

**Corporate Governance in Government-Linked Companies – Control Driven or
Performance Driven?**

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Abstract

We study the effect of the government transition on firm performance and board composition of government-linked companies (GLCs) and explore the motivations of board restructuring of GLCs. Specifically, we examine two questions: (1) what is the motivation of board restructuring, and (2) whether the change in the board composition affects the subsequent firm performance. The empirical results indicate that the policy factor is the key determinant in the board re-election of GLCs. The motivation of board restructuring after the powershift is mainly for control and spoils purposes rather than performance enhancement, which may explain why the market reacts negatively to the board restructuring announcement in GLCs. Finally, none of the board restructuring factors can explain the change in firm performance after the powershift, the only significant factor is the policy factor.

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Introduction

A plethora of studies have explored various aspects of corporate governance, such as ownership structure, board composition, and the dual leadership. Although much has been said about corporate governance, the results are not always consistent. We believe there is another important issue in corporate governance which has been relatively ignored in the literature, that is, the influence of politics on corporate governance. After the Asian financial crisis, much discussion has been raised about crony capitalism, where the economy is operated under an invisible spoil system in which the ruling power gives preferred treatment to friendly parties on a relationship base. The ruling party also depends on the spoil system to reward and strengthen its control muscle. As a result, a transition in the government, or powershift, would lead to a restructuring of the interwoven business-government network.

The question is: how would such powershift affect corporate governance and firm performance? Surprisingly little research can be found in this regard. Most literature concerning political influence is through the viewpoint of macroeconomics, exploring subjects such as the influence of congressional structure on macroeconomic policy and monetary performance (Grier, 1991) ¹. Others focus on the influence of macroeconomic factors on party policies (Lopez and Ramirez, 2000).

Agarawal and Knoeber (2001) is the pioneering study which takes the influence of political factors on corporate governance into consideration. They study the relationship between outside directors, politics and firm performance, and find that firm performance is negatively related with the degree of political involvement of the firm.

There are a few studies concerning the effect of *amakudari* (i.e., retired bureaucrats filling the board positions of private banks) on Japanese bank performance. Van Rixtel and Hassink (2002) find that distressed banks are more willing to employ retired bureaucrats from Ministry of Finance (MoF) and Bank of Japan (BoJ). Furthermore, the risky loan of the bank increases after ex-officials are recruited. Horiuchi and Shimizu (2001) have similar finding that risky investment increases if there are more ex-MoF officials in the bank.

There is reason to believe that political factor affects corporate governance, especially in government-linked companies. However, the related research is scant. How does the state shareholder act when it is the key minority or the major stockholder in the company? Would there be any private benefit in this case and what is the 'private benefit' of the state stockholder, if any? What are the motives of a state stockholder? Although the U.S. and some European countries have experienced many government

powershifts, there was no study exploring the motivation of the state stockholder or changes in corporate governance of state-linked firms. We attempt to fill this gap and investigate the motivation of board restructuring in GLCs using the government transition event in Taiwan.

Taiwan experienced its first powershift in March 2000, ending the KMT's position as the ruling party for over half a century, and with it the spoil system has reshuffled. This provides us a good opportunity to evaluate the effect of political intervention on GLC's corporate governance. Specifically, we want to find out (1) whether the board composition changes after the powershift, (2) what is the motivation of the board restructuring, (3) what determines the extent of state involvement, and (4) whether the change in board composition affects firm performance. To the best of our knowledge, this is the first study to explore the impact of powershift on corporate governance².

Based on a sample of 73 Taiwanese GLCs, we investigate the relationship between the change in board structure, firm performance and political-related factors. The empirical results show a strong relationship between policy control consideration and the extent of board restructuring. That is, the percentage change in board members is significantly higher for firms that are highly regulated, instrumental to policy implementation or having more resource. There is evidence that the motivation behind the restructure is

control-driven rather than performance-driven, and the negative market reaction after the board restructuring supports this view. Finally, we find that none of the board restructuring variables has any impact on the post-election firm performance. The only significant factor that explains firm performance change is whether the firm is policy-sensitive.

Background on Taiwan's GLCs

In March, 2000, the DPP party won the presidential election and ended the KMT's position as the ruling party in Taiwan for the first time. Shifting with it was the old business-government relationship. It is not unusual to observe a reshuffle of administrative positions in any country after a transition in the government, however, it is not so common to observe board restructuring in private sector after a powershift. About one third of the board members of listed government-linked companies³ were changed within the first year after the Taiwanese government transition, 40% changed the chairman of the board, and 33% changed their CEOs. New CEOs or chairmen of these GLCs were often DPP members or known to have the good relationship with the new DPP administration.

What and how are the changes in GLCs after the powershift? Table 1 gives us a quick

overview of the statistics in firm performance, board structure and board ownership of the GLCs. The statistics are shown separately for policy-sensitive firms and non-policy-sensitive firms. Policy sensitive firms refer to the firms in industries that are highly regulated and instrumental to policy implementation in Taiwan. These industries include banking, transportation, energy and telecommunication industry. The reason for distinguishing our sample into policy-sensitive and non-policy sensitive firms is that since we are interested in the motivation of state stockholder in GLCs, and since the influence of government public policies (e.g., monetary policy, energy policy or communication policy) are more dominant in these highly regulated industries, it is natural to separate these from the other GLCs. We do not include non-GLCs in our sample since our focus is on the motivation of the state stockholder and not private stockholders.

