italy (22.3%), and Finland (22.1%). Conversely, the countries with the lowest share of women serving on corporate boards are India (7.7%), Switzerland (10.0%), the United States (12.2%), Spain (12.5%), and Canada (13.1%).

Table 3.2 also demonstrates that the highest percentages of female directors are found in countries that initiated legislation of board gender quotas, whilst the lowest percentage is most apparent in countries that have only initiated self-regulated gender quotas. According to Terjesen et al. (2015a), several institutional factors may influence the enactment of gender quota legislation. These include the country's family policy welfare provision for females in the labour market, left-leaning government coalitions, and the legacy of initiatives to achieve gender equality. In addition, Terjesen and Singh (2008) found that women's representation on corporate boards may be shaped by social, political and economic structures in a particular

country. Grosvold and Brammer (2011) also demonstrated that the culture and the legal system are the main determinants of the presence of women on corporate boards in each country.

Debate is ongoing with regard to adopting corporate board gender quota legislation (Ferreira, 2015). The primary debate relates to the costs and benefits of imposing regulations, as firms affected by gender quota legislation are forced to hire female directors to comply with the law, whilst there is no presumption that the newly-appointed directors will be as qualified as the incumbents. For instance, Ahern and Dittmar (2012) pointed out that, when a new law took effect in 2003 in Norway, it imposed a 40% quota of female directors for Norwegian firms, whilst, at the time, only 9% of directors were female. Their study found that, upon the announcement of the new law in Norway, a significant drop in stock prices occurred, along with a large decline in performance measures (Tobin's Q) in the ensuing years. In addition, the findings revealed that the imposed quota led to younger and less experienced directors joining the board, which contributed to increases in leverage and acquisitions and deterioration of operating performance. Further, Bøhren and Staubo (2014) found that, as a consequence of the Norwegian law mandating 40% female board representation, half of firms chose to exit into an organisational form that was not subject to the law, as the regulation shrank the pool of competent directors and reduced shareholder value.

Table 3.1 General Corporate Governance Features of the Sample Countries

SN	Country	First Code Issued	Issuer	Year of issuance	Board Structure
Civil Law Countries					
1	Belgium	Corporate Governance for Belgian-Listed Companies.	The Belgian Commission on Corporate Governance.	1998	Unitary*
2	Denmark	Nørby Committee's Report on Corporate Governance in Denmark.	The Nørby Committee.	2000	Two-Tier
3	Finland	Corporate Governance Recommendations for Listed Companies.	Hex plc, the Central Chamber of Commerce of Finland and the Confederation of Finnish Industry and Employers.	2003	Unitary*
4	France	Vienot Report I.	AFEP and MEDEF.	1995	Unitary*
5	Italy	The Preda Code of Conduct.	Italia Borsa.	1999	Unitary*
6	The Netherlands	Peters Report.	The Corporate Governance Committee.	1997	Two-Tier
7	Norway	The Norwegian Code of Practice for Corporate Governance.	The Norwegian Corporate Governance Board.	2004	Unitary
8	Spain	The Report Managers' Circle of Madrid.	The Managers' Circle of Madrid and the Association of Spanish Businessmen.	1996	Unitary
9	Sweden	Corporate Governance Policy.	The Swedish Shareholders Association.	2001	Unitary
10	Switzerland	Swiss Code of Best Practice for Corporate Governance.	The economiesuisse.	2002	Unitary*
Common Law Countries					
11	Australia	The Bosch Report.	The Business Council, the Australian Stock Exchange, the Australian Institute of Company Directors, and the professional accounting bodies.	1995	Unitary
12	Canada	The Dey Report.	The Toronto Stock Exchange.	1994	Unitary
13	India	Desirable Corporate Governance in India: A Code.	The Confederation of Indian Industry.	1998	Unitary
14	Ireland	Corporate Governance, Share Options and Other Incentive Schemes.	The Irish Association of Investment Managers.	1999	Unitary
15	The United Kingdom	The Cadbury Report.	The Financial Reporting Council.	1992	Unitary
16	The United States	The Role and Composition of the Board of Directors of the Large Publicly Owned Corporation.	The Business Roundtable.	1978	Unitary
*Other structures also available.					

Table 3.2 National Statistics and Regulations on Gender Diversity

SN	Country	Share of Women on Boards*	Quota Regulations in Place	Other National Measures in Place (Self-Regulation)
Civil Law Countries				
1	Belgium	18.3%	By 2017 for large listed companies and by 2019 for listed SMEs, 33% of executives and non-executives must be women.	The Corporate Governance Code of 2009 recommends that the composition of a board be determined on the basis of gender diversity.
2	Denmark	21.8%	Legislation passed in Denmark in 2013 requires that all listed companies, large non-listed companies and state-owned companies consider the gender equality of their corporate boards. Specific quotas are not stated.	No
3	Finland	22.1%	State-owned firms are required by law to consider the gender equality of their corporate boards. Specific quotas are not stated.	No
4	France	29.9%	There must be 40% representation of both genders by January of 2017; this applies to listed firms in regulated markets, firms whose revenues or total assets exceed 50 million and firms whose total number of employees exceeds 500 for three consecutive years. For firms with 250 employees, this legislation will be applicable in 2020.	The Corporate Governance Code for Listed Firms, published in 2010, recommends that listed firms have 20% female representation by 2013 and 40% by 2016.
5	Italy	22.3%	By 2015, listed companies and state-owned companies must achieve 33% representation. Applicable to management boards and supervisory boards (i.e., executives and non-executives).	No
6	The Netherlands	17.3%	A target of 30% representation for the executive boards and supervisory boards of large companies is mandated; this target is enforced according to a 'comply or explain' mechanism. No sanctions are in place. Measure is to expire in 2016.	Diversity clauses in the Dutch Corporate Governance Code of 2008 recommend that the nomination of female directors must be considered when making appointments to a supervisory board.
7	Norway	36.7%	By the beginning of 2008, 40% of a corporate board's seats should be allocated to female directors; applicable to all listed firms.	No
8	Spain	12.5%	By 2015, state-owned companies with 250 or more employees should achieve 40% representation for both executives and non-executives. No sanctions are in place, thus this policy is rather like a recommendation in nature.	The Corporate Governance Code of 2006 recommends adequate gender diversity on corporate boards (for all board members, both executives and non-executives).
9	Sweden	24.4%	State-owned firms are required by law to consider the gender equality of their corporate boards. A specific quota is not stated.	No
10	Switzerland	10.0%	No	The Swiss Code of Best Practice for Corporate Governance, issued in 2014, recommends that corporate boards be comprised of members of both genders.

Table 3.2 Continued

Common Law Countries				
SN	Country	Share of Women on Boards*	Quota Regulations in Place	Other National Measures in Place (Self-Regulation)
11	Australia	15.1%	No	The Corporate Governance Principles and Recommendations, issued in 2010, recommend that listed firms annually disclose the proportion of women on their boards and in management positions.
12	Canada	13.1%	The province of Quebec in Canada issued a quota whereby 50% of board member positions should be occupied by female directors; this quota applies to state-owned firms, and full compliance is expected by 2011.	The Canadian Securities Administration requires firms to disclose several aspects of gender diversity, including firm policy relating to the representation of female directors, the number of women considered for executive position appointments, the number of female directors on a board and in executive positions and target figures with regard to their appointment to boards and executive positions.
13	India	7.7%	The Companies Act of 2013 requires firms to appoint at least one female director to their board; this requirement is applicable to listed firms, public firms with paid-up share capitals of 1 billion Indian Rupees and firms with turnovers of 3 billion INR or more.	No
14	Ireland	14.4%	No	A policy target of 40% female participation on all state boards and committees is in place.
15	The United Kingdom	15.6%	No	Beginning in 2012, based on the Principles of UK Corporate Governance (following Lord Davies' recommendation), the recommended target for listed companies in the FTSE 100 is 25% female representation by 2015 (applicable to all board members). FTSE 350 companies are recommended to establish their own aspirational targets, to be achieved by 2013 and 2015.
16	The United States	12.2%	No	The Thirty Percent Coalition, the 30% Club and the Organisation of Women 2020 recommend that 30%, 30% and 20%, respectively, of the board seats of listed firms be held by female directors.
<p>*As of 2015 (Deloitte, 2015).</p> <p>Source: European Commission (2016) and Deloitte (2015).</p>				

3.12. Chapter Summary

This chapter has highlighted the international features of global corporate governance. First, it discussed the importance of corporate boards, illustrated possible board structures that listed firms around the world can adopt and indicated the importance of key subcommittees (audit, compensation and nomination). The chapter then moved on to a discussion of the role and importance of financial crises, legal systems and ownership structures in corporate governance. Next, various comparative features related to the global governance system were highlighted; to this end, the chapter compared insider versus outsider systems and hard law versus soft law models. The last portion of this chapter reviewed the main corporate governance features of the various countries under study, providing a brief outline of the history of corporate governance development in each country.

Chapter 4

4.0 Institutional Investors and Corporate Governance

4.1. Introduction

The purpose of this chapter is to provide an understanding of the role of institutional investors in corporate governance. This chapter opens with an identification of the various types of institutional investors, followed by a discussion of the tools used by institutional investors to engage with their investee firms. This chapter then examines the transnational and national stewardship codes and guidelines that are issued around the world, ultimately concluding with a discussion of the empirical literature review. Therefore, this chapter is organised as follows: section 4.2 illustrates the types of institutional investors, section 4.3 outlines the tools that are adopted by institutional investors in order to enhance corporate governance within their investee firms, section 4.4 discusses the key transnational and national stewardship codes published across the globe, section 4.5 reviews several empirical studies that examine the role of institutional investors in the improvement of corporate governance and section 4.6 offers a chapter summary.

4.2. Types of Institutional Investors

This section identifies the main varieties of institutional investors. These investors may operate in the form of pension funds, mutual funds, insurance companies, hedge funds, private equity firms or sovereign wealth funds.

Pension Funds

Pension funds are a major player in the world of institutional investment, and such funds have a legal obligation to provide retirement income to participants. Pension funds are typically associated with a long-term perspective, as they hold their portfolios within their investee firms (Tilba and McNulty, 2013). The assets of pension funds operating in OECD countries have increased over the past six consecutive years, in particular following the recent financial crisis

of 2008–2009 (OECD, 2015). Since the end of 2008, these funds have grown by 8.1% annually, ultimately reaching a total of 25.2 trillion dollars by the end of 2014. To exercise influence over their investee firms, pension funds may utilise various representative bodies that act as professional groups (Mallin, 2016). For instance, in the UK, large pension funds typically belong to the National Association of Pension Funds (NAPF).

Mutual Funds

Mutual funds are common investment vehicles designed for investors who seek to enter and exit a market or company within a short period; these investors are entitled to withdraw their investments at any time (Monks and Minow, 2011). In many countries, mutual funds are considered to be one of the primary investment vehicles. In 2012, for instance, roughly 46% of American households invested in a mutual funds scheme; as such, this industry is worth approximately \$13 billion in the US (Brown and Wu, 2016).

Insurance Companies

The core objective of insurance companies is to eliminate the financial risk associated with a customer (a business or individual); this is accomplished by transferring that risk from the customer to the insurance company (Newton, 2015). Insurance companies manage complex portfolios involving a variety of risks and finance their operations using several methods, including the issuance of underwritten premiums that are paid by policyholders, the collection of subordinated debts from debt holders and the gathering of equity capital from shareholders (Milidonis and Stathopoulos, 2011). Insurance companies are largely governed by the regulations of a particular country; as such, they are required to comply with the regulations of the country in which they operate (Newton, 2015). As with listed firms, insurance companies are likely to adopt investment strategies that enable them to maintain growth and profitability in order to maximise the surpluses of their policyholders (Newton, 2015). Similar to pension funds, insurance companies typically belong to associations that allow them to gain influence

in the marketplace. In the UK, for example, the Association of British Insurers (ABI) was formed in 1985 and now counts approximately 250 companies as members, which represents 90% of the British insurance market (ABI, 2017).

Hedge Funds

Unlike pension funds and mutual funds, hedge funds have the ability to exert significant pressure over the boards of directors and management teams of their investee firms due to the key differences that arise as a result of their unique organisational form and the distinct stresses that they encounter (Brav et al., 2008). Hedge funds employ highly skilled managers to handle a large and unregulated pool of money. As hedge funds are not governed by the same regulations as are pension funds and mutual funds, they can concentrate their shareholdings in a small number of firms, and they can exercise control over those firms via the use of leveraging and derivatives. In sum, hedge funds are better qualified to act as informed monitors of their investee firms than are other types of institutional investors.

Private Equity Firms

Private equity firms invest large amounts of money in the acquisition of limited liability companies, to include listed firms (Mallin, 2016). Furthermore, these funds may also contribute venture capital in order to expand existing businesses or to kick-start new start-up companies; some even seek out unique investment opportunities and choose to buy distressed companies (Tricker, 2015). The investment choices of private equity firms are mainly associated with high levels of risk and the expectation of high returns. Private equity firms obtain their funds mainly via institutional investors or from wealthy individuals (Tricker, 2015). Private equity funds typically operate in a secretive environment and are required to disclose little about their activities; thus, information on their ownership, investment strategy and partners is often difficult to come by (see Tricker, 2015). For this reason, several guidelines have been published in an attempt to enhance the commitment of these private equity firms and to promote the

disclosure of their activities within investee firms. Among these recommendations are the Walker Guidelines for Disclosure and Transparency in Private Equity, which were drawn up by the British Private Equity and Venture Capital Association (Mallin, 2016). These guidelines highlight the necessity for private equity firms to provide financial performance information on the companies that they have acquired (Mallin, 2016). Furthermore, the guidelines also argue that private equity firms should be required to disclose the accounts of the large companies that they control within six months of the close of the financial year (Mallin, 2016).

Sovereign Wealth Funds

Sovereign wealth funds are government-owned funds that are influential and very large in size²⁵ (Mallin, 2016). As with private equity firms, the corporate governance systems of sovereign wealth funds are often criticised for their secrecy and lack of transparency; such funds neither issue their objectives nor publish information on their portfolio allocations (Mallin, 2016; Tricker, 2015). To this end, an international working group of sovereign wealth funds²⁶ published a list of generally accepted principles and practices, titled the Santiago Principles and Practices, in 2008. The purpose of these principles was to identify frameworks for sovereign wealth funds that would reflect their objectives and investment practices (Mallin, 2016). Additionally, as one of the largest sovereign wealth funds in the world, Norway's oil fund has approved efforts aimed at encouraging the fund to play a greater role in the corporate governance of its investee firms; one such effort involves the ability of the fund to exercise influence over the appointment of directors (Tricker, 2015).

4.3. Institutional Investors' Tools of Engagement

The worldwide growth of institutional investment practices has provided investors with a comparative advantage by granting them the opportunity to act as good monitors of their

²⁵ Globally, sovereign wealth funds account for more than \$6 trillion (Tricker, 2015).

²⁶ The group consisted of 26 countries and met three times to formulate the Santiago Principles and Practices (Mallin, 2016).

investee firms (Gillan and Starks, 2003; Ferreira and Matos, 2008). Institutional investors face continuous pressure to improve their governance practices; this pressure comes from many sources, including government agencies, stock markets and the investors' ultimate beneficiaries (Mallin, 2016). According to Hirschman's (1970) framework, institutional investors may pursue one of two options if and when they become dissatisfied with the governance practices of their investee firms. They can choose to exercise their voting rights in order to promote change, or they can elect to leave the company by selling their shares; this is known as the 'Vote or Exit Concept'. Since the selling option may not be viable, as it is often considered costly, most institutional investors opt to engage with their investee firms in an attempt to alter any unfavourable governance structures (Jin, 2006; McCahery et al., 2016). Institutional investors can adopt many tools in order to facilitate a dialogue with their investee firms, such as one-to-one meetings, voting, shareholder proposals and resolutions, focus lists and corporate governance rating systems (Martin et al., 2007; Goranova and Ryan, 2014; Mallin, 2016). Behind-the-scenes engagement is also considered important, as private negotiation is a favoured tactic of many institutional investors (McCahery et al., 2016). All of these tools are discussed below.

4.3.1. One-to-One Meetings

Meetings between institutional investors and their investee firms are considered an essential means of communication (Mallin, 2016). As such, the Cadbury Report emphasised that institutional investors should hold regular one-to-one meetings with the corporate boards of their investee firms (Solomon, 2013). According to the Cadbury Report, 'institutional investors should encourage regular, systematic contact at [the] senior executive level to exchange views and information on strategy, performance, board membership [and] quality of management' (Solomon, 2013). This type of meeting is considered to be an advantage for the institutional investor as compared to other investors, as companies normally reserve such meetings for those

institutional investors who hold larger stakes in the company (Mallin, 2016). In the context of the UK, firms usually arrange to meet with large-scale institutional investors on a one-to-one basis over the course of a year; such meetings typically involve key members of the corporate board. In these meetings, the targeted audience of institutional investors includes large-scale shareholders, brokers' analysts and any significant investors who are seeking to underwrite or sell their shares. Furthermore, investee firms typically reach out to those institutional investors who have been absent for longer than one year, and any institutional investors who attend these meetings are contacted to ensure that all concerns have been discussed (Mallin, 2016).

Marston (2008) conducted a comparison study of investor relations meetings held by the top 500 UK firms between 1991 and 2002. He reported that the one-to-one meeting was the most important communication tool that existed between institutional investors and their investee firms; he also noted that the demands of institutional investors for this type of communication increased during the period under study (Marston, 2008). Furthermore, he pointed out that a higher number of meetings was associated with the number of institutional investors and analysts present (Marston, 2008). Moreover, the results revealed that companies kept records of previous meetings in order to better prepare for future meetings, which reveals the importance of these meetings (Marston, 2008).

Additionally, companies sometimes initiate new investor relations programs whereby they may increase the number of meetings with investors in an attempt to attract institutional investments. Using a sample of small and mid-cap firms that were either listed in the Nasdaq or that operated over the counter (OTC) between 1998 and 2004, Bushee and Miller (2012) reported that companies that initiated investor relations programs that included face-to-face meetings with investors were found to attract more institutional investments and greater analyst followings. This indicates that institutional investors also value those firms that initiate investor

relations programs and encourage one-to-one meetings. The introduction of such activities by a company was also found to attract media coverage and increase market value.

It is also important to note that institutional investors may engage with their investee firms through private negotiations, ‘widely known as behind the scene[s] engagement’ (McCahery et al., 2016). This type of intervention is seen as an effective tool that can encourage efficient corrective actions within an investee firm. Carleton et al. (1998) investigated the extent to which the TIAA-CREF²⁷, using behind-the-scenes tactics, influenced governance issues within its 45 investee firms between 1992 and 1996. Their results suggested that the TIAA-CREF facilitated agreement with investee firms on several governance issues more than 95% of the time (Carleton et al., 1998). Furthermore, it was found that in 70% of these cases, agreement was reached through private negotiations, thus indicating the effectiveness of this tool in altering the governance practices of a particular investee firm (Carleton et al., 1998).

More recently, McCahery et al. (2016) conducted a study to examine the extent to which institutional investors exercise behind-the-scenes engagement; to this end, he distributed a survey to ICGN members for two subsequent years, 2012 and 2013. The study surveyed the 143 largest institutional investors in the world, 36% being from continental Europe, 24% from the United States, 16% from the United Kingdom, and the remainder from other parts of the world. The results of this study revealed that behind-the-scenes engagement is considered to be a common channel that exists between institutional investors and their investee firms (McCahery et al., 2016). For example, they found that 63% of respondents engaged in direct discussions with the management team in the preceding five years, whilst 45% had private discussions with a company’s board without the attendance of the management team.

²⁷ TIAA-CREF is one of the largest pension funds in the US, and it holds approximately 1% of the total US equity market (Carleton et al., 1998).

McCahery et al. (2016) also reported that the investor's horizon (long-term versus short-term) had an impact on the intervention. For instance, long-term institutional investors intervened more intensively than their short-term counterparts, discussing issues such as corporate governance structure and firm strategy. The institutional investors involved in the study emphasised that the exit option could be a viable strategy, 49% of respondents stating that they had chosen the exit option as a result of performance dissatisfaction. Another 39% of respondents reported that the exit was due to dissatisfaction with governance structure. The investors emphasised that they considered the exit option complementary to, rather than a substitute for, the voice, as institutional investors typically engaged with their investee firms prior to the potential exit.

McCahery et al. (2016) further illustrated that institutional investors face multiple hurdles, the major difficulty being the free rider problem. In addition, the study demonstrated that 63% of the respondents used proxy advisors, about half of them using the services of more than one proxy advisor. Furthermore, institutional investors using proxy advisors indicated that they engaged more intensively with their investee firms rather than substituting proxy advice for their own voice, which indicates that the presence of proxy advisors does not necessarily mean that institutional investors take a passive governance role.

McCahery et al. (2016) also found that institutional investors who hold more liquid stocks report more engagement with their investee firms, as they might find the exit is the most viable option in these firms. This finding is consistent with Edmans et al. (2013), who argued that stock liquidity determines whether institutional investors choose to voice or exit. Examining the activist hedge funds that engaged in block acquisitions between 1995 and 2010, Edmans et al. (2013) reported that liquidity attracted hedge funds to acquire a block, especially in firms with high managerial incentives. Once the block was formed, the blockholder was more likely to choose the exit option over the voice option, as demonstrated by a lower propensity for active

investment (filing Schedule 13D) than passive investment (filing Schedule 13G). The results also indicate that 13D filing is associated with positive announcement returns and improvements in operating performance, especially in liquid firms.

4.3.2. Voting

The right to vote is considered to be an influential tool used by institutional investors to weigh in on all issues raised during the annual general meeting (Mallin, 2016). In an effort to enhance the activism of institutional investors, the Cadbury Report (1992) encouraged institutional investors to make positive use of their voting rights. Furthermore, there have been clear statements from various international organisations regarding voting rights and the responsibilities of share-owners. For instance, OECD has dedicated one of its six principles to the rights of shareholders and key ownership functions. This principle stated that ‘shareholders should be able to vote in person or in absentia, and equal effect should be given to votes whether cast in person or in absentia’ (OECD, 2004). Furthermore, in its global corporate governance principles, which were revised in 2009, the International Corporate Governance Network (ICGN) stated that ‘shareholders should actively vote at annual and extraordinary general meetings, and votes should always be cast in a considered manner’ (ICGN, 2009).

In the context of institutional investor voting in the UK, institutional investors used to register their views of a vote by using the postal service; however, nowadays this process can be completed electronically where such a service is available (Mallin, 2016). Generally, institutional investors attempt to sort out any conflicting views prior to a vote date, even pursuing private negotiations with the management in an effort to do so. However, if these private negotiations fail, institutional investors may abstain or vote against a particular resolution (Mallin, 2016). The dissatisfaction of shareholders is taken into consideration by a corporate board during attempts to alter the governance structure of a firm. It is also important to note that, for the voting process to be effective, the regulations and laws of the country must

support the casting of meaningful votes. Examining the activism of US institutional investors by investigating their vote casting in 43 countries outside of the US between 2003 and 2009, Iliev et al. (2015) found that the laws and regulations governing shareholder voting in non-US countries allowed for meaningful votes to be cast. In addition, the study revealed that voter dissent was more frequently reported when the institutional investors feared expropriations. In addition, greater voter dissent was associated with higher director turnover and increased mergers and acquisitions.

Del Guercio et al. (2008) studied the extent to which a campaign of ‘just vote no’ could influence a corporate board’s decision to improve corporate governance structures; to this end, the team examined 112 US-listed companies in operation between 1999 and 2003. They found that activist institutional investors often convinced their fellow investors to also withhold their votes when it came time to elect directors during a general meeting, which frequently led to the embarrassment of the corporate board (Del Guercio et al., 2008). As a result of such campaigns, several improvements were noted in terms of governance structure and the performance of investee firms, including abnormal discipline related to CEO turnover and the improved performance of the firm. More recently, Aggarwal et al. (2015) examined the US securities lending market in an attempt to investigate the behaviours and attitudes of institutional investors towards any shares that were on loan prior to the record date. In the securities lending market, shares cannot be voted upon if they are on loan on the day of voting. This study emphasised that the supply of lendable shares was very low prior to the proxy record date, as institutional investors began to recall their loaned shares before the voting date (Aggarwal et al., 2015). The study also showed that the corporate governance practices of investee firms was one of the major reasons behind the recalling of shares, as institutional investors recalled shares from weak governance firms (Aggarwal et al., 2015). More significantly, the types of proposals listed in the voting agenda determined which shares needed

to be recalled; additionally, the level of recalled shares was noted to be high when antitakeover or compensation proposals were listed in the voting agenda (Aggarwal et al., 2015).

4.3.3. Shareholder Proposals/Resolutions

Shareholder proposals, or shareholder resolutions, are quite common in the US as compared to the UK (Mallin, 2016). On average, between 800 and 900 shareholder proposals are introduced in the US per year, most of which are related to the social environment and ethical issues; there is an expectation that this number will increase in the future due to widespread dissatisfaction with regard to executive remuneration packages (Mallin, 2016). In the UK, however, the relatively low number of shareholder proposals presented in the AGM is the result of a process in which a resolution must be requested by (i) members who own at least 5% of the company's voting power, or (ii) 100 or more shareholders whose paid-up capital averages at least £100 each. Given the difficulty of meeting these two conditions, the number of shareholder proposals tends to be low in the UK, normally not exceeding 10 per year (Mallin, 2016). Although, the number increased following the financial crisis.

As far as the US is considered, private negotiations between institutional investors and their investee firms may cause many shareholder proposals to be withdrawn prior to the AGM date. For instance, Bauer et al. (2015) examined the determinants of proposal withdrawals by considering 1,200 proposals filed by institutional investors in S&P1500 firms between 1997 and 2009. The results demonstrated that shareholder proposals were often withdrawn prior to the AGM because institutional investors were able to reach an agreement with their investee firms through private dialogues (Bauer et al., 2015). Their results also showed that the withdrawal cases were mainly initiated by influential institutional investors rather than their private investor counterparts (Bauer et al., 2015). Furthermore, long-term and passively investing institutions were positively associated with proposal withdrawals if the withdrawal

was initiated by institutional investors; however, negative relationships between CEO ownership and withdrawal cases were documented (Bauer et al., 2015).

4.3.4. Focus Lists

A number of institutional investors have established ‘focus lists’ with regard to underperforming companies (Mallin, 2016). These types of indices also identify those firms that do not respond to the queries of institutional investors. Examining a sample of 93 firms appearing on the focus list of the Council of Institutional Investors from 2000 to 2005, Ward et al. (2009), reported that institutional investors reduced their holdings in firms that appeared on the focus list; this was seen as a signal for underperforming firms to improve their performance. However, this relationship was moderated by the composition of a corporate board. In particular, a board’s level of independence was found to mediate the reduction of institutional holdings in these types of firms, thus indicating that institutional investors pay particular attention to the composition of corporate boards within these firms (Ward et al., 2009). The study also reported that firms with higher levels of independence tend to be more responsive to institutional concerns than their counterparts; consequently, these firms adopt various reactive measures, such as scrutinising the incentives given to the company’s CEO (Ward et al., 2009).

4.3.5. Corporate Governance Rating Systems

For several years, many parties around the world have assessed and scored governance quality at the firm and country levels. According to Mallin (2016), the most well-known firms to have initiated corporate governance rating systems are Deminor, Standard and Poor’s (S&P), and Governance Metrics International (GMI). Deminor focuses on European countries, while S&P concentrates on other countries including Russia. The GMI rating covers a range of countries and regions, including the US, Europe and various countries in Asia-Pacific (Mallin, 2016). These rating systems adopt various approaches and methodologies to assess the level and

quality of corporate governance. However, corporate board structures and processes are of the main categories involved in most corporate governance rating systems (Van den Berghe and Levrau, 2004).

Corporate governance rating systems are beneficial for the investor as well as for the country. For instance, such systems enable investors to assess the governance quality of their investee firms and of the companies in which they intend to invest in the future. Additionally, such systems allow governments to assess their governance quality in comparison to that of other countries; thus, they may be able to enhance the overall governance structure of their country in order to attract foreign investors (Mallin, 2016).

4.4. Stewardship Codes and Guidelines

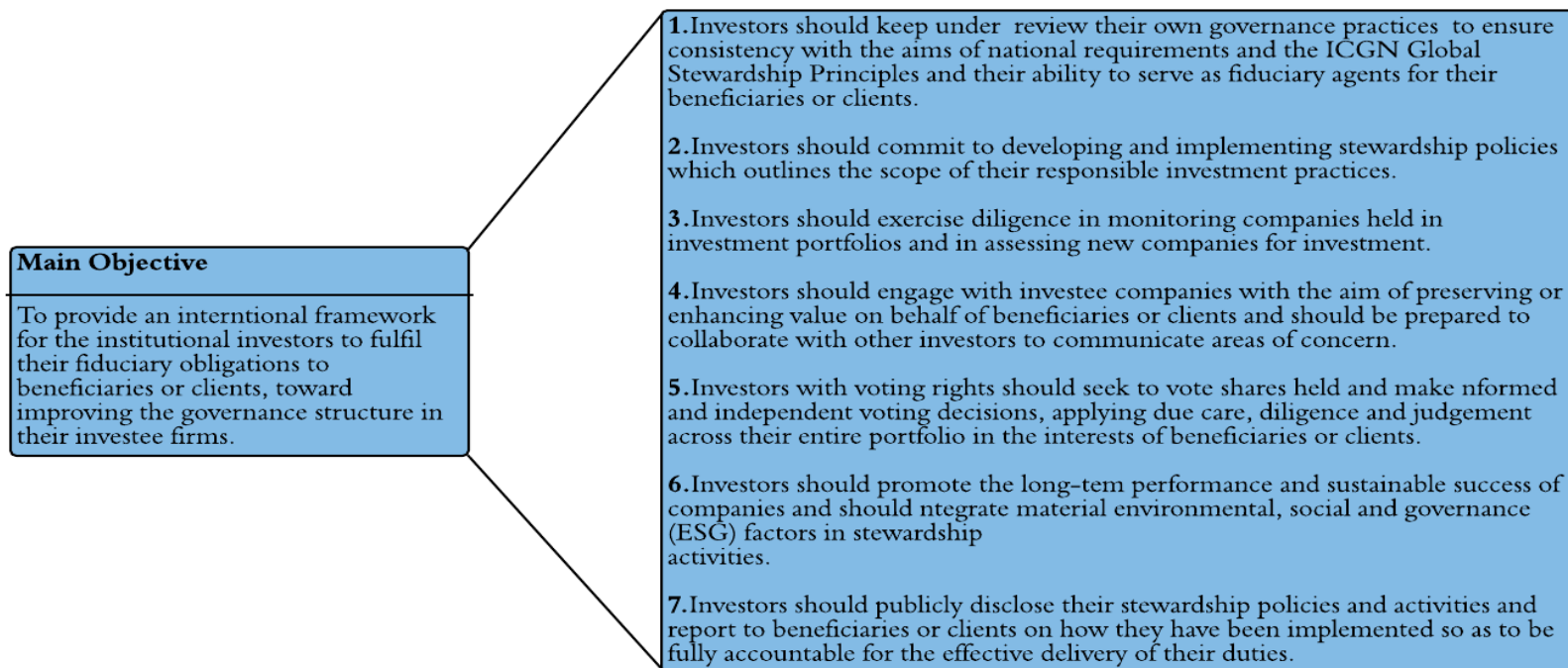
In the context of improving the engagement between institutional investors and their investee firms, several stewardship codes and guidelines have been published on the international and national levels. This section discusses both the transnational and national stewardship codes and guidelines that have been published to date.

4.4.1. Transnational Stewardship Codes and Guidelines

Aside from the stewardship codes developed at the country level, several international organisations concerned with the improvement of international corporate governance practices across the globe have published stewardship codes. Among them, the International Corporate Governance Network (ICGN) published its first Global Stewardship Code in 2016 in an attempt to develop a global framework aimed at achieving good practices with regard to the stewardship of institutional investors. This Code was divided into two parts; the first section summarised the principles, while the second segment discussed how best to implement these principles in practice (ICGN, 2016). The Code included seven principles that covered various topics aimed at enhancing engagement between institutional investors and their investee firms (see Figure 4.1). These principles provided guidance for institutional investors on several

matters, including the establishment of a solid foundation of stewardship practices that are in line with national and transnational stewardship codes, the implementation of stewardship practices, the undertaking of regular assessments to measure investee firms' performance, the establishment of engagement dialogues with investee firms in order to enhance the value of beneficiaries, the exercise of voting rights, the promotion of long-term value creation, the maintenance of environmental and social governance attributes during all stewardship activities and the enhancement of transparency, which is achieved by disclosing all stewardship activities to the beneficiaries.

Figure 4.1 The Key Principles of the ICGN Global Stewardship Code.



Source: ICGN (2016).

4.4.2. National Stewardship Codes and Guidelines

The UK Stewardship Code was generally heralded as the first of its kind when it was initiated by the Financial Reporting Council (FRC) in 2010²⁸; it was later revised in 2012. Considered to complement the UK's Corporate Governance Code, its main aim was to enhance engagement between institutional investors and their investee firms in an effort to improve corporate governance practices (Roach, 2011; Mallin, 2016). According to Mallin (2016), the Stewardship Code, as published in 2010, was rooted in previous recommendations issued by several parties that were concerned with the level of institutional investor activism in the UK. For example, the Myners Report on Institutional Investment was issued in 2001 by HM Treasury (Myners, 2001). This report focused more on the trusteeship of institutional investors and on trustees' legal requirements and aimed to promote the activism of institutional investors, especially within underperforming investee firms. Moreover, the Institutional Shareholders Committee (ISC)²⁹ published their Statement of Principles on the Responsibilities of Institutional Shareholders in 2002. This statement addressed several topics that institutional investors needed to consider when attempting to fulfil their fiduciary obligations; such topics included possible means of monitoring investee firms, various policy explanations regarding investee firms' compliance with the Combined Code, the implementation of policies for meeting with the directors and senior management of investee firms, methods of handling conflicts between institutional investors and their investee firms, the adoption of intervention strategies, descriptions of various concerns for which further action should be taken (as well as the type of action that might be taken) and statements concerning voting policy. The ISC conducted an assessment of this statement in 2005, ultimately reporting an increase in the level of engagement between

²⁸ The Code was revised in 2012.

²⁹ The ISC is a group of associations that represents institutional investors in the UK; the group comprises the Association of British Insurers (ABI), the Investment Management Association (IMA), the National Association of Pension Funds (NAPF) and the Association of Investment Trust Companies (AITC). The name of the association was altered in 2011 and is now the Institutional Investors Committee (IIC); members include the IMA, the NAPF and the ABI (Mallin, 2016).

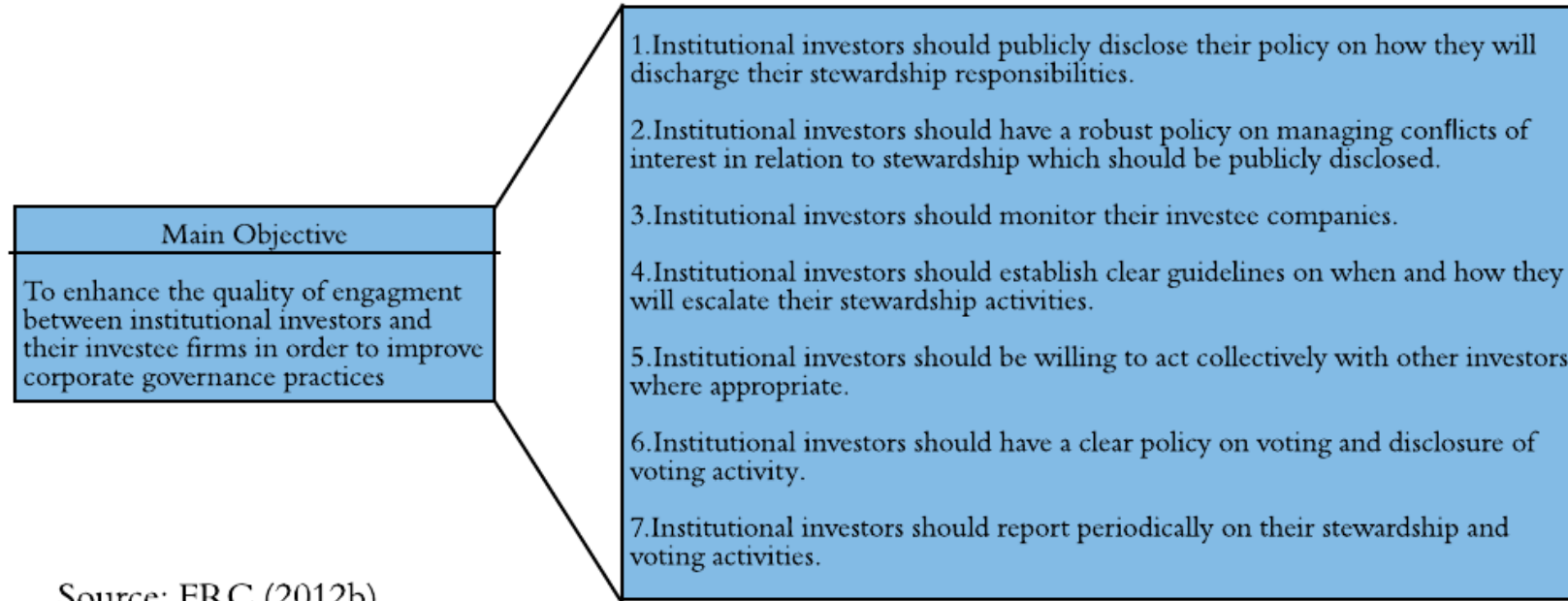
institutional investors and their investee firms. Another review was undertaken in 2007, which resulted in recommendations for institutional investors to better disclose their voting policies. In November of 2009, the Code of Responsibilities of Institutional Investors was issued by the ISC, which was built upon the previous statement regarding the responsibilities of institutional investors. This code mainly aimed to enhance the dialogue between institutional investors and their investee firms in order to improve various governance practices; as such, this code strove to improve decision-making processes in an effort to reduce associated risk and to increase shareholders' value within investee firms. Following the recent financial crisis, Sir David Walker published a review of the governance policies of UK banks in late 2009. The review included nine recommendations and discussed the engagement between institutional investors and their investee firms. When the UK Corporate Governance Code was issued in 2010, the UK Stewardship Code was also published in tandem.

The UK Stewardship Code was designed according to a 'comply or explain' basis and included seven main principles (See Figure 4.2). The first principle involved the disclosure and discharge of stewardship responsibilities, while the second focused on managing conflicts of interest in relation to stewardship. The third principle highlighted the importance of monitoring investee firms. To this end, the Code explained the process of monitoring by emphasising three vital procedures: checking the effectiveness of the corporate board and its subcommittees, maintaining a clear audit trail and attending the general meetings of companies in which institutional investors own the majority of shares. The fourth principle illustrated the activities of escalation wherein institutional investors are required to lay out the circumstances of intervention. In the fifth principle, the importance of acting collectively with other investors where appropriate was highlighted, and the need to disclose the policies related to these procedures was stressed. The sixth principle recommended that institutional investors have clear voting policies and methods by which they may disclose their voting activities, and the seventh

principle placed considerable emphasis on the periodic reporting of their stewardship and voting activities (FRC, 2012b).

Following the issuance of the UK Stewardship Code, a significant number of stewardship codes and guidelines were published in several countries. Table 4.2 provides a list of the key stewardship codes and guidelines issued at the international and national levels.

Figure 4.2 The Key Principles of the UK Stewardship Code.



Source: FRC (2012b).

Table 4.1 Transnational and National Stewardship Codes

Country/Organisation	Code Name	Year of issuance	Issuer
Transnational Codes and Guidelines			
ICGN	ICGN Global Stewardship Principles	2016	ICGN
National Codes and guidelines			
Australia	FSC Standard 23: Principles of Internal Governance and Asset Stewardship	2015	Financial Services Council
Canada	Principles for Governance Monitoring, Voting and Shareholder Engagement	2010	Canadian Coalition for Good Governance
Hong Kong	Consultation Paper on the Principles of Responsible Stewardship	2015	Securities and Futures Commission
Italy	Stewardship Principles for the Exercise of Administrative and Voting Rights in Listed Companies	2013	Assogestioni (The Italian Association of Asset Management)
Japan	Principles for Responsible Institutional Investors	2014	Financial Services Agency
Kenya	Draft Stewardship Code for Institutional Investors	2015	Capital Markets Authority
Malaysia	Code for Institutional Investors	2014	Minority Shareholders Watchdog Group
Netherlands	Best Practices for Engaged Share-Ownership	2011	EUMEDION Corporate Governance Forum
Singapore	Singapore Stewardship Code	Forthcoming	Monetary Authority of Singapore
South Africa	Code for Responsible Investing	2011	Institute of Directors of Southern Africa
Switzerland	Guidelines for Institutional Investors, Governing the Exercising of Participation Rights in Public Limited Companies	2013	Ethos Foundation
Taiwan	Stewardship Principles for Institutional Investors	2016	Taiwan Stock Exchange
United Kingdom	The UK Stewardship Code	2010	Financial Reporting Council

Source: ICGN (2017).

4.5. Institutional Investors and Corporate Governance: An Empirical Literature Review

To date, several studies have examined the activism of institutional investors with respect to the improvement of corporate governance within investee firms (Goranova and Ryan, 2014). These studies vary in their scope of coverage, though most focus on one country and are largely based on US data (Chung et al. 2002; Hartzell and Starks, 2003; Parrino et al., 2003; Velury et al., 2003; Kane and Velury, 2004; Almazan et al., 2005; Brav et al., 2008; Wang, 2014; Hadani et al., 2011; Ruiz-Mallorquí and Santana-Martín, 2011; Chhaochharia et al., 2012; Helwege et al., 2012; Muniandy et al., 2016). It is important to note that a limited number of studies have considered international samples (Ferreira and Matos, 2008; Aggarwal et al., 2011; De-la-Hoz and Pombo, 2016; Kim et al., 2016). This section reviews the key empirical studies dedicated to this topic based on their scope, whether they are international studies or studies based on a single country.

In the context of international studies, Ferreira and Matos (2008) examined the role of institutional investors in the improvement of firm performance by examining listed firms in 27 countries between 2000 and 2005. They found that across the globe, foreign and independent institutional investors promoted greater firm value and operating performance (Ferreira and Matos, 2008). Their results also revealed that investors with fewer business ties were better monitors than were their counterparts who maintained close relationships with their investee firms (Ferreira and Matos, 2008). Consistent with this view, Aggarwal et al. (2011) examined the role of institutional investors in the improvement of corporate governance; to this end, the team scrutinised the activities of businesses in 23 countries from 2003 to 2008 using a governance index that included 41 attributes. Adopting OLS and fixed effects estimations, they found that non-local institutional investors were the main promoters of governance outcomes around the world (Aggarwal et al., 2011). In particular, foreign institutions and institutions originating in countries with strong shareholder protections took the lead in promoting better

governance structures outside the US (Aggarwal et al., 2011). Their results indicated that the activism and monitoring of institutional investors extended beyond borders, yielded better governance outcomes and increased the performance of investee firms outside the US (Aggarwal et al., 2011). Additionally, their results illustrated that firms with greater numbers of institutional investors were more likely to terminate the services of poorly performing CEOs (Aggarwal et al., 2011). Furthermore, they also found that foreign institutional investors tended to be associated with a more shareholder-friendly board structure; this was typically accomplished by considering board size, board independence and CEO duality (Aggarwal et al., 2011).

De-la-Hoz and Pombo (2016) investigated a sample of listed firms in Latin-American countries between 1997 and 2011 and reported that the greater the presence of institutional investors as dominant shareholders, the higher the firm value. Moreover, they reported that different types of institutional investors had different effects on firm valuation (De-la-Hoz and Pombo, 2016). While independent institutional investors were found to enhance firm value, grey institutional investors were found to reduce value (De-la-Hoz and Pombo, 2016). Kim et al. (2016) consulted a sample of listed firms from 29 countries during the period of 2001 to 2013 in order to investigate the role of institutional investors in mitigating earning management. Their results revealed that domestic institutional investors were better able to lessen earning management as compared to their foreign counterparts, likely benefiting from the proximity of their monitoring practices (Kim et al., 2016). However, their results also described the effectiveness of foreign institutional investors in monitoring earning management; essentially, their ability improved when they became familiar with the host country's accounting practices and culture (Kim et al., 2016). Furthermore, they found that foreign institutional investors from common law countries reduced earning management in firms located in civil law countries (Kim et al., 2016).

With regard to single country studies, Chhaochharia et al. (2012) examined all firms associated with 13(f) institutions, as compiled by Thomson Reuters, between 1980 and 2007. They reported that local institutional investors were good monitors of their investee firms and that these firms were profitable and less likely to engage in management earning (Chhaochharia et al., 2012). Furthermore, they observed that local institutions were more likely to introduce shareholder proposals, increase CEO turnover and monitor CEO compensation schemes (Chhaochharia et al., 2012). Additionally, Muniandy et al. (2016) investigated the impact of institutional investors on firm performance via an examination of all Australian-listed firms in operation from 2000 to 2012. Their findings emphasised that institutional investors, as a homogenous group, improved firm performance (Muniandy et al., 2016). However, this result did not stand when the researchers separated institutional investors into two groups: pressure-resistant and pressure-sensitive investors. They found that while pressure-resistant investors had the ability to improve the short-term performance of investee firms, this result was not true for the pressure-sensitive group (Muniandy et al., 2016). Moreover, their results suggested that nominee or trustee shareholders were positively associated with the long-term performance of firms (Muniandy et al., 2016).

Based on a sample of Spanish-listed firms in practice between 1996 and 2009, Ruiz-Mallorquí and Santana-Martín (2011) examined whether more dominant institutional investors (banks versus investment funds) could influence firm valuation. Using GMM estimation methods, the authors found that the relationship between institutional investors and firm valuation was dependent on whether the dominant owner was a bank or an investment fund (Ruiz-Mallorquí and Santana-Martín, 2011). The authors also discovered that this relationship was negative where banks were concerned, thus indicating that banks are able to maintain private relationships with their investee firms, which enables them to more easily extract benefits (Ruiz-Mallorquí and Santana-Martín, 2011). This result was also found to be consistent when

the second- and third-dominant owners were banks, which suggests that banks create self-dealing coalitions from among a firm's other shareholders (Ruiz-Mallorquí and Santana-Martín, 2011). Conversely, the relationship was found to be positive when the dominant shareholder was an investment fund, thus indicating that this type of investor is likely to properly monitor the management team in order to increase value for the ultimate beneficiaries; furthermore, such investors were found to be unlikely to engage in expropriation practices due to the nature of their activities (Ruiz-Mallorquí and Santana-Martín, 2011). When the second- and third-dominant investors were investment funds, this result was deemed consistent; this suggests that these dominant investors engage in lobbying to enhance the value of their investee firms (Ruiz-Mallorquí and Santana-Martín, 2011).

Various other studies have focused on the role of institutional investors in influencing managerial compensation schemes. For instance, using a sample of 1,914 US-listed firms in practice from 1992 to 1997, Hartzell and Starks (2003) investigated whether institutional investor concentrations influenced executive compensation packages. Ultimately, they found that institutional investors did, in fact, influence managerial compensation: the higher the concentration of institutional investors, the more likely the compensation scheme was to be sensitive to the performance of the company (Hartzell and Starks, 2003). Furthermore, their results revealed that institutional investors were negatively associated with compensation incentives. Almazan et al. (2005) consulted the same dataset as was used in the study performed by Hartzell and Starks (2003) and found that the role of an institutional investor in influencing a compensation scheme was determined by the institutional investor's type (active versus passive). Their results indicated that active institutional investors (i.e., investment advisors and investment companies) provided better monitoring of compensation schemes as compared to their passive counterparts (banks, insurance companies and other institutions) (Almazan et al., 2005). Pay-for-performance packages were found to be positively associated with active

institutional investors, and changes to the concentration of active institutional investors drove future changes in pay-for-performance sensitivity (Almazan et al., 2005). The study also uncovered a negative relationship between both types of institutions and the level of compensation, thus indicating that while all institutions monitor compensation schemes, only active institutions have a significant effect on pay-for-performance packages.

Other researchers have investigated the role of institutional investors in influencing earning management. Among them, Wang (2014) examined a sample of all UK-listed firms in operation between 1997 and 2010. Her study revealed that institutional investors with a 10–20% threshold of ownership, an active investment strategy and a moderate investment duration were negatively associated with the probability of income-inflating abnormal accruals; conversely, they were positively associated with the likelihood of income-deflating abnormal accruals (Wang, 2014). The results also showed that passive institutional investors were positively associated with the probability of increasing accruals management during times of financial crisis (Wang, 2014). Analysing a sample of US-listed firms taken from 2001 to 2004, Hadani et al. (2011) reported that institutional investors, as large owners, had the ability to curb the earning management of their investee firms. Furthermore, the researchers reported that higher numbers of shareholder proposals were found to be associated with subsequent earning management, thus indicating that institutional investors use the ‘shareholder proposals’ tool to inhibit earning management (Hadani et al., 2011).

Moreover, further studies have focused on the role of institutional investors in improving the auditing quality of their audit firms. Velury et al. (2003), for instance, examined the influence of institutional investors on the selection of auditing firms using a sample taken from the Compustat database of firms in practice from 1992 to 1996. Their 2SLS estimation revealed that the higher the number of institutional investors, the greater the likelihood that an industry-specialist auditor would be appointed to perform auditing services for the investee firm (Velury

et al., 2003). Their results indicated that institutional investors were likely to employ higher quality auditors in an attempt to enhance the financial reporting of their investee firms (Velury et al., 2003). Using the same sample, Kane and Velury (2004) examined whether the presence of institutional investors served to provide better monitoring of management via the use of large auditing firms tasked with carrying out annual audit responsibilities. They reported that the higher the number of institutional investors, the greater the likelihood that the investee firm would be audited by a large, global auditing firm (Kane and Velury, 2004).

The review of the key empirical studies conducted within this field demonstrates that the majority of these studies were conducted in the context of one country (see Table 4.2). Furthermore, most of these studies were based largely on US data, which implies a need to investigate the topic using an international sample. Unfortunately, few studies have yet to utilise such global samples (see, for example, Ferreira and Matos 2008; Aggarwal et al., 2011; De-la-Hoz and Pombo, 2016; Kim et al., 2016). However, it is important to note that these previous global studies considered a limited number of corporate board characteristics (see Aggarwal et al., 2011; Chhaochharia et al., 2012). Therefore, this study aims to fill the gap by investigating the role of institutional investors in the improvement of corporate governance via the consideration of a wide range of corporate board characteristics, namely the various corporate board attributes (composition, activity, entrenchment and busyness) and board diversity characteristics (gender, age, nationality and education) at play in 15 countries around the world. These countries include Australia, Belgium, Canada, Denmark, Finland, France, India, Ireland, Italy, the Netherlands, Norway, Spain, Sweden, Switzerland and the UK. Additionally, this study sheds additional light on the role of institutional investors in efforts to improve the composition and activity of a board's key subcommittees (audit, compensation and nomination). Furthermore, previous studies have failed to consider the institutional environments that surround investee firms—such as a nation's economic condition, legal

system and ownership structure—with the exception of Aggarwal et al. (2011), who investigated this relationship within different legal systems using a corporate governance index. Therefore, this study instead considers the use of the board attributes index in conjunction with an investigation of individual attributes during this effort to understand which board characteristics are most significantly influenced by institutional investors within different legal systems.

Table 4.2 Summary of Key Studies

SN	Author (Year and Journal)	Period	Key Variables	Sample and Methodology	Primary Findings
International Studies					
1	Ferreira and Matos (2008, JFE)	2000–2005	DV: Tobin Q, ROA, NPM & CAPEX IV: Institutional ownership	Listed firms in 27 countries (FE & RE)	1. The presence of foreign and independent institutional investors promotes better firm value and increases operating performance within their investee firms. 2. Institutional investors with fewer potential business ties to their investee firms exhibit better monitoring as compared to their counterparts who maintain close relationships with their investee firms.
2	Aggarwal et al. (2011, JFE)	2003–2008	DV: Corporate governance index IV: Institutional ownership	Listed firms in 23 countries (OLS, FE & Probit)	1. Foreign institutional investors are the main drivers of corporate governance around the world. 2. Foreign institutions and institutions from countries with strong shareholder protections take the lead in promoting healthy governance structures within their investee firms. 3. Firms with higher levels of institutional ownership exhibit greater valuation and are more likely to terminate CEOs who demonstrate poor performance.
3	De-la-Hoz and Pombo (2016, EMR)	1997–2011	DV: Tobin Q and ROA IV: Institutional ownership	562 non-financial listed firms in six Latin-American countries (FE)	1. The greater the presence of institutional investors as dominant shareholders in a firm, the higher the firm valuation in Latin-American countries. 2. Firm values in Latin-American countries are enhanced by independent institutional investors and are reduced by grey institutional investors.
4	Kim et al. (2016, JCF)	2001–2013	DV: Earning management IV: Institutional ownership	Listed firms in 29 countries (OLS & FE)	1. Domestic institutional investors are better able to constrain earning management as compared to their foreign counterparts, likely due to the proximity of monitoring information. 2. As institutional investors become more familiar with the accounting practices and culture of the host country, they grow to be as effective as their domestic counterparts. 3. Foreign institutions from countries with strong shareholder protections (common law countries) are the main monitors of earning management in countries with weak shareholder protections (civil law countries).

Single-Country Studies					
5	Chhaochharia et al. (2012, JAE)	1980–2007	DV: ROA, shareholder proposals, CEO turnover, CEO compensation IV: Institutional ownership and distance from investee firms	All common stock holdings of 13(f) institutions, as compiled by Thomson Reuters (Logit, OLS)	1. Local institutional investors are good monitors of their investee firms; these firms are profitable and less likely to engage in earning management activities. 2. Local institutional investors are more likely to introduce shareholder proposals, increase CEO turnover and monitor CEO compensation schemes.
6	Muniandy et al. (2016, PBFJ)	2000–2012	DV: Tobin Q and ROA IV: Institutional ownership	All Australian-listed firms (GMM)	1. Institutional investors, as a homogenous group, promote better firm performance. 2. Pressure-resistant institutional investors have the ability to improve short-term performance; this is not true for pressure-sensitive institutional investors. 3. Nominee and trustee institutional investors have the ability to improve long-term firm value.
7	Ruiz-Mallorquí and Santana-Martín (2011, JBF)	1996–2009	DV: Tobin Q IV: Bank and investment fund investors	111 Spanish-listed firms (GMM)	1. Bank dominant shareholders are negatively associated with firm value. 2. Investment fund dominant shareholders are positively associated with firm value. 3. The existence of other large shareholders in the firm influences firm valuation when institutional investors are the first-dominant investor.
8	Hartzell and Starks (2003, JF)	1992–1997	DV: Salary and total direct compensation; the sensitivity of value of option grants to changes in stock price; cash compensation and total direct compensation IV: Institutional ownership concentration	Firms listed in the S&P index (OLS)	1. The greater the concentration of institutional investors, the more likely compensation schemes are to be measured by company performance. 2. Institutional investors are negatively associated with compensation incentives.
9	Almazan et al. (2005, FM)	1992–1997	DV: Pay level; pay-for-performance sensitivity (the sensitivity of option grants to changes in stock price; the sensitivity of option grants; stock grants' sensitivity to changes in stock price) IV: Active institutional investors concentration; passive institutional investors concentration; total institutional investors concentration	Firms listed in the S&P index (OLS, Tobin, and change-on-change regressions)	1. Active institutional investors (i.e., investment advisers and investment companies) provide better monitoring of compensation schemes as compared to their passive counterparts (banks, insurance companies and other institutions). 2. Pay-for-performance is positively associated with the presence of active institutional investors, but not with the existence of passive institutional investors. 3. Both types of institutional investors (active and passive) monitor the level of compensation.

10	Wang (2014, CGIR)	1997–2010	DV: Total current accruals IV: The presence of institutional investors, as classified based on block-holding levels; investment strategies and investment durations	All UK-listed firms (change-on-change and probit)	1. Institutional investors with a 10–20% threshold of ownership, an active investment strategy and a moderate investment duration are negatively associated with the probability of income-inflating abnormal accruals and positively associated with the likelihood of income-deflating abnormal accruals. 2. Passive institutional investors are positively associated with the probability of increasing accruals management during times of financial crisis.
11	Hadani et al. (2011, JBR)	2001–2004	DV: Earning management IV: Largest percentage of institutional investors	Firms listed in the S&P (RE)	1. Large institutional investors lessen earning management in their investee firms. 2. A higher number of shareholder proposals are found to be related to earning management.
12	Velury et al. (2003, RQFA)	1992–1996	DV: Proportion of industry sales audited by an auditor IV: Percentage of institutional investors	US-listed firms available in Compustat tapes and in the Compact Disclosure database (2SLS)	1. The higher the number of institutional investors, the more likely the firm is to demand a high quality external auditor.
13	Kane and Velury (2004, JBR)	1992–1996	DV: Dummy variable equals one if the firm is audited by a Big 6 audit firm; otherwise, dummy variable is zero. IV: Percentage of institutional investors	US-listed firms available in Compustat tapes and in the Compact Disclosure database (Logit)	1. The higher the number of institutional investors, the higher the likelihood that the firm will be audited by a large audit firm.

4.6. Chapter Summary

This chapter provides an understanding of the role of institutional investors in the improvement of corporate governance. This chapter began by identifying the various types of institutional investors, followed by an explanation of the many tools that are adopted by those investors to engage with their investee firms. Next, the chapter discussed the key transnational and national stewardship codes that have been published around the world in an effort to enhance engagement between institutional investors and their investee firms. Lastly, the chapter reviewed a number of key studies that have been conducted in this field to date.

Chapter 5

5.0 Hypotheses Development

5.1. Introduction

Previous chapters have discussed corporate governance theories, the corporate governance background, the nature of institutional investors and various related issues in an attempt to explain the underlying framework of this research and to develop the hypotheses for this study. These hypotheses can be divided into two categories. The first set concerns the role of institutional investors in the improvement of various corporate board and key subcommittee attributes related to composition, activity, entrenchment and busyness. The second series, alternatively, discusses the role of institutional investors in improving board diversity attributes related to gender, age, nationality and education diversity.

Accordingly, this chapter is organised as follows: section 5.2 presents the hypotheses related to the attributes of a corporate board and its key subcommittees (composition, activity, entrenchment and busyness), section 5.3 explains the hypotheses related to board diversity (gender, age, nationality and education diversity), and section 5.4 offers a chapter summary.

5.2. Institutional Investors and Board Attributes

The increasing trend towards cross-border investment, as well as the recent financial crisis that occurred in many parts of the world, has led institutional investors to look more carefully at the corporate governance structures of their investee firms (Mallin, 2016). Highly-skilled institutional investors have increased investment growth over the past few decades and have created the expectation that good corporate governance practices should be established within their investee firms (OECD³⁰, 2011). Furthermore, there has been increasing pressure from governments and various global stockholders for institutional investors to engage with their investee firms (Mallin, 2016). Due to the high monitoring costs associated with the collection

³⁰ Refers to the Organisation for Economic Co-operation and Development.

and analysis of information, as well as the costs associated with acting on the resulting findings (Fich et al. , 2015), institutional investors are better able to provide for the active monitoring of their investee firms than are their smaller-investing counterparts. This is attributable to the fact that large owners can bear the high costs of monitoring because the potential returns associated with monitoring exceed the attendant costs (Gillan and Starks, 2000).

As the corporate board is considered the main internal governance mechanism and the centre of decision-making in the company (Bebchuk and Weisbach, 2010; Solomon, 2013; Mallin, 2016), it is not surprising that institutional investors focus on enhancing the characteristics of the corporate board in their investee firms. McCahery et al. (2016) reported that corporate governance is a significant factor for institutional investors who are seeking to establish a healthy portfolio; indeed, a number of such investors are willing to enter into a dialogue with their investee firms in order to improve their governance structures. In their studies, which involve the 143 largest institutional investors across the globe, they reported that 63% of the surveyed sample have direct discussions with the management team, while 43% have private discussions with the corporate board without the involvement of the management team. The study also reported corporate governance structure is one of the main discussions of the institutional investors with long-term investment horizons. In addition, Coombes and Watson (2000), following the completion of an international survey of 200 institutional investors, found that institutional investors consider the corporate board as important as the financial indicators. This is consistent with several studies that reported that institutional investors are attracted to well-composed corporate boards (for examples, see Useem et al., 1993; Chung and Zhang, 2011; Schnatterly and Johnson, 2014).

The agency theory (Jensen and Meckling, 1976) stems from the separation between ownership (shareholders) and control (managers). This separation provides a chance for the managers (agents) to act in their own interests rather than the interests of the stockholders (principals).

The agency literature recognises that the corporate board is considered to be a primary monitoring mechanism that protects shareholders' interests and helps to align the interests of managers and shareholders (Mallin, 2016; Fama and Jensen, 1983; Bebchuk and Weisbach, 2010). Institutional investors can therefore efficiently contribute in reducing the agency problem by monitoring the managerial behaviour in their investee firms (Bushee, 1998).

Drawing from the assumptions of the stewardship theory, Hernandez (2012; 174) defines stewardship as the 'extent to which an individual willingly subjugates his or her personal interests to act in protection of others' long-term welfare'. Institutional investors as stewards are encouraged to engage with their investee firms and to look at the long-term value of their beneficiaries (McNulty and Nordberg, 2016). The issuance of the stewardship codes in the UK (FRC, 2010, revised 2012) is considered a significant move towards encouraging institutional investors to engage with their investee firms and enhance the governance structure. Upon the first issuance of the first UK stewardship code in 2010, several countries have issued their own stewardship codes and guidelines (see Table 4.1 in chapter 4).

The institutional theory notes that the external environment surrounding the entities and organizations may affect the way they behave (Scott, 2004). In this context, both institutional investors and their investee firms are also influenced by the stewardship codes and corporate governance codes respectively. The stewardship codes that have been published at transnational and national levels (see Table 4.1) also contribute to the way the institutional investors monitor their investee firms. According to recent reports, upon the issuance of the UK stewardship code, the majority of the institutional investor signatories have committed to the statement of the stewardship codes and improved their reporting as well as their engagement with their investee firms (FRC, 2018). In addition, ICGN published its first stewardship code, 'ICGN Global Stewardship Principles', in 2016 in order to enhance the engagement of international institutional investors and their investee firms across the globe

(ICGN, 2016). Schnatterly and Johnson (2014) found that, due to the institutional pressure, institutional investors prefer companies with a good governance structure (i.e. higher board independence).

The stakeholder theory suggests that a firm is required to take into account the interests of all the stockholders to maximise its value (Freeman, 1984). The main assumption of the theory states that the survival of the firm is largely dependent on its stakeholders (Hill and Jones, 1992). According to Freeman (1984), stakeholders can be defined as any groups or individuals who can affect or be affected by the firm. In this case, given the activism and the size of institutional investor groups around the globe, their investee firms are expected to maintain their views and suggestions with regard to the structure of the corporate governance. Integrating the above empirical evidence and the theoretical assumptions drawn from the agency, stewardship, institutional and stakeholder theories, I posit that institutional investors, through their engagement with investee firms, will improve the attributes of a corporate board and its key subcommittees.

H1. *The higher the presence of institutional investors, the better the corporate governance in their investee firms.*

‘Better corporate governance’ is measured by the Board Attributes Index (GOV₁₄) as explained in Table 6.4.

5.2.1. Board and Key Subcommittees Composition

As one function of board monitoring is the reduction of agency costs, great attention has been paid to the composition of corporate boards (Fama and Jensen, 1983). Eisenhardt (1989), from the perspective of the agency theory, stated that the role of the corporate board is to monitor the managers on behalf of the shareholders and ensure that shareholders’ interests are aligned with those of the managers. The monitoring role of the board relies on the independent directors who can play an important role in mitigating agency costs and balance the interests of managers

and shareholders (Fama and Jensen, 1983; Rosenstein and Wyatt, 1990). It is argued by Adams and Ferreira (2007), that the monitoring quality of a corporate board is determined by the effectiveness of its independent directors. From the perspective of agency theory, a board and its key subcommittees (audit, compensation and nomination) should possess a majority composition of independent directors, as these members are considered to be the key figures of a corporate board and are responsible for monitoring the actions of firm managers (Hermalin and Weisbach, 2003). Board composition is also regarded as a central issue related to corporate governance codes around the world. According to Mallin (2016), national and international corporate governance bodies across the globe recommend that a board be largely composed of independent directors and that key subcommittees (audit, compensation and nomination) be primarily (or even entirely) comprised of independent directors. Using a sample of US-based insurance companies in operation between 1992 and 1993, Beasley and Petroni (2001) found that the greater a board's independence, the higher the likelihood that the firm would be audited by one of the Big 6 accounting firms; this indicates that an auditing company that is independent from a company's management system is more likely to be hired if the board demonstrates greater independence. Furthermore, Osma (2008) discovered that independent directors reduced the likelihood of accounting accrual manipulation; an examination of all UK-based non-financial firms between 1989 and 2002 led Osma to conclude that independent directors had the expertise and competence to efficiently monitor earnings management. Using a sample taken from the S&P 1500 in 2006, Sharma (2011) found that the higher a board's independence, the higher the dividends paid to shareholders. This result illustrates that independent directors are more likely to protect shareholder interests. Additionally, Ben-Amar and Zeghal (2011) reported that board independence was associated with improved information disclosure concerning the compensation of executives in Canadian-listed firms.

Considering the composition of a board's key subcommittees (audit, compensation and nomination), academic studies have shown that independence can contribute to the effectiveness of decisions issued by the corporate board as a whole (Anderson and Reeb, 2004). In line with the agency theory, the establishment of the board's key subcommittees allows more involvement of the independent directors to monitor and represent the interest of the shareholders (Brennan and McDermott, 2004). Previous research on board committees' structures revealed that independent directors can only perform effective monitoring if they are involved in the appropriate subcommittees (see Klein, 1998). Empirical evidence showed the fruitful outcome of the subcommittees' compositions. For instance, examining a sample of US-listed firms in operation between 1999 and 2003, Persons (2009) found that firms with a greater number of independent directors on their audit committees were associated with earlier voluntary ethics disclosures and were less likely to be engaged in financial reporting fraud. Investigating a selection of 500 firms listed in the major US stock exchanges, Abbott and Parker (2000) found that firms with a greater level of independence among their audit committee members were more likely to select large auditing firms to carry out their annual audits. A study of 492 US firms in 2001 by Abbott et al. (2003) uncovered an inverse relationship between audit committee independence and financial restatement. Additionally, Klein (2002) found that a higher level of independence among boards and audit committees resulted in decreased earnings management in US-based firms; this illustrates the argument that independent directors play a significant role in scrutinising the process of financial reporting. Using US Fortune firms as a sample, Newman and Mozes (1999) reported that CEOs were likely to receive excessive compensation packages when insiders dominated compensation committees at the expense of shareholders; this result calls for a greater number of independent directors to sit on compensation committees in order to facilitate the proper monitoring of compensation schemes. It is also the case that when a nomination committee is

dominated by independent directors, a board is more likely to appoint more skilful independent directors who are better able to monitor managers and enhance the decisions issued by the board (Vafeas, 1999a). Therefore, given the role of institutional investors in mitigating agency cost and the importance of independent directors in corporate boards and their key subcommittees, I posit the following hypotheses:

H2a. *The higher the presence of institutional investors, the higher the independence of the board.*

H2b. *The higher the presence of institutional investors, the higher the independence of the board's key subcommittees.*

‘The independence of the board’ is measured by the proportion of independent directors on the board.

‘The independence of the board's key subcommittees’ is measured by the proportion of independent directors on the board's key subcommittees.

5.2.2. Board and Key Subcommittees Activity

Board activity is another key factor of corporate governance that is used to measure a director's level of diligence and commitment to a firm. From the theoretical lens of the agency theory, the activity of the corporate board and its key subcommittees highlights the directors' commitments towards the shareholders' interests, which contributes to the reduction of agency costs (Vafeas, 1999b). Lipton and Lorsch (1992) investigated the relationship between board meeting frequency and the effectiveness of board monitoring and found that boards who held frequent meetings were more active and thus ensured that a firm was operated according to the best interests of its shareholders; this indicates that improved monitoring reduces agency costs. Bebchuk and Weisbach (2010) argue that board meetings help outside directors to obtain the required information about company activities, which in turn influences the quality of

monitoring and decision-making. An increased number of meetings has been shown to lead to the sharing of information among directors, which in turn leads to better decision-making (Bianco et al., 2015). Moreover, increased meeting frequency on the part of a corporate board and its key subcommittees enables that board to better monitor managers and thus to increase firm performance (Brick and Chidambaran, 2010). Furthermore, Vafeas (1999b) found that firms that engaged in frequent board meetings witnessed improvements to their operating performance. Lin et al. (2014) further found that the board attendance rate was positively associated with firm performance; this suggests that such an attendance rate signals a high quality of supervision, which in turn improves the performance of a firm.

At the key subcommittee level, the increased meeting frequency of various monitoring committees of a board enables them to efficiently fulfil their duties. Xie et al. (2003) found that active audit committees were associated with weaker earnings management, thus indicating that audit committees who hold frequent meetings are able to better monitor the financial reporting process, which in turn prevents earnings management. Cheung et al. (2010) found that frequent committee meetings were positively associated with both higher stock returns and lower levels of risk. Additionally, Hoque et al. (2013) reported a positive association between financial performance and the frequency of meetings held by audit and remuneration committees. Furthermore, it has been shown that audit committees who hold more frequent meetings are able to proactively allocate additional external audit resources towards a particular auditing issue in a timely fashion (Abbott et al., 2003). Hence, as the increased frequency of corporate board and key subcommittee meetings results in improved governance outcomes, I posit that institutional investors will play a role in the improvement of board activities as well as those of its key subcommittees.

H3a. *The higher the presence of institutional investors, the higher the activity of the board.*

H3b. *The higher the presence of institutional investors, the higher the activity of the board's key subcommittees.*

‘The activity of the board’ is measured by the total number of meetings held by the board.

‘The activity of the board's key subcommittees’ is measured by the total number of meetings held by the board's key subcommittees.

5.2.3. Board Entrenchment (Tenure)

The period of time during which a director serves on a board has received significant attention from academic scholars; thus far, the study of director tenure has resulted in mixed evidence in terms of board effectiveness and functionality. Given the experience perspective, for instance, Vafeas (2003) proposed that directors who enjoy a long period of service on a board are better informed about the firm and the environment in which the company operates, resulting in greater levels of commitment and allowing the board members to become more effective monitors of management figures. This view is consistent with the findings of Dou et al. (2015), who discovered that long-serving directors were associated with improved board meeting attendance, greater committee membership and lower CEO pay in US firms. Furthermore, Beasley's (1996) study of 150 public US firms found that as the tenure of an outside director increased, the occurrence of financial statement fraud decreased; this demonstrates that long-serving directors possess a greater ability to scrutinise the actions of top management than do their newer counterparts.

In contrast to this view, other scholars have revealed that long-serving directors are more likely to have established friendships with managers; this may limit their ability to properly monitor the actions of management and to protect shareholder interests. From the theoretical framework of agency theory, lengthy tenured directors may shift the director's allegiance from shareholders to the executives, contributing to lower monitoring and increased agency costs

(Miller, 1991). This is consistent with Hillman et al. (2011), who argue that directors who serve on boards for long periods reduce their degree of independence and their ability to monitor the management. For example, Boone et al. (2002) examined a sample, taken over 25 years, of the five largest newspaper companies in the Netherlands and found that long-tenured directors restricted the appointment of new directors to a board, which resulted in a lack of diversity and ineffective decision-making. Based on a study of various S&P 1500 firms, Berberich and Niu (2011) found that director tenure was positively associated with governance problems in overseen firms, thus indicating a need to limit directors' length of service. Barroso et al. (2011) further discovered that a long-tenured board did not support firm diversification in Spanish companies, thus suggesting that long-serving directors are likely to operate according to routines that are formed over time; thus, such directors are limited to specific environments, which makes their knowledge less valuable as the years progress. Consulting a sample of US-listed firms taken from 2001 to 2006, Jia (2016) found that companies with a higher percentage of directors with extended tenures were associated with lower innovation productivity. She also argued that when the proportion of long-tenured directors decreased due to director deaths, higher innovation performance ensued.

Aside from board tenure, CEO tenure has also received much attention from scholars, which suggests that it plays an important role in influencing the decisions delivered by a board (Hambrick and Fukutomi, 1991). Entrenched managers may establish certain strategies that enable them to increase their own benefits while neglecting the interests of shareholders. To this end, Miller (1991) claimed that CEO tenure may lead to deviation from the firm environment, which adversely affects organisational performance. Furthermore, a long-serving CEO may influence the director selection process, as such figures are more likely to have established close relationships with other directors on the board (Finkelstein and Hambrick, 1996; Cook and Burrell, 2013). Based on their analysis of a sample of US firms drawn from

1993 to 2004, Bebchuk et al. (2011) reported that the exercise of CEO power led to lower firm performance, which in turn contributed to increased agency costs. Following a study of US public firm performance between 1993 and 1999, Grinstein and Hribar (2004) found that CEOs who held greater power tended to negotiate larger merger deals; thus, their acquisition announcements sent negative signals to the market. In the context of imposing term limits on the members of a board of directors, a growing number of countries have adopted tenure-related guidelines. In the UK, for instance, the Corporate Governance Code requires that firms annually illustrate their rationale for determining that a director who has served more than nine years still qualifies as an independent director (see FRC, 2014). Given the above argument on long-tenured directors, I posit that institutional investors play a role in reducing directors' entrenchment.

H4. *The higher the presence of institutional investors, the lower the board entrenchment.*

'Board entrenchment' is measured by the average tenure of board members and the CEO's tenure.

5.2.4. Board Busyness

Board busyness refers to a situation in which a director holds multiple appointments to several boards. A common view among governance regulators is that directors who serve on a high number of boards are over-committed and have a limited ability to adequately monitor members of the management (Jiraporn et al., 2009). Thus, according to agency theory, director over-commitment and a lack of monitoring results in a weak governance structure and greater agency costs (Andres et al., 2013). Supporting this view, Lin et al. (2014) argued that overcommitted directors have less time to support the management team in developing business plans; their limited availability adversely affects their ability to detect managerial self-interest motives, contributing to the increase of agency costs. Fama and Jensen (1983) stated that service on high number of boards is a sign of director reputation and quality. They further

argued that directors who hold multiple appointments may be better advisors and can monitor management more efficiently than their counterparts. These characteristics also enable them to build their reputations and acquire additional directorships in the future (Shivdasani and Yermack, 1999). A number of studies have supported the idea that there are significant benefits associated with the holding of multiple directorships (Rosenstein and Wyatt, 1994; Ferris et al., 2003; Field et al., 2013).

Conversely, other scholars have argued that board busyness brings unfavourable results that negatively affect the performance and governance structure of a firm. For instance, Jiraporn et al. (2009) studied the relationship between board busyness and board meeting attendance in US-listed firms from 1998 to 2003 and found that directors with multiple board appointments were more likely to be absent from board meetings. These results are also supported by the work of Masulis and Mobbs (2014), who studied a sample of S&P 1500 firms from 1997 to 2006 and found that busy directors chose to spend their time and energy inequitably, granting unequal attention to each firm for whom they sat on a board. They found that busy directors attended more meetings and offered better monitoring for the firm that carried greater prestige and thus captured their time and energy. Using a sample of the largest firms listed in the Forbes 500 between 1989 and 2005, Fich and Shivdasani (2006) examined the effect of board busyness on firm performance and found that busy boards resulted in poor governance, weaker profitability and a lower sensitivity of CEO turnover to firm performance. They also reported that when busy outside directors departed from a board, positive abnormal returns were noted. Core et al. (1999) found that busy outside board directors were positively associated with greater CEO compensation in US public firms, thus resulting in higher agency costs. Hence, given the implication of the directors being overcommitted, institutional investors as active monitors are expected to decrease the number of directorships in their investee firms. Thus, I hypothesise that:

H5. *The higher the presence of institutional investors, the lower the board busyness.*

‘Board busyness’ is measured by the average directorship held by independent directors and the proportion of independent directors who hold three or more directorships in public firms.

5.3. Institutional Investors and Board Diversity

A diverse board is one wherein members have heterogeneous characteristics in terms of gender, age, ethnicity, experience and professional background (Anderson et al., 2011). Diverse boards are commonly recognised as being more likely to provide a wide range of experience, knowledge and competence as compared to homogeneous boards (Buse et al., 2016). Board diversity is an effective tool in corporate governance, as it creates value for a corporate board by enhancing the decision-making process (Adams and Ferreira, 2009; Anderson et al., 2011), improving managerial monitoring (Kim et al., 2013), satisfying the needs of stakeholders (Harjoto et al., 2015) and drawing additional attention to the ethical aspects of firm activities (Hafsi and Turgut, 2013). The increasing importance of corporate governance codes and government agencies, in conjunction with insistence from social activists, imposes greater pressure on firms to promote the improved diversity of their boards (Anderson et al., 2011; Farag and Mallin, 2016a).

Board diversity is traditionally underpinned by two main theories: resource dependence theory (Pfeffer and Salancik, 1978) and agency theory (Jensen and Meckling, 1976). These two theories are related to the service and control task of the board, respectively (Forbes and Milliken, 1999). Drawing on the agency theory, Hillman and Dalziel (2003) and Adams and Ferreira (2009) stated that corporate boards with an appropriate mix of experience and background have a better ability to monitor managerial behaviour and assess business strategies. This is consistent with Carter et al. (2003), who argue that directors with different genders, ethnicities, or cultural backgrounds might ask questions that might not come from directors with traditional backgrounds. This indicates that boards with diverse directors might

be more active and have better monitoring roles compared to non-diverse boards. Consistent with Farag and Mallin (2017), the resource dependence theory provides the theoretical foundation for board diversity and suggests that boards with diverse directors have a broader range of skills and more talented and well-connected directors.

Using the Russell index³¹, Anderson et al. (2011) analysed the impact of board diversity on firm performance between 2003 and 2005. Their results revealed that diverse boards enhanced firm performance, and firms that operated in complex environments exhibited greater demand for heterogeneous directors. Furthermore, using a sample of US-listed firms in operation from 1999 to 2011, Harjoto et al. (2015) found that boards whose members had varied characteristics were positively associated with corporate social responsibility, thus indicating that heterogeneous board members enhance a firm's ability to satisfy stakeholders. More recently, Mallin and Farag (2017) examined the relationship between board diversity and firm performance using FTSE all-shares from 2004 to 2013; their results revealed that diverse boards drove improved firm performance in UK-listed firms.

Given the level of fiduciary responsibility held by institutional investors, I posit that such parties will view board diversity as an issue to be improved when considering the composition of their investee firms' corporate boards. Hence, the next hypothesis is formulated as follows:

H6. *The higher the presence of institutional investors, the higher the diversity of the board.*

'Diversity of the board' is measured by the Board Diversity Index (BDI₁₆) as explained in Table 6.5.

5.3.1. Board Gender Diversity

The gender diversity of corporate boards has received special attention and is one of the most studied topics in the field of demography diversity (Terjesen et al., 2009). Recognition of the

³¹ Represents the 1,000 largest US-listed firms with higher market capitalisation levels (Servaes and Tamayo, 2013).

importance of gender diversity has driven a number of countries to introduce compulsory legislation mandating the adoption of gender quotas for the boards of public firms (Terjesen et al., 2015a)³². In accordance with the agency theory, the presence of female directors on a corporate board may improve the board's monitoring ability, which in turn will trim down agency costs (Carter et al., 2003; Farag and Mallin, 2016b). From the perspective of the resource dependence theory, women directors may bring different resources and benefits to the company (Carter et al., 2010). This is consistent with Mateos de Cabo et al. (2012), who argue that women directors are likely to bring new opinions and perspectives which may improve and enhance firm performance. The enactment of gender-quota legislation in several countries has created pressure on corporate boards to employ more women on their boards (Grosvold and Brammer, 2011; Terjesen et al., 2015b), thus exemplifying the institutional theory (Scott, 2004). For instance, ten countries³³ have enacted quotas for female representatives on the corporate boards of public firms and state-owned businesses ranging from thirty-three to fifty percent with various sanctions, while fifteen countries³⁴ have introduced gender quotas under a system of 'comply or explain' (Terjesen et al., 2015b). The growing significance of government agencies and corporate governance codes and the demands of social activists puts additional pressure on firms to promote board diversity (Anderson et al., 2011; Farag and Mallin, 2016a).

It has been argued that women are more committed to their board responsibilities; this claim is supported by their higher rates of attendance (Adams and Ferreira, 2009), their greater risk aversion (Byrnes et al., 1999) and their increased conservatism when making investment decisions (Bernasek and Shwiff, 2001) as compared to their male counterparts. Carter et al.

³³ Norway, Spain, Finland, Quebec (Canada), Israel, Iceland, Kenya, France, Italy and Belgium.

³⁴ Australia, Austria, Denmark, Germany, Ireland, Luxembourg, Malawi, Malaysia, Netherlands, Nigeria, Poland, South Africa, Sweden, United Kingdom and United States.

(2003) examined Fortune 1000 firms in 1997 and reported a positive association between the gender diversity of a board and that firm's financial performance. Srinidhi et al. (2011) examined a sample of US-listed firms between 2001 and 2007 and reported that gender-diverse boards were associated with higher-quality earnings. This indicates that female participation in corporate boards leads to the improved oversight of manager reporting.

Torchia et al. (2011) examined a sample of Norwegian-listed firms and reported that a greater presence of female directors on a board led to a higher level of innovation within the firm. After investigating a sample of Chinese-listed firms in operation between 2001 and 2010, Cumming et al. (2015) found that a greater presence of female directors on a corporate board correlated with a reduced likelihood that a company would commit fraud or violate securities regulations. Their results also indicated that the presence of women on a board reduced the severity of fraud; this effect was even stronger in male-dominated industries. Francoeur et al. (2008) analysed a sample of the 500 largest Canadian firms between 2001 and 2003 and reported that a female board presence had a positive association with abnormal returns, especially for firms operating within a complex environment. Lucas-Pérez et al. (2015) examined a sample of Spanish-listed firms in operation between 2004 and 2009 and reported that a greater presence of female directors on a board correlated with a higher likelihood that manager compensation schemes would be properly designed and linked to firm performance. Given the need for female directors to join the ranks of corporate boards, I posit that institutional investors play a role in the improvement of board gender diversity.

H7. *The higher the presence of institutional investors, the higher the gender diversity of the board.*

'Gender diversity of the board' is measured by the proportion of female directors serving on the board.

5.3.2. Board Age Diversity

Heterogeneity of board directors' ages may prevent groupthink and improve monitoring by balancing the energy and enthusiasm of younger directors with the experience and risk aversion of older directors (Ararat et al., 2015). According to the resource dependence theory, a firm with a homogenous board may display poor performance because it lacks the required mixture of skills and expertise. Age diversity is seen as one of the important characteristics that provides a greater range of opinions and expertise to the corporate board (Ali et al., 2014). Supporting this view, Hafsi and Turgut (2013) argued that age diversity in the corporate board is likely to bring more balanced decision-making that considers the interests of the firm's various stakeholders. Companies who target customers of various ages should hire directors of multiple age groups; such an age diverse board will provide a firm with a variety of perspectives that will positively impact the company's reputation and financial outcomes (Fombrun, 1996; Kang et al., 2007). This is consistent with Jhunjhunwala and Mishra (2012), who argue that a board that is dominated by older directors may lack knowledge of current technologies.

Several studies have reported that age diversity in corporate boards improves governance outcomes. For instance, Goergen et al. (2015) examined a sample of the largest German-listed firms in operation between 2005 and 2010 and found that the greater the age difference between the CEO and company chair, the better the monitoring and performance of the firm. Consistent with this view, Ararat et al. (2010) examined Turkey's largest firms and reported that greater age diversity was positively associated with firm valuation, thus indicating that board age diversity increases the monitoring of managers' actions and therefore alleviates agency problems. Furthermore, upon examining Mauritanian-listed firms in 2007, Mahadeo et al. (2012) found that firms with directors of diverse ages were positively associated with enhanced short-term performance. Analysing Korean-listed firms from 1999 to 2006, Kim and Lim

(2010) reported that firms whose independent directors were of diverse ages were associated with higher levels of firm performance. Hence, the next hypothesis is formulated as follows:

H8. *The higher the presence of institutional investors, the higher the diversity of directors' ages.*

'The diversity of directors' ages' is measured by the standard deviation of directors' ages divided by the mean age of all members of the board.

5.3.3. Board Nationality Diversity

The internationalisation of firms, whereby organisations operate across multiple countries, has led to a need to hire foreign directors who have the necessary knowledge and competence to link a firm to the environment in which it operates (Carpenter et al., 2001). The resource dependence theory considers the presence of international human resources as the most valuable and unique resources of a firm (Kaczmarek, 2009). With the increase of business diversification, firms demand dynamic resources that help to achieve a competitive advantage in the global capital markets (Katmon et al., 2017). Supporting this view, foreign directors can contribute valuable advice and bring foreign contacts to a company, thus allowing it to better understand the foreign market. This is especially beneficial to companies that engage in foreign operations or have plans for future international expansion (Adams et al., 2010). When companies expand their operations to other countries, they are likely to encounter a different legal, regulatory and cultural environment. For these firms, foreign directors who are native to the target country can be beneficial assets, as they are able to utilise their advantageous working knowledge of the local environment and of local customers' preferences (Masulis et al., 2012). Estelyi and Nisar (2016) examined sample of FTSE all-shares from 2001 to 2011 and found that UK-based firms whose boards had directors of diverse nationalities demonstrated improved operating performance. Their results also revealed that foreign directors were more likely to sit on a board's key subcommittees (on the compensation committee in particular),

which indicates that firms benefit from the experience of foreign directors when crafting compensation packages. Investigating a large sample of non-US firms, Miletkov et al. (2013) found that foreign directors were positively associated with firm performance, provided that they originated from a country with strong legal protections for investor rights. Thus, the next hypothesis is presented as follows:

H9. *The higher the presence of institutional investors, the higher the nationality diversity of the board.*

‘Nationality diversity of the board’ is measured by the proportion of foreign directors serving on the board.

5.3.4. Board Education Diversity

Board members with diverse educational backgrounds can bring multiple perspectives to a boardroom (Anderson et al., 2011). According to the resource dependence theory, an education-diverse board (level of education, e.g. postgraduate studies) may supply the corporate board with different viewpoints, cognitive paradigms and professional development (Anderson et al., 2011; Farag and Mallin, 2016b). The presence of heterogeneous education levels provides directors with different perspectives and insights that can be utilised to advance their career development and improve their social contacts (Anderson et al., 2011). Independent directors with advanced academic degrees and considerable work experience can convey insights to a board and thus contribute to the overall success of a firm (Terjesen et al., 2015b). Most corporate governance codes recommend that a company’s board establish committees to handle specific issues (i.e., audit, compensation, nomination and strategy committees). Therefore, a board should consider appointing directors with various educational backgrounds to its key subcommittees in order to facilitate the completion of specific tasks (Mahadeo et al., 2012).

Bell et al. (2010) conducted a meta-analysis and found that the inclusion of members with a variety of educational backgrounds tended to enhance the creativity, innovation and performance of a firm's top management team. Using a sample of non-financial Chinese-listed firms that initiated their IPOs between 1999 and 2012, Farag and Mallin (2016a) examined the relationship between board education diversity (as measured by the percentage of directors with postgraduate degrees) and firm performance. Their results revealed that boards with higher levels of education diversity were associated with better financial performance. Their results also indicated that directors with high levels of education brought different backgrounds and perspectives to their corporate boards. In addition, using a sample of twenty-five high-tech firms in the Fortune 500, Midavaine et al. (2016) investigated the effect to which board diversity (education, gender and tenure) influences firms to invest in research and development. The findings revealed that education and gender diversity are positively related to the investments in research and development, while tenure diversity is not. The study indicates that education-diverse boards tend to be more innovative and competitive. Therefore, the next hypothesis is formulated as follows:

H10. *The higher the presence of institutional investors, the higher the education diversity of the board.*

'Education diversity of the board' is measured by the proportion of directors with postgraduate degrees.

5.4. Chapter Summary

This chapter explained and developed the hypotheses used in this study. These hypotheses were divided into two groups: the first set focused on the role of institutional investors in the improvement of board attributes, while the second cluster concerned their role in improving board diversity. It is worth noting that these hypotheses will also be examined in light of different institutional environments, to include various economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. Table 5.1 provides a summary of the various hypotheses developed for this study.