There are 30 policy-sensitive GLCs and 43 non-policy-sensitive GLCs in our sample. As electronic firms encountered a drastic market downturn after 1999, we list the statistics for all samples, without electronic, and electronic only, in the non-policy-sensitive group. From Table 1 we can see that average firm performance of both policy-sensitive and non-policy-sensitive GLCs declined after the powershift. The average turnover of chairman of the board and CEO after powershift is 70% and 40%, respectively, for policy-sensitive GLCs, which is much higher than those for

non-policy-sensitive GLCs.

Motivations of Post-Powershift Board Restructuring

Upon the powershift, the ruling party gains the right to replace the CEO or previous state representatives on the board of GLCs, similar to management turnover in hostile takeovers. It is natural for any company to change directors, the chairman and the CEO at a three or four years interval. However, in crony capitalism (Raghuram and Zingales, 1998), after powershift board restructuring (e.g., changing state representative) may occur before the normal term is due. The question is why the government replaces some directors in a specific GLC instead of other GLCs. What is the motivation for board restructuring or management turnover in GLCs? Past research found that management turnover is higher if there is a large investor on the board (Brunello et al., 2003). Does the state, being a large or key minority shareholder, govern the GLCs the same way as a large private shareholder does in non-GLCs? Does the state shareholder, like a large private shareholder, have other motivations than performance enhancement? We establish three alternative hypotheses for the motivations of board restructuring in GLCs, as explained in the following.

Policy/resource control hypothesis

It is well understood that a large shareholder may use its control right to maximize its own welfare. When the large shareholder (or large minority shareholder) is the state, what would be the meaning of ‘personal welfare’ or ‘private benefit’? From the ruling party’s point of view, the power to control the firm’s decisions is an obvious benefit. In this way, the government can accomplish specific public policies (e.g., financial reform in banking sector) and paves the road to win the next election. This is especially true in policy-sensitive industries. In order to strengthen its policy implementation muscle, state representatives must be replaced after the powershift.

Another control-motivated purpose is resource related. Studies on corporate control tell us that firms with more liquid assets are more likely to be takeover targets, other things being equal. Similarly, we posit that GLCs with higher liquid assets are more likely to be ‘taken over’ by the new government and encountered a higher turnover in management after the powershift. Since control is the main purpose, firm performance is not necessarily related with the management turnover in this case.

The empirical implication of this hypothesis is that policy-sensitive GLCs and GLCs with high liquid assets will experience a higher turnover of management and directors

after the powershift, regardless of previous firm performance.

Spoils allocation hypothesis

Ruling party depends on spoils system as one of its reward mechanism. In addition to policy implementation and resource capture discussed above, the “private benefit” for the ruling party may take the form of allocating top positions in GLCs, such as the chairman or CEO, to party members or friendly supporters after the powershift. Such spoils system may jeopardize the wealth of other investors, if profit maximization is not the main concern in the allocation process.

The empirical implication of the spoils allocation hypothesis is similar to that of the policy/resource control hypothesis. Firm performance is not necessarily the determinant for the management turnover and board restructuring. A well-performing CEO is likely to be replaced. No significant relationship is expected between the pre-powershift firm performance and the percent of the management turnover and board restructuring.

Performance enhancement hypothesis

If the motivation of board restructuring is to enhance firm performance rather than obtain private benefits, firm performance before the powershift would be a major determinant for board restructuring.

The empirical implications under performance enhancement hypothesis are contrary to the previous two hypotheses. In order to improve poor firm performance, the board will be restructured to have more professional members and better monitoring ability. Therefore, we expect a significant negative relationship between pre-powershift firm performance and board restructuring. Moreover, leadership structure of the firm is more likely to be dual after the transition if the previous firm performance is poor⁴. In addition, unlike the policy/resource control hypothesis, the relationship between the extent of board restructuring and the policy-sensitivity of the firms should not be significant.

Data and Methodology

There are 90 government-linked companies listed in Taiwan Stock Exchange (TSE) and Gre Tai Securities Market. The financial data and market data of these firms are mainly

collected from monthly and quarterly financial statements and the Taiwan Economic Journal (TEJ). In addition, the prospectus of each sample firm is examined for details of the personal data of board members, e.g., the educational levels and backgrounds, working experiences, and party memberships. A number of firms were deleted because the prospectus was not available. This reduces our samples to 73 firms.

The study period covers from Jan 1996 to Dec 2001. In the analysis followed, pre-powershift refers to the period from Jan 1996 to Dec 2000, and post-powershift refers to the period from May 2000 to Dec 2001. The period crosses the inauguration of the new president in May 2000.

Definition of variables

We are mainly concerned with the relationships among four types of variables: the performance variables, the resource variable, the board restructuring variables, and the policy variable. These variables are described in the following.

To measure firm performance, we use Tobin Q (TOBINQ), which is computed as the sum of the market value of common equity plus the book value of preferred and debt, and then divided by the book value of total assets. The liquid asset of each firm

(LIQUID) is used as a proxy for resource available. The liquid asset is collected from the balance sheet of the sample companies. It includes cash, cash equivalent, short term investment, accounts receivables, inventory, and prepaid expenses. In order to test the hypotheses, TOBINQ and LIQUID are the average value from Jan. 1996 to Dec. 1999.