Table 5.1 Hypotheses Summary

Institutional Investors and Board Attributes
H1. <i>The higher the presence of institutional investors, the better the corporate governance in their investee firms.</i>
H2a. <i>The higher the presence of institutional investors, the higher the independence of the board.</i>
H2b. <i>The higher the presence of institutional investors, the higher the independence of the board's key subcommittees.</i>
H3a. <i>The higher the presence of institutional investors, the higher the activity of the board.</i>
H3b. <i>The higher the presence of institutional investors, the higher the activity of the board's key subcommittees.</i>
H4. <i>The higher the presence of institutional investors, the lower the board entrenchment.</i>
H5. <i>The higher the presence of institutional investors, the lower the board busyness.</i>
Institutional Investors and Board Diversity
H6. <i>The higher the presence of institutional investors, the higher the diversity of the board.</i>
H7. <i>The higher the presence of institutional investors, the higher the gender diversity of the board.</i>
H8. <i>The higher the presence of institutional investors, the higher the diversity of directors' ages.</i>
H9. <i>The higher the presence of institutional investors, the higher the nationality diversity of the board.</i>
H10. <i>The higher the presence of institutional investors, the higher the education diversity of the board.</i>

Chapter 6

6.0 Research Design and Methodology

6.1. Introduction

The previous chapter presented and developed the hypotheses to be investigated in this research study. Subsequently, this chapter is designed to provide a clear explanation of the research methodology that will be used to investigate the role of institutional investors in the improvement of a board's governance structure (with regard to board attributes and board diversity). Additionally, this chapter also illustrates the methodology that will be used to test how this relationship presents within various institutional settings, to include multiple economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. First, the study's research philosophy and approach are illustrated, then the sample selection procedures, data source and research period are identified. Next, this chapter explains the variables (dependent, independent and control variables) used in this study. The main estimation method is then explained, followed by an examination of the empirical models used in this research. Finally, this chapter demonstrates the techniques used to confirm the main results of the study.

Thus, the chapter is structured as follows: section 6.2 discusses the research philosophy and approach, section 6.3 describes the sample selection processes and data sources, section 6.4 illustrates the utilised variables, section 6.5 explains the study's main estimation method, section 6.6 illustrates the models used in the study, section 6.7 presents the techniques used for the study's robustness tests, and section 6.8 concludes the chapter.

6.2. Research Philosophy and Approach

According to Saunders et al. (2016), research philosophy refers to 'a system of beliefs and assumptions about the development of knowledge'. It is beneficial to understand the different types of research philosophy, as the assumptions contained in such philosophy can influence the

research process of investigating ideas, collecting data, selecting research methods and analysing findings (Crotty, 1998; Bryman, 2012; Saunders et al., 2016). This is consistent with Johnson and Clark (2006), who claim that in business and management-oriented research we need to have philosophical commitments toward research strategy, as this will have significant influence not only on what we do, but also on how we understand what we are examining and investigating. In this section, research philosophies and research approaches will be illustrated. Saunders et al. (2016) believe that most researchers, when they start the research, mainly focus on the required data and the technique of collection, which is the centre of the research onion (see Figure 6.1). However, in order for research to be taken seriously, a researcher needs to justify why he or she selected a particular method of data collection and research analysis (Crotty, 1998). Therefore, there are some important outer layers of the onion that a researcher needs to understand and justify rather than peel and throw away.

Saunders et al. (2016) claim that the researcher, while conducting his or her research, will make a number of assumptions at every stage of the research process. These include assumptions about human knowledge (epistemological assumptions), about the realities encountered while doing research (ontological assumptions) and the extent and ways values influence the research process (axiological assumptions). The choice of which research philosophy is more relevant depends on the epistemological, ontological and axiological assumptions of the research. Understanding these philosophical assumptions helps the researcher to clarify issues related to the research design, including what types of data or evidence are required, collected and interpreted. They also help the researcher to understand and answer the research questions (Bryman, 2012). Furthermore, according to Saunders et al. (2016), these philosophical assumptions can also help to constitute a credible research philosophy that underpins the methodological choice, research strategy, data collection techniques and analysis procedures,

which in turn help the researcher to design a coherent research project in which all the elements fit together.

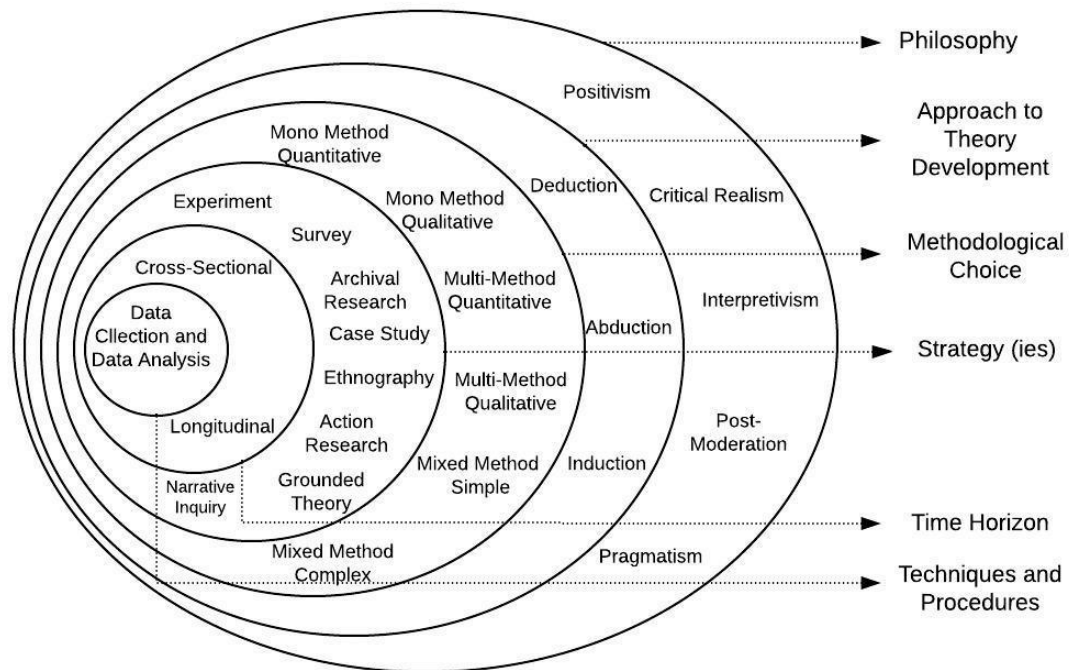
Ontology is concerned with the nature of reality. Blaikie (2000, p.8) defines ontology as ‘claims and assumptions that are made about the nature of social reality, what exists, what it looks like, what units make it up and how these units interact with each other. In short, ontological assumptions are concerned with what we believe constitutes social reality’. Gill and Johnson (2010, p.100) define ontology as the ‘branch of philosophy dealing with the essence of phenomena and the nature of their existence’. According to Burrell and Morgan (1979), the ontological assumption describes views on the nature of reality and asks specifically whether this is an objective reality that exists or is only created subjectively in our minds. Thus, ontology assists in finding out whether certain phenomena are real or illusive.

The second assumption is epistemology, which considers what constitutes acceptable knowledge in the field (Saunders et al., 2016). Epistemology answers the following question: how do we know whether or not a particular claim can be deemed acceptable? ‘That is, what do we mean by the concept “truth” and how do we know whether or not some claim is true or false?’ (Gill and Johnson, 2010 p.191). In order to best answer such questions, the researcher should look for evidence that enables him or her to validate the claim or reject it. In epistemological studies, the researcher may justify what they believe in their own way, which might be different from the justifications other researchers have (Saunders et al., 2016).

The third assumption is axiology, which refers to the role of values and ethics shaping the research process (Saunders et al., 2016). This incorporates questions about how the researcher treats his own values or those of the participants. Heron (1996) notes that all human actions are guided by values. For instance, choosing one topic over the other suggests that you think a particular topic is more important than the other. The same occurs when you place greater

importance on the data obtained through an interview, suggesting that you value personal-interaction data more than the data obtained through questionnaires.

Figure 6.1 The research onion



Source: Saunders et al. (2016)

Saunders et al. (2016) note that research philosophy in business and management can be classified into five types: positivism, interpretivism, critical realism, post-moderation and pragmatism (Figure 6.1).

Positivism considers the utilisation of the experimental, scientific observations to justify and test the causal effect relationship (Creswell, 2003). This is consistent with Saunders et al. (2016), who note that positivists believe that people and societies can be investigated in a natural, scientific manner, and they prefer to collect the data about an observable reality to investigate causal relationships. Neuman (1997) posits that positivist research discovers causal laws that can be used to predict general patterns of human activity. Therefore, the need for the formulation of hypotheses is emphasised when conducting empirical testing to search for persuasive

explanations of the causal relationships (Easterby-Smith et al., 2002), which can then be generalised to the wider population. In contrast, interpretivism is more subjective in terms of understanding differences between humans as social actors (Saunders et al., 2009). An interpretivist researcher will observe, look or listen and then interpret what he or she sees. The research approach or strategy applied under such assumptions will constitute the study of the social world, the people and their institutions, as opposed to that of positivism and natural sciences (Bryman and Bell, 2007).

Critical realism focuses on explaining what we see and experience in terms of the underlying structures of reality that shape observable events. For critical realists, the reality is seen as external and independent but not directly accessible through research observations and knowledge. According to Reed (2005), critical realism claims that there are two steps to understand the world. First, there are sensations and events that we experience. Second, there is mental processing that functions after the experience that helps the researcher to justify the reason associated with the underlying reality that caused the experience.

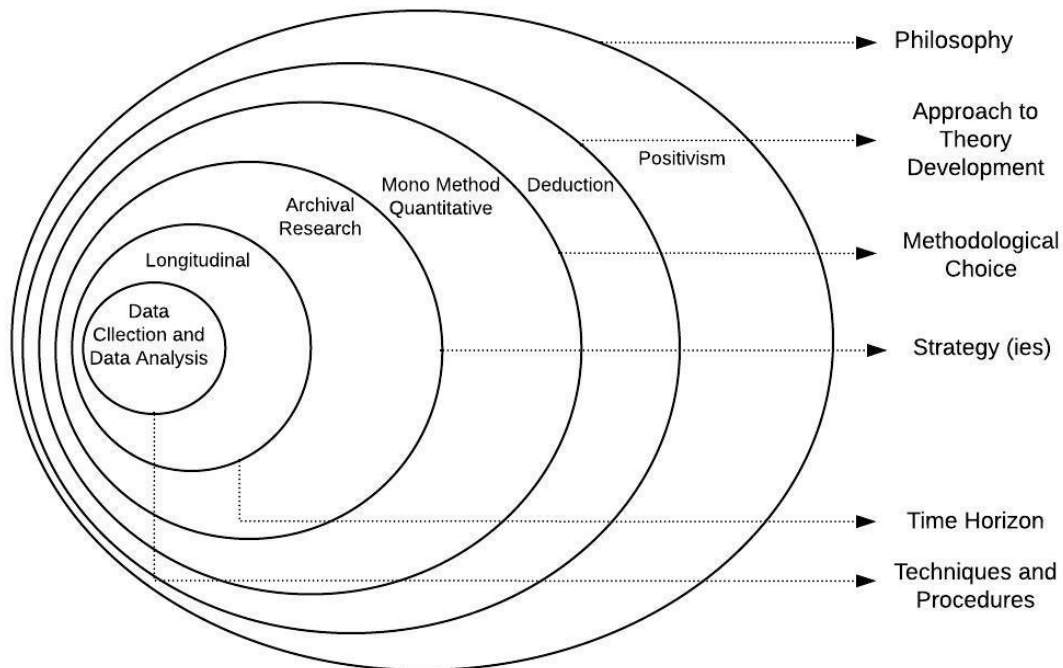
Post-moderation emphasises the role of language and of power relations, seeking to question accepted ways of thinking and giving voice to alternative, marginalised views (Saunders et al., 2016). Chia (2003) posits that the postmodernists believe that any sense of order is provisional and foundationless and can be only brought about through our language with its categories and classifications.

According to Kelemen and Rumens (2008), pragmatism asserts that concepts are relevant and acceptable only when they support actions. Reality matters for the pragmatists as practical effects of ideas, and knowledge is valued for enabling actions to be carried out successfully (Saunders et al., 2016). Pragmatists also believe that there are several ways to interpret the world and undertake research, and they emphasise that no single point can solve or explain the whole picture, as there are several realities linked to it (Saunders et al., 2016).

Given the above discussion of the research assumptions and the associated philosophies, this empirical study relies on an epistemological-positivist position. In this study the main question is about the role of institutional investors in the improvement of corporate governance and whether this relationship is determined by the institutional settings, including economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. Therefore, in order to investigate such questions, the researcher needs to collect archival data in order to investigate the causal relationship between institutional investors and corporate governance. This is consistent under the epistemology assumption.

Positivists argue that knowledge can be predicted and justified by observing the regularities of actions and the causal relationships between elements in the populations (Burrell and Morgan, 1979). This can be done by adopting the theories to construct a testable hypothesis which is then investigated to further develop these theories (Bryman, 2012). Therefore, accepting or rejecting these hypotheses is expected to contribute to the development of the examined theories (Bryman, 2012). In this research, several theories have been determined (i.e. agency theory, stewardship theory, resource-dependence theory, institutional theory and stakeholder theory) that are used to develop a set of hypotheses, as illustrated in the previous chapter. Furthermore, this research adopts the quantitative-research approach, and the archival data (secondary data) is collected to fulfil the research objectives (Creswell, 2009). Figure 6.2 illustrates the onion of this research. The data collection methods, the variables and the statistical methods that are used in a spirit of positivism in this study are discussed in the following sections.

Figure 6.2 The study's research onion

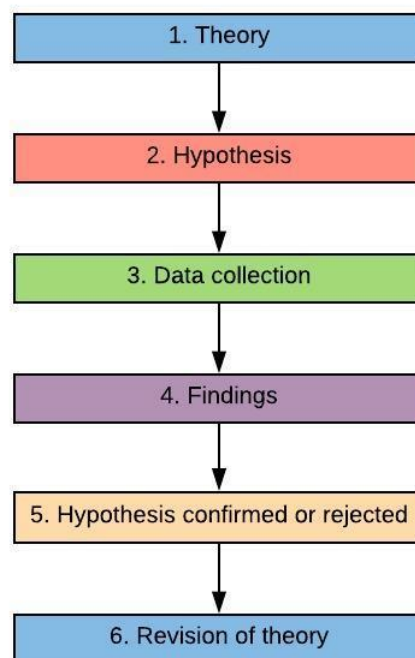


Source: Adapted from Saunders et al. (2016)

Determining the research approach is also a crucial step. Saunders et al. (2016) emphasise that there are three approaches of research: deductive, inductive and abduction. If you start with the theory/ies which normally develop from reading the academic literature, and you design your research to test the theory/ies, then you are following the deductive approach. Conversely, if you follow the opposite path by collecting the data to explore a particular phenomenon, and then you try to generate a new theory/ies, then you are following the inductive approach. However, if you collect data to explore phenomena, to generate or modify an existing theory/ies which subsequently is tested by additional data collection, then you are adopting the abductive approach. The deductive approach was adopted in this study. This is consistent with Ticehurst and Veal (1999), who argue that positivists typically adopt the deductive approach in their studies. The researcher started by reviewing the literature and then determined which theories explain the causal relationship between institutional investors and corporate governance (i.e. agency theory, stewardship theory, resource-dependence theory, institutional theory and

stakeholder theory). Then a set of hypotheses was developed, and appropriate archival data (secondary data) were collected to conduct the appropriate research. Based on the findings, the researcher decided whether to accept or reject the hypothesis, and the theory/ies were reviewed accordingly. Figure 6.3 explains the process of the deductive approach.

Figure 6.3 The process of deductive approach



Source: Bryman (2012)

6.3. Sample Selection and Data Collection

The scope of this research is international, involving companies listed in the major stock indices of 15 countries between 2006 and 2012. The main units of analysis are institutional ownership (total, domestic, foreign, common and civil) and the corporate boards of investee firms in the sample countries.

6.3.1. Sample and Selection Criteria

This research considers firms listed in the major stock indices of 15 countries around the world (see Table 6.2). The research sample comprises 10 civil law countries and 5 common law countries. The indices encompass firms with the highest levels of market capitalisation in each country. Accordingly, various selection criteria were imposed, which are as follows:

- (1) Financial firms (6000–6999) were excluded from the sample, as they abide by different regulations and reporting rules than do other types of listed firms.
- (2) Firms/years with missing data were excluded from the sample.
- (3) Firms with outlier observations were excluded.

The sample selection and exclusion criteria are summarised in Table 6.1. After taking into account all exclusion criteria, the final dataset was comprised of an unbalanced panel of 517 firms in operation from 2006 to 2012 (the list of firms considered in the study are provided in Appendix one)³⁵.

Table 6.1 Sample Selection Criteria

Criteria	Number of firms
Total unique number of firms listed in the major stock indices	760
Exclude financial firms	172
Exclude firms with missing data	64
Exclude firms with outlier observations	7
Final number of firms considered in the study	517

Table 6.2 describes firm statistics per country, index and year as well as the percentage of observations out of the total number of observations used in the study. It is clear that larger numbers of observations derive from the firms of the UK, Canada, France and Australia, while lesser numbers of observations originate from companies in Belgium, Denmark, Switzerland and Ireland.

³⁵ For this study, data from the US (S&P100) were also collected. After considering the sample selection criteria detailed in Table 6.1, a total of 105 US firms were considered in the study. However, following previous studies (see, for example, Ferreira and Matos, 2008; Aggarwal et al., 2011), only non-US observations were included in the main analysis.

6.2. Firms Statistics by Country and Year

0.2. Firms Statistics by Country and Year												
SN	Country	Index Name	Number of firms per year							Total Firms	Total Observations	Percentage (%)
			2006	2007	2008	2009	2010	2011	2012			
Civil Law Countries												
1	Belgium	BEL 20	12	12	13	13	13	12	13	16	88	3
2	Denmark	OMX 20	13	12	13	12	13	13	13	18	89	3
3	Finland	OMX 25	19	21	20	20	23	22	21	26	146	6
4	France	CAC 40	32	31	31	30	31	33	34	38	222	9
5	Italy	FTSE MIB	19	20	20	19	18	19	18	25	133	5
6	Netherland	AEX	17	18	18	19	19	20	20	26	131	5
7	Norway	OBX	17	19	21	21	20	22	23	32	143	5
8	Spain	IBEX 35	22	23	24	24	24	26	24	34	167	6
9	Sweden	OMX 30	19	20	22	23	23	22	21	25	150	6
10	Switzerland	SMI	17	13	13	13	14	12	13	20	95	4
Common Law Countries												
11	Australia	S&P/ASX 50	24	25	30	35	30	29	29	42	202	8
12	Canada	S&P/TSX 60	42	45	44	44	45	49	48	61	317	12
13	India	BSE 30	6	13	19	22	22	23	22	31	127	5
14	Ireland	ISEQ	10	10	10	14	15	16	17	20	92	4
15	United Kingdom	FTSE100	63	66	67	68	74	70	76	103	484	19
Total			332	348	365	377	384	388	392	517	2586	100

Table 6.3 depicts the distribution of the sample according to industry type. The table indicates that the sample data can be classified as belonging to nine different industries³⁶. It is evident that the sample comprises a higher number of firms from the industrials, basic materials and consumer services industries (the percentages of firms belonging to the aforementioned industries are 21%, 16% and 16%, respectively). All other industries (consumer goods, health care, oil and gas, technology, telecommunications and utilities) represent 5% to 12% of the total sample.

³⁶ This industry classification was obtained from the DataStream database.

Table 6.3 Industry Distribution by Number of Firms

SN	Industry name	Number of firms	Percentage (%)
1	Basic Materials	84	16
2	Consumer Goods	63	12
3	Consumer Services	82	16
4	Health Care	34	7
5	Industrials	109	21
6	Oil & Gas	63	12
7	Technology	24	5
8	Telecommunications	24	5
9	Utilities	34	7
Total		517	100

6.3.2. Data Source

This research utilises secondary data for several reasons. First, according to Walliman (2011), secondary data is often produced by well-known databases in which expert researchers are employed to build up this type of data. Second, secondary data are cost effective, as it reduces the amount of time required to complete a study, especially a study that utilises an international sample. Third, secondary data has the advantage of leading to a wide range of information that has been collected over a significant period of time, which enables a researcher to track the behaviour of firms over a long period.

For this study, several sources to extract the required data were used. First, data related to corporate board characteristics were obtained from the BoardEX database. Second, the Thomson One database was consulted in order to extract ownership data. Third, the Worldscope database was used to collect financial data; and finally, firms' annual corporate governance reports were examined to extract any missing data that was not available in the aforementioned databases³⁷. Access to all of these databases was granted by the University of East Anglia.

³⁷ Various other sources were also consulted in order to obtain specific data. These include the World Bank Database (to obtain the GDP figures and rule of law indices for each country), the Major Depositary Institutes, the U.S. Stock Exchange (to obtain ADR listings) and the Institutional Brokers Estimate System (IBES) (to obtain numbers with respect to how many analysts follow a given firm).

6.3.3. Sample Period

This study adopted panel data estimation methods in an effort to examine information that spans seven consecutive years (2006–2012), (Greene, 2012; Mertens et al., 2017). This period was chosen for several reasons; first, considerable international growth in terms of institutional investor activity occurred during this period (Kim et al., 2016; Mallin, 2016). Second, this period was chosen in order to fully capture the role of institutional investors in the improvement of corporate governance within various economic conditions (pre-crisis, crisis and non-crisis periods). Following in the manner of previous studies, this study used the decline of GDP as an indicator of crisis within each country (Dimitras et al., 2015). This process resulted in a total of 959 firm observations during pre-crisis periods, 1,156 firm observations during periods of crisis, and 471 firm observations during post-crisis periods. Likewise, in order to investigate the role of institutional investors in the promotion of governance structures within various shareholder rights environments, the sample was divided into two groups; following the example of La Porta et al. (2000), these classifications were made based on the legal regimes of the countries in question. This process resulted in a total of 1,364 firm observations in civil law countries and 1,222 firm observations in common law countries. To test whether ownership structures affected the roles of institutional investors in the improvement of governance outcomes, we classified our sample into two categories, family- and non-family-owned firms, as per Croci et al. (2012). The researcher also applied interaction variables between institutional investors and controlling shareholders (for both family- and non-family-owned firms) to account for the influence of institutional investors in the promotion of governance structures under different ownership structures (i.e., Croci et al., 2012).

6.4. Variable Definitions

This section describes the variable definitions used in this study. Table 6.6 provides a detailed description of all variables (dependent, independent and control variables) as well as the data source of each of the variables. It is also worth noting that this study applied individual variables in conjunction with corporate governance indices to proxy the governance levels of the sample firms.

6.4.1. Dependent Variables

The dependent variables used in this study were divided into two groups, board attributes and board diversity variables, which are discussed below. Notably, this study's dependent variables were mainly represented by two corporate governance indices, the Board Attributes Index and the Board Diversity Index. However, following in the tradition of other studies that have criticised the corporate governance index (see, for example, Daines et al., 2010), this study also considered individual attributes when attempting to proxy the corporate governance levels of the sample firms. These attributes were related to board composition, activity, entrenchment and busyness (corporate board attributes) as well as gender, age, nationality and educational diversity (board diversity attributes).

The Board Attributes Index (GOV₁₄) was first used to proxy the governance structure of a board and its key subcommittees. This index covers the main attributes related to the structure and function of a corporate board and its key subcommittees. The Board Attributes Index (GOV₁₄) assigns a value of one to each of 14 selected attributes, provided that the company meets the criteria for each attribute; a value of zero is given if these criteria are not met (see Table 6.4). These attributes were mainly adopted from the index used by Aggarwal et al. (2011).

Table 6.4 Board Attributes Index (GOV₁₄)

1. Board size is greater than five but less than 16.
2. Board is controlled by more than 50% independent outside directors.
3. Board-approved succession plan in place for the CEO.
4. Board performance is reviewed annually.
5. Audit committee composed solely of independent directors.
6. Compensation committee composed solely of independent directors.
7. The majority members of nomination committee are independent directors.
8. All directors attended 75% of board meetings.
9. Chair and CEO positions are separated or there is lead director.
10. CEO is not serving on nomination committee.
11. Chair is INED.
12. Board is not busy (at least half of the INEDs hold \leq two directorships in public companies).
13. CEO is not busy (CEO holds \leq two directorships in public companies).
14. Chair is not busy (Chair holds \leq two directorships in public companies).

Board Composition was calculated using two different measures. The first measure concerns the percentage of independent directors sitting on a corporate board (Osma, 2008; Sharma, 2011), while the second measure involves the percentage of independent directors appointed to key subcommittees (audit, compensation and nomination) (as per Eminent and Guedri, 2010).

Board Activity was measured by determining the meeting frequency of a board and its key subcommittees (audit, compensation and nomination) (following the example of Brick and Chidambaran; 2010; Hoque et al., 2013).

Board Entrenchment was measured by calculating and combining two proxies: CEO tenure (Cook and Burrell, 2013) and average board tenure (Barroso et al., 2011).

Board Busyness was measured using two proxies: the average number of directorships held by independent non-executive directors (INEDs) and the percentage of INEDs who are busy (as per Cashman et al., 2012).

The Board Diversity Index (BDI₁₆) was constructed as a proxy of the diversity of a board in general. Table 6.5 explains the methodology used to construct the index (as per the work of Anderson et al., 2011 and Mallin and Farag, 2017). The Board Diversity Index consists of four main attributes: gender, age, nationality, and education. Each of these attributes was calculated

for each company for every year and then compared with the average attributes of the entire sample. Attributes were then classified and ranked into four quartiles, with scores ranging from one to four, with one representing least diversity and four representing maximum diversity. The final step was to calculate the score of each of the four board diversity index attributes. Data from 2012 for National Grid plc was used for illustration purposes in Table 6.5.

The first attribute, gender diversity, is measured according to the percentage of female members on the board. Of a total of 13 directors, National Grid's board had three female directors in 2012. Therefore, the percentage of female directors was 23%. After classifying the proportion of females for the whole study sample into four quartiles, National Grid's gender diversity fell into the fourth quartile, and, therefore, National Grid scored 4 out of 4 for gender diversity.

The second attribute, age diversity, is measured by the coefficient variation of age of all board members in each year. In the case of National Grid, the directors' average age in 2012 was 57.3, and the standard deviation was 7.5. Therefore, the coefficient variation of age was 0.13. After the classification of the entire sample into four quartiles, the coefficient variation of age diversity fell into the third quartile, meaning that National Grid scored 3 out of 4 for the age diversity attribute.

Nationality diversity, the third attribute, is measured by the percentage of foreign directors across the full board. National Grid had four foreign directors, and, therefore, the percentage of nationality diversity was 0.31. After the classification of the entire sample into four quartiles, the nationality diversity of National Grid in 2012 fell into the third quartile. Therefore, National Grid scored 3 out of 4 for the nationality diversity attribute.

To measure the fourth attribute, education diversity, the directors' level of education was taken into consideration. The Herfindahl index was used to calculate the education diversity based on the percentage of directors with no college degree, with a bachelor's degree, and with a

master's degree or higher. National Grid had one director with no college degree, eight with bachelor's degrees, and four with master's degrees or higher. Therefore, the Herfindahl index for education diversity is $(1/13)^2 + (8/13)^2 + (4/13)^2 = 0.48$, which fell into the third quartile. As a result, National Grid scored 3 out of 4 for education diversity.

The final step is to sum the scores for all diversity attributes (gender = 4, age = 3, nationality = 3, and education = 3). Thus, National Grid's final diversity index score for the year 2012 was 13 (see Table 6.5).

Gender Diversity was measured by calculating the proportion of female directors sitting on a corporate board (following the example of Carter et al., 2003; Cumming et al., 2015).

Age Diversity was measured by determining the standard deviation of directors' ages divided by the across-the-board mean (Ali et al., 2014).

Nationality Diversity was measured by calculating the number of foreign directors divided by the total number of directors sitting on a board (Gracia-Meca, 2015).

Education Diversity was measured by assessing the percentage of directors who hold postgraduate degrees (Farag and Mallin, 2016a).

Table 6.5 An Illustrative Example of Constructing Board Diversity Index – National Grid plc in 2012

Name	Role	Gender	Age	Nationality	No Degree	Bachelor	Master or above
Andrew Bonfield	GFD	M	49	British	No	Yes	No
Steve Holliday	CEO	M	55	British	No	Yes	No
Tom King	RP	M	50	American	No	Yes	No
Nick Winser	DP	M	51	British	No	Yes	No
Linda Adamany	INED	F	60	American	Yes	No	No
Phil Aiken	INED	M	63	Australian	No	Yes	No
Sir Peter Gershon	Chairman	M	65	British	No	Yes	No
Doctor Paul Golby	INED	M	61	British	No	No	Yes
Ken Harvey	Senior INED	M	71	British	No	Yes	No
The Rt. Hon. Ruth	INED	F	43	British	No	No	Yes
Stephen Pettit	INED	M	60	British	No	No	Yes
Maria Richter	INED	F	57	American	No	No	Yes
George Rose	INED	M	60	British	No	Yes	No
GFD: General Financial director; CEO: Chief Executive Officer; RP: Regional President; DP: Division President; INED: Independent Non-Executive Director.							
1. Gender Diversity: is measured by the percentage of female members setting on the board. There are three female directors sitting on National Grid’s board in 2012 out of 13 directors. Therefore, the proportion of female directors is 23%. After classifying the proportion of females for the whole sample in the study into four quartiles, National Grid’s gender diversity falls into the fourth quartile and therefore scores 4 out of 4.							
First Quartile		Second Quartile		Third Quartile		Fourth Quartile	
CV gender < .06		0.06 ≤ CV gender < .13		.13 ≤ CV gender < .21		CV gender ≥ .21	
2. Age Diversity: is measured by the coefficient variation of age across board members in each year. For National Grid, the directors’ average age in 2012 is 57.3 and the standard deviation is 7.5 Therefore, the CV of age = .13. After the classification of the entire sample into four quartiles, CV of age diversity falls into the third quartile, and therefore scores 3 out of 4.							
First Quartile		Second Quartile		Third Quartile		Fourth Quartile	
CV age < .11		0.11 ≤ CV age < .13		.13 ≤ CV age < .16		CV age ≥ .16	
3. Nationality Diversity: is measured by the percentage of foreign directors across the full board. For National Grid, there are four foreign directors and therefore, the percentage of nationality diversity is .31. After the classification of the entire sample into four quartiles, the national diversity of National Grid in 2012 falls into the third quartile.							
First Quartile		Second Quartile		Third Quartile		Fourth Quartile	
CV Nat < .07		0.07 ≤ Nat < .18		.18 ≤ Nat < .38		CV Nat ≥ .38	
4. Education Diversity: is measured using directors’ level of education. I adopt Herfindahl index directors to calculate education diversity based on percentage of directors with no college degree, bachelor degree and master or above degree. For National Grid, there is one director with no college degree, 8 with bachelor degrees and 4 with master or above degree. Therefore, the Herfindahl index for education diversity is (1/13) ² + (8/13) ² + (4/13) ² =.48, which falls into the third quartile. (Note: Herfindahl index is an inverse measure which indicate smaller values have greater diversity).							
First Quartile		Second Quartile		Third Quartile		Fourth Quartile	
Edu. ≥ .57		0.50 ≤ Edu. < .57		.41 ≤ Edu. < .50		CV Edu. < .41	
Aggregating the four diversity scores: the final step is to sum the diversity measures for all the attributes (gender, age, nationality, education and experience). For National Grid, the final diversity index score in 2012 is as follows:							
Diversity Index							Final
Gender							4
Age							3
Nationality							3
Education							3
Total diversity index score							13

6.4.2. Independent Variables

The independent variable used in this study, institutional ownership, was classified into five types in the tradition of Aggarwal et al. (2011): total, foreign, domestic, common law and civil law.

6.4.3. Control Variables

In addition to the main explanatory variables, this study considered several control variables that might also have the ability to influence corporate governance levels (board attributes and board diversity variables). Omitting control variables may lead to biased results regarding the role of institutional investors in corporate governance. Therefore, as per Aggarwal et al. (2011), this study considered several control variables³⁸, which are as follows:

Firm Size has been documented by several studies to be one of the main factors that influences governance structure. For instance, several studies have reported that corporate board characteristics are influenced by firm size. For instance, Boone et al. (2007) and Baker and Gompers (2003) found that board composition (i.e., size and independence) was positively associated with firm size. Other scholars found that large firms were less likely to be associated with weak governance practices (i.e., earning management) as compared to their smaller counterparts (Kim et al., 2016; Chaney et al., 2011). In this study, firm size was measured as the natural logarithm of total assets.

Sales Growth is normally used to proxy the growth opportunities of a firm. Several studies have reported that sales growth is one of the main drivers of board characteristics. For instance, Knyazeva et al. (2013) uncovered a negative relationship between board independence and sales growth. Additionally, Vafeas (1999b) found that sales growth was positively associated

³⁸ For reasons of consistency, all financial control variables were directly extracted in US dollars.

with the meeting frequency of a corporate board. In this study, sales growth was measured by calculating the annual changes in net sales divided by the previous year's net sales.

Leverage is typically used to proxy a firm's financial risk (Hahn and Lasfer, 2016). A considerable number of studies have shown that a firm's leverage is associated with its governance structure. For example, Denis and Sarin (1999) reported that the higher a firm's leverage, the higher its board size and independence. Additionally, Hahn and Lasfer (2016) reported that the meeting frequency of a corporate board was significantly associated with the firm's financial risk (i.e., leverage). In this study, leverage was measured by calculating a firm's total debt divided by its total assets.

With regard to **Cash**, it has been argued that weakly-governed firms are more likely to waste their cash reserves than are their well-governed counterparts (Dittmar and Mahrt-Smith; 2007; Harford, 2012). Aggarwal et al. (2011) found that the lower a company's cash holdings, the lower the firm's governance level. In this study, cash ratio was calculated by determining the total amounts of cash and short-term investments divided by a firm's total assets.

Capital Expenditure measures the extent to which a firm has the potential for growth; it is normally used to proxy the costs of monitoring (Boone et al., 2007). Firms with higher levels of capital expenditure require more monitoring from outside directors. Boone et al., (2007) found that board size and board independence had negative and positive associations, respectively, with capital expenditure. Aggarwal et al. (2011) found that the higher a firm's capital expenditure, the lower its governance level. In this study, capital expenditure was determined by calculating a company's total capital expenditures divided by its total assets.

Market-to-Book Value is one measure of firm valuation. Indeed, Aggarwal et al. (2011) found that the higher the ratio of market-to-book value, the more favourable were a company's governance outcomes. In this study, market-to-book value was measured by calculating a company's total market value of equity divided by its book value of equity.

Return on Assets is considered to be one of the main proxies of company profitability. For instance, Aggarwal et al. (2011) found that the higher a firm's profitability (as measured by return on assets), the better its governance structure. In this study, return on assets was calculated by determining the total net income before extraordinary items plus interest expenses divided by total assets.

Property, Plants and Equipment measures the asset tangibility of a firm. Previous studies have documented the importance of a firm's tangibility in determining the quality of its governance structure. Knyazeva et al. (2013) found that firms with high levels of tangible assets were negatively associated with CEO turnover. However, Aggarwal et al. (2011) found no relationship between asset tangibility and the corporate governance index. In this study, asset tangibility was measured by calculating the total amount of property, plants, and equipment divided by total assets.

Analyst Coverage, or analyst following, is another key factor that has been shown to influence the governance structure of a firm. For instance, Yu (2008) argued that analyst following plays an indirect role in the monitoring of managers who might otherwise misbehave with regard to their actions within a firm; therefore, such coverage serves to align the interests of both the shareholders and the managers of a firm. Kim et al. (2016) found that higher levels of analyst following were negatively associated with earning management. In the context of this research, analyst following may influence how the corporate board of a firm is structured. In this study, analyst coverage was measured by determining the number of analysts who follow a firm.

Cross-Listing Dummies is another potential determinant of a firm's governance level; this variable describes a company's access to foreign stock exchanges. One common means of cross-listing is for a company to be listed on the American Depositary Receipt (ADR)³⁹.

³⁹ Firms listed on the ADR (levels II and III) are required to comply with SEC disclosure requirements and with the listing rules of the stock exchange on which they are listed (Doidge et al., 2007).

Aggarwal et al. (2011) found that firms with second and third ADR listings were positively and significantly associated with better governance structures.

The Rule of Law is an index that measures the extent to which a company's agents have confidence in and abide by the rules of society (Essen et al., 2013). Several studies have argued that the rule of law shapes the quality of corporate governance in a given country. To this end, Kim and Ozdemir (2014) found that the composition of a corporate board can be determined by assessing the strength of the rule of law in a particular country.

The Identity of Ultimate Owners (or controlling shareholders), several scholars have argued, must be considered when studying corporate governance, as each type of investor has its own strategies for and perceptions of the governance structures of investee firms (Aguilera et al., 2012; Adams et al., 2010). Following the methods laid out by Faccio and Lang (2002), this study adopted a 20% cut-off policy to identify the controlling shareholders of an investee firm, and dummy variables were used to represent whether a firm is controlled by institutional investors (IO 20%), the state (State 20%), a family (Family 20%), or whether it is widely held (Widely Held 20%).

Economic Conditions, and their effects, must be accounted for; thus, this study used dummy variables to control for several economic conditions (pre-crisis, crisis, and post-crisis periods).

Table 6.6 List of Variables

Variables	Variable Definition	Data Source
Dependent Variables: Board Attributes		
Board attributes index (GOV ₁₄)	Firm level governance measured by the main attributes related to the structure and function of the corporate board and key subcommittees (see Table 6.4).	BoardEX
Board independence (BOARD INED)	The proportion of independent directors on the board.	BoardEX
Audit committee independence (AC INED)	The proportion of independent directors on the audit committee.	BoardEX
Compensation committee independence (CC)	The proportion of independent directors on the compensation committee.	BoardEX
Nomination committee independence (NC)	The proportion of independent directors on the nomination committee.	BoardEX
Board meeting frequency (BOARD MF)	Total number of meetings held by the board during the fiscal year.	Annual Reports
Attendance rate (ATTEND RATE)	Average attendance of board of directors' meetings.	Annual Reports
Audit committee meeting frequency (AC MF)	Total number of meetings held by the audit committee during the fiscal year.	Annual Reports
Compensation committee meeting frequency	Total number of meetings held by the compensation committee during the fiscal year.	Annual Reports
Nomination committee meeting frequency	Total number of meetings held by the nomination committee during the fiscal year.	Annual Reports
CEO tenure (CEO TENURE)	Total number of years that CEO has served on the board.	BoardEX
Board tenure (BOARD TENURE)	Total number of years that board members have served on the board divided by total number of board members.	BoardEX
Busy board (BUSY BOARD)	Average directorships held by INEDs.	BoardEX
Busy board % (BUSY BOARD %)	Proportion of the INEDs who hold three or more directorship in public firms.	BoardEX
Dependent Variables: Board Diversity		
Board diversity index (BDI ₆)	Firm diversity level measured by board diversity dimensions; gender, age, nationality and education (see Table 6.5).	BoardEX
Board Gender Diversity (GENDER DIV)	The proportion of female directors across the board.	BoardEX
Board Age Diversity (AGE DIV)	The standard deviation of directors' ages divided by the mean across the board.	BoardEX
Board Nationality Diversity (NATION DIV)	The percentage of foreign directors across the board.	BoardEX
Board Education Diversity (EDU DIV)	The percentage of directors with postgraduate degrees across the board.	BoardEX
Independent Variables: Institutional Ownership		
Total IO (IO TOTAL)	Holdings by all institutions as a fraction of market capitalization.	ThomsonOne
Foreign IO (IO FOR)	Holdings by institutions located in a different country from where the stock is listed as a fraction of market capitalization.	ThomsonOne
Domestic IO (IO DOM)	Holdings by institutions located in the same country where the stock is listed as a fraction of market capitalization.	ThomsonOne
Common-law IO (IO COMMON)	Holdings by institutions located in common-law countries as a fraction of market capitalization.	ThomsonOne
Civil-law IO (IO CIVIL)	Holdings by institutions located in civil-law countries as a fraction of market capitalization.	ThomsonOne
Control Variables: Firm and Country Characteristics		
Firm size (SIZE)	Log of total assets in thousands of U.S. dollars (WS02999).	Worldscope
Sales growth (SGROWTH)	Two-year geometric average of annual growth rate in net sales in U.S. dollars (WS01001).	Worldscope
Leverage (LEV)	Total debt (WS03255) divided by total assets (WS02999).	Worldscope
Cash (CASH)	Cash and short-term investments (World scope item 02001) divided by total assets (WS02999).	Worldscope
Capital expenditures (CAPEX)	Capital expenditures (WS 04601) divided by total assets (WS02999).	Worldscope
Market-to-book (MB)	Market value of equity (WS item 08001) divided by book value of equity (WS03501).	Worldscope
Return on assets (ROA)	Ratio of net income before extraordinary items (WS01551) plus interest expenses (WS01151) to total assets (WS02999).	Worldscope
Property, plant and equipment (PPE)	Property, plant, and equipment (WS02501) divided by total assets (WS02999).	Worldscope
Analyst coverage (ANALYST)	Number of analysts following a firm (IBES).	IBES
Cross-listing dummy (ADR)	Dummy that equals one if a firm is cross-listed on a U.S. exchange through a level 2–3 ADR or direct listing of ordinary share, and zero otherwise.	Major Depository institutions
Rule of law (RULE)	Index measures the extent to which the agent has confidence in and abide by the rules of the society in a particular country.	World Bank
Pre-crisis dummy (PRE-CRISIS)	Dummy that equals one if the observation falls into pre- crisis period, and zero otherwise.	World Bank
crisis dummy (CRISIS)	Dummy that equals one if the observation falls into crisis period, and zero otherwise.	World Bank
Post-crisis dummy (POST-CRISIS)	Dummy that equals one if the observation falls into post- crisis period, and zero otherwise.	World Bank
Institutional owner controlling 20% (IO)	Dummy that equals one if the ultimate owner is institutional investor and owns greater than 20%, and zero otherwise.	ThomsonOne and Annual Reports
State controlling 20% (STATE)	Dummy that equals one if the ultimate owner is state and owns greater than 20%, and zero otherwise.	ThomsonOne and Annual Reports
Family controlling 20% (FAMILY)	Dummy that equals one if the ultimate owner is family and owns greater than 20%, and zero otherwise.	ThomsonOne and Annual Reports
Widely held at 20% (WIDLEY)	Dummy that equals one if the firm is widely held at 20%, and zero otherwise.	ThomsonOne and Annual Reports

6.5. Panel Data Estimation Method

In order to examine the relationship that exists between institutional investors and corporate board characteristics, this study employed an unbalanced panel dataset (Aggarwal et al, 2011; Kim et al, 2016). Panel data describes a dataset in which entities (i.e., companies, states, individuals, countries, etc.) are observed over a period of time. Hence, panel data observations have at least two dimensions: a cross-sectional dimension, as indicated by the subscript 'i', and a time-series dimension, as denoted by the subscript 't'.

Panel data analysis has become a common tool of quantitative studies due to the fact that its use largely eliminates various concerns that are generally tied to traditional techniques. According to Baltagi (2001), the use of panel data provides several advantages over more conventional time-series and cross-sectional datasets. First, panel data account for firm heterogeneity, as such data assume that the entities in a sample are heterogeneous; time-series and cross-sectional regressions, however, do not account for such heterogeneity and hence might lead to biased results. Second, by combining time-series and cross-sectional observations, panel data provide 'more informative data, more variability, less collinearity among the variables, more degree[s] of freedom and more efficiency' (Baltagi, 2001, p. 8). Third, panel data can handle more complicated models than can time-series and cross-sectional models. A fourth important advantage of panel data is that such data are better able to investigate dynamics of change. A cross-sectional distribution, though it may appear relatively stable, cannot capture changes over a period of time. Panel data, however, are well-suited to capture changes over a given timespan that might otherwise go undetected by cross-sectional or time-series techniques.

There are two common techniques of estimation associated with panel data: fixed effect (FE) and random effect (RE). FE examines the relationship between the dependent and explanatory variables within an entity (i.e., a company). The assumption of FE is that there is something

within an entity that may influence or bias the predictors or the outcome variables and that therefore must be controlled for. Thus, FE control over unobservable time-invariant observations (i.e., observations that do not change over time) is achieved by eliminating their effects so that the net effect of the predictor can be assessed (Mertens et al., 2017). In contrast to the FE supposition, the RE model carries the assumption that variations across entities are random and do not correlate with the model's predictors; therefore, time-invariant variables are considered to act as explanatory variables in RE models (Mertens et al., 2017). Furthermore, in RE models, both within-unit and between-unit variabilities are exploited by weighting and partitioning the relevance of these two sources of variability. The advantage of using RE is that a researcher can consider variables that are time-invariant within a model; this indicates that RE can employ richer data as compared to FE (Mertens et al., 2017).

Many researchers utilise the Hausman specification test when attempting to choose between these two models. According to Mertens et al. (2017), the Hausman specification test is used to examine whether the coefficients of the two models (FE and RE) are different. The null hypothesis of the Hausman test is that there are no systematic differences. If the results lead to a significant p-value ($\text{Prob} > \chi^2$ less than 0.05), the FE model should be applied. Alternatively, an RE model should be chosen if the results illustrate otherwise. After conducting the Hausman test, the results of this study revealed that an FE model should be applied.

Serial Correlation and Heteroscedasticity Tests

Baltagi (2001) emphasised the importance of testing for serial correlation and heteroscedasticity in panel data. The presence of serial correlation may bias standard errors and therefore provide results that lack efficiency (Wooldridge, 2009). The existence of serial correlation in panel data yields smaller coefficients of standard error and higher R-squared values. In this study, the Wooldridge test was applied to investigate whether serial correlation exists within the FE model (Wooldridge, 2009). Stata 14 command 'xtserial' was applied to

investigate this issue of serial correlation. The null hypotheses (H_0) of the Wooldridge test assumes that serial correlation does not exist. Therefore, in order to reject the null hypotheses, the Wooldridge value should be less than 5%.

The presence of heteroscedasticity in the panel data is another issue that must be considered. In panel data regressions, the standard errors component of the model assumes that regression disturbance is homoscedastic and thus has the same variance across time and entities (Baltagi, 2001). However, this might be a restrictive assumption when using panel data, as cross-sectional units may vary in size, thus leading to variation (Baltagi, 2001). As a result, the standard errors of the panel estimations will be biased unless a researcher corrects for the possible presence of heteroscedasticity. According to Baltagi (2001), large panels with longer time-spans have more opportunity to become overwhelmed with heteroscedasticity (Baltagi, 2001). In this study, the Breusch-Pagan estimator was applied in an effort to investigate the presence of heteroscedasticity. The null hypothesis of the Breusch-Pagan test assumes that FE models of study have constant variance levels. Therefore, in order to reject the null hypothesis of this test, the finding should have a value of less than 5%.

The results of both tests were less than 5%, which indicates that serial correlation and heteroscedasticity exist in the study's panel data. In response, a 'cluster' command was applied to resolve the serial correlation concern, and a 'robust' command was applied to settle the heteroscedasticity issue; thus, standard errors were normalised in all models, as per the examples of Aggarwal et al. (2011) and Ferreira and Matos (2008).

6.6. Empirical Models

The empirical models used in this research study were divided into two groups. The first group was used to investigate the role of institutional investors in the improvement of corporate board attributes, while the second group was utilised to examine the role of institutional investors in the improvement of board diversity. All the independent variables were lagged by one period

so that the relationship between the explanatory variables and the future board attributes could be tested. All models are described below in the following two sections.

6.6.1. Models for Institutional Investors and Board Attributes

Five main models were constructed to investigate the role of institutional investors in the improvement of corporate board attributes: the Board Attributes Index, the composition of a board and its key subcommittees, the activity of a board and its key subcommittees, board entrenchment and board busyness. These models are as follows:

Model 1 is used to test the association between institutional investors and Board Attributes Index (GOV_{14}), and it considers the following hypothesis:

H1. *The higher the presence of institutional investors, the better the corporate governance in their investee firms.*

$$(GOV_{14}) = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \\ IO\ COMMO_{(t-1)} \\ IO\ CIVIL_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2\ SIZE_{(t-1)} + \beta_3\ SGROWTH_{(t-1)} + \beta_4\ LEV_{(t-1)} + \beta_5\ CASH_{(t-1)} + \beta_6\ CAPEX_{(t-1)} \\ + \beta_7\ MB_{(t-1)} + \beta_8\ ROA_{(t-1)} + \beta_9\ PPE_{(t-1)} + \beta_{10}\ ANALYST_{(t-1)} + \beta_{11}\ ADR_{(t-1)} + \\ \beta_{12}\ RULE_{(t-1)}\beta_{13}\ PRE - CRISIS_{(t-1)} + \beta_{14}\ CRISIS_{(t-1)} + \beta_{15}\ POST - CRISIS_{(t-1)} \\ + \beta_{16}\ IO_{(t-1)} + \beta_{17}\ STATE_{(t-1)} + \beta_{18}\ FAMILY_{(t-1)} + \beta_{19}\ WIDELY_{(t-1)} + \varepsilon \end{pmatrix} \quad (\text{Equation 1})$$

Model 2 is used to test the association between institutional investors and the independence of the board and its key subcommittees, and it considers the following two hypotheses:

H2a. *The higher the presence of institutional investors, the higher the independence of the board.*

H2b. *The higher the presence of institutional investors, the higher the independence of the board's key subcommittees.*

$$\begin{pmatrix} BOARD\ INED \\ AC\ INED \\ CC\ INED \\ NC\ INED \end{pmatrix} = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2\ SIZE_{(t-1)} + \beta_3\ SGROWTH_{(t-1)} + \beta_4\ LEV_{(t-1)} + \beta_5\ CASH_{(t-1)} + \beta_6\ CAPEX_{(t-1)} \\ + \beta_7\ MB_{(t-1)} + \beta_8\ ROA_{(t-1)} + \beta_9\ PPE_{(t-1)} + \beta_{10}\ ANALYST_{(t-1)} + \beta_{11}\ ADR_{(t-1)} + \\ \beta_{12}\ RULE_{(t-1)}\beta_{13}\ PRE - CRISIS_{(t-1)} + \beta_{14}\ CRISIS_{(t-1)} + \beta_{15}\ POST - CRISIS_{(t-1)} \\ + \beta_{16}\ IO_{(t-1)} + \beta_{17}\ STATE_{(t-1)} + \beta_{18}\ FAMILY_{(t-1)} + \beta_{19}\ WIDELY_{(t-1)} + \varepsilon \end{pmatrix} \quad (\text{Equation 2})$$

Model 3 is used to test the association between institutional investors and the activity of the board and its key subcommittees, and it considers the following two hypotheses:

H3a. *The higher the presence of institutional investors, the higher the activity of the board.*

H3b. *The higher the presence of institutional investors, the higher the activity of the board's key subcommittees.*

$$\begin{pmatrix} \text{BOARD MF} \\ \text{AC MF} \\ \text{CC MF} \\ \text{NC MF} \end{pmatrix} = \beta_0 + \beta_1 \begin{pmatrix} \text{IO TOTAL}_{(t-1)} \\ \text{IO FOR}_{(t-1)} \\ \text{IO DOM}_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2 \text{SIZE}_{(t-1)} + \beta_3 \text{SGROWTH}_{(t-1)} + \beta_4 \text{LEV}_{(t-1)} + \beta_5 \text{CASH}_{(t-1)} + \beta_6 \text{CAPEX}_{(t-1)} \\ + \beta_7 \text{MB}_{(t-1)} + \beta_8 \text{ROA}_{(t-1)} + \beta_9 \text{PPE}_{(t-1)} + \beta_{10} \text{ANALYST}_{(t-1)} + \beta_{11} \text{ADR}_{(t-1)} + \\ \beta_{12} \text{RULE}_{(t-1)} \beta_{13} \text{PRE} - \text{CRISIS}_{(t-1)} + \beta_{14} \text{CRISIS}_{(t-1)} + \beta_{15} \text{POST} - \text{CRISIS}_{(t-1)} \\ + \beta_{16} \text{IO}_{(t-1)} + \beta_{17} \text{STATE}_{(t-1)} + \beta_{18} \text{FAMILY}_{(t-1)} + \beta_{19} \text{WIDELY}_{(t-1)} + \varepsilon \end{pmatrix} \quad (\text{Equation 3})$$

Model 4 is used to test the association between institutional investors and board entrenchment, and it considers the following hypothesis:

H4. *The higher the presence of institutional investors, the lower the board entrenchment.*

$$\begin{pmatrix} \text{CEO TENURE} \\ \text{BOARD TENURE} \end{pmatrix} = \beta_0 + \beta_1 \begin{pmatrix} \text{IO TOTAL}_{(t-1)} \\ \text{IO FOR}_{(t-1)} \\ \text{IO DOM}_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2 \text{SIZE}_{(t-1)} + \beta_3 \text{SGROWTH}_{(t-1)} + \beta_4 \text{LEV}_{(t-1)} + \beta_5 \text{CASH}_{(t-1)} + \beta_6 \text{CAPEX}_{(t-1)} \\ + \beta_7 \text{MB}_{(t-1)} + \beta_8 \text{ROA}_{(t-1)} + \beta_9 \text{PPE}_{(t-1)} + \beta_{10} \text{ANALYST}_{(t-1)} + \beta_{11} \text{ADR}_{(t-1)} + \\ \beta_{12} \text{RULE}_{(t-1)} \beta_{13} \text{PRE} - \text{CRISIS}_{(t-1)} + \beta_{14} \text{CRISIS}_{(t-1)} + \beta_{15} \text{POST} - \text{CRISIS}_{(t-1)} \\ + \beta_{16} \text{IO}_{(t-1)} + \beta_{17} \text{STATE}_{(t-1)} + \beta_{18} \text{FAMILY}_{(t-1)} + \beta_{19} \text{WIDELY}_{(t-1)} + \varepsilon \end{pmatrix} \quad (\text{Equation 4})$$

Model 5 is used to test the association between institutional investors and board busyness, and it considers the following hypothesis:

H5. *The higher the presence of institutional investors, the lower the board busyness.*

$$\begin{pmatrix} \text{BUSY BOARD} \\ \text{BUSY BOARD \%} \end{pmatrix} = \beta_0 + \beta_1 \begin{pmatrix} \text{IO TOTAL}_{(t-1)} \\ \text{IO FOR}_{(t-1)} \\ \text{IO DOM}_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2 \text{SIZE}_{(t-1)} + \beta_3 \text{SGROWTH}_{(t-1)} + \beta_4 \text{LEV}_{(t-1)} + \beta_5 \text{CASH}_{(t-1)} + \beta_6 \text{CAPEX}_{(t-1)} \\ + \beta_7 \text{MB}_{(t-1)} + \beta_8 \text{ROA}_{(t-1)} + \beta_9 \text{PPE}_{(t-1)} + \beta_{10} \text{ANALYST}_{(t-1)} + \beta_{11} \text{ADR}_{(t-1)} + \\ \beta_{12} \text{RULE}_{(t-1)} \beta_{13} \text{PRE} - \text{CRISIS}_{(t-1)} + \beta_{14} \text{CRISIS}_{(t-1)} + \beta_{15} \text{POST} - \text{CRISIS}_{(t-1)} \\ + \beta_{16} \text{IO}_{(t-1)} + \beta_{17} \text{STATE}_{(t-1)} + \beta_{18} \text{FAMILY}_{(t-1)} + \beta_{19} \text{WIDELY}_{(t-1)} + \varepsilon \end{pmatrix} \quad (\text{Equation 5})$$

6.6.2. Models for Institutional Investors and Board Diversity

Five main models were constructed to investigate the role of institutional investors in the improvement of corporate board diversity: the Board Diversity Index, board gender diversity,

board age diversity, board nationality diversity, and board education diversity. These models are as follows:

Model 6 is used to test the association between institutional investors and the Board Diversity Index (BDI_{16}), and it considers the following hypothesis:

H6. *The higher the presence of institutional investors, the higher the diversity of the board.*

$$(BDI_{16}) = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \\ IO\ COMMO_{(t-1)} \\ IO\ CIVIL_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2\ SIZE_{(t-1)} + \beta_3\ SGROWTH_{(t-1)} + \beta_4\ LEV_{(t-1)} + \beta_5\ CASH_{(t-1)} + \beta_6\ CAPEX_{(t-1)} \\ + \beta_7\ MB_{(t-1)} + \beta_8\ ROA_{(t-1)} + \beta_9\ PPE_{(t-1)} + \beta_{10}\ ANALYST_{(t-1)} + \beta_{11}\ ADR_{(t-1)} + \\ \beta_{12}\ RULE_{(t-1)}\beta_{13}\ PRE - CRISIS_{(t-1)} + \beta_{14}\ CRISIS_{(t-1)} + \beta_{15}\ POST - CRISIS_{(t-1)} \\ + \beta_{16}\ IO_{(t-1)} + \beta_{17}\ STATE_{(t-1)} + \beta_{18}\ FAMILY_{(t-1)} + \beta_{19}\ WIDELY_{(t-1)} + \varepsilon \end{pmatrix}$$

(Equation 6)

Model 7 is used to test the association between institutional investors and board gender diversity, and it considers the following hypothesis:

H7. *The higher the presence of institutional investors, the higher the gender diversity of the board.*

$$(GENDER\ DIV) = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2\ SIZE_{(t-1)} + \beta_3\ SGROWTH_{(t-1)} + \beta_4\ LEV_{(t-1)} + \beta_5\ CASH_{(t-1)} + \beta_6\ CAPEX_{(t-1)} \\ + \beta_7\ MB_{(t-1)} + \beta_8\ ROA_{(t-1)} + \beta_9\ PPE_{(t-1)} + \beta_{10}\ ANALYST_{(t-1)} + \beta_{11}\ ADR_{(t-1)} + \\ \beta_{12}\ RULE_{(t-1)}\beta_{13}\ PRE - CRISIS_{(t-1)} + \beta_{14}\ CRISIS_{(t-1)} + \beta_{15}\ POST - CRISIS_{(t-1)} \\ + \beta_{16}\ IO_{(t-1)} + \beta_{17}\ STATE_{(t-1)} + \beta_{18}\ FAMILY_{(t-1)} + \beta_{19}\ WIDELY_{(t-1)} + \varepsilon \end{pmatrix}$$

(Equation 7)

Model 8 is used to test the association between institutional investors and board age diversity, and it considers the following hypothesis:

H8. *The higher the presence of institutional investors, the higher the diversity of directors' ages.*

$$(AGE\ DIV) = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2\ SIZE_{(t-1)} + \beta_3\ SGROWTH_{(t-1)} + \beta_4\ LEV_{(t-1)} + \beta_5\ CASH_{(t-1)} + \beta_6\ CAPEX_{(t-1)} \\ + \beta_7\ MB_{(t-1)} + \beta_8\ ROA_{(t-1)} + \beta_9\ PPE_{(t-1)} + \beta_{10}\ ANALYST_{(t-1)} + \beta_{11}\ ADR_{(t-1)} + \\ \beta_{12}\ RULE_{(t-1)}\beta_{13}\ PRE - CRISIS_{(t-1)} + \beta_{14}\ CRISIS_{(t-1)} + \beta_{15}\ POST - CRISIS_{(t-1)} \\ + \beta_{16}\ IO_{(t-1)} + \beta_{17}\ STATE_{(t-1)} + \beta_{18}\ FAMILY_{(t-1)} + \beta_{19}\ WIDELY_{(t-1)} + \varepsilon \end{pmatrix}$$

(Equation 8)

Model 9 is used to test the association between institutional investors and board nationality diversity, and it considers the following hypothesis:

H9. *The higher the presence of institutional investors, the higher the nationality diversity of the board.*

$$(NATION\ DIV) = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2 SIZE_{(t-1)} + \beta_3 SGROWTH_{(t-1)} + \beta_4 LEV_{(t-1)} + \beta_5 CASH_{(t-1)} + \beta_6 CAPEX_{(t-1)} \\ + \beta_7 MB_{(t-1)} + \beta_8 ROA_{(t-1)} + \beta_9 PPE_{(t-1)} + \beta_{10} ANALYST_{(t-1)} + \beta_{11} ADR_{(t-1)} + \\ \beta_{12} RULE_{(t-1)} \beta_{13} PRE - CRISIS_{(t-1)} + \beta_{14} CRISIS_{(t-1)} + \beta_{15} POST - CRISIS_{(t-1)} \\ + \beta_{16} IO_{(t-1)} + \beta_{17} STATE_{(t-1)} + \beta_{18} FAMILY_{(t-1)} + \beta_{19} WIDELY_{(t-1)} + \varepsilon \end{pmatrix}$$

(Equation 9)

Model 10 is used to test the association between institutional investors and board education diversity, and it considers the following hypothesis:

H10. *The higher the presence of institutional investors, the higher the education diversity of the board.*

$$(EDU\ DIV) = \beta_0 + \beta_1 \begin{pmatrix} IO\ TOTAL_{(t-1)} \\ IO\ FOR_{(t-1)} \\ IO\ DOM_{(t-1)} \end{pmatrix} + \begin{pmatrix} \beta_2 SIZE_{(t-1)} + \beta_3 SGROWTH_{(t-1)} + \beta_4 LEV_{(t-1)} + \beta_5 CASH_{(t-1)} + \beta_6 CAPEX_{(t-1)} \\ + \beta_7 MB_{(t-1)} + \beta_8 ROA_{(t-1)} + \beta_9 PPE_{(t-1)} + \beta_{10} ANALYST_{(t-1)} + \beta_{11} ADR_{(t-1)} + \\ \beta_{12} RULE_{(t-1)} \beta_{13} PRE - CRISIS_{(t-1)} + \beta_{14} CRISIS_{(t-1)} + \beta_{15} POST - CRISIS_{(t-1)} \\ + \beta_{16} IO_{(t-1)} + \beta_{17} STATE_{(t-1)} + \beta_{18} FAMILY_{(t-1)} + \beta_{19} WIDELY_{(t-1)} + \varepsilon \end{pmatrix}$$

(Equation 10)

6.7. Robustness Tests

Endogeneity concerns are the most-often-encountered challenge in studies of corporate governance (Boyd et al., 2017; Wintoki et al., 2012). The presence of endogeneity in a research models can lead to ineffective results. In order to alleviate endogeneity concerns within the scope of this study, the study adopted various techniques, such as testing for reverse causality, applying a system GMM and adopting alternative means of measuring the dependent variables of the main models (Cameron and Trivedi, 2005; Greene, 2012; Wintoki et al., 2012) . All of these techniques are discussed and illustrated below, as are the specific endogeneity concerns they were meant to address.

6.7.1. Reverse Causality

According to Wintoki et al. (2012), simultaneity is one of the main sources of endogeneity. Simultaneity arises when the dependent variable and one or more of the independent variables are determined to be in equilibrium. Thus, it can be said that independent variables can

occasionally cause dependent variables; however, the reverse is also true, as sometimes a dependent variable can bring about the independent variable (Roberts and Whited, 2012). In the context of this study, the relationship between institutional investors and board attributes might not necessarily be driven by the activism of institutional investors to improve these attributes; there is also the possibility that institutional investors may be attracted to firms with good board structures (see Aggarwal et al., 2011).

Furthermore, unobserved heterogeneity is another source of endogeneity; the presence of such heterogeneity may imply that the relationship between one or more variables in a model is driven by another variable that the researcher has not observed (Wintoki et al., 2012). The main concern associated with this type of endogeneity is that such unobserved variables can influence error terms even if they are not placed as independent variables. In the context of this study, institutional investors might be associated with various unobserved firm characteristics that may influence the corporate board structures of their investee firm (see Aggarwal et al., 2011).

To address these issues of reverse causality and unobserved heterogeneity, change score regressions were used to examine whether changes to institutional ownership drive changes in corporate board characteristics or whether the opposite holds true (see Lewis-Beck et al., 2004). Additionally, this technique has the advantage of reducing any measurement errors that may arise from the presence of unobserved or omitted variables (Lewis-Beck et al., 2004). Furthermore, this study also utilised FE regression models to control for unobserved heterogeneity (Greene, 2012).

6.7.2. Dynamic Generalised Method of Moments (GMM)

Another concern related to endogeneity involves the issue of dynamic endogeneity (Wintoki et al., 2012). This type of endogeneity refers to the possibility that a firm's current actions will affect its control environment and future performance, which will in turn affect its future

control environment (see Wintoki et al., 2012). In the context of this study, due to the dynamic relationship between institutional investors and board attributes—and because of the potential for reverse causality between institutional ownership and board attributes as well as the possibility of other underlying and unobservable board attribute factors—the GMM was used to estimate the panel data parameters with endogenous explanatory variables (Roodman, 2006; Blundell and Bond, 1998; Arellano and Bond, 1991).

According to Roodman (2009), this type of estimation is particularly suitable for panels with small T and large N values, which is the case in this study. The study therefore applied a two-step dynamic panel GMM estimator, which is also widely-known as a system GMM (Arellano and Bover, 1995; Blundell and Bond, 1998).

According to Wintoki et al. (2012), the validity of a system GMM application is conditional on two specification tests, which are: testing the autocorrelation of the differenced residuals and testing for the exogeneity of instrumental variables. The autocorrelation of the differenced residuals is typically investigated using the Arellano-Bond test, or AR (2), which has a null hypothesis of ‘no serial correlation’. By default, STATA reports two values of the Arellano-Bond test, AR (1) and AR (2). AR (1) tests for first-order differences in residuals and normally rejects the null hypothesis, whereas AR (2) tests for second-order serial correlations between the residuals. The other specification test, the Hansen test, investigates whether instrumental variables are exogenous; this test has a null hypothesis of ‘the instruments as a group are exogenous’. Therefore, the validity of the GMM results are not efficient unless these two tests are satisfied.

6.7.3. Alternative Measures

Several scholars criticised studies that depended solely on corporate governance indices to draw conclusions (see as an example Daines et al., 2010). Instead, they recommended considering alternative measures to verify the results. Hence, this study utilizes the individual

attributes of the Board Attributes Index (GOV₁₄) as alternative measures. As these individual attributes are binary variables, the study applied probit regression models⁴⁰ to investigate the role of institutional investors in the improvement of various index attributes. These attributes which represent the dependent variables, are related to board and its key subcommittees composition (items 2, 5, 6 and 7), board activity (item 8), board entrenchment (item 9), and board busyness (item 12).

6.8. Chapter Summary

This chapter provided a detailed description of the research methodology considered in this study. The chapter first described the sample criteria, data sources and the research period. As explained, the sample covers all firms listed in the major indices of the 15 countries under study for the period of 2006 to 2012. Furthermore, the chapter explained that this study employed the use of secondary data, which were extracted from several sources available to the University of East Anglia, namely the BoardEX, ThomsonOne, Worldscope and Worldbank databases, as well as various corporate governance annual reports. Additionally, this chapter detailed the dependent, independent and control variables considered in the utilised models. Then, the chapter detailed the selection of the major estimation method, the ‘fixed effect regressions’ model, used in this study. Next, the empirical models, which were classified into two groups (the board attributes model and the board diversity model), were illustrated. The chapter concluded with an identification of the robustness tests used to confirm the results of the study. These tests were, primarily, the change score model, system GMM, and various alternative measures.

⁴⁰ According to Gujarati (2011), the probit model is recommended over the logit model when the error term has a normal distribution, which is the case with the models used in this study.

Chapter 7

7.0 Research Results and Analysis: Institutional Investors and Board Attributes

7.1. Introduction

This chapter provides an analysis of the results of the institutional investors' role in the improvement of board attributes. This chapter begins by outlining the descriptive statistics of the variables used in this study. This is followed by an examination of the measures used to test the correlations between variables. The empirical results of these measures are then described and discussed, and finally, the results of the robustness tests are illustrated.

Accordingly, this chapter is organised as follows: section 7.2 provides a summary of the descriptive statistics, section 7.3 describes the correlation analysis, section 7.4 outlines the empirical results of an examination of the role of institutional investors in the improvement of board attributes, section 7.5 discusses the robustness tests and section 7.6 offers a chapter summary.

7.2. Summary of the Descriptive Statistics

This section highlights the descriptive statistics of the dependent variables (board attributes), independent variables (institutional investors) and control variables (firm and country characteristics). Table 7.1 presents the descriptive statistics of the variables used in this study's empirical models. These descriptive statistics were applied to explore the means, standard deviations, minimum and maximum data points and total observations.

Table 7.1 Descriptive Statistics

Variables	Mean	SD	MIN	MAX	No. of Observations
Dependent Variables: Board Attributes					
GOV ₁₄	10	2	3	14	2,586
INED BOARD	64%	22%	0%	100%	2,586
INED AC	85%	27%	0%	100%	2,586
INED CC	80%	30%	0%	100%	2,586
INED NC	71%	34%	0%	100%	2,586
BOARD MF	10	4	4	31	2,586
AC MF	5	3	0	20	2,586
CC MF	4	2	0	14	2,586
NC MF	4	3	0	14	2,586
CEO TENURE	5.0	4.8	0	28.9	2,586
Board TENURE	6.0	2.7	0	15.8	2,586
BUSY BOARD	2.6	0.9	0	7	2,586
BUSY BOARD %	43%	25%	0%	100%	2,586
Independent Variables: Institutional Ownership					
IO TOTAL	36%	23%	1%	99%	2,586
IO FOR	20%	16%	1%	99%	2,586
IO DOM	16%	17%	1%	99%	2,586
IO COMMON	28%	23%	1%	99%	2,586
IO CIVIL	8%	11%	1%	68%	2,586
Control Variables: Firm and Country Characteristics					
FSIZE	7.0	0.6	5	8.6	2,586
SGROWTH	12%	24%	-43%	116%	2,586
LEV	26%	15%	0%	67%	2,586
CASH	11%	10%	0%	62%	2,586
CAPEX	6%	5%	0%	26%	2,586
MB	3.2	3.0	0.30	20.2	2,586
ROA	11%	7%	-9%	36%	2,586
PPE	35%	24%	1%	90%	2,586
ANALYST	18	9	0	55	2,586
ADR	0.19	0.39	0	1	2,586
RULE	91%	12%	52%	100%	2,586
Pre-Crisis	0.37	0.48	0	1	2,586
Crisis	0.45	0.50	0	1	2,586
Post-Crisis	0.18	0.39	0	1	2,586
FAMILY	20%	40%	0	1	2,586
STATE	9%	27%	0	1	2,586
IO	3%	17%	0	1	2,586
WIDELY	68%	46%	0	1	2,586
GOV ₁₄ = Board attributes index, INED BOARD = Board independence, INED AC = Audit committee Independence, INED CC= Compensation committee independence, INED NC = Nomination committee independence, BOARD MF = Board meeting frequency, AC MF = Audit committee meeting frequency, CC MF= Compensation committee meeting frequency, NC MF= Nomination committee meeting frequency, CEO TENURE = CEO tenure, Board TENURE = Board tenure, BUSY BOARD = Busy board, BUSY BOARD % = Busy Board %, , IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, IO = Institutional investor controlling at 20%, WIDELY = Widely held at 20%.					

Table 7.1 demonstrates that the Board Attributes Index (GOV_{14}) ranges from a minimum of 3 to a maximum of 14 for the entire sample. Figure 7.1 shows that on average, the countries with the highest GOV_{14} scores in 2012 were Ireland (90.8%), Canada (90.0%), the UK (88.1%), Australia (87.7%) and Finland (84.0%). Conversely, the countries with the lowest GOV_{14} scores were India (52.3%), Denmark (62.6%), France (64.7%), Belgium (67.0%) and Italy (67.9%).

Figure 7.1 Board Attributes Index (GOV_{14}) by Country and Year (2006–2012)

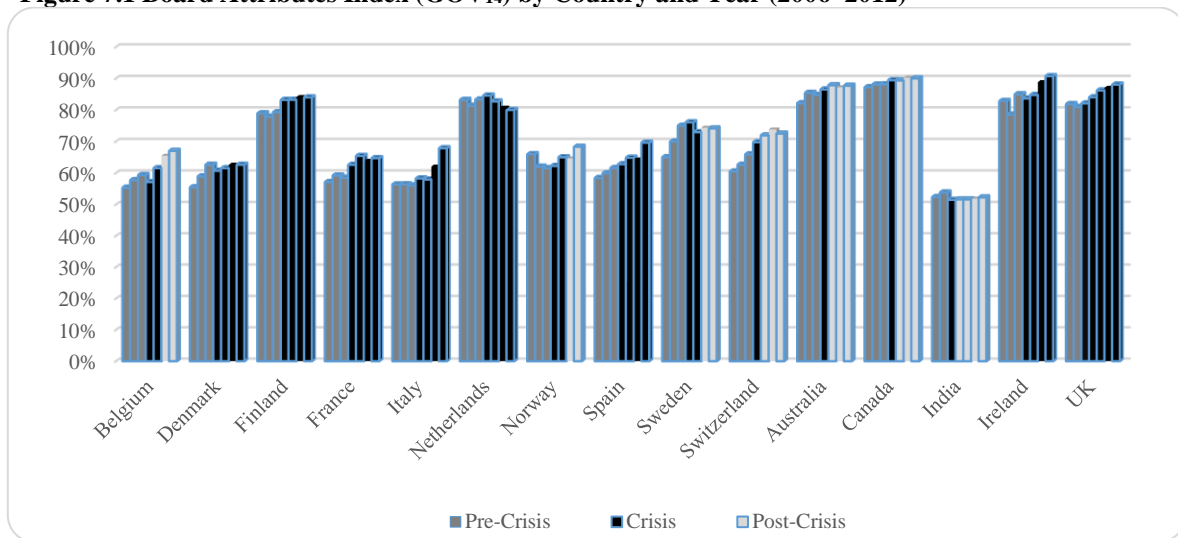
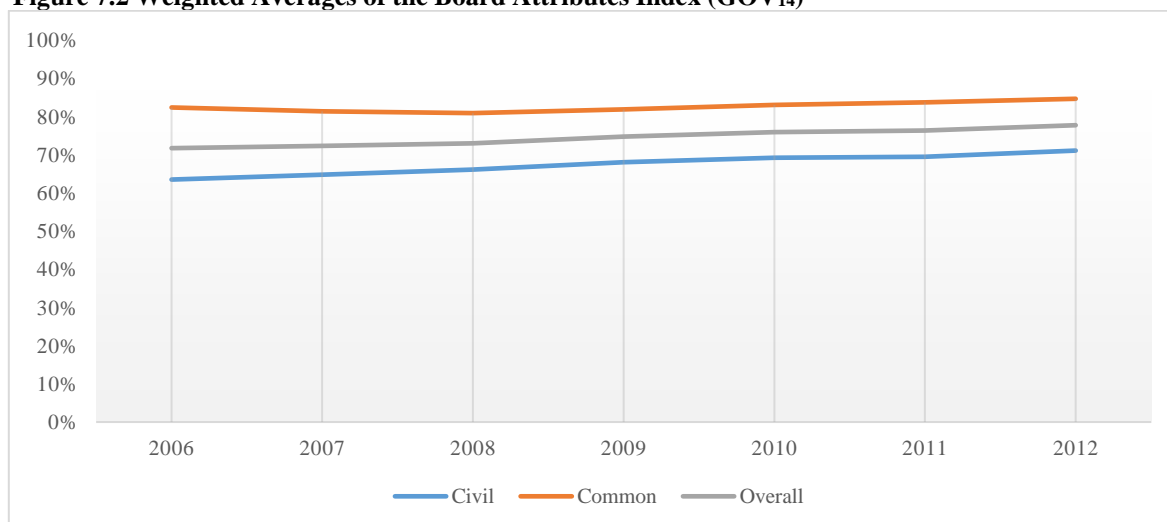


Figure 7.2 displays the weighted averages of the Board Attributes Index (GOV_{14}) for firms located in both civil law countries and common law countries. Overall, the figure illustrates that on average, common law countries had more favourable board attributes than did their civil law counterparts.

Figure 7.2 Weighted Averages of the Board Attributes Index (GOV₁₄)



Additionally, Table 7.1 shows that the independence levels of boards and their key subcommittees (audit, compensation and nomination) had average values of 64%, 85%, 80% and 71%, respectively. The line graph further indicates that board independence steadily increased throughout the study period (2006–2012) (see Figure 7.3). The same trend was observed with regard to the independence of subcommittees; notably, audit committees typically retained high levels of independence and nomination committees demonstrated low independence, while the independence of compensation committees lied somewhere in between.

Figure 7.3 Weighted Averages of Corporate Board and Key Subcommittee Composition

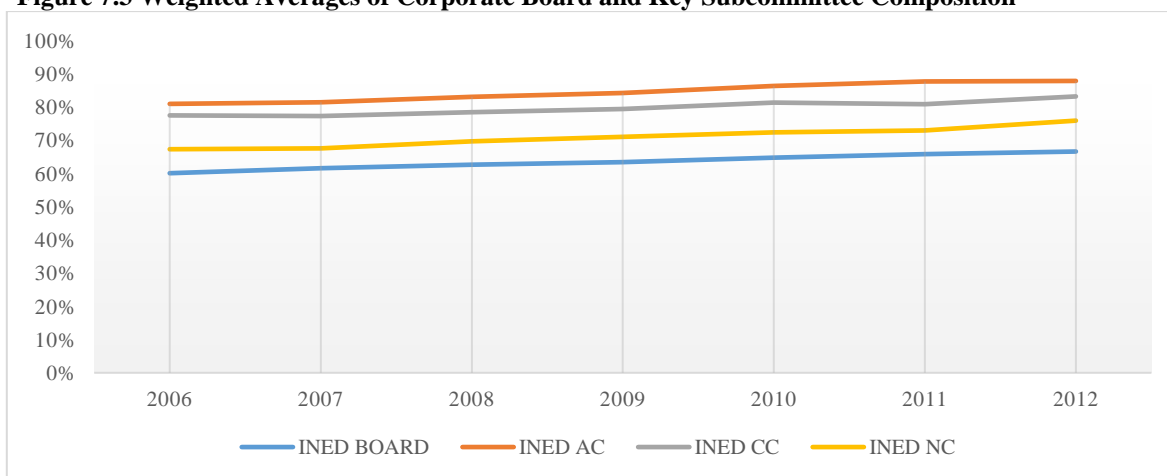


Table 7.1 also demonstrates that the average number of meetings held at the board and key subcommittee levels (audit, compensation and nomination) throughout the study period was 10, 5, 4 and 4, respectively. Figure 7.4 presents the weighted averages of corporate board and key subcommittee activity; as such, the graph indicates that in this sample, the number of meetings held decreased slightly to just under nine in 2010, though in 2012, this figure reclaimed its previous level of 10 annual meetings. However, meeting frequency at the subcommittee level held steady throughout the study period (see Figure 7.4).

Figure 7.4 Weighted Averages of Corporate Board and Key Subcommittee Activity

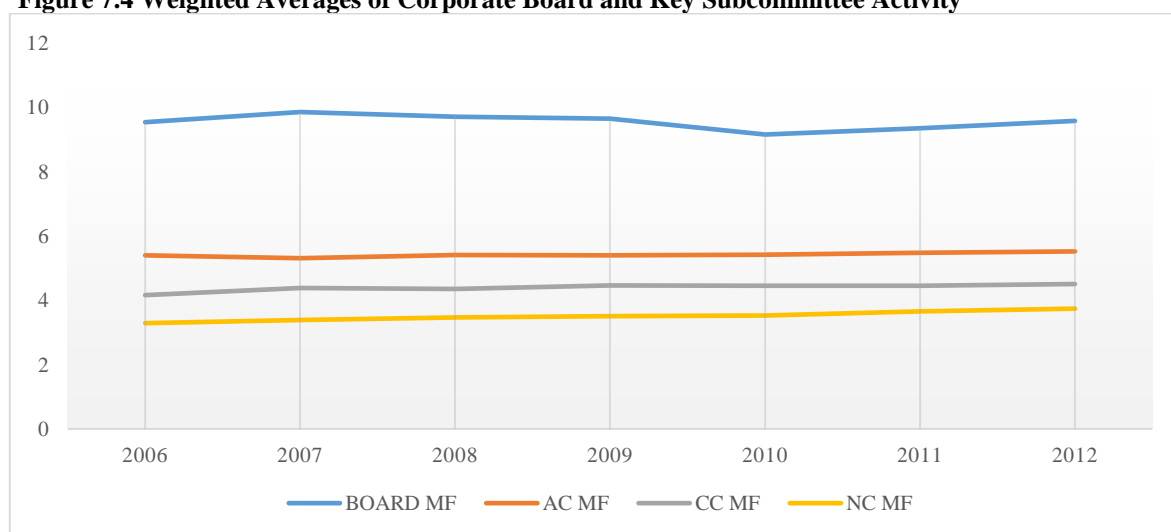


Table 7.1 further reveals that for the entire sample, the average length of CEO tenure was five years, while the average length of board tenure was six years. Figure 7.5 displays the weighted averages of the board entrenchment variables. Thus, this graph shows that there was an overall slight increase in both CEO tenure and board tenure. CEO tenure rose from roughly 4.6 to nearly 5.8 years, while board tenure climbed from approximately 5.8 to 6.2 years. These increases in both measures primarily occurred after the year 2008 (see Figure 7.5).

Figure 7.5 Weighted Averages of the Board Entrenchment Variables

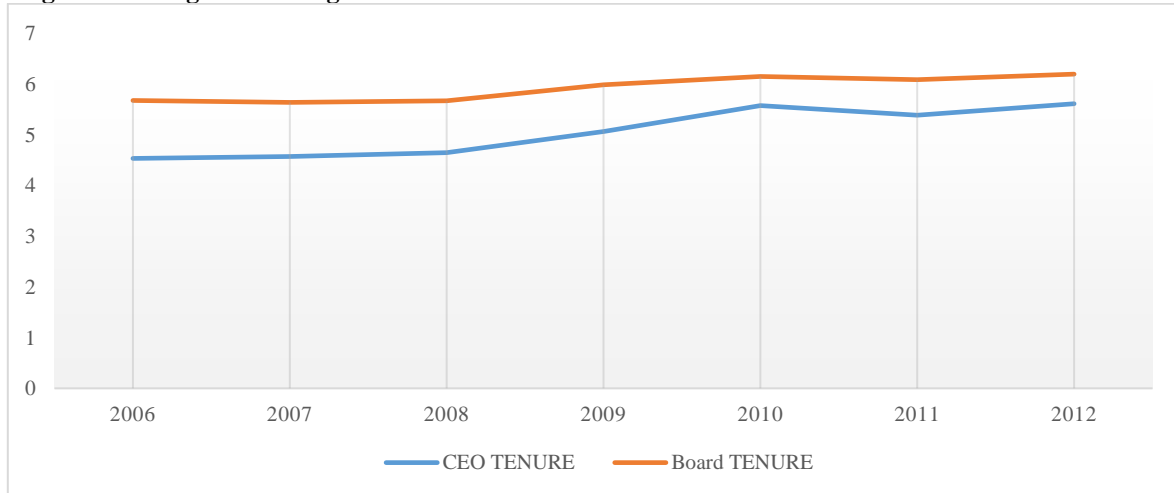


Table 7.1 also demonstrates that the average number of directorships held by each INED in the sample was 2.6; furthermore, an average of 43% of the boards in the sample were classified as ‘busy’. Figures 7.6 and 7.7 show the weighted averages of the average number of directorships held by INEDs as well as the percentages of INEDs who were deemed ‘busy’. Both figures show that there was an overall slight decline in board busyness in the sample over the course of the research period. Figure 7.6 illustrates that the average number of directorships held by INEDs declined from 2.7 to roughly 2.5. Furthermore, Figure 7.7 indicates that INED busyness decreased from 46% to 41% during the years under study.

Figure 7.6 Weighted Average of the Average Board Directorships Held by INEDs

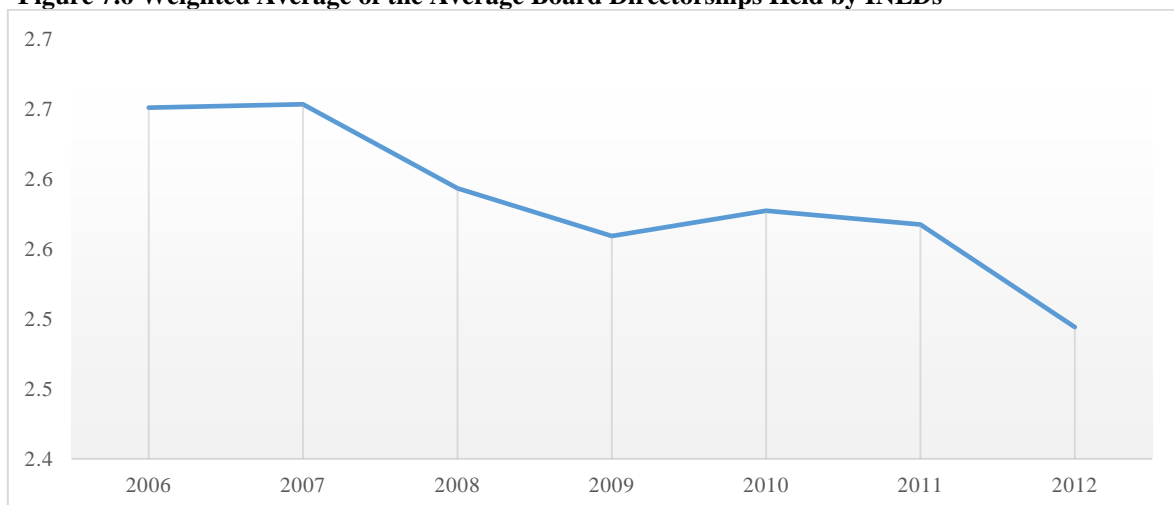


Figure 7.7 Weighted Average of the Percentage of ‘Busy’ INEDs

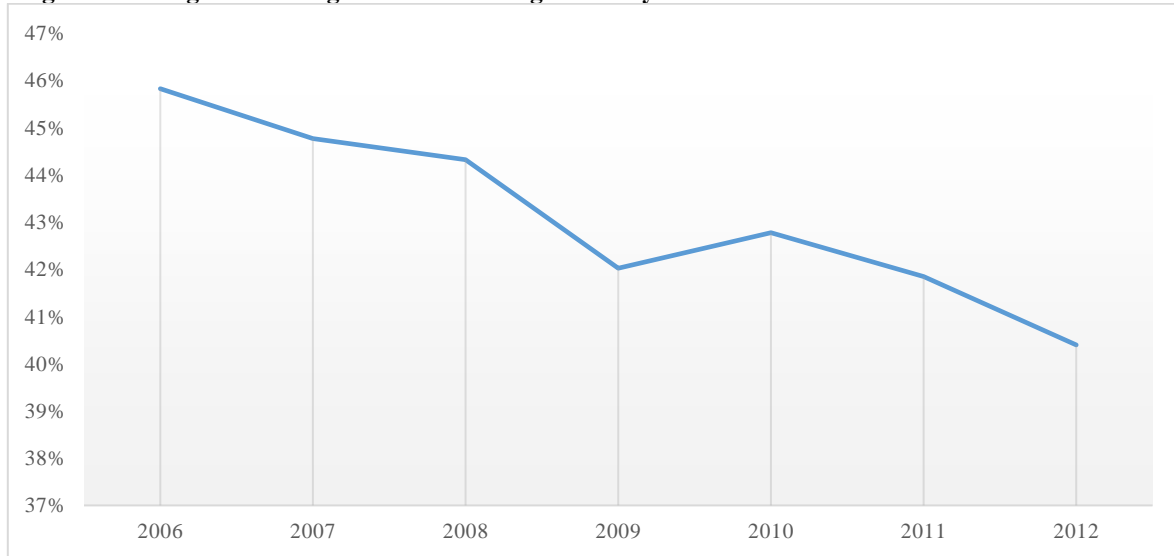


Table 7.1 further demonstrates that the level of institutional investor presence ranged from 1% to 99% for all types—with the exception of civil law institutional investors, for whom figures ranged from 1% to 68%. The average number of holdings controlled by total, foreign, domestic, common law and civil law institutional investors in the sample countries were 36%, 20%, 16%, 28% and 8%, respectively. Figure 7.8 indicates that on average, the presence of all types of institutional investors rose from 2006 to 2008, at which point their presence began to decline (until 2010). The onset of the financial crisis could be the cause of this decline. However, this graph shows that after 2010, institutional investors of all types began to reclaim their previous levels of investment in the stock markets of the sample countries.