Regarding board restructuring, we analyze the extent of board restructuring from three aspects - the board turnover percentage after the powershift (CHANGE); whether the chairman of the board is replaced (CHAIRMAN, a dummy variable), and whether the CEO is replaced after the powershift (CEO, a dummy variable).

In addition, we also measure the caliber of the new board members (KNOW). The caliber of the board is measured by examining the professional experience and the educational background of each director. If his or her experience and education are relevant to the operation of the company, KNOW is equal to 1, otherwise is 0. Finally, we compute the ratio of directors with related professional experience on the board for each firm.

It is worth noting that changes in the board of directors could take place simply because their terms were due and had little to do with the powershift. In order to distinguish

these regular changes from the board restructuring due to the powershift, the average turnover of board members in the previous four years before the powershift, PCHANGE, is computed to control for the turnover due to routine elections.

Dummy variable (POLICY) is used to distinguish between policy-sensitive firms and non-policy-sensitive firms. POLICY is equal to one if the firm belongs to highly regulated and policy sensitive industries such as banking, energy, transportation and telecommunication industries.

In addition to board restructuring variables, other ownership structure, board composition and industry variables are included in this research to be control variables. We include institutional ownership (INST), blockholder ownership (BLOCK)⁵, and board ownership (BDOWN) to control ownership structure. The percentage of inside directors (INSIDE) and the leadership structure of the company, i.e., whether the chairman of board and the CEO are the same person (DUAL) are also included to control board composition. When the chairman of board and the CEO are the same person, the dummy variable, DUAL equals to one, otherwise equals to zero. The ratio of industry Tobin Q (IND_Q) is also included.

The Empirical Results

How does market react to board turnover after powershift?

We compute the cumulative abnormal return of GLCs around the announcement day of the board restructuring ⁶, both with and without industry return adjustment. For comparison purpose, the GLCs in the same industry that did not encounter board restructuring during the study period are used as the control sample. We use the announcement day of the restructured firm as the event day of the firm in the control sample. As short-term trading is predominant in the Taiwanese stock market, we use a short event window from -2 to +60 days.

Figure 1 depicts the CAR of non-policy-sensitive GLCs in the (-2, +60) window around the board election announcement after the powershift. Figure 2 shows the CAR for the policy-sensitive GLCs. It is clear that the market reacts negatively to the board restructuring announcement in both groups, and the negative response is even more prominent after adjusting for industry returns. The market's negative response to the policy-sensitive firms seems to have been a little overreacting in the first month, suggesting investors are more sensitive to changes in these firms. The CAR results indicate that the market does not welcome the turnover in the board and top

management in the first election after the powershift.

Figure 3 shows the CAR for the control group that does not have board elections. It is surprising to see that the industry-adjusted CAR for the control group is also negative, even though these GLCs did not have board elections during the period. This result implies a spill-over effect on stock prices from the restructured GLCs to the other GLCs in the same industry. The market seems to anticipate similar restructuring in the control sample, which leads to a drop of the stock price in these firms.

What is the motivation of board restructuring after powershift?

In order to test the alternative hypotheses on the motivation for board restructuring after the powershift, we run several regressions for various board restructuring variables. The three dependent variables are the percentage turnover of the board members (CHANGE), the turnover of the chairman of the board (CHAIRMAN), and the turnover of CEO after the powershift (CEO). The explanatory variables are POLICY, TOBINQ, and LIQUID.

Table 2 summarizes the test results on the motivations of board turnover (CHANGE), chairman turnover (CHAIRMAN) and CEO turnover (CEO). POLICY has a significant

positive relationship with CHANGE and CHAIRMAN, while TOBINQ and LIQUID are both insignificant in explaining the turnover. That is, the turnover of top management has little to do with the performance of the GLCs. The result is consistent with the policy control hypothesis and/or the spoils allocation hypothesis but not the performance enhancement hypothesis ⁷. The significant positive relationship indicates that policy-sensitive GLCs have higher turnovers in both the board and the chairman of the board. It is worth noting that whether or not the firm is policy-sensitive does not affect the turnover of the CEO. The main determining factor for the replacement of the CEO is whether the chairman is replaced.

Furthermore, the board and management turnover may be affected by other factors such as board composition and ownership structure. (Shleifer and Vishny, 1997; Weisbach, 1988; Coles 2002; Kaplan and Minton, 1994) These variables are added in the regressions in Table 3 to Table 5. In order to control for the turnover due to routine elections, the average turnover of board members in the four years before the powershift, PCHANGE, is included in the extended regression. Finally, the firm size and the industry Tobin Q (IND_Q) are also included as control variables.

Table 3 to Table 5 show the regression results on CHANGE, CHAIRMAN and CEO, respectively, with the above factors included ⁸. The results in Table 3 and Table 4

confirm what we find in Table 2, that is, taking other factors into consideration, POLICY is still the single most significant factor in explaining the turnover of the board members as well as the turnover of the chairman.