Figure 7.8 Weighted Averages of Institutional Ownership

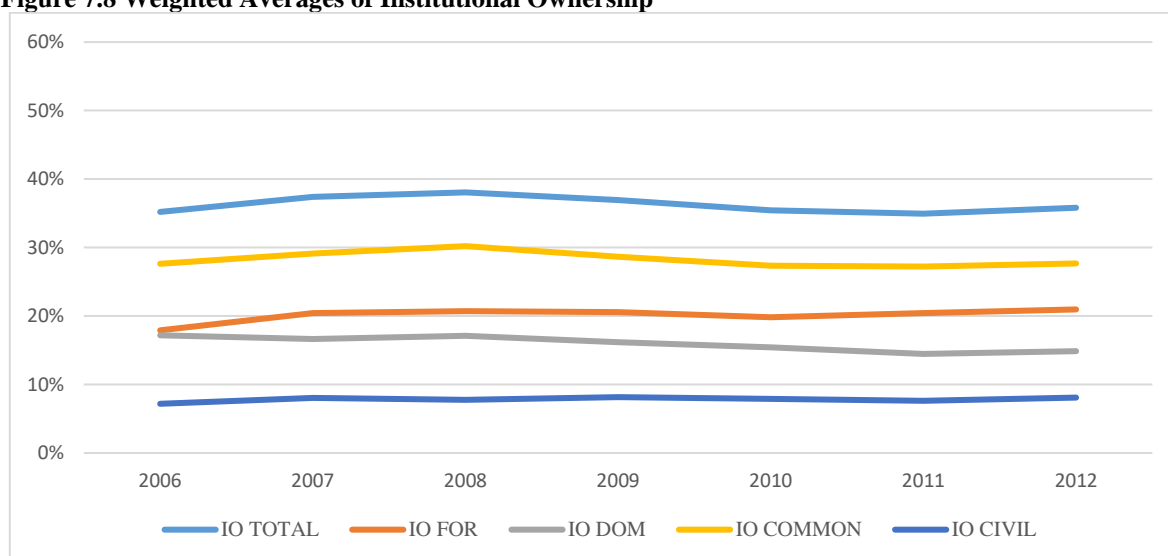


Table 7.1 also presents the statistics of the control variables. The average firm size was 7, and sales growth ranged from -43% to 116%, with an average of 12%. Figures for leverage, cash, and capital expenditures had a mean value of 26%, 11% and 6%, respectively. Table 7.1 also demonstrates that market-to-book value had a mean value of 3.2 and return on assets figures ranged from -9% to 36%, while property, plant and equipment scores ranged from 1% to 90%. The average level of analyst coverage for the entire sample was 18, with a minimum of 0 analysts following and a maximum of 55. In this sample, the average figure for companies with an ADR listing was 19%, and the rule of law index ranged from 52% to 100%. Table 7.1 also demonstrates that 37% of the total observations were classified as occurring during pre-crisis periods, 45% occurred during times of crisis and 18% occurred during post-crisis periods. With regard to the statistics for ultimate ownership, an average of 68% of companies in this sample were widely held, 20% were family-owned, 9% were state-owned and 3% were owned by institutional investors.

7.3. Correlation Analysis

This section describes the Pearson correlation matrix that exists between governance characteristics (board attributes), institutional ownership and the control variables. The main

aim of the correlation matrix is to investigate the possible presence of high correlation among the independent variables. When conducting this test, a researcher allocates a single number that measures the extent to which any two variables are related; in so doing, the direction of this relationship can be illustrated. The problem of collinearity, however, means that two variables have a relatively perfect linear correlation, which in turn renders the model estimation meaningless and difficult to interpret. According to Gujarati (2004), if the correlation between two variables exceeds 80%, the validity of the results may be threatened. Table 7.2 shows that the highest absolute correlation between explanatory variables (IO Total and IO Common) was 89%—well above the 80% threshold assigned to indicate a multi-collinearity threat (Gujarati, 2004). However, these two variables were not combined in any of the regressions used in this analysis. All correlations between other independent variables fell below this threshold (see Table 7.2).

An alternative measure used to describe the correlation issue between independent variables is to compute the variance inflation factor (VIF), which is calculated as follows:

$$VIF = \frac{1}{\text{Tolerance}}, \text{ where tolerance} = 1 - R^2, \text{ and } R^2 \text{ is the coefficient of determinations.}$$

Studenmund (2001) argued that the VIF value should not exceed 5; a higher value may be an indication that multi-collinearity threats exist within the model. In order to calculate the VIF value, an OLS model (shown below) was applied using the Board Attributes Index (GOV₁₄) as a dependent variable. Table 7.3 illustrates the results of this test and shows that multi-collinearity threats were not a factor in the utilised models, as all values were less than 5.

$$(GOV_{14}) = \beta_0 + \beta_1 (IO\ TOTAL_{(t-1)}) + \left(\begin{array}{l} \beta_2 SIZE_{(t-1)} + \beta_3 SGROWTH_{(t-1)} + \beta_4 LEV_{(t-1)} + \beta_5 CASH_{(t-1)} + \beta_6 CAPEX_{(t-1)} \\ + \beta_7 MB_{(t-1)} + \beta_8 ROA_{(t-1)} + \beta_9 PPE_{(t-1)} + \beta_{10} ANALYST_{(t-1)} + \beta_{11} ADR_{(t-1)} + \\ \beta_{12} RULE_{(t-1)} + \beta_{13} PRE - CRISIS_{(t-1)} + \beta_{14} CRISIS_{(t-1)} + \beta_{15} POST - CRISIS_{(t-1)} \\ + \beta_{16} IO_{(t-1)} + \beta_{17} STATE_{(t-1)} + \beta_{18} FAMILY_{(t-1)} + \beta_{19} WIDELY_{(t-1)} + \end{array} \right) \varepsilon$$

Table 7.2 Pearson Correlation Matrix

	GOV ₁₄	INED Board	INED AC	INED CC	INED NC	BOARD MF	AC MF	CC MF	NC MF	CEO TENURE	BOARD TENURE	BUSY BOARD	BUSY BOARD %	IO TOTAL	IO FOR	IO DOM
GOV ₁₄	1.000															
INED	0.644	1.000														
INED AC	0.594	0.602	1.000													
INED CC	0.686	0.621	0.647	1.000												
INED NC	0.653	0.561	0.475	0.711	1.000											
BOARD MF	0.117	0.067	-0.004	0.070	0.041	1.000										
AC MF	0.078	0.051	0.170	0.160	0.123	0.266	1.000									
CC MF	0.325	0.168	0.222	0.328	0.308	0.259	0.430	1.000								
NC MF	0.220	0.115	0.088	0.190	0.366	0.166	0.323	0.663	1.000							
CEO	-0.013	-0.039	0.033	0.044	0.038	-0.127	-0.081	-0.052	-0.068	1.000						
BOARD	-0.031	-0.025	-0.009	-0.010	0.004	-0.171	-0.036	-0.049	-0.046	0.376	1.000					
BUSY	-0.178	0.136	0.201	0.091	0.113	-0.116	0.032	-0.057	-0.041	-0.020	0.063	1.000				
BUSY	-0.124	0.158	0.190	0.120	0.152	-0.058	0.021	-0.012	-0.010	-0.047	0.025	0.825	1.000			
IO TOTAL	0.397	0.181	0.277	0.252	0.254	-0.040	-0.143	0.106	-0.016	0.056	0.000	-0.080	-0.027	1.000		
IO FOR	0.241	0.149	0.113	0.119	0.124	-0.053	-0.070	0.010	-0.042	0.047	0.059	-0.137	-0.105	0.702	1.000	
IO DOM	0.323	0.100	0.278	0.238	0.232	-0.005	-0.125	0.144	0.021	0.031	-0.063	0.015	0.057	0.732	0.039	1.000
IO	0.437	0.158	0.325	0.309	0.288	-0.050	-0.068	0.178	0.009	0.065	0.030	-0.067	-0.011	0.890	0.626	0.661
IO CIVIL	-0.090	0.040	-0.103	-0.126	-0.080	0.025	-0.154	-0.154	-0.052	-0.021	-0.072	-0.026	-0.033	0.227	0.162	0.152
SIZE	-0.049	0.012	0.045	0.125	0.123	0.069	0.335	0.253	0.242	-0.062	-0.014	0.196	0.203	-0.288	-0.272	-0.139
SGROWTH	-0.021	-0.061	-0.039	-0.030	-0.019	0.011	-0.008	-0.065	-0.060	0.016	-0.023	0.005	-0.006	0.008	0.028	-0.017
LEV	-0.114	-0.101	-0.122	-0.069	-0.073	0.050	-0.003	-0.014	-0.026	0.005	0.012	-0.122	-0.133	-0.027	-0.040	0.002
CASH	0.002	-0.029	-0.012	-0.036	-0.024	-0.076	0.005	-0.067	-0.045	0.002	0.029	-0.012	-0.017	-0.025	0.062	-0.095
CAPEX	0.017	0.023	-0.034	-0.016	0.002	-0.007	-0.015	-0.062	-0.024	0.007	-0.035	-0.024	-0.046	-0.073	-0.055	-0.049
MB	-0.030	-0.075	-0.029	-0.062	-0.060	-0.164	-0.123	-0.096	-0.056	0.024	0.012	0.039	0.010	0.057	0.013	0.065
ROA	-0.015	0.003	0.012	-0.037	-0.024	-0.165	-0.069	-0.064	-0.009	0.005	0.026	0.065	0.045	-0.014	-0.030	0.012
PPE	0.131	0.108	0.058	0.080	0.110	0.087	0.071	0.082	0.029	-0.044	-0.098	-0.040	-0.075	0.000	-0.026	0.031
ANALYST	-0.218	-0.107	-0.071	-0.085	-0.096	-0.073	0.138	0.033	0.090	0.026	0.009	0.156	0.096	-0.204	-0.144	-0.142
ADR	0.260	0.263	0.232	0.242	0.239	-0.018	0.240	0.187	0.130	0.007	0.105	0.095	0.147	0.183	0.107	0.154
RULE	0.408	0.284	0.039	0.153	0.276	0.079	-0.282	0.109	0.113	0.006	-0.005	-0.165	-0.032	0.312	0.204	0.233
PRE-CRISIS	-0.111	-0.067	-0.120	-0.079	-0.076	0.053	-0.012	-0.041	-0.034	-0.083	-0.056	0.025	0.046	-0.016	-0.005	-0.020
CRISIS	0.081	-0.023	0.055	0.055	0.020	-0.048	0.015	0.086	0.049	0.063	-0.019	-0.140	-0.114	0.055	0.054	0.032
POST-	0.035	0.114	0.079	0.028	0.069	-0.004	-0.005	-0.058	-0.021	0.023	0.095	0.149	0.088	-0.051	-0.064	-0.016
FAMILY	-0.273	-0.255	-0.177	-0.261	-0.194	-0.063	-0.048	-0.199	-0.107	-0.025	0.127	0.014	-0.031	-0.317	-0.190	-0.257
STATE	-0.167	-0.148	-0.155	-0.106	-0.207	0.181	0.198	0.057	0.021	-0.047	-0.206	-0.093	-0.099	-0.282	-0.193	-0.204
IO	-0.112	-0.163	-0.127	-0.114	-0.080	-0.057	-0.006	0.024	0.039	0.009	-0.023	-0.004	-0.024	0.037	0.022	0.044
WIDELY	0.376	0.367	0.292	0.330	0.320	-0.034	-0.074	0.129	0.066	0.047	0.023	0.045	0.095	0.430	0.273	0.328

Table 7.2 continued

	IO COMMON	IO CIVIL	FSIZE	SGROWTH	LEV	CASH	CAPEX	MB	ROA	PPE	ANALYST	ADR	RULE	PRE- CRISIS	CRISIS	POST- CRISIS	FAMILY	STATE	IO	WIDELY
IO COMMON	1.000																			
IO CIVIL	-0.236	1.000																		
SIZE	-0.196	-0.190	1.000																	
SGROWTH	0.031	-0.047	-0.043	1.000																
LEV	-0.032	0.009	0.116	-0.049	1.000															
CASH	-0.030	0.006	-0.158	0.045	-0.279	1.000														
CAPEX	-0.019	-0.107	-0.021	0.095	0.055	-0.082	1.000													
MB	0.086	-0.063	-0.308	0.106	0.029	0.186	0.030	1.000												
ROA	0.012	-0.050	-0.218	0.113	-0.290	0.129	0.180	0.432	1.000											
PPE	0.083	-0.169	0.137	0.071	0.175	-0.246	0.645	-0.103	0.028	1.000										
ANALYST	-0.224	0.050	0.372	-0.078	-0.076	0.080	-0.078	0.057	0.132	-0.167	1.000									
ADR	0.264	-0.172	0.259	0.028	-0.057	-0.052	0.081	0.026	0.064	0.184	-0.012	1.000								
RULE	0.205	0.218	-0.061	-0.043	-0.022	-0.041	-0.065	-0.036	-0.037	0.017	-0.268	0.136	1.000							
PRE-CRISIS	-0.028	0.019	-0.048	0.177	0.038	-0.028	0.045	0.098	0.095	0.005	-0.149	0.012	0.058	1.000						
CRISIS	0.048	0.020	0.049	-0.171	0.019	0.028	-0.170	-0.075	-0.120	-0.127	0.105	-0.044	0.037	-0.690	1.000					
POST-CRISIS	-0.027	-0.048	-0.003	-0.001	-0.072	-0.002	0.162	-0.026	0.035	0.158	0.050	0.042	-0.121	-0.362	-0.424	1.000				
FAMILY	-0.273	-0.088	-0.027	0.020	0.018	0.002	0.005	-0.047	-0.019	-0.036	-0.037	-0.152	-0.171	0.009	0.008	-0.021	1.000			
STATE	-0.266	-0.028	0.177	-0.017	0.039	-0.061	0.060	-0.092	-0.007	0.127	0.133	-0.130	-0.168	-0.005	0.005	0.000	-0.152	1.000		
IO	-0.030	0.158	0.035	-0.014	0.090	-0.036	-0.053	-0.024	-0.027	0.011	0.045	-0.054	-0.013	0.022	0.023	-0.057	-0.085	-0.052	1.000	
WIDELY	0.406	0.036	-0.096	-0.002	-0.071	0.048	-0.022	0.105	0.030	-0.049	-0.064	0.229	0.253	-0.013	-0.018	0.038	-0.739	-0.451	-0.253	1.000

The correlation coefficients at 5% are in bold. GOV14= Board attributes index, INED BOARD = Board independence, INED AC = Audit committee Independence, INED CC= Compensation committee independence, INED NC = Nomination committee independence, BOARD MF = Board meeting frequency, AC MF = Audit committee meeting frequency, CC MF = Compensation committee meeting frequency, NC MF = Nomination committee meeting frequency, CEO TENURE = CEO tenure, Board TENURE = Board tenure, BUSY BOARD = Busy board, BUSY BOARD % = Busy Board %, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, PRE-CRISIS= Pre-Crisis Dummy, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, IO = Institutional investor controlling at 20%, WIDELY = Widely held at 20%.

Table 7.3 VIF Tests

Table 10: VIF Tests

	VIF	1/VIF
WIDELY	3.52	0.28
FAMILY	2.86	0.35
PPE	2.17	0.46
CAPEX	1.93	0.52
FSIZE	1.86	0.54
IO TOTAL	1.58	0.63
ROA	1.52	0.66
ANALYST	1.48	0.67
MB	1.47	0.68
IO	1.36	0.74
ADR	1.32	0.76
LEV	1.32	0.76
Crisis	1.24	0.81
RULE	1.23	0.82
Post-Crisis	1.22	0.82
CASH	1.2	0.83
SGROWTH	1.08	0.93
Mean VIF	1.67	

IO TOTAL = Total institutional investors, SIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, PRE-CRISIS= Pre-Crisis Dummy, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, IO = Institutional investor controlling at 20%, WIDELY = Widely held at 20%.

7.4. Institutional Investors and Board Attributes: Panel Data Analysis

7.4.1. Board Attributes Index

A firm fixed effects panel regression was applied to investigate the role of institutional ownership in corporate governance. The dependent variable was the Board Attributes Index, and the independent variable was institutional ownership (see Table 7.4). All independent variables were lagged by one period so that the relationship between explanatory variables and future board attributes could be tested. The regressions also included the control variables mentioned in the previous chapter. These regressions corrected for the standard errors that occur when observations are clustered at the firm level, as per the work of Aggarwal et al. (2011).

Model 1 of Table 7.4 indicates that there was a positive and significant association between total institutional ownership and the Board Attributes Index (GOV₁₄) at 5% (with coefficient = 0.006, p-value = 0.033, and R-Squared value = 0.098). The results support those who find that

institutional investors improve several governance attributes in their investee firms, including firm valuation (Ruiz-Mallorquí and Santana-Martín, 2011; Muniandy et al., 2016); antitakeover amendments (Brickley et al., 1988); CEO turnover decisions (Parrino et al., 2003; Helwege et al., 2012); the selection of auditing firms (Kane and Velury, 2004); managerial compensation schemes (Hartzell and Starks, 2003; Almazan et al., 2005); dividend pay-outs, operating performance and CEO turnover (Brav et al., 2008); and earnings management (Hadani et al., 2011). The results are also consistent with the view that one of the major issues discussed behind the scenes between institutional investors and their investee firms is the governance structure (McCahery et al., 2016).

Model 2 of Table 7.4 demonstrates that there was a positive and significant association between foreign institutional ownership and the Board Attributes Index (GOV₁₄) at 1% (with coefficient = 0.009, p-value = 0.008, and R-Squared value = 0.101), whereas Model 3 demonstrates that the coefficient was negative but insignificant for domestic institutions (with coefficient = -0.001, p-value = 0.758, and R-Squared value = 0.095). Notably, these results were wholly consistent with the findings of Aggarwal et al. (2011), who argued that foreign institutional investors promote favourable governance outcomes as compared to their domestic counterparts. This also reflects previous studies (e.g. Gillan and Starks, 2003; Ferreira and Matos, 2008; Beuselinck et al., 2017; Luong et al., 2017) that contended that foreign institutional investors have fewer ties to their investee firms because of their independent positions and therefore are expected to exert greater pressure over the management of an investee firm in an effort to establish a strong governance structure. Additionally, Models 4 and 5 show that the coefficient was positive but insignificant for both common law and civil law institutions⁴¹ (with coefficient = 0.005 and 0.008, p-value = 0.110 and 0.313, and R-

⁴¹ When the empirical analysis is repeated including the US observations, the study obtained consistent findings.

Squared value = 0.097 and 0.096, respectively). Overall, the results were partially consistent with H1 and are consistent with the agency, stewardship, stakeholder and institutional theories. The findings particularly contribute to the literature of corporate governance that corporate board attributes are important for the institutional investors and that they enhance these attributes when they engage with their investee firms, with the foreign institutional investors playing a lead role in the improvement of board attributes. The results also imply that attributes of the corporate board are deemed to be crucial for the institutional investors, as the attributes of the corporate board reflect its effectiveness in the reduction of agency cost and in fulfilling its duties (Zahra and Pearce, 1989; Aguilera et al., 2012; Mallin, 2016).

Table 7.4 Institutional Investors and the Board Attributes Index

GOV ₁₄					
	(1)	(2)	(3)	(4)	(5)
<i>Panel A: Firm Fixed Effects(All Observations)</i>					
IO TOTAL	0.006** (0.033)				
IO FOR		0.009*** (0.008)			
IO DOM			-0.001 (0.758)		
IO COMMON				0.005 (0.110)	
IO CIVIL					0.008 (0.313)
FSIZE	-0.665** (0.023)	-0.672** (0.021)	-0.714** (0.014)	-0.686** (0.018)	-0.695** (0.018)
SGROWTH	0.048 (0.668)	0.051 (0.652)	0.052 (0.650)	0.051 (0.655)	0.048 (0.676)
LEV	0.500 (0.308)	0.533 (0.273)	0.474 (0.334)	0.516 (0.293)	0.455 (0.357)
CASH	-1.061** (0.047)	-1.063** (0.045)	-1.048** (0.050)	-1.048* (0.050)	-1.051** (0.049)
CAPEX	-2.134** (0.039)	-2.241** (0.034)	-2.312** (0.027)	-2.200** (0.036)	-2.219** (0.030)
MB	0.014 (0.450)	0.014 (0.436)	0.012 (0.497)	0.013 (0.476)	0.013 (0.470)
ROA	1.300** (0.036)	1.297** (0.035)	1.169* (0.055)	1.270** (0.040)	1.196* (0.051)
PPE	0.211 (0.734)	0.240 (0.702)	0.285 (0.644)	0.273 (0.657)	0.220 (0.728)
ANALYST	0.004 (0.599)	0.004 (0.611)	0.004 (0.602)	0.004 (0.608)	0.004 (0.588)
ADR	0.399 (0.332)	0.382 (0.352)	0.413 (0.315)	0.402 (0.330)	0.412 (0.315)
RULE	-0.043 (0.190)	-0.045 (0.171)	-0.043 (0.197)	-0.045 (0.172)	-0.040 (0.220)
CRISIS	0.002 (0.984)	0.026 (0.818)	-0.002 (0.989)	0.001 (0.991)	-0.005 (0.966)
POST-CRISIS	-0.138 (0.365)	-0.106 (0.488)	-0.139 (0.360)	-0.139 (0.361)	-0.141 (0.354)
FAMILY	0.826*** (0.004)	0.830*** (0.005)	0.722** (0.013)	0.764*** (0.007)	0.816*** (0.007)
STATE	0.249 (0.491)	0.251 (0.512)	0.121 (0.746)	0.150 (0.681)	0.270 (0.478)
WIDELY	0.572** (0.013)	0.578** (0.016)	0.490** (0.045)	0.515** (0.024)	0.581** (0.023)
N	2028	2028	2028	2028	2028
R-Squared	0.098	0.101	0.095	0.097	0.096

Table 7.4 continued

GOV ₁₄					
	(1)	(2)	(3)	(4)	(5)
Panel B: Firm Fixed Effects (Pre-Crisis Observations)					
IO TOTAL	0.003				
	(0.738)				
IO FOR		0.002			
		(0.740)			
IO DOM			0.004		
			(0.832)		
IO COMMON				0.002	
				(0.800)	
IO CIVIL					0.009
					(0.686)
N	551	551	551	551	551
R-Squared	0.042	0.042	0.042	0.042	0.042
Panel C: Firm Fixed Effects (Crisis Observations)					
IO TOTAL	0.004				
	(0.373)				
IO FOR		0.010*			
		(0.072)			
IO DOM			-0.009		
			(0.108)		
IO COMMON				0.001	
				(0.873)	
IO CIVIL					0.013
					(0.278)
N	1047	1047	1047	1047	1047
R-Squared	0.106	0.111	0.107	0.105	0.108
Panel D: Firm Fixed Effects (Post-Crisis Observations)					
IO TOTAL	0.022***				
	(0.005)				
IO FOR		0.015			
		(0.112)			
IO DOM			0.033**		
			(0.012)		
IO COMMON				0.018*	
				(0.059)	
IO CIVIL					0.070***
					(0.000)
N	430	430	430	430	430
R-Squared	0.090	0.072	0.083	0.076	0.100
Panel E: Firm Fixed Effects (Interaction Effects)					
IO TOTAL * FAMILY			-0.002		
			(0.717)		
IO FOR * FAMILY			-0.002		
			(0.651)		
IO DOM * FAMILY			-0.002		
			(0.887)		
IO TOTAL * Non-FAMILY			0.008***		
			(0.008)		
IO FOR * Non-FAMILY			0.013***		
			(0.000)		
IO DOM * Non-FAMILY			-0.001		
			(0.796)		

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. GOV₁₄= Board attributes index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, WIDELY = Widely held at 20%.

The investigation then moved to an examination of whether the role of institutional investors in the improvement of governance structures was determined by economic conditions (pre-crisis, crisis and post-crisis periods). The firm fixed effects regression revealed that institutional investors had no significant influence over the governance outcomes of their investee firms during pre-crisis periods (see Table 7.4, Panel B). This is consistent with previous studies that claim that institutional investors took excessive risks before the crisis (Erkens et al., 2012; Díez-Esteban et al., 2016). This may also explain why institutional investors did not enhance board attributes (GOV₁₄) in their investee firms prior to the financial crisis. Adams (2012) also found that the governance structure of non-financial firms is weaker compared to their financial counterparts prior to the recent financial crisis. Several scholars have blamed both the institutional investors and the corporate boards alike for their inability to mitigate the aforementioned crisis (Conyon et al., 2011; Reisberg, 2015).

The results also showed that in times of crisis, only foreign institutions had a positive and significant relationship at 10% (with coefficient = 0.010, p-value = 0.072, and R-Squared value = 0.111), (see Table 7.4, Panel C). However, the results further demonstrated that during post-crisis periods, all types of institutional investors (total, foreign, domestic, common and civil) had positive and significant associations with the Board Attributes Index, with the exception of foreign institutional investors (with coefficient = 0.022, 0.015, 0.033, 0.018 and 0.070, p-value = 0.005, 0.112, 0.012, 0.059, 0.000, and R-Squared value = 0.090, 0.072, 0.083, 0.076 and 0.100, respectively), (see Table 7.4, Panel D). Overall, the results are consistent with the institutional theory, and they indicate the institutional investors' awareness of the importance of corporate board attributes after the recent financial crisis. Following the crisis, the OECD published a report on governance lessons learned from the recent financial crisis that clearly illustrates that the weaknesses of corporate governance was one of the key reasons the crisis occurred (Kirkpatrick, 2009).

Next, the study examined the role of institutional investors in the improvement of governance outcomes in light of various ownership structures; this was accomplished by considering the interactions between institutional investors and family- and non-family-controlled firms (see Table 7.4, Panel E). The firm fixed effects regression showed that institutional investors (total and foreign) had the ability to improve the governance structures of non-family-owned firms only (with coefficient = 0.008 and 0.013, and p-value = 0.008 and 0.000, respectively). However, this result did not hold true for family-owned firms. Drawing from the institutional theory, these results also complement the other studies that emphasised the contingency of ownership structure when investigating the adoption of corporate governance mechanisms in a particular firm (Desender et al., 2013; Judge, 2011, 2012; Sure et al., 2013) by showing that the role of institutional investors in improving board attributes is determined by the ownership structure (family vs non-family-controlled firms). The results are also consistent with the second type of the agency problem (Principal-Principal conflict), which occurs when minority shareholders fear the expropriation by the controlling shareholders (Shleifer and Vishny, 1997). Fernando et al. (2014) argued that institutional investors avoid investing in family-controlled firms, as they fear the expropriation of their wealth.

The study then examined whether the role of institutional investors in corporate governance was derived from the legal system of the country wherein an investee firm operated (civil law versus common law countries). Table 7.5 conveys the results of a firm fixed effects regression of the Board Attributes Index (GOV_{14}); these results are reported separately according to whether the firm was located in a civil law or a common law country. Models 1 and 2 of Table 7.5 show that total and foreign institutional investors had positive but insignificant associations with the Board Attributes Index in civil law countries (with coefficient = 0.005 and 0.005, p-value = 0.329 and 0.348, and R-Squared value = 0.110 and 0.110, respectively). In contrast, Model 3 demonstrates that the coefficient was negative but insignificant for domestic

institutions (with coefficient = -0.001, p-value = 0.940, and R-Squared value = 0.109). Conversely, in common law countries, total and foreign institutional investors had a positive and significant relationship at the 10% and 1% significance level, respectively (with coefficient = 0.005 and 0.011, p-value = 0.069 and 0.001, and R-Squared value = 0.146 and 0.154, respectively). This result indicates that the role of institutional investors in the improvement of governance structures was indeed dependent on the legal system of the country in which a firm was listed. The institutional investors' inability to improve board attributes in civil law countries can be understood in light of the ownership concentration in civil law countries (La Porta et al., 1999), which results in 'Principal-Principal conflict' (Shleifer and Vishny, 1997). Drawing from the institutional theory, the results complement the other studies that ascertained that the legal system should be considered when investigating the adoption of corporate governance practices across countries (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014). In particular, the findings reveal that the activism of institutional investors towards improving board attributes in their investee firms is also attributed to the legal system of a particular country.

Table 7.5 Institutional Investors and the Board Attributes Index: The Role of Legal Origin

GOV ₁₄						
	Civil Law Countries			Common Law Countries		
	Panel A: Firm Fixed Effects Panel			Panel B: Firm Fixed Effects Panel		
	(1)	(2)	(3)	(4)	(5)	(6)
IO TOTAL	0.005 (0.329)			0.005* (0.069)		
IO FOR		0.005 (0.348)			0.011*** (0.001)	
IO DOM			-0.001 (0.940)			-0.001 (0.718)
SIZE	-0.995* (0.094)	-1.021* (0.083)	-1.041* (0.083)	-0.326 (0.249)	-0.279 (0.321)	-0.366 (0.193)
SGROWTH	-0.128 (0.548)	-0.122 (0.566)	-0.120 (0.578)	0.138 (0.236)	0.129 (0.263)	0.145 (0.216)
LEV	0.666 (0.346)	0.692 (0.324)	0.686 (0.336)	-0.139 (0.788)	-0.086 (0.865)	-0.227 (0.662)
CASH	-1.354* (0.100)	-1.387* (0.091)	-1.380* (0.093)	-1.046* (0.073)	-1.003* (0.086)	-1.003* (0.083)
CAPEX	-3.535** (0.043)	-3.619** (0.043)	-3.597** (0.043)	-0.949 (0.345)	-0.992 (0.324)	-1.191 (0.233)
MB	0.066* (0.071)	0.065* (0.073)	0.065* (0.076)	-0.008 (0.591)	-0.005 (0.719)	-0.009 (0.556)
ROA	1.837* (0.062)	1.783* (0.069)	1.751* (0.069)	0.501 (0.433)	0.643 (0.305)	0.374 (0.554)
PPE	-0.442 (0.649)	-0.430 (0.657)	-0.439 (0.653)	0.662 (0.303)	0.683 (0.323)	0.784 (0.213)
ANALYST	-0.009 (0.432)	-0.010 (0.414)	-0.009 (0.416)	0.017* (0.085)	0.017* (0.072)	0.018* (0.068)
ADR	1.076* (0.059)	1.074* (0.060)	1.102* (0.050)	0.036 (0.805)	0.012 (0.929)	0.031 (0.823)
RULE OF LAW	-0.078 (0.143)	-0.079 (0.141)	-0.083 (0.122)	-0.036 (0.423)	-0.048 (0.280)	-0.030 (0.510)
CRISIS	0.428*** (0.002)	0.429*** (0.002)	0.415*** (0.003)	0.167 (0.148)	0.183 (0.115)	0.170 (0.143)
POST-CRISIS	0.375* (0.056)	0.373* (0.057)	0.351* (0.073)	-0.195 (0.249)	-0.157 (0.352)	-0.172 (0.307)
FAMILY	0.365 (0.313)	0.348 (0.344)	0.267 (0.463)	1.397*** (0.000)	1.388*** (0.000)	1.335*** (0.000)
STATE	-0.274 (0.537)	-0.305 (0.512)	-0.403 (0.359)	1.381** (0.027)	1.406** (0.034)	1.318** (0.049)
WIDELY	0.130 (0.686)	0.111 (0.736)	0.040 (0.903)	1.065*** (0.000)	1.087*** (0.000)	1.028*** (0.000)
N	1089	1089	1089	939	939	939
R-Squared	0.110	0.110	0.109	0.146	0.154	0.143

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. GOV₁₄ = Board attributes index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, WIDELY = Widely held at 20%.

7.4.2. Board and Key Subcommittees Composition

Table 7.6 presents the results of a firm fixed effect panel regression that aimed to examine the role of institutional ownership in the improvement of board composition as well as the composition of its key subcommittees (audit, compensation and nomination). The independence of the board and its key subcommittees was used to investigate this relationship. According to the results, institutional investors promoted the improvement of board composition as well as the composition of its key subcommittees (with the exception of the nomination committee). Drawing from the agency theory, the results are consistent with those

who ascertained that institutional investors are attracted by firms whose board independence is high (Useem et al., 1993; Chung and Zhang, 2011; Miletkov et al., 2014). Several scholars emphasised the importance of corporate board independence in the reduction of the agency costs (Anderson and Reeb, 2004; Bebchuk and Weisbach, 2010). Table 7.6 indicates a positive and significant association between board independence and total institutional ownership at the 5% significance level (with coefficient = 0.001, p-value = 0.036 and R-Squared value = 0.077). In contrast, the coefficient was positive but insignificant for foreign and domestic institutions (see Table 7.6, Panel A).

The results also revealed that total institutional ownership promoted the improved independence of audit and compensation committees (with coefficient = 0.001 and 0.001, p-value = 0.003 and 0.002, and R-Squared value = 0.054 and 0.039, respectively). Given the monitoring role of institutional investors, these results reflect other studies that emphasised the importance of the composition of audit and compensation committees in mitigating the agency costs (Newman and Mozes, 1999; Abbott and Parker, 2000; Klein, 2002; Abbott et al., 2003; Zaman et al., 2011). Conversely, total institutional ownership had a negative but insignificant relationship with nomination committee independence. Moreover, results indicated that domestic and foreign institutions promoted audit committee independence (with coefficient = 0.001 and 0.001, p-value = 0.082 and 0.027, and R-Squared value = 0.049 and 0.051, respectively), while foreign institutions promoted the independence of compensation committees (with coefficient = 0.001, p-value = 0.009 and R-Squared = 0.038). The results are consistent with the agency theory framework and support the view that the majority of the decisions are made by the board subcommittees, which are forwarded later to the corporate board for voting (Lorsch MacIver, 1989; Mahadeo et al., 2012); since the foreign institutional investors have a higher monitoring cost because of their remoteness, as well as linguistic and cultural differences to the investee compared to their domestic counterparts (Kim et al., 2016),

the results could be explained by the fact that foreign institutional investors choose to improve the composition of more subcommittees to ensure that the monitoring and the quality of the work undertaken by such committees in their investee firms is effective. Both types of institutional investors (domestic and foreign) had an insignificant association with the independence of the nomination committee, however (see Table 7.6, Panel A). Collectively, these results supported the agency theory and were consistent with both H2a and H2b. The results contribute to the literature by showing that not only the independence of the corporate board is deemed important to the institutional investors when they enter into dialogue with their investee firms, but also the independence of board key subcommittees (i.e. audit and compensation committees) is also important. The results imply that the activism of institutional investors expanded to include not only the corporate board composition but also the structure of the board key subcommittees around the globe.

The study next compared the role of institutional investors in the improvement of board composition according to various economic conditions (see Table 7.6, Panels B, C and D). The results showed that during pre-crisis periods, institutional investors had mixed but insignificant influence over the independence of a board and its key subcommittees. However, during times of crisis, total institutional investors had positive and significant relationships with the independence of audit committees at 5% (with coefficient = 0.001, p-value = 0.020 and R-Squared = 0.071), but negative and significant relationships with the independence of nomination committees at 1% (with coefficient = -0.001, p-value = 0.068 and R-Squared = 0.067). Furthermore, foreign institutional investors had positive and significant associations with the independence of boards and their audit committees at 10% and 5% respectively (with coefficient = 0.001 and 0.002, p-value = 0.054 and 0.014 and R-Squared = 0.080 and 0.075, respectively). The results support the institutional theory and are consistent with those who found that board independence may bring fruitful governance outcomes during crises. For

instance, Francis et al. (2012) and Yeh et al. (2011) found that board independence and audit committee independence improved firm performance during the time of the crisis, respectively. Finally, the results revealed that during post-crisis periods, only domestic institutional investors had positive and significant associations with the independence of audit and nomination committees at 5% and 10% respectively (with coefficient = 0.004 and 0.003 p-value = 0.030 and 0.092 and R-Squared = 0.123 and 0.108, respectively).

Table 7.6 Institutional Investors and the Composition of Boards and their Subcommittees

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
	INED BOARD			INED AC			INED CC			INED NC		
Panel A: Firm Fixed Effects (All Observations)												
IO TOTAL	0.001** (0.036)			0.001*** (0.003)			0.001*** (0.002)			-0.000 (0.632)		
IO FOR		0.000 (0.104)			0.001** (0.027)			0.001*** (0.009)			-0.000 (0.666)	
IO DOM			0.001 (0.319)			0.001* (0.082)			0.001 (0.278)			0.000 (0.796)
N	2028	2028	2028	2028	2028	2028	2028	2028	2028	2028	2028	2028
R-Squared	0.077	0.076	0.075	0.054	0.051	0.049	0.039	0.038	0.034	0.046	0.046	0.046
Panel B: Firm Fixed Effects (Pre-Crisis Observations)												
IO TOTAL	0.001 (0.121)			-0.000 (0.715)			0.000 (0.525)			0.000 (0.917)		
IO FOR		0.001 (0.209)			-0.000 (0.728)			0.000 (0.629)			0.000 (0.803)	
IO DOM			0.001 (0.327)			-0.000 (1.000)			0.001 (0.604)			0.000 (0.994)
N	551	551	551	551	551	551	551	551	551	551	551	551
R-Squared	0.122	0.119	0.119	0.080	0.080	0.080	0.106	0.106	0.106	0.042	0.042	0.042
Panel C: Firm Fixed Effects (Crisis Observations)												
IO TOTAL	0.001 (0.300)			0.001** (0.020)			0.000 (0.871)			-0.001* (0.068)		
IO FOR		0.001* (0.054)			0.002** (0.014)			0.000 (0.669)			-0.001 (0.129)	
IO DOM			-0.001 (0.205)			0.000 (0.785)			-0.000 (0.721)			-0.001 (0.464)
N	1047	1047	1047	1047	1047	1047	1047	1047	1047	1047	1047	1047
R-Squared	0.073	0.080	0.072	0.071	0.075	0.060	0.035	0.036	0.035	0.067	0.066	0.062
Panel D: Firm Fixed Effects (Post-Crisis Observations)												
IO TOTAL	-0.000 (0.752)			0.001 (0.104)			0.001 (0.210)			0.002 (0.145)		
IO FOR		0.000 (0.980)			0.000 (0.776)			0.001 (0.392)			0.001 (0.410)	
IO DOM			-0.000 (0.865)			0.004** (0.030)			0.002 (0.149)			0.003* (0.092)
N	430	430	430	430	430	430	430	430	430	430	430	430
R-Squared	0.145	0.145	0.145	0.108	0.097	0.123	0.083	0.079	0.082	0.108	0.102	0.108

Table 7.6 continued

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
	INED BOARD			INED AC			INED CC			INED NC		
Panel E: Firm Fixed Effects (Common Law Observations)												
IO TOTAL	-0.000 (0.954)			0.000 (0.147)			0.000 (0.126)			-0.001 (0.126)		
IO FOR		0.000 (0.560)			0.000 (0.127)			0.001 (0.177)			-0.001 (0.231)	
IO DOM			-0.000 (0.368)			0.000 (0.692)			0.000 (0.504)			-0.000 (0.716)
N	939	939	939	939	939	939	939	939	939	939	939	939
R-Squared	0.142	0.143	0.143	0.060	0.060	0.057	0.053	0.054	0.051	0.106	0.105	0.103
Panel F: Firm Fixed Effects (Civil Law Observations)												
IO TOTAL	0.001** (0.020)			0.002** (0.016)			0.002** (0.016)			-0.000 (0.882)		
IO FOR		0.001 (0.183)			0.001* (0.081)			0.002** (0.031)			-0.000 (0.943)	
IO DOM			0.003* (0.088)			0.003 (0.184)			0.002 (0.393)			0.000 (0.976)
N	1089	1089	1089	1089	1089	1089	1089	1089	1089	1089	1089	1089
R-Squared	0.101	0.095	0.106	0.089	0.085	0.087	0.062	0.060	0.056	0.052	0.052	0.052
Panel G: Interaction Effects (Firm Fixed Effects)												
IO TOTAL * FAMILY		0.001 (0.279)			0.002** (0.045)			-0.001 (0.302)			-0.001 (0.318)	
IO FOR * FAMILY		0.000 (0.375)			0.001* (0.074)			-0.000 (0.532)			-0.001 (0.351)	
IO DOM* FAMILY		0.002 (0.360)			0.004 (0.156)			-0.000 (0.951)			-0.000 (0.993)	
IO TOTAL * Non-FAMILY		0.000* (0.072)			0.001** (0.010)			0.001*** (0.000)			-0.000 (0.989)	
IO FOR * Non-FAMILY		0.000 (0.213)			0.001* (0.078)			0.002*** (0.003)			-0.000 (0.975)	
IO DOM* Non-FAMILY		0.000 (0.528)			0.001 (0.295)			0.001 (0.242)			0.000 (0.786)	
Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 7.4. INED BOARD = Board independence, INED AC = Audit committee Independence, INED CC= Compensation committee independence, INED NC = Nomination committee independence, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.												

The study then investigated whether legal systems affected the role of institutional investors in the improvement of board composition and that of its key subcommittees (see Table 7.6, Panels E and F). Overall, institutional investors are found to promote more favourable board and key subcommittee compositions in civil law countries as compared to common law countries; this result did not hold true, however, for nomination committees. The results revealed that total institutional investors have a positive and significant association with the independence of the board and audit and compensation committees at a 5% significance level (with coefficient = 0.001, 0.002 and 0.002, p-value = 0.020, 0.016 and 0.016, and R-Squared value = 0.101, 0.089 and 0.062, respectively).

The findings may be explained by the institutional theory perspective, in that institutional investors improve the composition of the board and its key subcommittees in civil law countries in order to mitigate the weak shareholder protections in civil law countries compared to their common law counterparts (La Porta et al., 1998). Gaitán et al. (2018) showed that board independence is among the factors leading to firm productivity in civil law countries. This is consistent with Yeh et al. (2011), who argue that the influence of the audit committee's independence on firm performance is greater in civil law countries compared to their common law counterparts. The results also revealed that while domestic institutions encouraged board independence (with coefficient = 0.003, p-value = 0.088, and R-Squared value = 0.106), foreign institutions promoted the independence of audit and compensation committees (with coefficient = 0.001 and 0.002, p-value = 0.081 and 0.031, and R-Squared value = 0.085 and 0.060, respectively). This could be attributed to the fact that foreign institutional investors are more independent monitors of the investee firms and are less prone to local political pressure (Gillan and Starks, 2003; Ferreira and Matos, 2008); therefore, they are expected to more carefully scrutinise the composition of the subcommittees compared to their domestic counterparts.

Next, the study examined whether the ownership structure of investee firms influenced the role of institutional investors in the improvement of corporate board composition and that of its key subcommittees (see Table 7.6, Panel G). The results indicated that the presence of institutional investors did indeed improve the composition of a board and its key subcommittees (with the exception of nomination committees) in non-family-owned firms. For instance, total institutional investors had a positive and significant relationship with the independence of the board and the independence of the audit and compensation committees at 10%, 5% and 1% respectively (with coefficient = 0.000, 0.001 and 0.001, and p-value = 0.072, 0.010 and 0.000, respectively). In addition, foreign institutional investors had a positive and significant relationship with the independence of audit and compensation committees at 10% and 1% respectively (with coefficient = 0.001 and 0.002, and p-value = 0.078 and 0.003, respectively). In family-owned firms, however, the results indicated that the activity of institutional investors (foreign and total) only improved the independence of audit committees (with coefficient = 0.001 and 0.002, and p-value = 0.074 and 0.045, respectively). Overall, the results support the second type of the agency theory (Principal-Principal conflict) (Shleifer and Vishny, 1997), as the influence of institutional investors on improving the independence of the corporate board and its key subcommittees is more evident in non-family firms. The results also emphasised the contingency of ownership structure, which influences the adoption of governance practices (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014), and highlighted the tendency of foreign institutional investors to improve the governance practices in their investee firms due to their independence from the investee firms compared to their domestic counterparts (Ferreira and Matos, 2008; Aggarwal et al., 2011; Kim et al., 2016).