From Table 2 we know that the CEO turnover depends on whether the chairman of the board is replaced. However, CHAIRMAN and POLICY are significantly related (see Table 2, and Table 4), there is multicollinearity problem if both variables are included in the regression. Since both variables are important for our analysis, we compute the residual of CHAIRMAN, RCHAIR, by regressing CHAIRMAN on POLICY, and use RCHAIR in the regression for CEO turnover. The result in Table 5 shows that the only significant factor that explains the turnover of the chief executive officer is still the turnover of the chairman, when other variables are included.

Does the change in the board composition affect the subsequent firm performance?

To test the various motivation hypotheses regarding the relation between performance and turnover, we measure the change in firm performance by calculating the change ratio of TOBINQ from Dec. 1997 to Dec. 2001 and examine its relation with the policy control variable(POLICY), board turnover(CHANGE), changes in the professional caliber of the board (KNOW) and board ownership.

Table 6 gives the regression result on the factors explaining the firm performance change after board restructuring. The variables are as defined in section 4.1, and Δ indicates changes before and after board restructuring. Note that as board turnover (CHANGE) is significantly correlated with POLICY, we regress CHANGE on POLICY and use the residual of CHANGE, RCHANGE, in Table 6 and 7 to avoid multicollinearity. Taking all into consideration, the only significant factors in explaining the performance change after the powershift are POLICY and Δ IND_Q, both are significantly positive. Neither the board turnover nor the change in the professional caliber affects the performance change⁹. It is easy to understand why performance change is positively related to industry performance, however, it is puzzling that performance change is positively related with policy-sensitive GLCs.

A closer examination of Table 1 suggests that the drastic downturn in the non-policy-sensitive electronic industry after the powershift might have contributed to the significant positive sign for policy sensitive firms (POLICY)¹⁰. Therefore, we run the regression again without the electronic firms. The result is shown in Table 7. The significance of POLICY still holds. To sum up, the performance regression results tell us that firm performance has little to do with board restructuring after powershift. Combing the facts that policy-sensitive GLCs have higher board turnover and better

performance change, and that higher board turnover in general does not lead to better performance change, our findings suggest that the relative importance of policy-sensitive GLCs to the administration's policy control and implementation may cause the new government to exert extra effort in the board restructuring in these firms.

Conclusions

The relationship between political involvement and corporate governance is an important but little studied issue. Being a large minority shareholder, the state has both control right and cash flow right. But this minority state shareholder may enjoy more control rights than its cash flow rights, especially in policy-sensitive firms. The 'private benefits' of state shareholders may appear in the form of spoils allocation and policy control right, which may be detrimental to the value of the firm.

On the other hand, the state representatives on the board may enhance the monitoring ability and thereby improve firm performance. By examining the board restructuring cases of Taiwanese GLCs after the transition of the government, we find that the motivation of the board restructuring in GLCs is consistent with the policy control or the spoils allocation hypothesis, rather than the performance enhancement hypothesis. That is, policy-sensitive GLCs are more likely to restructure the board after the

powershift. However, firm performance is not relevant to board restructuring. This result implies that the government may use these state representatives to control resources, instead of improving firm performance of GLCs. The findings of this study shed light on how political restructure affects corporate governance and performance.

Moreover, this research also examine whether the professional ability of directors improve firm performance in Taiwanese GLCs. Unfortunately, this variable is not significant in our empirical analysis. This result implies that professional ability of directors is not the panacea for improving firm performance.

Figure 1

The CAR of non-policy-sensitive GLCs in the (-2,+60) window around the board restructure after the powershift.

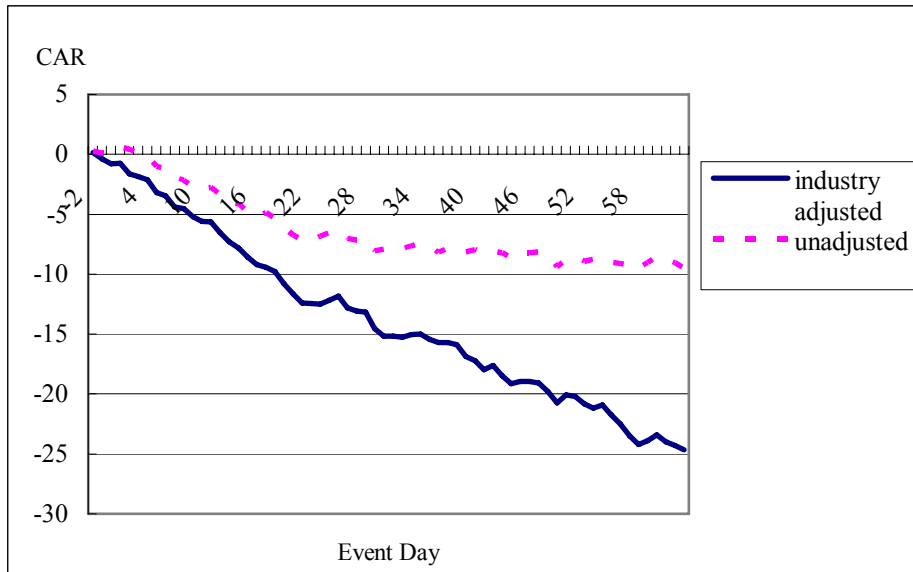


Figure 2

The CAR of policy-sensitive GLCs in the (-2,+60) window around the board restructure after the powershift.

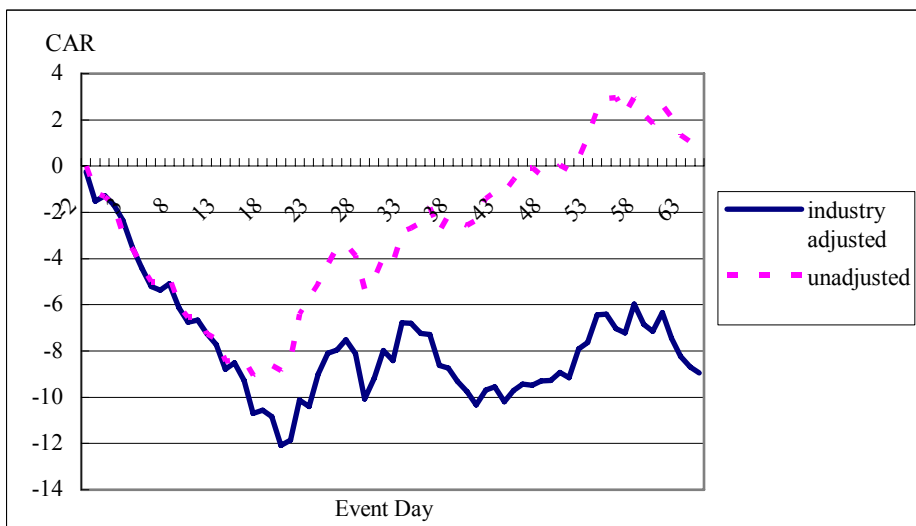


Figure 3

The CAR of GLCs that did not experience board restructure around the the same period.

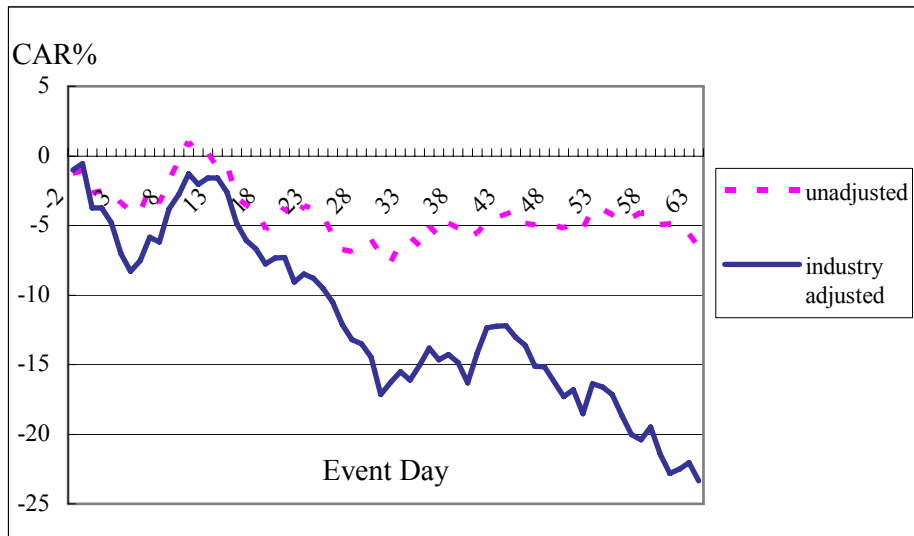


Table 1 Summary Statistics of GLCs

	<u>before powershift</u>	<u>after powershift</u>	<u>percent change%</u>
Policy sensitive firms			
Performance average			
Tobin Q	0.64	0.41	-39.03
EPS	0.23	1.15	40.59
Stock return (%)	-18.58	-40.35	-161.66
Percentage of change			
Board members (%)	23.41	49.33	147.43
Chairman (%)			70.00
CEO (%)			40.00
Blockholder ownership ¹ (%)	2.25	1.99	-10.33
Board ownership (%)	39.27	41.90	7.12
Government ownership (%)	22.89	22.13	-0.08
Inside director (%)	12.06	10.34	15.77
Board size	16.45	15.58	-6.14
Non policy sensitive firms			
Performance average			
Tobin Q	1.80 ²	0.55	-60.36
	(1.10 ³ , 3.55 ⁴)	(0.99, 0.40)	(-28.70, -132.67)
EPS	1.36	0.25	-90.64
	(1.00, 2.98)	(0.44, 0.20)	(-80.76, -99.78)
Stock return (%)	14.43	-70.90	-433.45
	(10.44, 50.91)	(-69.99, -273.71)	(-293.57, -690.49)
Percentage of turnover			
Board members (%)	17.02	47.74	70.26
	(17.36, 19.81)	(48.56, 30.03)	(52.03, 44.06)
Chairman (%)			18.60
			(19.92, 11.29)
CEO (%)			27.91
			(17.57, 35.98)
Blockholder ownership ⁵ (%)	3.64	3.59	-0.53
	(3.91, 3.63)	(4.51, 3.41)	(7.53, -16.13)
Board ownership (%)	35.54	30.93	-12.22
	(50.68, 31.97)	(43.82, 30.77)	(-12.84, -11.99)
State ownership (%)	3.65	4.11	33.76
	(4.73, 1.01)	(5.88, 1.35)	(43.87, 21.64)
Inside director (%)	10.53	11.93	31.18
	(13.37, 9.99)	(15.62, 10.89)	(41.22, 19.78)
Board size	13.33	12.76	-0.79
	(16.57, 12.48)	(15.77, 11.02)	(-0.61, -0.99)

-
1. If we delete firms with zero blockholder ownership, the average blockholder ownership before (after) the powershift is 14.77% (41.06%).
 2. total non -policy sensitive firms, 3. without electronic industry, 4. electronic industry.
 5. If we delete firms with zero blockholder ownership, the average blockholder ownership before (after) the powershift is 16.10% (13.74%).