7.4.3. Board and Key Subcommittees Activity

This study then continued on to an investigation of whether institutional investors promoted the activity of a board and its key subcommittees. Meeting frequency at the board and subcommittee levels was used to examine this relationship. Table 7.7 presents the results of a firm fixed effect panel regression, which indicated that total, foreign and domestic investors had mixed and insignificant relationships with the meeting frequency of corporate boards and their compensation and nomination subcommittees (see Table 7.7, Panel A). In contrast, institutional investors (total and domestic) had a positive association with the meeting frequency of audit committees at 10% and 5% respectively (with coefficient = 0.007 and 0.010, p-value = 0.089 and 0.046, and R-Squared value = 0.034 and 0.034, respectively). The results contribute to the literature about the tendency of institutional investors to improve the activity of the audit committee. Drawing from the agency theory, these results are consistent with several studies that argued that the activism of the audit committee leads to higher firm performance (Hoque et al., 2013), lower earnings management (Xie et al., 2003) and employment of an industry-specialist auditor (Abbott et al., 2000). Accordingly, the results partially support the agency theory, and they are determined to reject H3a and partially accept H3b.

The study also compared the role of institutional investors in efforts to improve the activity of a corporate board and its key subcommittees according to various economic conditions (see Table 7.7, Panels B, C and D). The results revealed that during pre-crisis periods, total and domestic institutional investors had a negative association with the meeting frequency of a corporate board and compensation committee respectively at 1% (with coefficient = -0.029 and -0.048, p-value = 0.098 and 0.062, and R-Squared value = 0.171 and 0.058, respectively). However, this relationship waned during crisis and post-crisis periods. Furthermore, the association between institutional investors and the meeting frequency of key subcommittees

was mixed and insignificant in all economic environments. . The results are consistent with other scholars who blamed the institutional investors and the corporate board for the occurrence of the recent financial crisis (see Conyon et al., 2011; Reisberg, 2015). Consequently, the previously mentioned OECD report on governance lessons emphasises that board access to information is key, which can primarily be shared via more board meetings (Kirkpatrick, 2009). Hahn and Lasfer (2016) also observed that the recent financial crisis did not improve the board meetings in UK firms. Following a comparison of this relationship within different legal systems, results indicated that domestic and total institutional investors had positive and significant associations with the meeting frequency of audit and nomination committees, respectively, in common law countries at 10% (with coefficient = 0.010 and 0.012, p-value = 0.050 and 0.063, and R-Squared value = 0.078 and 0.042, respectively). In civil law countries, while foreign institutional investors had positive and significant relationship with the meeting frequency of audit committee (with coefficient = 0.012, p-value = 0.058, and R-Squared value = 0.068), they had negative and significant association with the meeting frequency of corporate board at 10% (with coefficient = -0.020, p-value = 0.077, and R-Squared value = 0.046). Results also showed that total institutional investors had negative and significant relationship with the activity of the nomination committees at 10% (with coefficient = -0.010, p-value = 0.092, and R-Squared value = 0.059) (see Table 7.7, Panels E and F). The research then examined whether the relationship between institutional investors and the activity of a corporate board and its key subcommittees was driven by a company's ownership structure. The results revealed that the association between institutional investors and the activity of a corporate board and its key subcommittees was mixed and insignificant in both family- and non-family-owned firms (see Table 7.7, Panel G). Finally, the findings showed that total and domestic institutions had negative and significant associations in family firms at the 10% significance level (with coefficient = -0.023 and -0.044, and p-value value = 0.061 and 0.097,

respectively). Consistent with the institutional theory, these results complement the other studies on the influence of the legal system (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014) and ownership structure (Desender et al., 2013; Judge, 2011, 2012; Sure et al., 2013) in shaping governance practices by showing that the role of the institutional investors in improving the activity of the corporate board and key subcommittees is partially explained by the economic conditions and legal system, but not by the ownership structure.

Table 7.7 Institutional Investors and the Activity of Boards and their Subcommittees

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
	Board MF			AC MF			CC MF			NC MF		
Panel A: Firm Fixed Effects (All Observations)												
IO TOTAL	-0.004 (0.674)			0.007* (0.089)			-0.001 (0.847)			0.001 (0.887)		
IO FOR		-0.008 (0.354)			0.006 (0.205)			-0.001 (0.875)			-0.003 (0.508)	
IO DOM			0.012 (0.456)			0.010** (0.046)			0.003 (0.674)			0.009 (0.180)
N	2028	2028	2028	2028	2028	2028	2028	2028	2028	2028	2028	2028
R-Squared	0.043	0.043	0.044	0.034	0.033	0.034	0.024	0.024	0.024	0.031	0.031	0.032
Panel B: Firm Fixed Effects (Pre-Crisis Observations)												
IO TOTAL	-0.029* (0.098)			0.004 (0.481)			-0.010 (0.298)			-0.003 (0.756)		
IO FOR		-0.009 (0.573)			0.009 (0.130)			0.001 (0.947)			-0.010 (0.418)	
IO DOM			-0.089 (0.197)			-0.013 (0.412)			-0.048* (0.062)			0.015 (0.594)
N	551	551	551	551	551	551	551	551	551	551	551	551
R-Squared	0.171	0.164	0.179	0.081	0.084	0.082	0.040	0.035	0.058	0.040	0.043	0.041
Panel C: Firm Fixed Effects (Crisis Observations)												
IO TOTAL	-0.011 (0.420)			-0.005 (0.503)			-0.003 (0.714)			-0.008 (0.311)		
IO FOR		-0.018 (0.206)			-0.008 (0.306)			-0.005 (0.544)			-0.009 (0.306)	
IO DOM			0.009 (0.678)			0.006 (0.402)			0.003 (0.853)			-0.001 (0.936)
N	1047	1047	1047	1047	1047	1047	1047	1047	1047	1047	1047	1047
R-Squared	0.063	0.065	0.061	0.048	0.049	0.047	0.027	0.027	0.026	0.037	0.037	0.035
Panel D: Firm Fixed Effects (Post-Crisis Observations)												
IO TOTAL	0.030 (0.190)			-0.007 (0.613)			-0.006 (0.627)			0.003 (0.819)		
IO FOR		0.017 (0.611)			-0.029 (0.288)			-0.004 (0.793)			-0.008 (0.581)	
IO DOM			0.043 (0.499)			0.045 (0.251)			-0.013 (0.614)			0.030 (0.242)
N	430	430	430	430	430	430	430	430	430	430	430	430
R-Squared	0.051	0.048	0.050	0.074	0.083	0.083	0.046	0.046	0.046	0.060	0.061	0.066

Table 7.7 continued

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
	Board MF			AC MF			CC MF			NC MF		
Panel E: Firm Fixed Effects (Common Law Observations)												
IO TOTAL	0.007 (0.554)			0.004 (0.411)			0.003 (0.593)			0.012* (0.063)		
IO FOR		0.009 (0.529)			-0.001 (0.879)			0.004 (0.567)			0.004 (0.677)	
IO DOM			0.007 (0.687)			0.010* (0.050)			0.003 (0.695)			0.015 (0.111)
N	939	939	939	939	939	939	939	939	939	939	939	939
R-Squared	0.103	0.103	0.103	0.075	0.074	0.078	0.051	0.051	0.051	0.042	0.037	0.042
Panel F: Firm Fixed Effects (Civil Law Observations)												
IO TOTAL	-0.017 (0.156)			0.010 (0.148)			-0.007 (0.137)			-0.010* (0.092)		
IO FOR		-0.020* (0.077)			0.012* (0.058)			-0.006 (0.320)			-0.007 (0.283)	
IO DOM			-0.001 (0.968)			0.004 (0.736)			-0.009 (0.393)			-0.013 (0.279)
N	1089	1089	1089	1089	1089	1089	1089	1089	1089	1089	1089	1089
R-Squared	0.045	0.046	0.042	0.067	0.068	0.063	0.044	0.043	0.042	0.059	0.057	0.057
Panel G: Interaction Effects (Firm Fixed Effects)												
IO TOTAL * FAMILY		-0.023* (0.061)			0.009 (0.193)			-0.011 (0.108)			-0.006 (0.349)	
IO FOR * FAMILY		-0.016 (0.210)			0.009 (0.104)			-0.011 (0.174)			-0.009 (0.217)	
IO DOM* FAMILY		-0.044* (0.097)			0.016 (0.380)			-0.011 (0.339)			0.007 (0.498)	
IO TOTAL * Non-FAMILY		0.003 (0.738)			0.005 (0.218)			0.003 (0.451)			0.003 (0.541)	
IO FOR * Non-FAMILY		-0.004 (0.675)			0.004 (0.437)			0.003 (0.483)			-0.001 (0.876)	
IO DOM* Non-FAMILY		0.018 (0.233)			0.008 (0.154)			0.004 (0.505)			0.008 (0.242)	
Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 7.4. BOARD MF = Board meeting frequency, AC MF = Audit committee meeting frequency, CC MF = Compensation committee meeting frequency, NC MF = Nomination committee meeting frequency, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.												

7.4.4. Board Entrenchment

This study also required an examination of whether the presence of institutional investors served to reduce board entrenchment. To this end, two measures were used to proxy board entrenchment: CEO tenure and board tenure. Table 7.8 presents the results of firm fixed effect panel regressions; these regressions indicated that total, foreign and domestic institutional investors had a positive but insignificant relationship with CEO tenure (see Table 7.8, Panel A). In contrast, institutional investors (total, foreign and domestic) had a negative association with board tenure; this association, however, was only significant with domestic institutions at the 10% significance level (with coefficient = -0.011, p-value = 0.053, and R-Squared = 0.100). Therefore, the findings were determined to partially support H4. Drawing from the theoretical framework of agency theory, the results are consistent with those who argued that long-tenured directors may become less effective in monitoring the firm, as they are likely to form friendships and become closer to the managers (Vafeas, 2003; Barroso et al., 2011). Others also argued that firms with long-tenured boards are likely to be more resistant to change (Musteen et al., 2006; Jia, 2017). Several studies also demonstrate that boards whose members have long tenures are associated with a lower degree of international diversification (Barroso et al., 2011), fewer patents and lower research and development (Jia, 2017). More recently, Godos-Díez et al. (2018) found that the firms that established a limited tenure for independent directors are associated with higher corporate social responsibility engagement. The results contribute to the literature by revealing that institutional investors do contribute to controlling the length of the directors' tenure in companies in which they invest. This is also consistent with corporate governance recommendations in the UK that also recommend that companies limit the period of service for the independent directors to nine years (FRC, 2016).

The study also compared the role of institutional investors in the reduction of board entrenchment according to various economic conditions (see Table 7.8, Panels B, C and D).

Results indicated that during pre-crisis periods, institutional investors (total and domestic) had positive and significant association with board entrenchment (CEO tenure) (with coefficient = 0.063 and 0.172, p-value = 0.082, 0.069, and R-Squared value = 0.125 and 0.148, respectively); however, this trend waned during crisis and post-crisis periods. In addition, the results are consistent with the other studies that blamed corporate boards and the institutional investors alike for the occurrence of the recent financial crisis (Conyon et al., 2011; Reisberg, 2015). The results support Francis et al. (2012), who documented that CEO tenure did not contribute to the stock performance during the crisis.

The results of a comparison of this relationship under different legal systems showed that institutional investors had mixed but insignificant associations with board entrenchment measures (CEO tenure and board tenure) in common law countries. In civil law countries, though, domestic institutional investors had negative and significant associations with board tenure at 5% (with coefficient = -0.026, p-value = 0.016, and R-Squared value = 0.133) (see Table 7.8, Panels E and F). The results support the institutional theory framework and may be explained by institutional investors reducing board tenure as a governance tool in civil law countries where the shareholder protections are weak. La Porta et al. (2000) argue that corporate governance mechanisms could be utilised by the outside investors to protect their wealth against the expropriation of the insiders (controlling shareholders and managers). The study then examined whether the relationship between institutional investors and board entrenchment was driven by a company's ownership structure. The results revealed that the association between institutional investors and board entrenchment was mixed and insignificant in both family-owned and non-family-owned firms (see Table 7.8, Panel G). Ultimately, with respect to non-family-owned firms, the findings showed a negative and significant relationship between domestic institutions and board tenure at the 10% significance level (with coefficient = - 0.010, and p-value = 0.090). The results support the Principal-

Principal conflict (Shleifer and Vishny, 1997) by showing that (domestic) institutional investors have the ability to reduce board entrenchment only in non-family-owned firms. The results are also consistent with the institutional theory and complement the other studies that highlight the importance of the ownership structure in the adoption of governance practices (Desender et al., 2013; Judge, 2011, 2012; Sure et al., 2013).

Table 7.8 Institutional Investors and Board Entrenchment

Table 7.8 Institutional Investors and Board Entrenchment						
	(1)	(2)	(3)	(4)	(5)	(6)
	CEO TENURE			BOARD TENURE		
Panel A: Firm Fixed Effects (All Observations)						
IO TOTAL	0.009 (0.538)			-0.006 (0.103)		
IO FOR		0.011 (0.549)			-0.003 (0.507)	
IO DOM			0.009 (0.631)			-0.011* (0.053)
N	2028	2028	2028	2028	2028	2028
R-Squared	0.050	0.050	0.049	0.099	0.098	0.100
Panel B: Firm Fixed Effects (Pre-Crisis Observations)						
IO TOTAL	0.063* (0.082)			-0.005 (0.478)		
IO FOR		0.027 (0.262)			-0.003 (0.661)	
IO DOM			0.172* (0.069)			-0.018 (0.325)
N	551	551	551	551	551	551
R-Squared	0.125	0.091	0.148	0.059	0.057	0.062
Panel C: Firm Fixed Effects (Crisis Observations)						
IO TOTAL	-0.010 (0.668)			0.003 (0.565)		
IO FOR		-0.016 (0.588)			0.002 (0.791)	
IO DOM			0.011 (0.723)			0.003 (0.743)
N	1047	1047	1047	1047	1047	1047
R-Squared	0.055	0.056	0.054	0.068	0.068	0.068
Panel D: Firm Fixed Effects (Post-Crisis Observations)						
IO Total	0.022 (0.567)			0.008 (0.437)		
IO FOR		0.070 (0.232)			0.015 (0.230)	
IO DOM			-0.000 (0.865)			-0.013 (0.438)
N	430	430	430	430	430	430
R-Squared	0.053	0.065	0.145	0.101	0.105	0.101
Panel E: Firm Fixed Effects (Common Law Observations)						
IO TOTAL	0.018 (0.529)			-0.004 (0.424)		
IO FOR		0.010 (0.787)			0.000 (0.979)	
IO DOM			0.026 (0.206)			-0.009 (0.193)
N	939	939	939	939	939	939
R-Squared	0.062	0.060	0.063	0.117	0.116	0.119
Panel F: Firm Fixed Effects (Civil Law Observations)						
IO TOTAL	0.001 (0.939)			-0.007 (0.158)		
IO FOR		0.015 (0.238)			-0.003 (0.612)	
IO DOM			-0.053 (0.210)			-0.026** (0.016)
N	1089	1089	1089	1089	1089	1089
R-Squared	0.084	0.087	0.091	0.128	0.126	0.133
IO TOTAL * FAMILY		0.015 (0.126)			-0.003 (0.481)	
IO FOR * FAMILY		0.011 (0.319)			-0.004 (0.473)	
IO DOM* FAMILY		0.041 (0.160)			-0.004 (0.818)	
IO TOTAL * Non-FAMILY		0.006 (0.736)			-0.006 (0.178)	
IO FOR * Non-FAMILY		0.010 (0.674)			-0.002 (0.674)	
IO DOM* Non-FAMILY		0.003 (0.859)			-0.010* (0.090)	

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 7.4. CEO TENURE = CEO tenure, BOARD TENURE = Board Tenure, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.

7.4.5. Board Busyness

Finally, the study tested whether institutional investors played a role in the reduction of board busyness. Two main variables were used to proxy board busyness: the average number of directorships held by INEDs and the percentage of INEDs who were classified as ‘busy’. Panel A of Table 7.9 demonstrates that foreign institutional investors had a negative and insignificant association with both measures (with coefficient = -0.001 and -0.000, p-value = 0.776 and 0.554, and R-Squared value = 0.041 and 0.037, respectively), while total and domestic institutions had a positive but insignificant association with the same variables. Accordingly, these results do not support the agency theory and led to the rejection of H5. The results are consistent with those who found that busy directors may be beneficial to the firm, as their experience and connection with other firms makes them competent compared to their non-busy counterparts on the board. For instance, firms with a busy board have been found to perform better (Pombo and Gutiérrez, 2011; Field et al., 2013), bargain better deals and acquisitions of other firms (Benson et al., 2015; Harris and Shimizu, 2004), and meet at a higher frequency (Baccouche et al., 2014). The results contribute to the literature by revealing that board busyness is not within the institutional investors’ agenda for improving the governance structure in their investee firms. The results suggest that the policy makers must not limit the number of directorships in other firms, as the benefits may outweigh the costs.

The research then investigated whether this relationship stemmed from the economic conditions of the countries in which these companies operated. Ultimately, in terms of board busyness, institutional investors were found to behave differently within different economic conditions. The study found that while total institutional investors had positive association for both measures of board busyness in times of crisis (with coefficient = 0.004 and 0.001, p-value = 0.039 and 0.061, and R-Squared value = 0.077 and 0.060, respectively) (see Table 7.9, Panel C), this influence was not evident during pre-crisis and post-crisis periods (see Table 7.9,

Panels B and D). The results support the institutional theory and are consistent with Francis et al. (2012), who argued that, during the crisis, the advising function of the board is more important than monitoring. Therefore, these results may imply that, during the crisis period, busy directors may bring to the table the knowledge and expertise that they have gained from other boards to support the firm through the crisis (Francis et al., 2012).

Next, the study examined whether the association between institutional investors and board busyness was influenced by the legal system of the country in which companies operated. The study found that the tendency of institutional investors to reduce board busyness was mixed and insignificant within both legal systems (see Table 7.9, Panels E and F); this result did not hold, however, for total institutional investors, who had a negative and significant association with busyness in common law countries at 10% (with coefficient = -0.002, p-value = 0.081 and R-Squared value = 0.099). The institutional investors' inability to reduce board busyness in civil law countries may be explained by the existence of the ownership concentration in civil law countries (La Porta et al., 1999), which results in the Principal-Principal conflict (Shleifer and Vishny, 1997). The results are also consistent with Ferris et al. (2018), who found that board busyness was less prevalent in common law countries than those headquartered in civil law countries, which might be due to the fact that institutional investors play a part in reducing board busyness in common law countries. In addition, drawing from the institutional theory, the results complement those studies that argued that the legal system of the country is an important factor in explaining the adoption of corporate governance (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014). The research then moved on to an examination of whether the ownership structure of an investee firm had an effect on the ability of institutional investors to reduce board busyness. The results revealed that foreign institutional investors reduced board busyness in non-family-owned firms; in such firms, the relationship with foreign institutions was negative for both measures of board busyness and

significant at 10% (with coefficient value = - 0.003 and -0.001, and p-value = 0.064 and 0.057, respectively) (see Table 7.9, Panel G). Consistent with the implication of the Principal-Principal conflict (Shleifer and Vishny, 1997), the results indicated that institutional investors can influence board busyness in non-family firms only. In addition, the results support the institutional theory and complement those who emphasised that the adoption of governance practices should be studied in light of the ownership structure (Desender et al., 2013; Judge, 2011, 2012; Sure et al., 2013).

Table 7.9 Institutional Investors and Board Busyness

	(1)	(2)	(3)	(4)	(5)	(6)
	BUSY BOARD			BUSY BOARD %		
Panel A: Firm Fixed Effects (All Observations)						
IO TOTAL	0.000 (0.931)			0.000 (0.812)		
IO FOR		-0.001 (0.776)			-0.000 (0.544)	
IO DOM			0.002 (0.400)			0.001 (0.117)
N	2028	2028	2028	2028	2028	2028
R-Squared	0.041	0.041	0.042	0.036	0.037	0.039
Panel B: Firm Fixed Effects (Pre-Crisis Observations)						
IO TOTAL	-0.001 (0.592)			-0.000 (0.786)		
IO FOR		-0.001 (0.621)			-0.000 (0.872)	
IO DOM			0.002 (0.768)			-0.000 (0.898)
N	551	551	551	551	551	551
R-Squared	0.094	0.094	0.093	0.058	0.058	0.058
Panel C: Firm Fixed Effects (Crisis Observations)						
IO TOTAL	0.004** (0.039)			0.001* (0.061)		
IO FOR		0.003 (0.167)			0.001 (0.190)	
IO DOM			0.004 (0.163)			0.001 (0.203)
N	1047	1047	1047	1047	1047	1047
R-Squared	0.077	0.073	0.073	0.060	0.057	0.057
Panel D: Firm Fixed Effects (Post –Crisis Observations)						
IO TOTAL	-0.005 (0.144)			-0.001 (0.520)		
IO FOR		-0.003 (0.484)			0.000 (0.867)	
IO DOM			-0.009 (0.100)			-0.003 (0.203)
N	430	430	430	430	430	430
R-Squared	0.119	0.115	0.121	0.065	0.064	0.071
Panel E: Firm Fixed Effects (Common Law Observations)						
IO TOTAL	-0.002* (0.081)			-0.000 (0.757)		
IO FOR		-0.002 (0.251)			-0.001 (0.320)	
IO DOM			-0.001 (0.423)			0.000 (0.555)
N	939	939	939	939	939	939
R-Squared	0.099	0.097	0.095	0.067	0.068	0.067
Panel F: Firm Fixed Effects (Civil Law Observations)						
IO TOTAL	0.003 (0.314)			0.000 (0.575)		
IO FOR		0.002 (0.623)			0.000 (0.854)	
IO DOM			0.012 (0.150)			0.002 (0.230)
N	1089	1089	1089	1089	1089	1089
R-Squared	0.055	0.053	0.059	0.047	0.046	0.050
Panel G: Interaction Effects (Firm Fixed Effects)						
IO TOTAL * FAMILY		0.007* (0.094)			0.001 (0.190)	
IO FOR * FAMILY		0.006 (0.140)			0.002 (0.149)	
IO DOM* FAMILY		0.012 (0.146)			0.001 (0.538)	
IO TOTAL * Non-FAMILY		-0.002 (0.202)			-0.000 (0.566)	
IO FOR * Non-FAMILY		-0.003* (0.064)			-0.001* (0.057)	
IO DOM* Non-FAMILY		0.001 (0.796)			0.001 (0.152)	
Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 7.4. BUSY BOARD = Busy board, BUSY BOARD % = Busy board %, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.						

7.5. Robustness Tests

As described in the previous chapter, this study employed several robustness tests to confirm the main results. These tests utilised reverse causality, system GMM and alternative measures to verify the models and their results. The results of these tests are described in the following sections.

Reverse Causality

As discussed in Chapter Six, reverse causality might be of concern in this study, as it has the potential to lead to ineffective results. To address this issue, change score regressions were applied in an effort to determine whether changes in institutional ownership drove changes in governance outcomes or whether the reverse held true (Aggarwal et al., 2011). Panel A of Table 7.10 demonstrates the results of these tests. In these tests, a change in the Board Attributes Index (ΔGOV_{14}) from period $t-1$ to t represented the dependent variable. The main explanatory variables were changes in institutional ownership (ΔIO) from period $t-2$ to $t-1$. All other independent variables were expressed in terms of change; these variables were lagged by one period relative to the Board Attributes Index. Panel A of Table 7.10 shows that changes in total and foreign institutions drove improved outcomes with respect to board attributes (with coefficient = 0.004 and 0.006, p -value = 0.074 and 0.090, and R-Squared value = 0.032 and 0.033, respectively). The results also indicated an insignificant relationship between the Board Attributes Index outcomes and changes in common, civil and domestic institutions.

Panel B of Table 7.10 demonstrates the results of the reverse relationship analysis, which was conducted in an effort to study whether changes in governance outcomes drove changes in institutional ownership. In this analysis, the dependent variables were changes in institutional ownership (ΔIO) from period $t-1$ to t . The main explanatory variable was a change in the Board Attributes Index (ΔGOV_{14}) from period $t-2$ to $t-1$. All other independent variables were expressed in terms of change; they were also lagged by one period relative to institutional

ownership. Panel B of Table 7.10 shows that most types of institutional investors had negative and insignificant associations with governance outcomes. These results were consistent with those of Aggarwal et al. (2011) and showed that while changes in institutional investment activity drove changes in corporate governance outcomes, the opposite was not true. Therefore, these results alleviated concerns that the main results (see Table 7.4 for comparison) were driven by the causality between institutional investors and corporate governance structures.

Table 7.10 Changes in Institutional Ownership and Changes in Board Attributes

	ΔGOV_{14} coefficient	N	R-Squared
Panel A: Yearly Changes (Changes in Institutional Ownership and Changes in Corporate Governance)			
<i>$\Delta \text{IO TOTAL}$</i>	0.004* (0.074)	1553	0.032
<i>$\Delta \text{IO FOR}$</i>	0.006* (0.090)	1553	0.033
<i>$\Delta \text{IO DOM}$</i>	0.000 (0.990)	1553	0.030
<i>$\Delta \text{IO COMMON}$</i>	0.003 (0.480)	1553	0.031
<i>$\Delta \text{IO CIVIL}$</i>	0.010 (0.128)	1553	0.032
Panel B: Yearly Changes (Changes in Corporate Governance and Changes in Institutional Ownership)			
<i>$\Delta \text{IO TOTAL}$</i>	-0.080 (0.777)	1553	0.031
<i>$\Delta \text{IO FOR}$</i>	-0.043 (0.864)	1553	0.038
<i>$\Delta \text{IO DOM}$</i>	-0.011 (0.892)	1553	0.044
<i>$\Delta \text{IO COMMON}$</i>	0.002 (0.992)	1553	0.036
<i>$\Delta \text{IO CIVIL}$</i>	-0.046 (0.751)	1553	0.031
Note: Regressions also include year, country and industry dummies and standard errors corrected for country-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 7.4. GOV_{14} = Board attributes index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors.			

System GMM

As discussed in the previous chapter, this study adopted a system GMM technique as a robustness test. To this end, the `xtabond2` dynamic panel estimator in STATA 14 was considered, and adapted the procedure of Wintoki et al. (2012) to model the association between institutional investors and corporate board characteristics (the Board Attributes Index). Table 7.11 describes the results of this system GMM, which was used to examine the role of institutional investors in improving the Board Attributes Index (GOV_{14}). The first test is related to second-order serial correlation AR (2), with a P value $> 5\%$. The second test is the Hansen J test of over-identification, which is used to determine whether an instrument is uncorrelated with the error term in the models, with a P value $> 5\%$. The results, as reported in Table 7.11, indicated that there was no serial correlation (with AR (2) ranges from 0.323 to 0.342) and that the instruments used in the system GMM were valid and uncorrelated with the error term (with the Hansen J test value ranges from 0.182 to 0.208).

Table 7.11 illustrates that total and foreign institutional investors have a positive and significant association with the board attributes index (GOV_{14}) at 1% (with coefficient value = 0.005 and 0.008, and p-value = 0.007 and 0.000, respectively), which reveals that the results are consistent with Table 7.4. However, the only exception is the common and civil law institutional investors, who had positive and significant associations with GOV_{14} at 5% and 1%, respectively (with coefficient value = 0.004 and 0.010, and p-value = 0.025 and 0.083, respectively). In the main results, the coefficient was positive but insignificant for both common and civil institutions (see Table 7.4 for comparison).

Table 7.11 Institutional Investors and the Board Attributes Index (System GMM)

	(1)	(2)	(3)	(4)	(5)
	GOV₁₄				
GOV₁₄	0.706***	0.698***	0.709***	0.706***	0.711***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
IO TOTAL	0.005***				
	(0.007)				
IO FOR		0.008***			
		(0.000)			
IO DOM			-0.001		
			(0.801)		
IO COMMON				0.004**	
				(0.025)	
IO CIVIL					0.010*
					(0.083)
FSIZE	0.050	0.037	-0.038	0.010	0.008
	(0.510)	(0.601)	(0.592)	(0.895)	(0.908)
SGROWTH	0.108	0.098	0.121	0.114	0.115
	(0.304)	(0.350)	(0.249)	(0.281)	(0.274)
LEV	-0.276	-0.258	-0.254	-0.272	-0.251
	(0.214)	(0.249)	(0.257)	(0.225)	(0.254)
CASH	-0.092	-0.140	-0.117	-0.112	-0.074
	(0.762)	(0.645)	(0.703)	(0.714)	(0.808)
CAPEX	-0.510	-0.586	-0.684	-0.582	-0.604
	(0.574)	(0.521)	(0.454)	(0.524)	(0.503)
MB	0.003	0.002	-0.000	0.001	0.002
	(0.795)	(0.878)	(0.978)	(0.924)	(0.825)
ROA	0.201	0.209	0.103	0.158	0.143
	(0.602)	(0.585)	(0.787)	(0.681)	(0.707)
PPE	0.112	0.086	0.139	0.119	0.139
	(0.542)	(0.639)	(0.456)	(0.523)	(0.445)
ANALYST	0.003	0.002	0.004	0.003	0.003
	(0.526)	(0.589)	(0.394)	(0.462)	(0.463)
ADR	0.007	0.000	0.028	0.014	0.022
	(0.929)	(1.000)	(0.727)	(0.858)	(0.775)
RULE	-0.006	-0.007	-0.005	-0.007	-0.002
	(0.845)	(0.826)	(0.876)	(0.812)	(0.951)
CRISIS	0.033	0.050	0.041	0.037	0.035
	(0.800)	(0.696)	(0.751)	(0.776)	(0.789)
POST-CRISIS	0.012	0.038	0.021	0.016	0.016
	(0.943)	(0.816)	(0.898)	(0.924)	(0.921)
FAMILY	0.398***	0.400***	0.300**	0.337**	0.404***
	(0.005)	(0.004)	(0.030)	(0.015)	(0.008)
STATE	0.465***	0.472***	0.369**	0.394**	0.497***
	(0.005)	(0.003)	(0.019)	(0.013)	(0.006)
WIDELY	0.494***	0.508***	0.468***	0.465***	0.536***
	(0.001)	(0.001)	(0.002)	(0.002)	(0.001)
AR(1)	0.000	0.000	0.000	0.000	0.000
AR(2)	0.323	0.342	0.329	0.327	0.324
Hansen	0.182	0.186	0.208	0.196	0.192
N	2028	2028	2028	2028	2028

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. GOV₁₄= Board attributes index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, WIDELY = Widely held at 20%.

Alternative Measures

The study further tested the robustness of the main findings by considering various items of the Board Attributes Index (GOV₁₄) as substitutes for the variables used in the main analysis. Table 7.12 presents the probit panel regressions of the role of institutional investors in the improvement of several items of the Board Attributes Index (GOV₁₄). These attributes are related to corporate board and its key subcommittees composition (items 2, 5, 6 and 7), board activity (item 8), board entrenchment (item 9), and board busyness (item 12).

Table 7.12 demonstrates that total institutional investors have a positive and significant association with the independence of the board dummy, the independence of the key subcommittees dummies (audit, compensation and nomination) and also with the chairman and CEO dummy (with coefficient value = 0.018, 0.019, 0.024, 0.010 and 0.048, and p-value = 0.075, 0.000, 0.004, 0.049 and 0.054, respectively). On the other hand, the foreign institutions were found to be positively associated with only the independence of the board dummy and the independence of audit- and compensation-committees dummies (with coefficient value = 0.030, 0.013 and 0.029, and p-value = 0.008, 0.004 and 0.002, respectively). In addition, Table 7.12 illustrates that domestic institutional investors have a negative and significant association with the independence of the board dummy (with the coefficient value = -0.007, and p-value = 0.096), and a positive and significant association with the independence of the audit committee dummy (with the coefficient value = 0.024, and p-value = 0.082). Collectively, these results were consistent with the findings of the main analysis (see Tables 7.6, 7.7, 7.8 and 7.9 for comparison).

Table 7.12 Institutional Investments and Items of the Board Attributes Index

	IO TOTAL	IO FOR	IO DOM	N
<i>Panel A: (All Observations)</i>				
<i>INED BOARD Dummy</i>	0.018 [*] (0.075)	0.030 ^{***} (0.008)	-0.007 [*] (0.096)	1908
<i>INED AUD Dummy</i>	0.019 ^{***} (0.000)	0.013 ^{***} (0.004)	0.024 [*] (0.082)	2028
<i>INED COM Dummy</i>	0.024 ^{***} (0.004)	0.029 ^{***} (0.002)	0.004 (0.655)	2028
<i>INED NOM Dummy</i>	0.010 ^{**} (0.049)	0.010 (0.140)	0.014 (0.113)	1690
<i>BOARD ATTENDANCE Dummy</i>	0.005 (0.539)	0.011 (0.539)	-0.011 (0.230)	1359
<i>CHAIRMAN CEO Dummy</i>	0.048 [*] (0.054)	0.0551 (0.109)	0.0334 (0.533)	1386
<i>BUSY BOARD Dummy</i>	-0.000 (0.941)	-0.001 (0.886)	0.001 (0.881)	2028

Regressions also include industry, country and year dummies and robust p-values corrected for country-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 7.4. IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, INED BOARD Dummy = the board has more than 50% of independent directors (item 2), INED AUD Dummy= audit committee composed solely of independent directors (item 5), INED COM Dummy= compensation committee composed solely of independent directors (item 6), INED NOM Dummy = the majority members of nomination committee are independent directors (item 7), BOARD ATTENDANCE Dummy = All directors attended 75% of the board meeting (item 8), CHAIRMAN CEO Dummy = Chair and CEO positions are separated or there is lead directors (item 9), and BUSY BOARD Dummy = at least half of the INEDs hold \leq two directorships in public companies (item 12).

7.6. Chapter Summary

This chapter outlined the research analysis procedures and findings of the institutional investors' role in the improvement of board attributes, beginning with a descriptive examination of the variables used in this study. The chapter then discussed the results of the correlation analysis and VIF tests. Next, the chapter outlined the results of the hypothesis tests (H1–H5), which were developed in Chapter Five of this thesis. Furthermore, this chapter illustrated the results of efforts to test these hypotheses according to various institutional settings, to include diverse economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. Finally, this chapter concluded with an explanation of the results of various robustness tests including reverse causality and system GMM and alternative measures.

Chapter 8

8.0 Research Results and Analysis: Institutional Investors and Board Diversity

8.1. Introduction

This chapter provides an analysis of the results of the institutional investors' role in improving board diversity. This chapter starts by illustrating the descriptive statistics of the variables used to examine the relationship between institutional investors and board diversity. This is followed by an examination of the measures used to test the correlations between variables. The empirical results are then discussed, and finally, the results of the robustness tests are illustrated.

Accordingly, this chapter is organised as follows: section 8.2 provides a summary of the descriptive statistics, section 8.3 describes the correlation analysis, section 8.4 highlights the empirical results of the analysis of the institutional investors' role in the enhancement of board diversity characteristics, section 8.5 discusses the robustness tests and section 8.6 offers a chapter summary.

8.2. Summary of the Descriptive Statistics

This section illustrates the descriptive statistics of the dependent variables (board diversity), independent variables (institutional investors) and control variables (firm and country characteristics). Table 8.1 provides the descriptive statistics of the variables used in an effort to examine the role of institutional investors in the improvement of board diversity in their investee firms. The table mainly reports means, standard deviations, minimum and maximum data points and the total observations to describe the descriptive statistics.

Table 8.1 Descriptive Statistics

Variables	Mean	SD	MIN	MAX	No. of Observations
Dependent Variables: Board Diversity					
BDI ₁₆	10	2	4	16	2,586
GENDER DIV	14%	12%	0%	60%	2,586
AGE DIV	13%	4%	3%	36%	2,586
NATION DIV	25%	23%	0%	100%	2,586
EDU DIV	51%	21%	0%	100%	2,586
Independent Variables: Institutional Ownership					
IO TOTAL	36%	23%	1%	99%	2,586
IO FOR	20%	16%	1%	99%	2,586
IO DOM	16%	17%	1%	99%	2,586
IO COMMON	28%	23%	1%	99%	2,586
IO CIVIL	8%	11%	1%	68%	2,586
Control Variables: Firm and Country Characteristics					
FSIZE	7.0	0.6	5	8.6	2,586
SGROWTH	12%	24%	-43%	116%	2,586
LEV	26%	15%	0%	67%	2,586
CASH	11%	10%	0%	62%	2,586
CAPEX	6%	5%	0%	26%	2,586
MB	3.2	3.0	0.30	20.2	2,586
ROA	11%	7%	-9%	36%	2,586
PPE	35%	24%	1%	90%	2,586
ANALYST	18	9	0	55	2,586
ADR	0.19	0.39	0	1	2,586
RULE	91%	12%	52%	100%	2,586
Pre-Crisis	0.37	0.48	0	1	2,586
Crisis	0.45	0.50	0	1	2,586
Post-Crisis	0.18	0.39	0	1	2,586
FAMILY	20%	40%	0	1	2,586
STATE	9%	27%	0	1	2,586
IO	3%	17%	0	1	2,586
WIDELY	68%	46%	0	1	2,586
BDI ₁₆ = Board diversity index, GENDER DIV = Board gender diversity, AGE DIV = Board age diversity, Nation DIV = Board nationality diversity, EDU DIV = Board education diversity, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, IO = Institutional investor controlling at 20%, WIDELY = Widely held at 20%.					

Table 8.1 demonstrates that the Board Diversity Index (BDI_{16}) ranges from a minimum of 4 to a maximum of 16 for the entire sample. Figure 8.1 shows that on average, the countries with the highest BDI_{16} scores in 2012 were France (76.8%), Norway (73.1%), Sweden (70.2%), Denmark (69.7%) and the UK (69.2%). Moreover, the countries with the lowest BDI_{16} scores were India (48.9%), Canada (59.0%), Finland (60.7%), Australia (61.0%) and Switzerland (61.5%).

Figure 8.1 Board Diversity Index (BDI_{16}) by Country and Year (2006–2012)

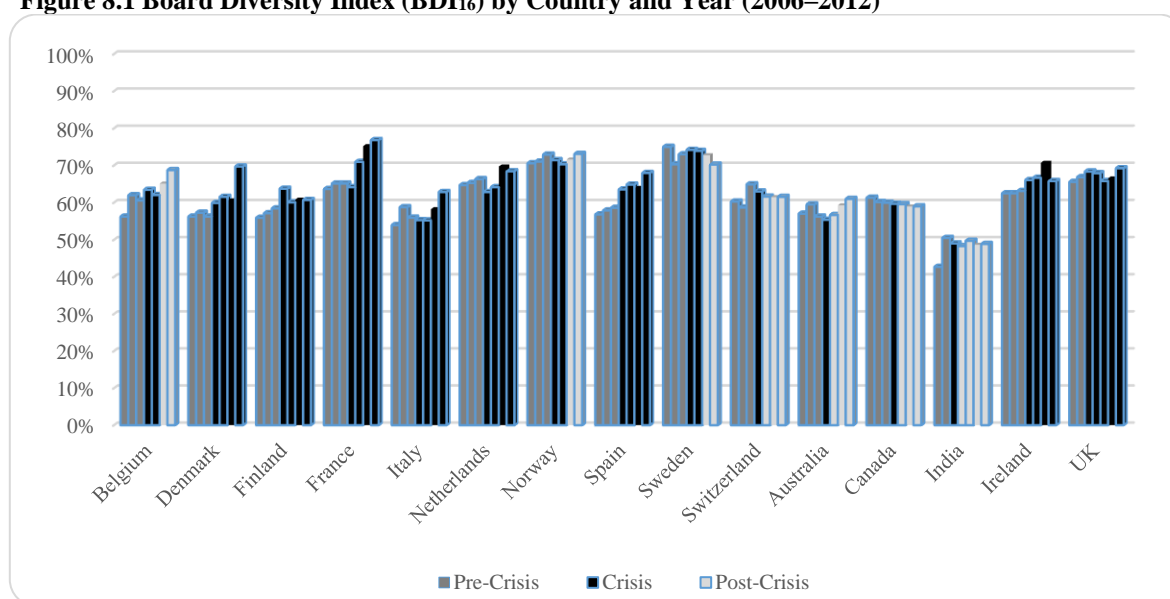


Figure 8.2 displays the weighted averages of the BDI_{16} scores for firms located in civil law countries and common law countries; the figure also illustrates that on average, higher levels of board diversity were found in civil law countries than in their common law counterparts. Notably, variations in board diversity between both legal systems began to grow more apparent following the financial crisis of 2007–2008.

Figure 8.2 Weighted Averages of the Board Diversity Index (BDI₁₆)

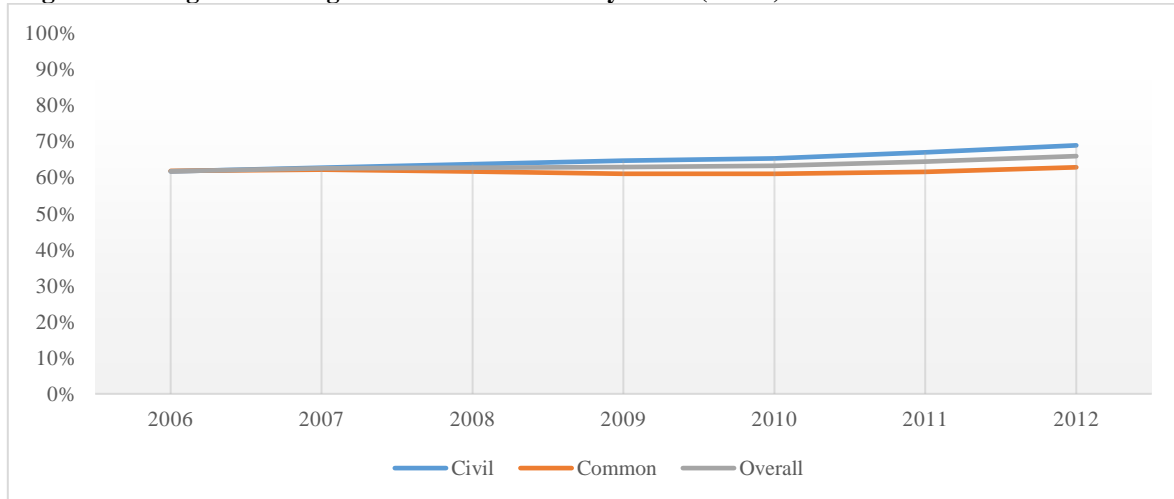


Table 8.1 also presents the statistics of the individual attributes of corporate board diversity: gender, age, nationality and education diversity. The table shows that on average, these attributes were 14%, 13%, 25% and 51%, respectively. Figure 8.3 describes the weighted averages of these attributes and indicates that age, nationality and education diversity remained stable throughout the years under study. In contrast, however, gender diversity held constant until 2010, at which point it gradually increased until the end of the study period. This might be explained by the introduction of gender quotas with regard to corporate boards that were initiated in several countries during this period (see Terjesen et al., 2015a).

Figure 8.3 Weighted Averages of Board Diversity Attributes

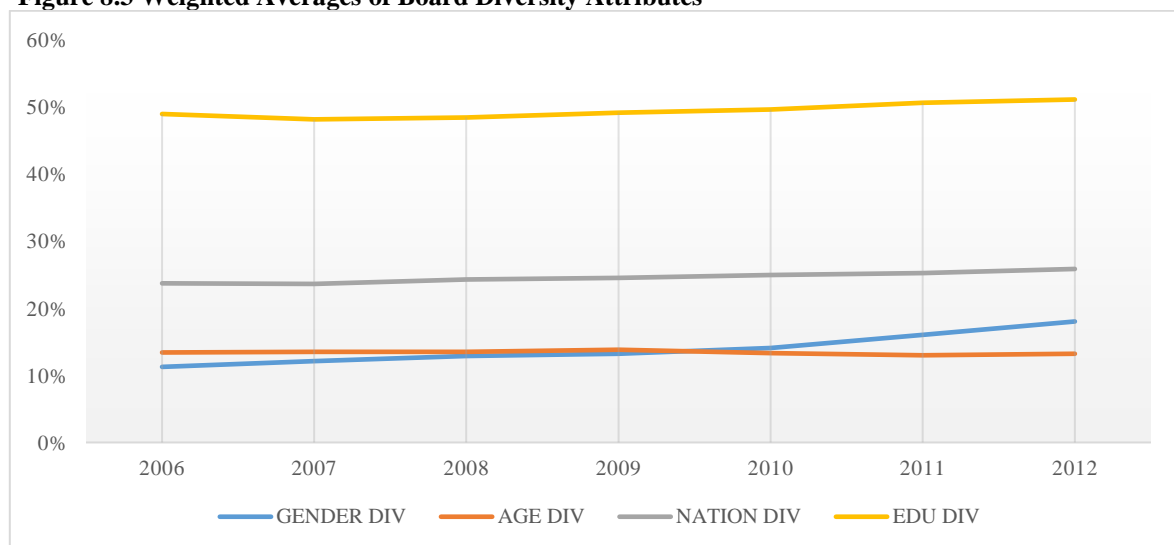


Table 8.1 further illustrates that for all types, the level of institutional investor presence ranged from 1% to 99%. However, civil law institutional investors are an exception, for whom their presence ranged from 1% to 68%. The average number of holdings owned by total, foreign, domestic, common law and civil law institutional investors in the sample countries were 36%, 20%, 16%, 28% and 8%, respectively. Figure 8.4 shows that on average, the presence of all types of institutional investors rose from 2006 to 2008, at which point their presence began to decline (until 2010). This decline could be due to the occurrence of the financial crisis. However, this graph shows that after 2010, institutional investors of all types began to reclaim their previous levels of investment in the stock markets of the sample countries.