Table 2 Regression results of the motivation for turnovers

$$CHANGE_{i,t1,t2} = a_0 + a_1POLICY_{i,t1} + a_2TOBINQ_{i,t1} + a_3LIQUID_{i,t1} + \varepsilon$$

$$Logit(CHAIRMAN_{i,t1,t2}) = a_0 + a_1POLICY_{i,t1} + a_2TOBINQ_{i,t1} + a_3LIQUID_{i,t1} + \varepsilon$$

$$Logit(CEO_{i,t1,t2}) = a_0 + a_1POLICY_{i,t1} + a_2TOBINQ_{i,t1} + a_3LIQUID_{i,t1} + a_4CHAIRMAN_{i,t1,t2} + \varepsilon$$

CHANGE: the percentage turnover of board members at the first board election after powershift.

*CHAIRMAN*_{*i,t1,t2*} : equals to 1 where chairman is replaced after the powershift and 0 otherwise. *CEO*_{*i,t1,t2*} : equals to 1 where CEO is replaced after the powershift and 0 otherwise; *POLICY*: equals to 1 if the firm is policy-sensitive (i.e., banking, transportation, telecommunication and energy industry) and 0 otherwise; *TOBINQ*: sum of market value of common stocks, the book value of debt and preferred stocks, divided by book value of assets. The value here is the average value from Jan. 1996 to Dec. 1999. *LIQUID*: the average liquid assets value of the firm before powershift value from Jan. 1996 to Dec. 1999. Before powershift refers to the period Jan 1996 to Dec 1999.

Varibales	constant	TOBINQ	LIQUID	POLICY	CHAIRMAN
CHANGE	-0.0015 (0.99)	-0.0006 (0.97)	0.0000 (0.15)	0.2275 (0.00)***	
CHAIRMAN	-2.5038 (0.02)**	-0.4663 (0.20)	0.0000 (0.28)	1.6157 (0.01)**	
CEO	-1.7559 (0.04)**	-0.1084 (0.58)	1.0693 (0.49)	-0.3330 (0.63)	0.0000 (0.09)*

p<0.1, ** p<0.05, *** p<0.001

Table 3 Regression result on board turnover (CHANGE)

The dependent variable is CHANGE. CHANGE: the percentage change of board members in the first election after the power shift. The independent variables are: *POLICY*: equals to 1 if the firm is policy-sensitive (i.e., banking, transportation, telecommunication and energy industry) and 0 otherwise. *TOBINQ*: sum of market value of common stocks, the book value of debt and preferred stocks, divided by book value of assets. The value here is the average value from Jan. 1996 to Dec. 1999. *INST*: the average percentage of institutional ownership before powershift. *BLOCK*: the average percentage of blockholder ownership before powershift. *BDOWN*: the average percentage of board ownership before powershift. *INSIDE*: the average percentage of inside directors before powershift. *IND_Q*: the average industry Tobin Q before powershift. *FIRMSIZE*: natural log of the sum of market value of common equity plus book value of debt and preferred stocks before powershift. *PCHANGE*: the average turnover of board members in the previous four years before the powershift. Before powershift refers to the period Jan. 1996 to Dec. 1999.

	beta	t-value	significance	multicollinearity tolerance	VIF
constant	-0.09	-0.26	0.80		
POLICY	0.28	5.27	0.00***	0.79	1.27
TOBINQ	0.00	-0.22	0.83	0.82	1.22
INST	0.15	1.27	0.21	0.81	1.23
BLOCK	0.27	0.56	0.57	0.73	1.37
BDOWN	0.02	0.14	0.89	0.75	1.34
INSIDE	-0.13	-0.47	0.64	0.88	1.14
FIRMSIZE	0.01	1.02	0.31	0.78	1.28
IND_Q	0.05	0.66	0.51	0.85	1.18
PCHANGE	-0.25	-1.09	0.28	0.88	1.14

Adjusted R-square=0.29 * p<0.1, ** p<0.05, *** p<0.001

Table 4 Regression result on chairman turnover

The dependent variable is CHAIRMAN, CHAIRMAN: equals to 1 if the chairman of board is changed after powershift, and 0 otherwise. The independent variables include: POLICY: equals to 1 if the firm is policy-sensitive (i.e., banking, transportation, telecommunication and energy industry) and 0 otherwise. TOBINQ: sum of market value of common stocks, the book value of debt and preferred stocks, divided by book value of assets. The value is the average value from Jan. 1996 to Dec. 1999. INST: the average percentage of institutional ownership before powershift. BLOCK: the average percentage of blockholder ownership before powershift. BDOWN: the average percentage of board ownership before powershift. INSIDE: the average percentage of inside directors before powershift. IND_Q: the average industry Tobin Q before powershift. FIRMSIZE: natural log of the sum of market value of common equity plus book value of debt and preferred stocks before powershift. Before powershift refers to the period Jan. 1996 to Dec. 1999.

	beta	t-value	significance
constant	-0.10	-0.13	0.90
POLICY	0.49	4.36	0.00***
TOBINQ	-0.03	-1.16	0.25
INST	0.26	1.00	0.32
BLOCK	0.71	0.67	0.50
BDOWN	0.34	1.06	0.29
INSIDE	0.07	0.12	0.90
IND_Q	-0.06	-0.37	0.71
FIRMSIZE	0.00	0.10	0.92

Adjusted R-square=0.23 * p<0.1, ** p<0.05, *** p<0.001

Table 5 Regression result on CEO turnover

The dependent variable is CEO, CEO: equals to 1 if CEO is replaced after powershift, and 0 otherwise. The independent variables are: POLICY: equals to 1 if the firm is policy-sensitive (i.e., banking, transportation, telecommunication and energy industry) and 0 otherwise. TOBINQ: sum of market value of common stocks, the book value of debt and preferred stocks, divided by book value of assets. The value is the average value from Jan. 1996 to Dec. 1999. IND_Q: the average industry Tobin Q before powershift. INST: the average percentage of institutional ownership before powershift. BLOCK: the average percentage of blockholder ownership before powershift. BDOWN: the average percentage of board ownership before powershift. INSIDE: the average percentage of inside directors before powershift. FIRMSIZE: natural log of the sum of market value of common equity plus book value of debt and preferred stocks before powershift. RCHAIR: regressing CHAIRMAN on POLICY, and use the residual to be RCHAIR in this regression. Before powershift refers to the period Jan. 1996 to Dec. 1999.

	beta	t-value	significance	multicollinearity	
				tolerance	VIF
constant	-0.86	-1.02	0.31		
POLICY	0.07	0.59	0.56	0.83	1.21
TOBINQ	-0.03	-0.98	0.33	0.80	1.24
INST	0.19	0.65	0.52	0.81	1.24
BLOCK	-0.16	-0.14	0.89	0.73	1.38
BDOWN	-0.03	-0.09	0.93	0.74	1.36
INSIDE	-0.06	-0.10	0.92	0.88	1.13
IND_Q	-0.02	-0.13	0.89	0.88	1.14
FIRMSIZE	0.05	1.44	0.15	0.78	1.28
RCHAIR	0.10	1.78	0.08*	0.94	1.07

Adjusted R-square=0.004

* p<0.1, ** p<0.05, *** p<0.001

Table 6 Regression result on performance change: all samples

The independent variable is $\Delta TOBINQ_{i,t1,t2}$: the percentage change in Tobin Q before and after powershift. Before powershift refers to the period from Jan. 1996 to Dec. 1999 and after powershift is the period from May 2000 to Dec. 2001. The independent variables are: POLICY: equals to 1 if the firm is policy-sensitive (i.e., banking, transportation, telecommunication and energy industry) and 0 otherwise. $\Delta KNOW_{i,t1,t2}$: the percentage change in the caliber of board of directors. $KNOW$ equals to 1 if the member is judged to possess relevant professional knowledge and 0 otherwise. The sum of $KNOW$ divided by the number of directors gives the percentage of professional directors on the board. Compute the change in this percentage before and after powershift gives $\Delta KNOW_{i,t1,t2}$. $\Delta DUAL_{i,t1,t2}$: equals to 1 if the leadership structure is improved after powershift (i.e., from single leader to dual leadership), and 0 otherwise. $\Delta INST_{i,t1,t2}$:the percentage change in institutional ownership before and after powershift. $\Delta BLOCK_{i,t1,t2}$: the percentage change in blockholder ownership before and after powershift. $\Delta BDOWN_{i,t1,t2}$: the percentage change in board ownership before and after powershift. $\Delta INSIDE_{i,t1,t2}$: the percentage change in the proportion of inside directors before and after powershift. $\Delta IND_Q_{t1,t2}$: the percentage change in industry TobinQ. RCHANGE: regressing CHANGE on POLICY and use the residual of CHANGE to be RCHANGE.

	beta	t-value	significance	multicollinearity	
				tolerance	VIF
constant	-0.52	-8.29	0.00***		
POLICY	0.24	3.62	0.00***	0.89	1.12
$\Delta KNOW_{i,t1,t2}$	-0.06	-1.09	0.28	0.85	1.18
$\Delta DUAL_{i,t1,t2}$	-0.07	-0.53	0.60	0.89	1.13
$\Delta INST_{i,t1,t2}$	-0.03	-0.66	0.51	0.99	1.01
$\Delta BLOCK_{i,t1,t2}$	-0.01	-0.33	0.74	0.88	1.13
$\Delta BDOWN_{i,t1,t2}$	-0.10	-0.57	0.57	0.46	2.16
$\Delta INSIDE_{i,t1,t2}$	0.01	0.25	0.80	0.46	2.18
$\Delta IND_Q_{t1,t2}$	0.20	2.01	0.05**	0.81	1.23
RCHANGE	-0.01	-0.45	0.65	0.94	1.06