Figure 8.4 Weighted Averages of Institutional Ownership

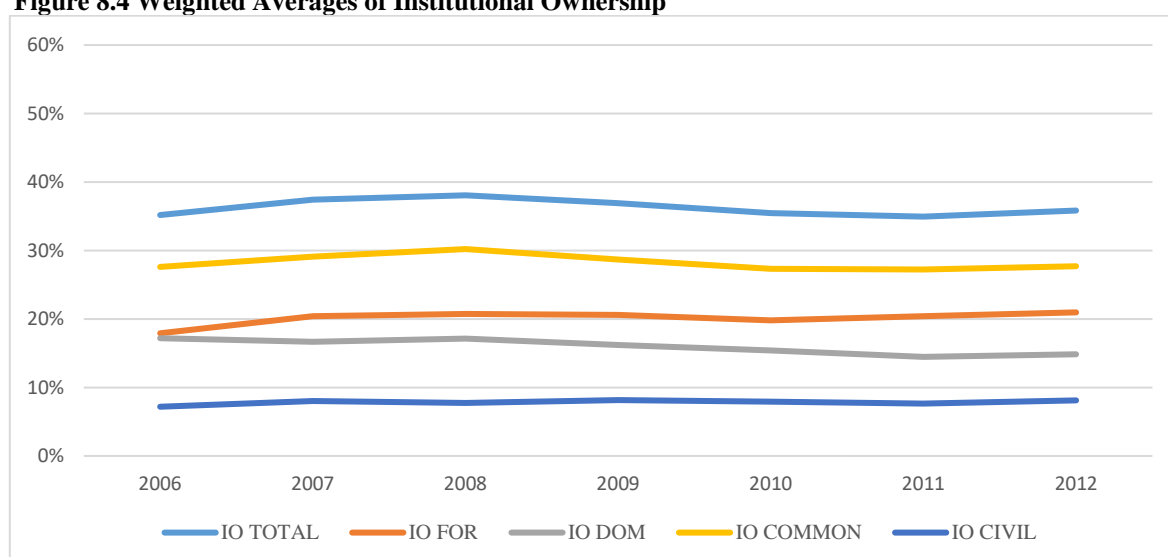


Table 8.1 also illustrates the statistics of the control variables. The average firm size was 7, with a minimum value of 5 and a maximum value of 8.6. Sales growth ranged from -43% to 116%, with an average of 12% and a standard deviation of 24%. Table 8.1 shows that leverage, cash and capital expenditures had a mean value of 26%, 11% and 6%, respectively. Table 8.1 also demonstrates that market-to-book value had a mean value of 3.2 and return on assets figures ranged from -9% to 36%, while property, plant and equipment scores ranged from 1% to 90%. The average level of analyst coverage for the entire sample was 18, with a minimum of 0 analysts following and a maximum of 55. In this sample, the average figure for companies

with an ADR listing was 19% with a standard deviation of 39%. The rule of law index ranged from 52% to 100%, with a minimum value of 52% and a maximum value of 100%. Table 8.1 also demonstrates that 37% of the total observations were classified as occurring during pre-crisis periods, 45% occurred during times of crisis and 18% occurred during post-crisis periods. With regard to the statistics for the controlling owner, the firms are classified to be controlled by institutional investors, state, family or widely held. On average, these types of owners controlled 3%, 9%, 20% and 68% in this sample, respectively.

8.3 Correlation Analysis

This section describes Pearson correlation matrix that exists between governance characteristics (board diversity), institutional ownership and the control variables. The main aim of the correlation matrix is to investigate the possible presence of high correlation among the independent variables. When conducting this test, a researcher allocates a single number that measures the extent to which any two variables are related; in so doing, the direction of this relationship can be illustrated. The problem of collinearity, however, means that two variables have a relatively perfect linear correlation, which in turn renders the model estimation meaningless and difficult to interpret. Gujarati (2004) argued that if the correlation between two variables exceeds 80%, the validity of the results may be threatened. Table 8.2 shows that the highest absolute correlation between explanatory variables (IO Total and IO Common) was 89%—well above the 80% threshold assigned to indicate a multi-collinearity threat (Gujarati, 2004). However, these two variables were not combined in any of the regressions used in this analysis. All correlations between other independent variables fell below this threshold (see Table 8.2).

As discussed in the previous chapter, an alternative measure used to describe the correlation issue between independent variables is to calculate the variance inflation factor (VIF). According to Studenmund (2001), VIF value should not exceed 5; a higher value may be an

indication that multi-collinearity threats exist within the model. In order to calculate the VIF value, an OLS model (shown below) was applied using the Board Diversity Index (BDI_{16}) as a dependent variable. Table 8.3 provides the results of this test and shows that multi-collinearity threats were not a factor in the utilised models, as all values were less than 5.

$$(BDI_{16}) = \beta_0 + \beta_1 (IO\ TOTAL_{(t-1)}) + \left(\begin{array}{l} \beta_2 SIZE_{(t-1)} + \beta_3 SGROWTH_{(t-1)} + \beta_4 LEV_{(t-1)} + \beta_5 CASH_{(t-1)} + \beta_6 CAPEX_{(t-1)} \\ + \beta_7 MB_{(t-1)} + \beta_8 ROA_{(t-1)} + \beta_9 PPE_{(t-1)} + \beta_{10} ANALYST_{(t-1)} + \beta_{11} ADR_{(t-1)} + \\ \beta_{12} RULE_{(t-1)} + \beta_{13} PRE - CRISIS_{(t-1)} + \beta_{14} CRISIS_{(t-1)} + \beta_{15} POST - CRISIS_{(t-1)} \\ + \beta_{16} IO_{(t-1)} + \beta_{17} STATE_{(t-1)} + \beta_{18} FAMILY_{(t-1)} + \beta_{19} WIDELY_{(t-1)} + \end{array} \right) \varepsilon$$

Table 8.2 Pearson Correlation Matrix

	BDI ₁₆	GENDER BOARD	AGE BOARD	NATION BOARD	EDU BOARD	IO TOTAL	IO FOR	IO DOM	IO COMMON	IO CIVIL	F SIZE	S GROWTH	LEV	CASH
BDI ₁₆	1.000													
GENDER DIV	0.426	1.000												
AGE DIV	0.461	0.012	1.000											
NATION DIV	0.337	-0.051	-0.100	1.000										
EDU DIV	-0.172	0.153	-0.237	0.220	1.000									
IO TOTAL	0.062	0.070	-0.115	0.006	-0.055	1.000								
IO FOR	0.069	0.015	-0.015	0.082	-0.012	0.702	1.000							
IO DOM	0.026	0.082	-0.144	-0.066	-0.065	0.732	0.039	1.000						
IO COMMON	0.019	-0.046	-0.136	0.014	-0.149	0.890	0.626	0.661	1.000					
IO CIVIL	0.097	0.251	0.046	-0.014	0.205	0.227	0.162	0.152	-0.236	1.000				
SIZE	0.072	-0.042	-0.079	0.189	0.035	-0.288	-0.272	-0.139	-0.196	-0.190	1.000			
SGROWTH	-0.057	-0.109	0.032	-0.032	-0.057	0.008	0.028	-0.017	0.031	-0.047	-0.043	1.000		
LEV	0.063	0.051	0.131	-0.136	-0.174	-0.027	-0.040	0.002	-0.032	0.009	0.116	-0.049	1.000	
CASH	0.002	-0.061	-0.014	0.145	0.069	-0.025	0.062	-0.095	-0.030	0.006	-0.158	0.045	-0.279	1.000
CAPEX	-0.061	-0.014	0.036	-0.095	-0.084	-0.073	-0.055	-0.049	-0.019	-0.107	-0.021	0.095	0.055	-0.082
MB	0.051	-0.025	0.028	-0.005	-0.008	0.057	0.013	0.065	0.086	-0.063	-0.308	0.106	0.029	0.186
ROA	0.032	0.052	-0.011	0.023	0.070	-0.014	-0.030	0.012	0.012	-0.050	-0.218	0.113	-0.290	0.129
PPE	-0.103	-0.010	-0.026	-0.143	-0.119	0.000	-0.026	0.031	0.083	-0.169	0.137	0.071	0.175	-0.246
ANALYST	0.071	0.065	-0.043	0.054	0.132	-0.204	-0.144	-0.142	-0.224	0.050	0.372	-0.078	-0.076	0.080
ADR	-0.025	-0.045	-0.132	0.187	0.042	0.183	0.107	0.154	0.264	-0.172	0.259	0.028	-0.057	-0.052
RULE	0.246	0.361	-0.099	0.207	0.181	0.312	0.204	0.233	0.205	0.218	-0.061	-0.043	-0.022	-0.041
PRE-CRISIS	-0.068	-0.103	0.027	-0.042	0.000	-0.016	-0.005	-0.020	-0.028	0.019	-0.048	0.177	0.038	-0.028
CRISIS	0.150	0.067	0.035	0.096	-0.013	0.055	0.054	0.032	0.048	0.020	0.049	-0.171	0.019	0.028
POST-CRISIS	-0.108	0.042	-0.079	-0.071	0.017	-0.051	-0.064	-0.016	-0.027	-0.048	-0.003	-0.001	-0.072	-0.002
FAMILY	0.134	-0.051	0.287	0.040	-0.112	-0.317	-0.190	-0.257	-0.273	-0.088	-0.027	0.020	0.018	0.002
STATE	-0.017	0.122	0.014	-0.109	0.011	-0.282	-0.193	-0.204	-0.266	-0.028	0.177	-0.017	0.039	-0.061
IO	-0.027	-0.048	0.030	-0.074	0.011	0.037	0.022	0.044	-0.030	0.158	0.035	-0.014	0.090	-0.036
WIDELY	-0.096	-0.011	-0.267	0.057	0.086	0.430	0.273	0.328	0.406	0.036	-0.096	-0.002	-0.071	0.048

Table 8.2 continued

	CASH	CAPEX	MB	ROA	PPE	ANALYST	ADR	RULE	PRE-CRISIS	CRISIS	POST-CRISIS	FAMILY	STATE	IO	WIDELY
CASH	1.000														
CAPEX	-0.082	1.000													
MB	0.186	0.030	1.000												
ROA	0.129	0.180	0.432	1.000											
PPE	-0.246	0.645	-0.103	0.028	1.000										
ANALYST	0.080	-0.078	0.057	0.132	-0.167	1.000									
ADR	-0.052	0.081	0.026	0.064	0.184	-0.012	1.000								
RULE	-0.041	-0.065	-0.036	-0.037	0.017	-0.268	0.136	1.000							
PRE-	-0.028	0.045	0.098	0.095	0.005	-0.149	0.012	0.058	1.000						
CRISIS	0.028	-0.170	-0.075	-0.120	-0.127	0.105	-0.044	0.037	-0.690	1.000					
POST-	-0.002	0.162	-0.026	0.035	0.158	0.050	0.042	-0.121	-0.362	-0.424	1.000				
FAMILY	0.002	0.005	-0.047	-0.019	-0.036	-0.037	-0.152	-0.171	0.009	0.008	-0.021	1.000			
STATE	-0.061	0.060	-0.092	-0.007	0.127	0.133	-0.130	-0.168	-0.005	0.005	0.000	-0.152	1.000		
IO	-0.036	-0.053	-0.024	-0.027	0.011	0.045	-0.054	-0.013	0.022	0.023	-0.057	-0.085	-0.052	1.000	
WIDELY	0.048	-0.022	0.105	0.030	-0.049	-0.064	0.229	0.253	-0.013	-0.018	0.038	-0.739	-0.451	-0.253	1.000
The correlation coefficients at 5% are in bold. BDI ₁₆ = Board diversity index, GENDER DIV = Board gender diversity, AGE DIV = Board age diversity, Nation DIV = Board nationality diversity, EDU DIV = Board education diversity, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, PRE-CRISIS= Pre-Crisis Dummy, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, IO = Institutional investor controlling at 20%, WIDELY = Widely held at 20%.															

Table 8.3 VIF Test

	VIF	1/VIF
WIDELY	3.52	0.28
FAMILY	2.85	0.35
PPE	2.12	0.47
CAPEX	1.90	0.52
ROA	1.52	0.65
IO TOTAL	1.49	0.66
MB	1.40	0.71
IO	1.36	0.73
ANALYST	1.35	0.74
LEV	1.33	0.75
FSIZE	1.30	0.76
Crisis	1.29	0.77
RULE	1.24	0.80
Post-Crisis	1.22	0.81
CASH	1.21	0.82
ADR	1.17	0.85
QUOTA	1.16	0.86
SGROWTH	1.08	0.92
Mean VIF	1.58	
IO TOTAL = Total institutional investors, SIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, PRE-CRISIS= Pre-Crisis Dummy, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, QUOTA = Gender Quota, STATE = State controlling at 20%, IO = Institutional investor controlling at 20%, WIDELY = Widely held at 20%.		

8.4 Institutional Investors and Board Diversity: Panel Data Analysis

8.4.1 Board Diversity Index

The first analysis in this chapter investigated the role of institutional ownership in the promotion of board diversity (see Table 8.4) using the Board Diversity Index (BDI_{16})⁴². The findings indicated that there was a positive but insignificant association between the diversity index and total, foreign and common institutional investors (with coefficient = 0.002, 0.003 and 0.004, p-value = 0.653, 0.510 and 0.366, and R-Squared value = 0.062, 0.062 and 0.063, respectively). However, the association between domestic and civil institutional investors (with coefficient = -0.003 and -0.007, p-value = 0.575 and 0.391, and R-Squared value = 0.062 and

⁴² It is argued that directors who serve on nomination committees are likely to select directors with similar attributes to fill additional board seats (see, for example, Hutchinson et al., 2015). When the empirical analysis of diversity models are repeated including various diversity aspects of the nomination committee, including gender, age, nationality and education, the study obtained consistent findings.

0.063, respectively) was negative but insignificant (see Table 8.4, Panel A)⁴³. The results do not support the agency and the resource dependence theoretical explanations, and therefore H6 was rejected. The results indicated that the institutional investors did not improve board diversity in their investee firms, which could be due to the cost associated with board diversity. Several scholars have argued that board diversity can also have a negative impact on the performance of the corporate board (Putnam, 2007; Adams et al., 2015; Estélyi and Nisar, 2016). It is highlighted by Estélyi and Nisar (2016) that the costs of board diversity may exceed its benefits, as there may be a communication breakdown among the directors, which in turn makes each director provide a radically different interpretation to a particular problem. This is also consistent with the view of Putnam (2007), who argued that directors with different personal attributes may create a lack of communication, leading to conflict and factions in the team.

The study then examined whether the role of institutional investors in the improvement of board diversity was influenced by various economic conditions (pre-crisis, crisis and non-crisis periods). The firm fixed effects regression indicated that the results were mixed but insignificant during all three periods (see Table 8.4, Panels B, C and D), though an exception was found for foreign institutional investors, who had positive and significant relationships with board diversity during pre-crisis periods at 10% (with coefficient = 0.020, p-value = 0.055, and R-Squared value = 0.110).

Next, the study examined the role of institutional investors in the improvement of board diversity outcomes according to various ownership structures. This was accomplished by considering the interactions between institutional investors and family-owned versus non-family-controlled firms (see Table 8.4, Panel E). Ultimately, the firm fixed effects regression

⁴³ When the empirical analysis is repeated including the US observations, the study obtained consistent findings.

showed that the results were mixed but insignificant for both ownership structures. Overall, the results do not support the institutional theory, and they complement those studies that argued that economic conditions and ownership structure are important elements to be considered when studying board diversity (Ben-Amar et al., 2013; Nekhili and Gatfaoui, 2013; Ararat et al., 2015; Sun et al., 2015; Farag and Mallin, 2016a). In general, the findings contribute to the governance literature by illustrating that the ownership structure does not determine the association between institutional investors and board diversity; however, institutional investors (foreign institutions) were found to promote board diversity only during pre-crises period.

Table 8.4 Institutional Investors and Board Diversity

	BDI ₁₆				
	(1)	(2)	(3)	(4)	(5)
	<i>Panel A: Firm Fixed Effects(All Observations)</i>				
IO TOTAL	0.002 (0.653)				
IO FOR		0.003 (0.510)			
IO DOM			-0.003 (0.575)		
IO COMMON				0.004 (0.366)	
IO CIVIL					-0.007 (0.391)
FSIZE	0.313 (0.505)	0.312 (0.504)	0.296 (0.528)	0.318 (0.495)	0.286 (0.542)
SGROWTH	-0.165 (0.276)	-0.164 (0.278)	-0.163 (0.285)	-0.165 (0.276)	-0.162 (0.286)
LEV	-0.689 (0.266)	-0.678 (0.272)	-0.697 (0.264)	-0.666 (0.280)	-0.683 (0.275)
CASH	-0.386 (0.549)	-0.386 (0.549)	-0.385 (0.550)	-0.383 (0.553)	-0.380 (0.556)
CAPEX	0.367 (0.793)	0.342 (0.805)	0.263 (0.852)	0.388 (0.780)	0.266 (0.849)
MB	-0.017 (0.351)	-0.017 (0.358)	-0.018 (0.342)	-0.017 (0.352)	-0.018 (0.326)
ROA	1.127 (0.244)	1.130 (0.246)	1.070 (0.274)	1.160 (0.233)	1.083 (0.271)
PPE	0.139 (0.871)	0.145 (0.867)	0.171 (0.844)	0.153 (0.859)	0.208 (0.809)
ANALYST	-0.005 (0.641)	-0.005 (0.638)	-0.005 (0.637)	-0.005 (0.637)	-0.005 (0.635)
ADR	0.447 [*] (0.080)	0.441 [*] (0.085)	0.449 [*] (0.079)	0.442 [*] (0.085)	0.453 [*] (0.076)
RULE OF LAW	-0.014 (0.722)	-0.015 (0.712)	-0.014 (0.725)	-0.016 (0.693)	-0.016 (0.684)
CRISIS	0.170 (0.242)	0.178 (0.225)	0.175 (0.217)	0.172 (0.237)	0.168 (0.245)
POST-CRISIS	-0.045 (0.832)	-0.034 (0.871)	-0.038 (0.857)	-0.043 (0.837)	-0.051 (0.810)
QUOTA	0.411 ^{***} (0.003)	0.410 ^{***} (0.003)	0.406 ^{***} (0.004)	0.410 ^{***} (0.003)	0.403 ^{***} (0.004)
FAMILY	0.301 (0.547)	0.307 (0.539)	0.250 (0.616)	0.298 (0.546)	0.205 (0.674)
STATE	0.403 (0.349)	0.408 (0.344)	0.342 (0.430)	0.383 (0.358)	0.259 (0.517)
WIDELY	0.071 (0.818)	0.076 (0.806)	0.030 (0.923)	0.063 (0.835)	-0.017 (0.954)
N	2028	2028	2028	2028	2028
R-Squared	0.062	0.062	0.062	0.063	0.063

Table 8.4 continued

BDI ₁₆					
	(1)	(2)	(3)	(4)	(5)
Panel B: Firm Fixed Effects (Pre-Crisis Observations)					
IO TOTAL	0.009 (0.303)				
IO FOR		0.020* (0.055)			
IO DOM			-0.031 (0.197)		
IO COMMON				0.013 (0.219)	
IO CIVIL					-0.001 (0.976)
N	551	551	551	551	551
R-Squared	0.095	0.110	0.101	0.098	0.090
Panel C: Firm Fixed Effects (Crisis Observations)					
IO TOTAL	-0.005 (0.446)				
IO FOR		-0.003 (0.677)			
IO DOM			-0.003 (0.730)		
IO COMMON				0.000 (0.992)	
IO CIVIL					-0.013 (0.162)
N	1047	1047	1047	1047	1047
R-Squared	0.095	0.094	0.094	0.094	0.096
Panel D: Firm Fixed Effects (Post-Crisis Observations)					
IO TOTAL	-0.002 (0.780)				
IO FOR		0.005 (0.673)			
IO DOM			-0.016 (0.367)		
IO COMMON				-0.009 (0.336)	
IO CIVIL					0.037 (0.150)
N	430	430	430	430	430
R-Squared	0.124	0.124	0.127	0.126	0.130
Panel E: Firm Fixed Effects (Interaction Effects)					
IO TOTAL * FAMILY			-0.000 (0.987)		
IO FOR * FAMILY			-0.000 (0.997)		
IO DOM * FAMILY			0.003 (0.853)		
IO TOTAL * Non-FAMILY			0.002 (0.645)		
IO FOR * Non-FAMILY			0.004 (0.503)		
IO DOM * Non-FAMILY			-0.004 (0.534)		
Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. BDI ₁₆ = Board diversity index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, QUOTA = Gender Quota, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, WIDELY = Widely held at 20%.					

The study then moved to an examination of whether the role of institutional investors in the promotion of board diversity was dependent upon the legal system of the country wherein a firm operated (civil law versus common law countries). Table 8.5 indicates that institutional investors had mixed and insignificant associations with board diversity in both legal systems. This finding does not support the institutional theory, whilst it does complement the other studies that call for the consideration of the legal system when studying board diversity (see Grosvold, 2011; Grosvold and Brammer, 2011). In particular, this study contributes to the literature that the legal system does not affect the relationship between institutional investors and board diversity.

Table 8.5 Institutional Investors and Board Diversity: The Role of Legal Origin

BDI ₁₆						
	Civil Law Countries			Common Law Countries		
	Panel A: Firm Fixed Effects Panel			Panel B: Firm Fixed Effects Panel		
	(1)	(2)	(3)	(4)	(5)	(6)
IO TOTAL	0.002			0.000		
	(0.759)			(0.952)		
IO FOR		0.001			0.004	
		(0.817)			(0.657)	
IO DOM			0.000			-0.007
			(0.970)			(0.317)
FSIZE	0.336	0.326	0.324	0.212	0.236	0.227
	(0.673)	(0.681)	(0.684)	(0.737)	(0.708)	(0.718)
SGROWTH	-0.338	-0.336	-0.337	0.010	0.006	0.010
	(0.131)	(0.131)	(0.135)	(0.958)	(0.974)	(0.958)
LEV	-0.232	-0.225	-0.228	-1.341	-1.304	-1.386
	(0.800)	(0.805)	(0.803)	(0.190)	(0.203)	(0.177)
CASH	-0.329	-0.340	-0.335	-0.446	-0.442	-0.415
	(0.706)	(0.697)	(0.706)	(0.652)	(0.656)	(0.672)
CAPEX	0.393	0.368	0.381	0.509	0.561	0.363
	(0.851)	(0.860)	(0.859)	(0.764)	(0.736)	(0.830)
MB	-0.013	-0.013	-0.013	-0.017	-0.016	-0.017
	(0.750)	(0.743)	(0.742)	(0.425)	(0.456)	(0.446)
ROA	2.000	1.978	1.977	0.097	0.167	0.064
	(0.203)	(0.213)	(0.211)	(0.927)	(0.876)	(0.953)
PPE	0.393	0.396	0.393	-0.245	-0.275	-0.201
	(0.791)	(0.790)	(0.791)	(0.790)	(0.768)	(0.830)
ANALYST	0.003	0.003	0.003	-0.012	-0.012	-0.010
	(0.828)	(0.835)	(0.830)	(0.483)	(0.482)	(0.521)
ADR	0.430	0.432	0.439	0.414	0.408	0.405
	(0.171)	(0.168)	(0.157)	(0.250)	(0.256)	(0.260)
RULE OF LAW	-0.122*	-0.123*	-0.124*	0.036	0.031	0.037
	(0.059)	(0.058)	(0.060)	(0.587)	(0.639)	(0.585)
CRISIS	0.597***	0.597***	0.594***	0.152	0.156	0.158
	(0.005)	(0.006)	(0.005)	(0.355)	(0.347)	(0.332)
POST-CRISIS	-0.027	-0.030	-0.035	0.203	0.209	0.232
	(0.886)	(0.876)	(0.855)	(0.477)	(0.467)	(0.407)
QUOTA	0.538***	0.536***	0.535***	0.316*	0.313*	0.314*
	(0.006)	(0.006)	(0.006)	(0.084)	(0.086)	(0.087)
FAMILY	0.505	0.490	0.473	0.148	0.158	0.069
	(0.464)	(0.469)	(0.484)	(0.762)	(0.744)	(0.889)
STATE	0.471	0.452	0.433	0.549	0.573	0.495
	(0.428)	(0.434)	(0.467)	(0.429)	(0.405)	(0.450)
WIDELY	0.151	0.137	0.123	-0.009	0.006	-0.055
	(0.757)	(0.773)	(0.796)	(0.972)	(0.982)	(0.848)
N	1089	1089	1089	939	939	939
R-Squared	0.099	0.099	0.099	0.053	0.054	0.055

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. BDI₁₆ = Board diversity index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, QUOTA = Gender Quota, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, WIDELY = Widely held at 20%.

8.4.2 Board Gender Diversity

Gender diversity in particular has received much attention in recent years compared to the other diversity attributes. This study examined whether the presence of institutional investors improved the gender diversity of the board. Gender diversity is measured by the proportion of female directors across a corporate board. Table 8.6 presents the firm fixed effects panel regression results; according to these results, institutional investors had mixed but insignificant relationships with board gender diversity (see Table 8.6, Panel A). The results indicated that the association between institutional investors (total, foreign and domestic) is positive but insignificant (with coefficient = 0.000, 0.000, 0.000, p-value = 0.316, 0.723 and 0.282, and R-Squared value = 0.213, 0.212 and 0.213, respectively). Thus, these findings do not support the agency, resource dependence and institutional theories and led to the rejection of H7. The findings reveal that there is no association between institutional investors and board gender diversity. The findings are consistent with the previous studies that argued that the presence of women on a corporate board may not necessarily bring a favourable governance outcome. For instance, several studies found no or negative association between a gender diverse board and firm performance (Rose, 2007; Chapple and Humphrey, 2014), the excess CEO compensation (Adams and Ferreira, 2009; Bugeja et al., 2016), equity risk (Sila et al., 2016) and dividend payments (Saeed and Sameer, 2017). More recently, Gaitán et al. (2018) found that a higher representation of women on a corporate board decreases productivity. Several studies criticised the appointment of women on corporate boards as being a response to social and media pressure only (see Martín-Ugedo and Minguez-Vera, 2014; Gregorič et al., 2017). Overall, the findings contribute to the literature that institutional investors consider the costs of gender diversity to outweigh its benefits. These findings have an important implication for policy makers when revising their policy towards the enactment of gender quota legislation and whether a country has to choose a gender quota binding approach or a ‘comply or explain’ approach.

The recent financial crisis is considered an important period of history to many companies, yet there is little known about whether the institutional investors promote gender diversity in different economic conditions. Therefore, the study also investigated whether the role of institutional investors in improving board gender diversity is determined by different economic conditions (pre-crisis, crisis and post-crisis periods). The results revealed that institutional investors had mixed and insignificant associations with board gender diversity in all three economic conditions (see Table 8.6, Panels B, C and D). The results do not support the institutional theory and are consistent with Engelen et al. (2012), who found that gender diversity did not contribute to better firm performance during the financial crisis. This is also consistent with Pathan and Faff (2013), who documented that gender diversity improved the performance of financial firms in the pre-Sarbanes-Oxley Act (SOX) period (1997–2002); however, this positive association disappeared in both the post-SOX (2003–2006) and the recent financial crisis periods (2007–2011).

The study then examined whether the association between institutional investors and gender diversity was dependent upon the legal system of the country in which a firm was listed. For both legal systems, the associations were mixed and insignificant (see Table 8.6, Panels E and F). The study then examined whether this role was driven by a firm's ownership structure. Ultimately, the associations between institutional investors and diversity attributes were mixed and insignificant for both family-owned and non-family-owned firms (see Table 8.6, Panel G). The results imply that the ownership concentration did not play a part in the institutional investors' role in the improvement of board gender diversity. Overall, the findings do not support the institutional theory and complement the other studies that claimed that the importance of the legal system (Grosvold, 2011; Grosvold and Brammer, 2011) and ownership structure (Ben-Amar et al., 2013; Nekhili and Gatfaoui, 2013; Ararat et al., 2015; Farag and Mallin, 2016a) are significant when studying board diversity. In particular, this study found

that these two factors (the legal system and the ownership structure) have no influence over the relationship between institutional investors and board gender diversity.

Table 8.6 Institutional Investors and Board Gender Diversity

	(1)	(2)	(3)
GENDER DIV			
<i>Panel A: Firm Fixed Effects (All Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.316)		
<i>IO FOR</i>		0.000 (0.723)	
<i>IO DOM</i>			0.000 (0.282)
<i>N</i>	2028	2028	2028
<i>R-Squared</i>	0.213	0.212	0.213
<i>Panel B: Firm Fixed Effects (Pre-Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.895)		
<i>IO FOR</i>		-0.000 (0.580)	
<i>IO DOM</i>			0.000 (0.532)
<i>N</i>	551	551	551
<i>R-Squared</i>	0.138	0.139	0.140
<i>Panel C: Firm Fixed Effects (Crisis Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.229)		
<i>IO FOR</i>		0.000 (0.775)	
<i>IO DOM</i>			0.001 (0.191)
<i>N</i>	1047	1047	1047
<i>R-Squared</i>	0.264	0.262	0.265
<i>Panel D: Firm Fixed Effects (Post-Crisis Observations)</i>			
<i>IO TOTAL</i>	0.001 (0.161)		
<i>IO FOR</i>		0.001 (0.242)	
<i>IO DOM</i>			0.000 (0.696)
<i>N</i>	430	430	430
<i>R-Squared</i>	0.223	0.223	0.218
<i>Panel E: Firm Fixed Effects (Common Law Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.635)		
<i>IO FOR</i>		-0.000 (0.466)	
<i>IO DOM</i>			0.000 (0.162)
<i>N</i>	939	939	939
<i>R-Squared</i>	0.211	0.212	0.214
<i>Panel F: Firm Fixed Effects (Civil Law Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.990)		
<i>IO FOR</i>		0.000 (0.752)	
<i>IO DOM</i>			-0.000 (0.504)
<i>N</i>	1089	1089	1089
<i>R-Squared</i>	0.240	0.240	0.241
<i>Panel G: Interaction Effects (Firm Fixed Effects)</i>			
<i>IO TOTAL * FAMILY</i>		-0.000 (0.313)	
<i>IO FOR * FAMILY</i>		-0.000 (0.345)	
<i>IO DOM * FAMILY</i>		-0.001 (0.506)	
<i>IO TOTAL * Non-FAMILY</i>		0.000 (0.144)	
<i>IO FOR * Non-FAMILY</i>		0.000 (0.437)	
<i>IO DOM * Non-FAMILY</i>		0.000 (0.201)	
<p>Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 8.4. GENDER DIV = Board gender diversity, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.</p>			

8.4.3. Board Age Diversity

Age diversity is considered as one of the most observable attributes in corporate board diversity. This study examined whether the presence of institutional investors served to improve age diversity. Age diversity is measured by the coefficient of variation (standard deviation/mean) of directors' ages across the board. Table 8.7 presents the results of firm fixed effect panel regressions; these regressions indicated that total and foreign institutional investors had a positive but insignificant relationship with an age diverse board (with coefficient = 0.000 and 0.000, p-value = 0.871 and 0.656, and R-Squared value = 0.039 and 0.040), and domestic institutional investors had a negative association (with coefficient = -0.000, p-value = 0.482, and R-Squared value = 0.040) (see Table 8.7, Panel A). Therefore, the findings are not consistent with the resource dependence theory and led to the rejection of H8. The possible explanation for this may be that board age diversity may hinder the decision-making process of the corporate board, as the views of the elder and the younger directors cannot be aligned and consensus may hardly be reached (Goergen et al., 2015). This is consistent with other studies that claimed that an age diverse board is likely to spark intragroup conflicts in the decision-making process, leading to lower firm performance (Ali et al., 2014; Talavera et al., 2018). Furthermore, Boon et al. (2004) found an insignificant relationship between age diversity and market-to-book value. Several studies documented that age diverse boards are associated with less corporate social-responsibility engagement (see Hafsi and Turgut, 2013; Harjoto et al., 2015). The results fill an important gap in corporate governance literature by showing that institutional investors consider the costs of age diversity to outweigh its benefits, and the implication of the results is important for policy makers when they revise corporate governance codes and stewardship codes alike.

The study then investigated whether the role of institutional investors in improving age diversity is determined by economic conditions (see Table 8.7, Panels B, C and D). The results

indicated that while domestic institutions had negative and significant relationships with board age diversity at 10% during pre-crisis periods (with coefficient = -0.001, p-value = 0.054, and R-Squared value = 0.095), total and foreign institutional investors had negative relationships with board age diversity at 10% during post-crisis periods (with coefficient = -0.000 and -0.000, p-value = 0.059 and 0.072, and R-Squared value = 0.065 and 0.066). However, this influence was not evident during the financial crisis. The results could be attributed to the fact that corporate boards need advising more than monitoring during the crisis time (Francis et al., 2012). Therefore, the results may imply that an age diverse board may bring to the table multiple perspectives and advice (Darmadi, 2011; Ararat et al., 2015) during the time of crisis. However, the results are also consistent with Katmon et al. (2017), who found that age diversity was negatively associated with corporate social responsibility after the period of the recent financial crisis.

The same relationship was then examined in a different legal system, and the results indicated that the association between institutional investors and board age diversity were mixed and insignificant (see Table 8.7, Panels E and F). However, domestic institutions were an exception; they had a negative and significant association in common law countries at 10% (with coefficient = -0.000, p-value = 0.056, and R-Squared value = 0.090). The results indicated that the legal system does determine the role of the institutional investors in improving age diversity. The study also examined whether the ability of institutional investors in improving age diversity is determined by the ownership structure (see Table 8.7, Panel G). The results indicated that the associations were mixed and insignificant for both family-owned and non-family owned firms. The findings are consistent with Kang et al. (2007), who found that shareholder concentration is not significantly associated with board age diversity in Australian firms. Complementing the studies which emphasised the importance of institutional settings in the adoption of board diversity (Grosvold, 2011; Grosvold and Brammer, 2011; Ben-Amar et

al., 2013; Nekhili and Gatfaoui, 2013; Ararat et al., 2015; Sun et al., 2015; Farag and Mallin, 2016a), this study particularly contributes to the literature by showing that the association between institutional investors and board age diversity is determined by the economic conditions and the legal system, but not the ownership structure of the investee firms.

Table 8.7 Institutional Investors and Board Age Diversity

	(1)	(2)	(3)
AGE DIV			
<i>Panel A: Firm Fixed Effects (All Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.871)		
<i>IO FOR</i>		0.000 (0.656)	
<i>IO DOM</i>			-0.000 (0.482)
<i>N</i>	2028	2028	2028
<i>R-Squared</i>	0.039	0.040	0.040
<i>Panel B: Firm Fixed Effects (Pre-Crisis Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.750)		
<i>IO FOR</i>		0.000 (0.205)	
<i>IO DOM</i>			-0.001* (0.054)
<i>N</i>	551	551	551
<i>R-Squared</i>	0.080	0.092	0.095
<i>Panel C: Firm Fixed Effects (Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.736)		
<i>IO FOR</i>		-0.000 (0.622)	
<i>IO DOM</i>			0.000 (0.614)
<i>N</i>	1047	1047	1047
<i>R-Squared</i>	0.032	0.032	0.032
<i>Panel D: Firm Fixed Effects (Post-Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.000* (0.059)		
<i>IO FOR</i>		-0.000* (0.072)	
<i>IO DOM</i>			-0.000 (0.676)
<i>N</i>	430	430	430
<i>R-Squared</i>	0.065	0.066	0.050
<i>Panel E: Firm Fixed Effects (Common Law Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.706)		
<i>IO FOR</i>		0.000 (0.626)	
<i>IO DOM</i>			-0.000* (0.056)
<i>N</i>	939	939	939
<i>R-Squared</i>	0.084	0.084	0.090
<i>Panel F: Firm Fixed Effects (Civil Law Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.982)		
<i>IO FOR</i>		-0.000 (0.921)	
<i>IO DOM</i>			0.000 (0.739)
<i>N</i>	1089	1089	1089
<i>R-Squared</i>	0.039	0.039	0.040
<i>Panel G: Interaction Effects (Firm Fixed Effects)</i>			
<i>IO TOTAL * FAMILY</i>		0.000 (0.991)	
<i>IO FOR * FAMILY</i>		0.000 (0.822)	
<i>IO DOM * FAMILY</i>		-0.000 (0.774)	
<i>IO TOTAL * Non-FAMILY</i>		0.000 (0.865)	
<i>IO FOR * Non-FAMILY</i>		0.000 (0.729)	
<i>IO DOM * Non-FAMILY</i>		-0.000 (0.535)	
<p>Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 8.4. AGE DIV = Board age diversity, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.</p>			

8.4.4. Board Nationality Diversity

The nationality diversity of corporate boards has also attracted the attention of scholars and policy makers. This study investigated whether institutional investors promote the nationality diversity of corporate boards (see Table 8.8). Board nationality diversity was measured by the proportion of foreign directors across the board. The results revealed that there was a negative but insignificant association between total and foreign institutional investors and nationality diversity (with coefficient = -0.000 and -0.000, p-value = 0.483 and 0.341, and R-Squared value = 0.081 and 0.082, respectively). However, the association between domestic institutional investors and board nationality diversity was positive but insignificant (with coefficient = 0.000, p-value = 0.981, and R-Squared value = 0.081). Therefore, H9 was rejected. The findings do not support the resource dependence theory, and they contribute to the literature by revealing that institutional investors do not promote nationality diversity of the corporate boards of their investee firms. The results could be due to the costs associated with appointing foreign directors on the corporate board. Several scholars argued that nationality diversity may prevent the board from functioning properly. For instance, Miletkov et al. (2013) asserted that directors with a variety of languages and cultural aspects may affect the communication opportunities, which adversely affects participation in making effective decisions. This is consistent with Piekkari et al. (2015), who demonstrated that board members with different languages found it difficult to participate and articulate the decision taken by the board in Nordic countries. Hahn and Lasfer (2016) showed that firms with a higher percentage of foreign directors sitting on the board experience lower attendance at corporate board meetings, leading to less shareholder return and higher compensation for both the CEO and the chairman of the firm. Other studies also documented that firms with a higher proportion of foreign directors engage in less corporate social responsibility (Katmon et al., 2017), exhibit poor performance, lower board meeting attendance, higher CEO compensation packages and greater

financial misreporting (Masulis et al., 2012). More recently, Mallin and Farag (2017) reported a negative relationship between nationality diversity and financial performance in the UK. The implication of these results is important for the policy makers when revising corporate governance boards and stewardship codes.

The study examined whether economic conditions (pre-crisis, crisis and post-crisis periods) determine the role of institutional investors in the promotion of nationality diversity (see Table 8.8, Panels B, C and D). The results were mixed and insignificant in all three periods. The study also examined whether the association between institutional investors and nationality diversity is determined by the legal system (see Table 8.8, Panels E and F). The results were mixed and insignificant. The final investigation in this section was performed to determine whether the role of institutional investors in board nationality diversity is driven by the ownership structure. Ultimately, the associations between institutional investors and diversity attributes were mixed and insignificant for both family-owned and non-family-owned firms, though an exception was found for foreign institutional investors, who had negative and significant relationships with board nationality diversity in non-family-owned firms at 10% (with coefficient = -0.000 and p-value = 0.099) (see Table 8.8, Panel G). The findings complement previous studies that claimed institutional settings (economic conditions, legal systems and ownership structure) are important when studying corporate board diversity (Grosvold, 2011; Grosvold and Brammer, 2011; Ben-Amar et al., 2013; Nekhili and Gatfaoui, 2013; Ararat et al., 2015; Sun et al., 2015; Farag and Mallin, 2016a). In particular, this study contributes to the governance literature that these institutional settings are found to play no role in institutional investors' activism towards improving board nationality diversity.

Table 8.8 Institutional Investors and Board Nationality Diversity

	(1)	(2)	(3)
Nation DIV			
<i>Panel A: Firm Fixed Effects (All Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.483)		
<i>IO FOR</i>		-0.000 (0.341)	
<i>IO DOM</i>			0.000 (0.981)
<i>N</i>	2028	2028	2028
<i>R-Squared</i>	0.081	0.082	0.081
<i>Panel B: Firm Fixed Effects (Pre-Crisis Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.778)		
<i>IO FOR</i>		0.000 (0.881)	
<i>IO DOM</i>			0.001 (0.686)
<i>N</i>	551	551	551
<i>R-Squared</i>	0.106	0.105	0.107
<i>Panel C: Firm Fixed Effects (Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.547)		
<i>IO FOR</i>		-0.000 (0.831)	
<i>IO DOM</i>			-0.000 (0.655)
<i>N</i>	1047	1047	1047
<i>R-Squared</i>	0.042	0.041	0.042
<i>Panel D: Firm Fixed Effects (Post-Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.001 (0.286)		
<i>IO FOR</i>		-0.001 (0.114)	
<i>IO DOM</i>			0.001 (0.462)
<i>N</i>	430	430	430
<i>R-Squared</i>	0.128	0.133	0.126
<i>Panel E: Firm Fixed Effects (Common Law Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.786)		
<i>IO FOR</i>		-0.000 (0.220)	
<i>IO DOM</i>			0.000 (0.627)
<i>N</i>	939	939	939
<i>R-Squared</i>	0.095	0.098	0.095
<i>Panel F: Firm Fixed Effects (Civil Law Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.621)		
<i>IO FOR</i>		-0.000 (0.865)	
<i>IO DOM</i>			-0.000 (0.668)
<i>N</i>	1089	1089	1089
<i>R-Squared</i>	0.103	0.102	0.103
<i>Panel G: Interaction Effects (Firm Fixed Effects)</i>			
<i>IO TOTAL * FAMILY</i>		0.000 (0.299)	
<i>IO FOR * FAMILY</i>		0.000 (0.225)	
<i>IO DOM * FAMILY</i>		0.000 (0.950)	
<i>IO TOTAL * Non-FAMILY</i>		-0.000 (0.231)	
<i>IO FOR * Non-FAMILY</i>		-0.000* (0.099)	
<i>IO DOM * Non-FAMILY</i>		0.000 (0.999)	

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 8.4. Nation DIV= Board nationality diversity, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.

8.4.5. Board Education Diversity

This study also examined whether the presence of institutional investors served to enhance board education diversity. Education diversity is measured by the percentage of directors with postgraduate degrees across the board. Table 8.9 presents the results of firm fixed effect panel regressions; these regressions indicated that total and domestic institutional investors had a positive but insignificant relationship with board education diversity (with coefficient = 0.000 and 0.001, p-value = 0.542 and 0.280, and R-Squared value = 0.056 and 0.057). In contrast, foreign institutional investors had a negative association with board education diversity (with coefficient = -0.000, p-value = 0.823, and R-Squared value = 0.056). Therefore, the findings were determined not to support the resource dependence theory, and H10 is rejected. The results are consistent with those who find that board diversity may not necessarily bring a fruitful outcome to the company. For instance, Rose (2007) finds no association between directors' educational backgrounds and firm performance. Supporting these findings, Chun (2006) found that education diversity of the outside directors does not affect IPO firm valuation.