Adjusted-R=0.16 * p<0.1, ** p<0.05, *** p<0.001

Table 7 Regression result of performance change: without electronic firms

The dependent variable is $\Delta TOBINQ_{i,t1,t2}$: the percentage change in Tobin Q before and after powershift. Before powershift refers to the period from Jan. 1996 to Dec. 1999 and after powershift is the period from May 2000 to Dec. 2001. The independent variables are: POLICY: equals to 1 if the firm is policy-sensitive (i.e., banking, transportation, telecommunication and energy industry) and 0 otherwise. $\Delta KNOW_{i,t1,t2}$: the percentage change in the caliber of board of directors. $KNOW$ equals to 1 if the member is judged to possess relevant professional knowledge and 0 otherwise. The sum of $KNOW$ divided by the number of directors gives the percentage of professional directors on the board. Compute the change in this percentage before and after powershift gives $\Delta KNOW_{i,t1,t2}$. $\Delta DUAL_{i,t1,t2}$: equals to 1 if the leadership structure is improved after powershift (i.e., from single leader to dual leadership), and 0 otherwise. $\Delta INST_{i,t1,t2}$: the percentage change in institutional ownership before and after powershift. $\Delta BLOCK_{i,t1,t2}$: the percentage change in blockholder ownership before and after powershift. $\Delta BDOWN_{i,t1,t2}$: the percentage change in board ownership before and after powershift. $\Delta INSIDE_{i,t1,t2}$: the percentage change in the proportion of inside directors before and after powershift. $\Delta IND_Q_{t1,t2}$: the percentage change in industry TobinQ. RCHANGE: regressing CHANGE on POLICY and use the residual of CHANGE to be RCHANGE.

	beta	t-value	significance	multicollinearity	
				tolerance	VIF
constant	-0.48	-6.16	0.00***		
POLICY	0.19	2.22	0.03**	0.85	1.17
$\Delta KNOW_{i,t1,t2}$	-0.06	-0.92	0.36	0.78	1.29
$\Delta DUAL_{i,t1,t2}$	-0.11	-0.56	0.58	0.81	1.23
$\Delta INST_{i,t1,t2}$	-0.01	-0.17	0.87	0.92	1.08
$\Delta BLOCK_{i,t1,t2}$	0.00	0.01	0.99	0.89	1.12
$\Delta BDOWN_{i,t1,t2}$	-0.26	-1.14	0.26	0.39	2.58
$\Delta INSIDE_{i,t1,t2}$	-0.01	-0.36	0.72	0.39	2.57
$\Delta IND_Q_{t1,t2}$	0.14	1.27	0.21	0.80	1.25
RCHANGE	-0.03	-0.57	0.57	0.85	1.18

Adjusted-R= 0.05 * p<0.1, ** p<0.05, *** p<0.001

Note: 21 electronic firms are excluded in this regression.

Note

1. Other issues include the influence of ideology on legislator's voting behavior. For example, Kau and Rubin (1993), Poole and Rosenthal (1996) and Kalt and Zupan (1993) find similar evidence that legislators are ideologues rather than the agents of their constituents.

2. Studies on state-owned firms focus either on IPO returns (e.g., Ma and Tsai, 1998) or performance after listing (e.g., Megginson et al., 1994, Boardman and Vining, 1989, Kole and Mulherin, 1997, Sun et al., 2002); none has examined the impact of powershift on the corporate governance of GLCs.

3. This research focuses on government-linked companies (GLCs). GLCs are not necessarily state-owned firms, which require majority ownership. In this research, GLCs refer to those firms that have at least one state representative or representative from a state-linked bank on the board. There are 44 listed companies having one state representative on the board and 46 listed companies having at least one representative from a state-linked bank. In total, there are 90 GLCs listed in Taiwan however, only 73 firms have complete data for this study.

4. Though the empirical results of the impact of leadership structure on firm

performance are mixed, such as Fosberg and Nelson (1999), Baliga et al. (1996) and Brickley et al. (1997), it is generally believed that dual leadership is better in terms of corporate governance.

5. Blockholders are non-board member shareholders that own more than 10% shares.

6. We use risk-adjusted returns model in this event study. OLS is used to regress the return individual share on the market return.

$$R_{it} = \alpha_i + \beta_i R_{mt} + \varepsilon_{it}$$

R_{mt} : the market return in time t

R_{it} : the individual return of company i in time t

According to the estimated equation, we can obtain the difference between the real return and estimated return.

$$AR_{iE} = R_{iE} - (\hat{\alpha}_i + \hat{\beta}_i R_{mE})$$

CAR is calculated as follows:

$$CAR(\tau_1, \tau_2) = \sum_{E=\tau_1}^{\tau_2} AR_E = \frac{1}{N} \sum_{i=1}^N \sum_{E=\tau_1}^{\tau_2} (AR_{iE}) \quad [\tau_1, \tau_2] \subseteq [t_3, t_4]$$

7. We also try to include the variable, the ratio of state ownership (GOVOWN), in the regression. Since the positive relationship between POLICY and GOVOWN is very

significant, we regress GOVOWN on POLICY first and use the residuals to be the new independent variable. The empirical result is similar to Table 2.

8. LIQUID is omitted in these regressions due to multicollinearity with other variables.

9. We also use EPS and stock return as performance measures; the regression results are similar to the result of using TOBINQ.

10. The TobinQ ratio of electronic firms dropped by more than 132%.

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