The study compared the association between the institutional investors and board education diversity in various economic conditions (pre-crisis, crisis and post-crisis periods). The results suggested that total and domestic institutional investors had positive and significant associations with education diversity during times of crisis at 1% and 10% respectively (with coefficient = 0.001 and 0.002, p-value = 0.067 and 0.001, and R-Squared value = 0.035 and 0.051). However, this influence was not detected during pre-crisis or post-crisis periods (see Table 8.9, Panels B, C and D). The results support the institutional theory and imply that institutional investors improved board education diversity during the period of crisis to help the company to get rid of the crisis. It is argued by Francis et al. (2012) that during a crisis, firms need more advising than monitoring, which indicates that institutional investors enhance

board education diversity in order for the firm to benefit from their experience and skills during the difficult time of crisis; however, these effects waned during pre- and post-crisis periods. The study also examined whether the legal system determines the association between institutional investors and education diversity (see Table 8.9, Panels E and F). The results indicated that the association is mixed and insignificant for both legal systems (civil law versus common law countries). This section concludes with an investigation of whether the role of the institutional investors in the promotion of board education diversity is determined by ownership structure (see Table 8.9, Panel G). The results were mixed and insignificant for both family-owned and non-family owned firms. Overall, the findings do not support the institutional theory framework, and they complement studies that emphasised the importance of the legal system (Grosvold, 2011; Grosvold and Brammer, 2011) and ownership structure (Ben-Amar et al., 2013; Nekhili and Gatfaoui, 2013; Ararat et al., 2015; Farag and Mallin, 2016a) in explaining board diversity by showing that these two settings (legal system and ownership structure) do not play a part in the relationship between institutional investors and board education diversity.

Table 8.9 Institutional Investors and Board Education Diversity

	(1)	(2)	(3)
EDU DIV			
<i>Panel A: Firm Fixed Effects (All Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.542)		
<i>IO FOR</i>		-0.000 (0.823)	
<i>IO DOM</i>			0.001 (0.280)
<i>N</i>	2028	2028	2028
<i>R-Squared</i>	0.056	0.056	0.057
<i>Panel B: Firm Fixed Effects (Pre-Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.858)		
<i>IO FOR</i>		-0.000 (0.598)	
<i>IO DOM</i>			0.001 (0.206)
<i>N</i>	551	551	551
<i>R-Squared</i>	0.097	0.099	0.102
<i>Panel C: Firm Fixed Effects (Crisis Observations)</i>			
<i>IO TOTAL</i>	0.001* (0.067)		
<i>IO FOR</i>		-0.000 (0.762)	
<i>IO DOM</i>			0.002*** (0.001)
<i>N</i>	1047	1047	1047
<i>R-Squared</i>	0.035	0.029	0.051
<i>Panel D: Firm Fixed Effects (Post-Crisis Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.978)		
<i>IO FOR</i>		0.000 (0.841)	
<i>IO DOM</i>			-0.000 (0.953)
<i>N</i>	430	430	430
<i>R-Squared</i>	0.076	0.076	0.076
<i>Panel E: Firm Fixed Effects (Common Law Observations)</i>			
<i>IO TOTAL</i>	0.000 (0.438)		
<i>IO FOR</i>		-0.000 (0.529)	
<i>IO DOM</i>			0.001 (0.241)
<i>N</i>	939	939	939
<i>R-Squared</i>	0.078	0.078	0.081
<i>Panel F: Firm Fixed Effects (Civil Law Observations)</i>			
<i>IO TOTAL</i>	-0.000 (0.688)		
<i>IO FOR</i>		-0.000 (0.976)	
<i>IO DOM</i>			-0.001 (0.428)
<i>N</i>	1089	1089	1089
<i>R-Squared</i>	0.076	0.076	0.077
<i>Panel G: Interaction Effects (Firm Fixed Effects)</i>			
<i>IO TOTAL * FAMILY</i>		-0.000 (0.734)	
<i>IO FOR * FAMILY</i>		-0.000 (0.787)	
<i>IO DOM * FAMILY</i>		-0.000 (0.845)	
<i>IO TOTAL * Non-FAMILY</i>		0.000 (0.365)	
<i>IO FOR * Non-FAMILY</i>		-0.000 (0.925)	
<i>IO DOM * Non-FAMILY</i>		0.001 (0.249)	
<p>Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 8.4. GENDER DIV = Board gender diversity, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors.</p>			

8.5. Robustness Tests

As described in chapter six, this study employed several robustness tests to confirm the main results. The tests utilised to confirm the results of the role of institutional investors and board diversity are reverse causality and system GMM tests. The results of these two tests are described in the following sections.

Reverse Causality

As discussed in Chapter Six, reverse causality might be of concern in this study, as it has the potential to lead to ineffective results. To address this issue, change score regressions were applied in an effort to determine whether changes in institutional ownership drove changes in board diversity or whether the reverse held true (Aggarwal et al., 2011). Panel A of Table 8.10 demonstrates the results of these tests. In these tests, a change in the Board Diversity Index (ΔBDI_{16}) from period $t-1$ to t represented the dependent variable. The main explanatory variables were changes in institutional ownership (ΔIO) from period $t-2$ to $t-1$. All other independent variables were expressed in terms of change; these variables were lagged by one period relative to the Board Diversity Index. Panel A of Table 8.10 shows that changes in total, foreign, domestic, common and civil institutional investors had a mixed and insignificant association with the Board Diversity Index (with coefficient value = -0.001, 0.001, -0.004, -0.000 and 0.001, p-value = 0.790, 0.767, 0.339, 0.906 and 0.848, and R-Squared = 0.033, 0.033, 0.033, 0.033 and 0.033, respectively).

Panel B of Table 8.10 demonstrates the results of the reverse relationship analysis, which was conducted in an effort to study whether changes in board diversity (BDI_{16}) drove changes in institutional ownership. In this analysis, the dependent variables were changes in institutional ownership (ΔIO) from period $t-1$ to t . The main explanatory variable was a change in the Board Diversity Index (ΔBDI_{16}) from period $t-2$ to $t-1$. All other independent variables were expressed in terms of change; they were also lagged by one period relative to institutional ownership.

Panel B of Table 8.10 shows that the association between institutional investors (total, foreign, domestic, common and civil institutions) and the Board Diversity Index was mixed and insignificant (with coefficient value = 0.026, 0.058, -0.041, -0.074 and 0.096, p-value = 0.897, 0.756, 0.530, 0.671 and 0.336, and R-Squared = 0.033, 0.041, 0.049, 0.040 and 0.033, respectively). Ultimately, the results were consistent with the main results of this study (see Table 8.4 for comparison).

Table 8.10 Changes in Institutional Ownership and Changes in Board Diversity

	ΔBDI_{16} coefficient	N	R Squared
Panel A: Yearly Changes (Changes in Institutional Ownership and Changes in Board Diversity)			
<i>ΔIO TOTAL</i>	-0.001 (0.790)	1553	0.033
<i>ΔIO FOR</i>	0.001 (0.767)	1553	0.033
<i>ΔIO DOM</i>	-0.004 (0.339)	1553	0.033
<i>ΔIO COMMON</i>	-0.000 (0.906)	1553	0.033
<i>ΔIO CIVIL</i>	0.001 (0.848)	1553	0.033
Panel B: Yearly Changes (Changes in Board Diversity and Changes in Institutional Ownership)			
<i>ΔIO TOTAL</i>	0.026 (0.897)	1553	0.033
<i>ΔIO FOR</i>	0.058 (0.756)	1553	0.041
<i>ΔIO DOM</i>	-0.041 (0.530)	1553	0.049
<i>ΔIO COMMON</i>	-0.074 (0.671)	1553	0.040
<i>ΔIO CIVIL</i>	0.096 (0.336)	1553	0.033
Note: Regressions also include year, country and industry dummies and standard errors corrected for country-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. All models include the control variables (coefficient not shown) used in Table 8.4. BDI_{16} = Board diversity index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors.			

System GMM

As discussed in chapter six, this study adopted a system GMM technique as a robustness test. To this end, the xtabond2 dynamic panel estimator in STATA 14 was considered, and the procedure of Wintoki et al. (2012) adapted to model the association between institutional investors and board diversity index (BDI_{16}). Table 8.11 presents the results of this GMM, which test the role of institutional investors in improving Board Diversity Index (BDI_{16}). When

running a system GMM, two diagnostic tests must be utilised in order to ensure the validity of this technique. The first test is related to second-order serial correlation AR (2), with a P value $> 5\%$. The second test is the Hansen J test of over-identification, which is used to determine whether an instrument is uncorrelated with the error term in the models, with a P value $> 5\%$. The results, as reported in Table 8.10, indicated that there was no serial correlation (with AR (2) ranges from 0.083 to 0.086), and that the instruments used in the system GMM were valid and uncorrelated with the error term (with the Hansen J test value ranges from 0.059 to 0.062). Table 8.11 shows that the association between total, foreign and common institutional investors and the Board Diversity Index (BDI_{16}) was positive but insignificant (with coefficient value = 0.002, 0.003 and 0.002, and p-value = 0.347, 0.272 and 0.250, respectively). However, the association between domestic and civil institutional investors was negative and insignificant (with coefficient value = -0.001 and -0.002, and p-value = 0.728 and 0.672, respectively). This result was consistent with the main results presented in Table 8.4.

Table 8.11 Institutional Investors and the Board Diversity Index (System GMM)

	(1)	(2)	(3)	(4)	(5)
	BDI₁₆				
BDI₁₆	0.836***	0.834***	0.834***	0.836***	0.835***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
IO TOTAL	0.002				
	(0.347)				
IO FOR		0.003			
		(0.272)			
IO DOM			-0.001		
			(0.728)		
IO COMMON				0.002	
				(0.250)	
IO CIVIL					-0.002
					(0.672)
FSIZE	0.120	0.116	0.088	0.117	0.086
	(0.156)	(0.162)	(0.271)	(0.155)	(0.285)
SGROWTH	0.119	0.116	0.121	0.119	0.124
	(0.423)	(0.435)	(0.412)	(0.423)	(0.402)
LEV	-0.091	-0.079	-0.078	-0.093	-0.082
	(0.678)	(0.719)	(0.726)	(0.671)	(0.712)
CASH	-0.357	-0.372	-0.368	-0.362	-0.367
	(0.264)	(0.243)	(0.249)	(0.259)	(0.253)
CAPEX	0.775	0.749	0.710	0.767	0.709
	(0.381)	(0.395)	(0.416)	(0.385)	(0.417)
MB	-0.000	-0.000	-0.001	-0.000	-0.001
	(0.998)	(0.986)	(0.936)	(0.981)	(0.925)
ROA	0.918*	0.918*	0.881*	0.915*	0.877*
	(0.061)	(0.061)	(0.072)	(0.062)	(0.073)
PPE	-0.002	-0.008	0.008	-0.003	0.010
	(0.993)	(0.966)	(0.966)	(0.987)	(0.958)
ANALYST	0.004	0.004	0.005	0.004	0.005
	(0.365)	(0.375)	(0.334)	(0.365)	(0.332)
ADR	-0.001	-0.004	0.006	-0.002	0.007
	(0.985)	(0.953)	(0.928)	(0.978)	(0.919)
RULE	-0.065*	-0.065*	-0.065	-0.066*	-0.066*
	(0.100)	(0.098)	(0.102)	(0.095)	(0.098)
CRISIS	0.204	0.209	0.207	0.205	0.205
	(0.193)	(0.181)	(0.187)	(0.191)	(0.191)
POST-CRISIS	0.096	0.103	0.101	0.097	0.098
	(0.617)	(0.591)	(0.600)	(0.612)	(0.610)
FAMILY	0.320	0.322	0.283	0.308	0.271
	(0.109)	(0.108)	(0.142)	(0.112)	(0.188)
STATE	0.040	0.041	0.003	0.023	-0.013
	(0.839)	(0.835)	(0.989)	(0.906)	(0.951)
WIDELY	0.082	0.083	0.069	0.071	0.060
	(0.622)	(0.617)	(0.677)	(0.668)	(0.733)
AR(1)	0.000	0.000	0.000	0.000	0.000
AR(2)	0.086	0.086	0.084	0.085	0.083
Hansen	0.061	0.061	0.062	0.059	0.061
N	2028	2028	2028	2028	2028

Note: Regressions also include year dummies and standard errors corrected for firm-level clustering. Robust p-values corrected for firm-level clustering are reported in parentheses. *, **, *** indicate significance at the 10%, 5%, and 1% levels respectively. BDI₁₆= Board diversity index, IO TOTAL = Total institutional investors, IO FOR = Foreign institutional investors, IO DOM = Domestic institutional investors, IO COMMON = Common law institutional investors, IO CIVIL = Civil law institutional investors, FSIZE = Firm size, SGROWTH = Sales growth, LEV = Leverage, Cash = Cash, CAPEX = Capital Expenditure, MB = Market-to-book value, ROA = Return on Asset, PPE = Property, plant and equipment, ANALYST = Analyst following, ADR = Cross listing dummy, Rule = Rule of law, CRISIS = Crisis dummy, POST-CRISIS = Post crisis dummy, FAMILY = Family controlling at 20%, STATE = State controlling at 20%, WIDELY = Widely held at 20%.

8.6. Chapter Summary

This chapter outlined the research analysis procedures and findings of the institutional investors' role in the improvement of board diversity, beginning with a descriptive examination of the variables used in this study. The chapter then discussed the results of the correlation analysis and VIF tests. The chapter outlined the results of the hypothesis tests (H6–H10) that were developed in Chapter Five of this thesis. Furthermore, this chapter illustrated the results of efforts to test these hypotheses according to various institutional settings and to include diverse economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. Finally, this chapter concluded with an explanation of the results of two main robustness tests: reverse causality and system GMM.

Chapter 9

9.0 Summary and Conclusion

9.1. Introduction

This chapter provides a concise summary of this research study. First, the research objectives and questions will be restated, and then the main results and study implications will be reviewed. Next, this chapter will describe the contributions of this study and outline its limitations; finally, possible avenues for future research will be presented.

Accordingly, this chapter is organised as follows: section 9.2 reviews the objectives and questions of this study, section 9.3 demonstrates the main findings and research implications, section 9.4 illustrates the study contributions and section 9.5 identifies the research limitations and suggests avenues for future research.

9.2. Restatement of the Research Objectives and Questions

The main objective of this study was to investigate the role of institutional investors in the improvement of corporate governance practices around the world. This was accomplished by analysing evidence regarding the various characteristics of numerous boards of directors. These characteristics were related to board attributes (composition, activity, entrenchment and busyness) and board diversity (gender, age, nationality and education). An additional purpose of this study was to examine this relationship within various institutional environments, to include multiple economic conditions (pre-crisis, crisis and post-crisis periods), national legal systems and ownership structures. To this end, this study aimed to answer six main empirical questions: (1) Do institutional investors influence corporate board attributes? (2) Do institutional investors influence the characteristics of a board's key subcommittees? (3) Do institutional investors influence board diversity? (4) Do institutional investors play different roles within different economic environments (pre-crisis, crisis and post-crisis periods)? (5) Do institutional investors play different roles within different legal systems? and (6) Do

institutional investors play different roles according to whether they operate within concentrated or dispersed ownership structures?

9.3. Summary of Findings and Research Implications

This study analysed a sample of companies that were in operation in 15 countries across the globe between 2006 and 2012 and found that institutional investors promoted more favourable corporate governance outcomes. Interestingly, foreign institutional investors took on a lead role in the improvement and convergence of corporate governance practices around the world. The results are consistent with the findings of previous studies, which argue that foreign institutional investors exert greater influence over the governance structures of their investee firms; this is likely because they possess fewer business relationships within their investee firms as compared to their counterparts (Aggarwal et al., 2011; Ferreira and Matos, 2008). This study also provided evidence that institutional investors promoted better composition of corporate boards and of their audit and compensation committees (though not of their nomination committees). Moreover, while institutional investors were not found to be positively associated with the activity of boards or of compensation and nomination committees, they were positively associated with audit committee activity. Results also demonstrated that institutional investors reduced board entrenchment, but not board busyness. The study also found no evidence that institutional investors promoted board diversity; thus, there was arguably no association between institutional ownership and various board diversity attributes such as gender, age, nationality and education.

The findings also revealed that a company's institutional environment influenced the role of institutional investors in corporate governance; such environmental aspects included various economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. To some extent, this result was found to be more closely related to corporate board attributes than to board diversity characteristics. For instance, the findings indicated that

institutional investors played a stronger role in the improvement of governance structures during crisis and post-crisis periods; their influence during pre-crisis periods, however, was less evident. This finding was also applicable to individual board attributes, including the independence of audit committees.

Furthermore, institutional investors were found to increase the independence of a board and its key subcommittees (with the exception of nomination committees) in civil law countries, though they reduced board busyness in common law countries. However, this study uncovered no evidence with respect to institutional investors' role in reducing board entrenchment within either legal system. Overall, this finding is consistent with the work of La Porta et al. (1998), who have argued that investors in countries with weak shareholder protections may seek out other means of protecting their investments.

Results also revealed that the presence of institutional investors led to improved governance outcomes in non-family-owned firms, but not in family-owned firms. These results may explain the importance of considering ownership structures when investigating the adoption of corporate governance mechanisms in a particular firm (see Desender et al., 2013; Sure et al., 2013; Desender et al., 2016). With regard to board diversity, the findings indicated that institutional investors were negatively associated with board age diversity during pre-crisis and post-crisis periods and positively associated with education diversity during times of crisis. Furthermore, while institutional investors demonstrated no influence over board diversity outcomes (i.e., gender, age, nationality and education) in civil law countries, they were found to be negatively associated with board age diversity in common law countries. The study's results also suggested that the associations between institutional investors and board diversity were mixed and insignificant within the various ownership structures (family- and non-family-owned firms).

The implications of this study are particularly meaningful for policymakers. On the one hand, these findings suggest that institutional investors play a meaningful and effective role in the improvement of governance structures within their investee firms. Thus, policymakers around the world are encouraged to continue to issue stewardship and corporate governance codes in order to increase awareness and encourage engagement between institutional investors and their investee firms. On the other hand, our results highlight the importance of considering a company's institutional environment when studying the ability of institutional investors to improve the governance structures of their investee firms. These settings include various economic conditions (pre-crisis, crisis and post-crisis periods), legal systems and ownership structures. Additionally, this study should draw the attention of policymakers across the globe and enlighten them as to the fact that institutional investors do not play a part in the improvement of board diversity. Therefore, policymakers are encouraged to increase the awareness of institutional investors in this regard and to exhort them to take part in addressing this matter of global concern.

In addition, despite the size of institutional investor groups around the globe, they do not seem to be promoting board diversity (gender, age, nationality and education), which could be due to the costs of board diversity exceeding its benefits. For instance, several studies have criticised the legislation of gender quotas on corporate boards, as it leads to the employment of incompetent and less-experienced directors, which negatively influences board and firm performance (Adams and Ferreira, 2009; Ahern and Dittmar, 2012; Bøhren and Staubo, 2014). Several scholars have noted that companies adopt the concept of board diversity by appointing ethnic minorities and women on their boards only to enhance their reputations and minimise the pressure from the media and stakeholders (Martín-Ugedo and Minguez-Vera, 2014; Gregorič et al., 2017). Therefore, the implications of this study are useful for policy makers when revising their policies with regard to the enactment of mandatory gender quotas.

9.4. Research Contribution

This research makes several contributions to the corporate governance literature. While the majority of previous studies have focused on data taken from one country (mainly the US market) (Chung et al., 2002; Hartzell and Starks, 2003; Parriino et al., 2003; Velury et al., 2003; Almazan et al., 2005; Brav et al., 2008; Wang, 2010; Hadani et al., 2011; Ruiz-Mallorquí and Santana-Martín, 2011; Chhaochharia et al., 2012; Helwege et al., 2012; Muniandy et al., 2016), this study utilised an international sample when investigating the role of institutional investors in the improvement of corporate governance. In fact, to the best of my knowledge, this study is the first to examine the role of institutional investors in the improvement of a wide range of corporate board characteristics, to include board attributes (composition, activity, entrenchment and busyness) and board diversity (gender, age, nationality and education diversity). While institutional investors are found to improve board attributes, their influence over board diversity is not evident. This might be due to the fact that the cost of board diversity exceeds its benefits. Several studies have reported that board gender diversity may not bring a fruitful governance outcome (Rose, 2007; Chapple and Humphrey, 2014; Bugeja et al., 2016; Sila et al., 2016; Saeed and Sameer, 2017; Gaitán et al., 2018); this is consistent with other studies that have reported similar results with other board diversity attributes, such as age (Boon et al., 2004; Hafsi and Turgut, 2013; Ali et al., 2014; Harjoto et al., 2015; Talavera et al., 2018), nationality (Masulis et al., 2012; Miletkov et al., 2013; Hahn and Lasfer, 2016; Katmon et al., 2017; Mallin and Farag, 2017) and education (Rose, 2007; Chun, 2006). Furthermore, this study sheds additional light on the role of institutional investors in efforts to improve the composition and activity of a board's key subcommittees (audit, compensation and nomination). While institutional investors were found to promote the composition of the board and its key sub-committees (with the exception of nomination committees), they only improve the activity of audit committees.

This research also serves to complement studies that call for the consideration of national institutional settings when examining corporate board attributes (Aguilera et al., 2008; Aguilera and Jackson, 2010). Various aspects of such settings include economic conditions (Essen et al., 2013), legal systems (Aguilera et al., 2008; Aguilera et al., 2012; Kim and Ozdemir, 2014) and ownership structures (Desender et al., 2013; Judge, 2011, 2012; Sure et al., 2013). This study thus opens a new line of research that might enhance our understanding when studying the role of institutional investors in the improvement of their investee firms' governance structures. This study also emphasises that the ability of institutional investors to improve the corporate board characteristics of their investee firms is to some extent determined by the firm's national institutional environment, to include its economic condition (whether it exists within a pre-crisis, crisis or post-crisis period), prevailing legal system and ownership structure. In addition, while the institutional settings (economic conditions, legal system and ownership structure) have been observed to determine the association between institutional investors and board attributes (composition, activity, entrenchment and busyness) to a greater extent, they are less evident in determining the relationship between institutional investors and board diversity (gender, age, nationality and education diversity). In particular, this study contributes to the bundle perspective of comparative corporate governance (Aguilera et al., 2008; Aguilera and Jackson, 2010; Judge, 2011, 2012; Aguilera et al., 2012; Desender et al., 2013; Sure et al., 2013; Kim and Ozdemir, 2014) the information that institutional investors generally improved board attributes during and after a financial crisis. While the institutional investors have the influence to improve board attributes in common law countries in general, the study also demonstrated that institutional investors choose to improve specific board attributes in civil law countries (i.e. board composition and board entrenchment). This can be explained as an attempt from the institutional investors to mitigate weak shareholder protection in civil law countries (La Porta et al., 1998). The study also contributes to the field of corporate governance

evidence to support the second type of agency cost, Principal-Principal conflict (Shleifer and Vishny, 1997). The findings revealed that the role of institutional investors in improving board attributes is determined to some extent by the ownership structure (family-owned vs non-family-owned firms), with greater improvement of board attributes occurring in non-family firms.

More importantly, following the recent call to broaden the theoretical scope of corporate governance studies (see Kumar and Zattoni, 2015; Zattoni and Van Ees; 2012), this research contributes to the corporate governance literature by considering multiple theoretical perspectives. As discussed in the second chapter of this study, several theories drawn from multiple disciplines were utilised to develop a fuller understanding of the role of institutional investors in the improvement of corporate governance outcomes around the globe. The findings of this study illustrated the applicability of agency theory, stewardship theory, resource dependence theory, institutional theory and stakeholder theory to explain the relationship between institutional investors and board attributes. However, there was little to no evidence that the agency, resource dependence and institutional theories explain the association between institutional investors and board diversity.

This study's final contribution is related to the insight it offers to policymakers. This study demonstrates the importance and ability of stewardship codes to enhance engagement between institutional investors and their investee firms. Furthermore, this study implies that in the future, policymakers may focus on board diversity when revising corporate governance and stewardship codes. Furthermore, this study provides an additional insight that may be useful to policymakers; namely, that a firm's national institutional setting should be considered when investigating the role of institutional investors in corporate governance.

9.5. Research Limitations and Future Research

Several limitations have been encountered while undertaking this study. One major constraint was a lack of time, which limits the study to include only those firms listed in the main indices of the sample countries. Therefore, future research should include all firms for whom information is available in the databases; this will allow the findings to gain additional generalisability.

Another limitation faced by the study involved a lack of data with respect to emerging and developing markets. Future studies should attempt to overcome this limitation as more data for such countries becomes available. This will enable future researchers to analyse the role of institutional investors in the improvement of corporate governance structures in a variety of capital markets.

Furthermore, future studies might consider cultural variances between countries and firms, as the culture of a country (Li and Harrison, 2008; Grosvold and Brammer, 2011) and of a firm (Guiso et al., 2015) can influence the level of governance within an investee firm. Such a consideration will allow researchers to gain insight into the topic of whether culture serves to influence the role of institutional investors in the improvement of corporate governance structures. More recently, several studies have argued that stock liquidity can also influence the behaviour of institutional investors in terms of whether they adopt the voice or exit strategy (McCahery et al., 2016; Edmans et al., 2013; Roosenboom et al., 2013). Therefore, future studies are recommended to investigate the role of institutional investors in improving corporate governance (e.g., board attributes and board diversity) in light of the stock liquidity of the investee firm.

Finally, while this study investigated the role of institutional investors in the improvement of a wide range of corporate board characteristics, future investigations on the topic should include additional corporate board characteristics such as experience and ethnicity.

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Appendices

Appendix one : List of Firms							
SN	Australia	33	LIHIR GOLD	64	ENERPLUS	97	SILVER WHEATON
1	AGL ENERGY	34	OIL SEARCH	65	FIRST QUANTUM MRLS.	98	BOMBARDIER 'B'
2	ARISTOCRAT LEISURE	35	ILUKA RESOURCES	66	GILDAN ACTIVEWEAR	99	METRO INC
3	AMCOR	36	OZ MINERALS	67	GOLDCORP	100	POTASH CORPORATION OF SASKATCHEWAN
4	ALUMINA	37	TOLL HOLDINGS	68	YAMA GOLD	101	ROGERS COMMS.'B'
5	BHP BILLITON	38	SONIC HEALTHCARE	69	HUSKY EN.	102	SAPUTO
6	BORAL	39	TRANSURBAN GROUP	70	KINROSS GOLD	103	SHAW COMMS.'B'
7	BLUESCOPE STEEL	40	WESFARMERS	71	LOBLAW	104	SHOPPERS DRUG MART
8	ASCIANO	41	WOODSIDE PETROLEUM	72	MAGNA INTL.	105	TECK RESOURCES 'B'
9	AURIZON HOLDINGS	42	WOOLWORTHS	73	IMPERIAL OIL	106	IAMGOLD
10	BRAMBLES	Belgium		74	ENBRIDGE	107	ALCAN
11	CSL	43	AGFA-GEVAERT	75	ARC RESOURCES	108	COTT
12	COLES GROUP	44	ANHEUSER-BUSCH INBEV	76	BARRICK GOLD	109	COGNOS
13	FOSTER'S GROUP	45	BEKAERT	77	CENOVUS ENERGY	110	FORDING CDN.COAL TST. UTS.
14	CROWN RESORTS	46	PROXIMUS	78	FORTIS	111	AIMIA
15	FORTESCUE METALS GP.	47	COLRUYT	79	BCE	112	INMET MINING
16	SYDNEY AIRPORT	48	DELHAIZE GROUP	80	TELUS	113	LUNDIN MINING
17	CONSOLIDATED MEDIA HDG	49	MOBISTAR	81	CRESCENT POINT ENERGY	114	NORDION
18	INTOLL GROUP	50	OMEGA PHARMA	82	CAMECO	115	NEXEN
19	CIMIC GROUP	51	UCB	83	CANADIAN OIL SANDS	116	NOVA CHEMICALS
20	ARRIUM	52	UMICORE	84	CANADIAN NATURAL RESOURCES	117	PETRO CANADA
21	COCA-COLA AMATIL	53	NYRSTAR	85	CANADIAN PACIFIC RY.	118	TIM HORTONS
22	COMPUTERSHARE	54	TELENET GROUP HOLDING	86	BLACKBERRY	119	URANIUM ONE
23	NEWCREST MINING	55	D'IETEREN	87	CANADIAN TIRE 'A'	Denmark	
24	ORICA	56	ELIA SYSTEM OPERATOR	88	AGRIUM	120	A P MOLLER - MAERSK 'B'
25	ORIGIN ENERGY (EX BORAL)	57	SOLVAY	89	TALISMAN EN.	121	BANG & OLUFSEN 'B'
26	QANTAS AIRWAYS	58	ENGIE	90	THOMSON REUTERS	122	CARLSBERG 'B'
27	RIO TINTO Ltd	Canada		91	TRANSCANADA	123	COLOPLAST 'B'
28	SANTOS	59	CANADIAN NATIONAL RAILWAY	92	TRANSALTA	124	TORM A
29	SPARK NEW ZEALAND (ASX)	60	SUNCOR ENERGY	93	WESTON GEORGE	125	DSV 'B'
30	TABCORP HOLDINGS	61	AGNICO EAGLE MINES	94	VALEANT PHARMS.INTL.	126	DMPKBT.NORDEN
31	TELSTRA	62	ELDORADO GOLD	95	SNC-LAVALIN GP.	127	FLSMIDTH & CO.'B'
32	INCITEC PIVOT	63	ENCANA	96	PENN WEST PETROLEUM	128	GN STORE NORD

Appendix one continued							
129	CHR HANSEN HOLDING	161	YIT	193	TECHNIP	225	HERO MOTOCORP
130	H LUNDBECK	162	UPONOR	194	TOTAL	226	COAL INDIA
131	NOVO NORDISK 'B'	163	TALVIVAARA MNG.CO.	195	VALLOUREC	227	GAIL (INDIA)
132	NKT	France		196	VEOLIA ENVIRONNEMENT	228	MAHINDRA & MAHINDRA
133	NOVOZYMES	164	VIVENDI	197	VINCI	229	JAIPRAKASH ASSOCIATES
134	VESTAS WINDSYSTEMS	165	MICHELIN	198	AIR FRANCE-KLM	230	JINDAL STEEL & POWER
135	WILLIAM DEMANT HLDG.	166	ALCATEL-LUCENT	199	PEUGEOT	231	STERLITE INDS.(INDIA)
136	PANDORA	167	GEMALTO	200	STMICROELECTRONICS	232	SUN PHARM.INDUSTRIES
137	TDC	168	ALSTOM	201	TECHNICOLOR	Ireland	
Finland		169	ACCOR	India		233	AER LINGUS GROUP
138	AMER SPORTS	170	AIR LIQUIDE	202	ACC	234	C&C GROUP
139	CARGOTEC 'B'	171	AIRBUS GROUP	203	BAJAJ AUTO	235	CRH (DUB)
140	ELISA	172	ARCELORMITTAL	204	BHARAT HEAVY ELS.	236	DCC (DUB)
141	FORTUM	173	RENAULT	205	BHARTI AIRTEL	237	ELAN
142	KESKO 'B'	174	BOUYGUES	206	GRASIM INDUSTRIES	238	GRAFTON GROUP (DUB)
143	HUHTAMAKI	175	CAP GEMINI	207	HINDALCO INDUSTRIES	239	GREENCORE GROUP (DUB)
144	KEMIRA	176	CARREFOUR	208	HINDUSTAN UNILEVER	240	DRAGON OIL
145	KONE 'B'	177	DANONE	209	INFOSYS (IND)	241	GLANBIA
146	KONECRANES	178	EDF	210	ITC	242	ARYZTA (DUB)
147	METSA BOARD 'B'	179	ESSILOR INTL.	211	LARSEN & TOUBRO	243	INDEPENDENT NEWS & MEDIA
148	METSO	180	GDF SUEZ	212	MARUTI SUZUKI INDIA	244	KERRY GROUP 'A'
149	NESTE	181	KERING	213	NTPC	245	KINGSPAN GROUP
150	NOKIA	182	L'OREAL	214	OIL & NATURAL GAS	246	MCINERNEY HOLDINGS
151	OUTOKUMPU 'A'	183	LAFARGE	215	RANBAXY LABS.	247	PADDY POWER
152	RAUTARUUKKI 'K'	184	LEGRAND	216	RELIANCE COMMUNICATIONS	248	RYANAIR HOLDINGS
153	OUTOTEC	185	LVMH	217	RELIANCE INDUSTRIES	249	SMURFIT KAPPA GROUP
154	SANOMA	186	ORANGE	218	RELIANCE INFRASTRUCTURE	250	IRISH CONT.GP.UNT.
155	ORION 'B'	187	PERNOD-RICARD	219	SATYAM COMPUTER SERVICES	251	KENMARE RESOURCES
156	STORA ENSO 'R'	188	PUBLICIS GROUPE	220	TATA CONSULTANCY SVS.	252	PROVIDENCE RES. (ESM)
157	TELIASONERA (HEL)	189	SAFRAN	221	TATA MOTORS	Italy	
158	TIETO OYJ	190	SANOFI	222	TATA STEEL	253	A2A
159	UPM-KYMMENE	191	SCHNEIDER ELECTRIC	223	TATA POWER	254	AUTOGRILL
160	WARTSILA	192	SOLVAY	224	WIPRO	255	BULGARI

Appendix one continued							
256	ENEL	288	BOSKALIS WESTMINSTER	320	TANDBERG	352	INDITEX
257	ENI	289	KPN KON	321	TELENOR	353	INDRA SISTEMAS
258	FIAT CHRYSLER AUTOS.	290	PHILIPS ELTN.KONINKLIJKE	322	TGS-NOPEC GEOPHS.	354	MEDIASET ESPANA COMUNICACION
259	FASTWEB	291	RELX	323	TOMRA SYSTEMS	355	NH HOTEL GR
260	ENEL GREEN POWER	292	ROYAL DUTCH SHELL	324	YARA INTERNATIONAL	356	RED ELECTRICA CORPN.
261	GRUPPO EDIT.L'ESPRESSO	293	RANDSTAD HOLDING	325	SEVAN MARINE	357	REPSOL YPF
262	LUXOTTICA	294	SBM OFFSHORE	326	SONGA OFFSHORE	358	TELEFONICA
263	MEDIASET	295	POSTNL	327	STATOIL FUEL & RETAIL	359	UNION FENOSA
264	ARNOLDO MONDADORI EDI.	296	TOM TOM	328	SCHIBSTED A	360	GRIFOLS ORD CL A
265	PARMALAT	297	UNILEVER NV	329	ROYAL CRBN.CRUISES (OSL)	361	IBERDROLA RENOVABLES
266	PIRELLI	298	VEDIOR	330	ALGETA	362	OBRASCON HUARTE LAIN
267	STMICROELECTRONICS (MIL)	299	WOLTERS KLUWER	331	CERMAQ	363	TECNICAS REUNIDAS
268	SAIPEM	300	TNT EXPRESS	332	DET NORSKE OLJESELSKAP	364	INTL.CONS.AIRL.GP. (MAD) (CDI)
269	SNAM	301	USG PEOPLE	333	ELECTROMAG.GEOSVS.	365	VISCOFAN
270	TELECOM ITALIA	302	AIR FRANCE-KLM	334	QUESTERRE ENERGY (OSL)	366	ARCELORMITTAL (MAD)
271	SEAT PAGINE GIALLE	303	ARCELORMITTAL	335	NORWEGIAN AIR SHUTTLE	367	EBRO FOODS
272	TENARIS	Norway		Spain		368	AMADEUS IT HOLDING
273	TERNA Spa	304	AKASTOR	336	ABERTIS INFRAESTRUCTURAS	369	DISTRIBUIDORA INTNAC.DE ALIMENTACION
274	TOD'S	305	DNO	337	ABENGOA	Sweden	
275	DAVIDE CAMPARI MILANO	306	FRED OLSEN ENERGY	338	ACCIONA	370	ABB LTD N (OME)
276	GEOX	307	FRONTLINE	339	ACERINOX 'R'	371	ASSA ABLOY 'B'
277	SALVATORE FERRAGAMO	308	MARINE HARVEST	340	ACS ACTIV.CONSTR.Y SERV.	372	ALFA LAVAL
Netherlands		309	GOLDEN OCEAN GROUP	341	AGUAS DE BARCELONA	373	ASTRAZENECA (OME)
278	AHOLD KON.	310	NORSK HYDRO	342	ALTADIS	374	ATLAS COPCO 'A'
279	AKZO NOBEL	311	NORSKE SKOGINDUSTRIER	343	ATRESMEDIA CORP	375	BOLIDEN
280	ASML HOLDING	312	OCEAN RIG	344	ENAGAS	376	ELECTROLUX 'B'
281	APERAM	313	ORKLA	345	ENDESA	377	ENIRO
282	CORPORATE EXPRESS	314	PETROLEUM GEO SERVICES	346	FERROVIAL	378	ERICSSON 'B'
283	DSM KONINKLIJKE	315	PROSAFE	347	FOMENTO CONSTR.Y CNTR.	379	HENNES & MAURITZ 'B'
284	BAM GROEP KON.	316	REC SILICON	348	GAMESA CORPN.TEGC.	380	GETINGE
285	GETRONICS	317	SEADRILL	349	GAS NATURAL SDG	381	LUNDIN PETROLEUM
286	HAGEMEYER	318	STATOIL	350	IBERDROLA	382	HOLMEN 'B'
287	HEINEKEN	319	SUBSEA 7	351	IBERIA	383	SKF 'B'

Appendix one continued							
384	NOKIA (OME)	415	BHP BILLITON	448	RANDGOLD RESOURCES	481	TESCO
385	SCANIA 'B'	416	AGGREKO	449	MELROSE INDUSTRIES	482	UNITED UTILITIES GROUP
386	MODERN TIMES GP.MTG 'B'	417	AMEC	450	PERSIMMON	483	BT GROUP
387	SANDVIK	418	INTERTEK GROUP	451	INTL.CON.S.AIRL.GP.(CDI)	484	CRODA INTERNATIONAL
388	SSAB 'A'	419	ROYAL DUTCH SHELL A(LON)	452	BRITISH AMERICAN TOBACCO	485	KAZ MINERALS
389	SECURITAS 'B'	420	VODAFONE GROUP	453	BAE SYSTEMS	486	ACACIA MINING
390	SKANSKA 'B'	421	BP	454	ASSOCIATED BRIT.FOODS	487	AUTONOMY CORP
391	SWEDISH MATCH	422	GLAXOSMITHKLINE	455	ANTOFAGASTA	488	BRITISH AIRWAYS
392	TELE2 'B'	423	UNILEVER (UK)	456	ANGLO AMERICAN	489	CAIRN ENERGY
393	TELIASONERA	424	RIO TINTO	457	ARM HOLDINGS	490	COBHAM
394	VOLVO 'B'	425	ASTRAZENECA	458	BRITISH SKY BCAST.GROUP	491	EURASIAN NATRES.CORP
Switzerland		426	DIAGEO	459	CAPITA	492	CORUS GROUP
395	ABB LTD N	427	SABMILLER	460	CARNIVAL	493	DRAX GROUP
396	ADECCO 'R'	428	BG GROUP	461	CENTRICA	494	DIXONS RETAIL
397	ACTELION	429	RECKITT BENCKISER GROUP	462	COMPASS GROUP	495	ENTERPRISE INNS
398	CIBA N	430	IMI	463	CRH PLC	496	ALLIANCE BOOTS
399	CLARIANT	431	ICTL.HTLS.GP.	464	EXPERIAN	497	EVRAZ
400	LAFARGEHOLCIM	432	KINGFISHER	465	FRESNILLO	498	FIRST GROUP
401	LONZA GROUP	433	MEGGITT	466	IMPERIAL TOBACCO GP.	499	HANSON
402	MERCK SERONO 'B'	434	PETROFAC	467	ITV	500	HOME RETAIL GROUP
403	NESTLE 'R'	435	SHIRE	468	MARKS & SPENCER GROUP	501	INTERNATIONAL POWER
404	NOBEL BIOCare HOLDING	436	TULLOW OIL	469	MORRISON (WM) SPMKTS.	502	LONMIN
405	NOVARTIS 'R'	437	WEIR GROUP	470	NATIONAL GRID	503	INMARSAT
406	RICHEMONT N	438	WOLSELEY	471	NEXT	504	INVENSYS
407	ROCHE HOLDING	439	WHITBREAD	472	PEARSON	505	RENTOKIL INITIAL
408	SWISSCOM 'R'	440	SSE	473	REED ELSEVIER	506	POLYMETAL INTERNATIONAL
409	SGS 'N'	441	REXAM	474	ROLLS-ROYCE HOLDINGS	507	SCOTTISH & NEWCASTLE
410	SYNGENTA	442	BUNZL	475	SAGE GROUP	508	SERCO GROUP
411	SYNTHES	443	BURBERRY GROUP	476	SAINSBURY (J)	509	SCOTTISH POWER
412	TRANSOCEAN LTD	444	G4S	477	SEVERN TRENT	510	VEDANTA RESOURCES
413	GIVAUDAN 'N'	445	GKN	478	SMITH & NEPHEW	511	TAYLOR WIMPEY
414	GEBERIT 'R'	446	JOHNSON MATTHEY	479	SMITHS GROUP	512	THOMAS COOK GROUP
United Kingdom		447	BABCOCK INTL.	480	TATE & LYLE	513	TUI TRAVEL

Appendix one continued							
514	WPP	546	CONOCOPHILLIPS	579	PROCTER & GAMBLE	612	INTERNATIONAL PAPER
515	XSTRATA	547	COSTCO WHOLESALE	580	QUALCOMM	613	L BRANDS
516	HIBU	548	DEVON ENERGY	581	RAYTHEON 'B'	614	MEDIMMUNE
517	WOOD GROUP (JOHN)	549	DOW CHEMICAL	582	SCHLUMBERGER	615	NATIONAL SEMICON.
United States		550	E I DU PONT DE NEMOURS	583	SOUTHERN	616	ROCKWELL AUTOMATION
518	APPLE	551	EMC	584	STARBUCKS	617	HILLSHIRE BRANDS
519	WALGREEN	552	EMERSON ELECTRIC	585	TARGET	618	TYCO INTERNATIONAL
520	ANADARKO PETROLEUM	553	EXELON	586	TEXAS INSTS.	619	WILLIAMS
521	PEPSICO	554	FEDEX	587	TIME WARNER	620	XEROX
522	FORD MOTOR	555	FREEPORT-MCMOR.CPR.& GD.	588	TWENTY-FIRST CENTURY FOX CL.A	621	WYETH
523	EXXON MOBIL	556	GENERAL DYMICS	589	UNION PACIFIC	622	GOOGLE
524	MICROSOFT	557	GILEAD SCIENCES	590	UNITED PARCEL SER.'B'		
525	JOHNSON & JOHNSON	558	HALLIBURTON	591	UNITED TECHNOLOGIES		
526	GENERAL ELECTRIC	559	HEWLETT-PACKARD	592	UNITEDHEALTH GP.		
527	3M	560	HOME DEPOT	593	VERIZON COMMUNICATIONS		
528	AT&T	561	HONEYWELL INTL.	594	WAL MART STORES		
529	AMER.ELEC.PWR.	562	INTEL	595	WALT DISNEY		
530	ABBOTT LABORATORIES	563	INTERNATIONAL BUS.MCHS.	596	EBAY		
531	ALTRIA GROUP	564	ELI LILLY	597	BAKER HUGHES		
532	AMAZON.COM	565	LOCKHEED MARTIN	598	AES		
533	ACCENTURE CLASS A	566	LOWE'S COMPANIES	599	ALCOA		
534	AMGEN	567	MCDONALDS	600	ALLEGHENY TECHS.		
535	APACHE	568	MEDTRONIC	601	AVON PRODUCTS		
536	BAXTER INTL.	569	MERCK & CO.	602	ANHEUSER-BUSCH COS.		
537	BOEING	570	MONDELEZ INTERNATIO L CL.A	603	BLACK & DECKER		
538	BRISTOL MYERS SQUIBB	571	MONSANTO	604	BURL.NTHN.SANTA FE C		
539	CVS CAREMARK	572	NIKE 'B'	605	CAMPBELL SOUP		
540	CISCO SYSTEMS	573	NATIONAL OILWELL VARCO	606	CBS 'B'		
541	COLGATE-PALM.	574	NORFOLK SOUTHERN	607	CIGNA		
542	CATERPILLAR	575	OCCIDENTAL PTL.	608	COVIDIEN		
543	CHEVRON	576	ORACLE	609	DELL		
544	COCA COLA	577	PFIZER	610	COMPUTER SCIS.		
545	COMCAST 'A'	578	PHILIP MORRIS INTL.	611	ENTERGY		