THE EFFECTIVENESS OF CORPORATE GOVERNANCE CODE REVISIONS: THE INTERNATIONAL EVIDENCE

OOI CHAI AUN

UNIVERSITI SAINS MALAYSIA

2018

THE EFFECTIVENESS OF CORPORATE GOVERNANCE CODE REVISIONS: THE INTERNATIONAL EVIDENCE

by

OOI CHAI AUN

Thesis submitted in fulfillment of the requirements for the degree of Doctor of Philosophy

May 2018

ACKNOWLEDGEMENT

It is graceful to complete this dissertation on the support of many people. I would like to give the first thanks to my parents for giving me infinite physical and mental support in completing the thesis. I appreciate their tolerance with me, and the best environment that they give me so that I am able to pay full attention in my research.

Second, I would like to thank my supervisor Assoc. Prof. Dr. Hooy Chee Wooi in giving the best guidance on research. With his supervision as well as his experience that he is willing to share with me, I faced lesser obstacles in completing my thesis. I also want to thank Dr. Hooy for supporting me to attend several workshops and conferences that have given me valuables skills and experiences on research. Also, I want to extend my appreciation to co-supervisor Dr. Hadi Zulkafli for his valuable advice and support in research.

Finally, I would like to thank all my friends who accompany and support me in anything. Also, I would like to thank MyBrain-MyPhD scholarship in giving me a financial support in research. Last but not least, I would like to thank myself for whatever hard works have been paid in completing this dissertation.

TABLE OF CONTENTS

ACKNOWLEDGEMENT ………………………………………………………… ii

TABLE OF CONTENTS……………………………………………………….. iii

LIST OF TABLES ………………...…………………………….………… vii

LIST OF FIGURES ……………………….…………………….…………… ix

LIST OF ABBREVIATIONS …..………………………………………………… x

LIST OF TERMINOLOGIES ……………………………………………….... xi

ABSTRAK ……………………………………………………………………… xii

ABSTRACT ……………………………………………………………………..xiv

CHAPTER 1 INTRODUCTION

1.1 Background of the Study 1

1.2 Motivation of the Study 3

1.3 Problem Statement 12

1.4 Research Questions 17

1.5 Objectives 18

1.6 Significance of the Study 18

1.7 Contribution of the Study 23

1.8 Chapter Summary 25

CHAPTER 2 CORPORATE GOVERNANCE CODE DEVELOPMENT

2.1 The Development of Corporate Governance 28

2.2 The Development of National Codes of Corporate Governance 33

2.3 The Corporate Governance Code Revisions 45

2.4 Chapter Summary 50

CHAPTER 3 LITERATURE REVIEW

3.1 The Relationship between Corporate Governance and Firm Value 52

3.2 The Studies of Corporate Governance: Single Aspect Study versus Holistic Aspects Study 53

3.3 The Matters of Compliance with the Codes of Corporate Governance 55

3.4 Theories 59

3.4.1 Agency Theory versus Institutional Theory 59

3.5 The Studies on Corporate Governance Index 64
3.6 The Relationship between Corporate Governance Index and Firm Value 66
3.7 The Relationship between Compliance with the National Code of Corporate Governance and Firm Value 68
3.8 The Number of New Practices Released in Each Corporate Governance Code Revision 76
3.9 The Influences of Corporate Governance Code Revisions to the Relationship between Corporate Governance Sub-score and Firm Value 80
3.9.1 The Influences of Corporate Governance Code Revisions towards the Board Structure and Board Function 81
3.9.2 The Influences of the Corporate Governance Code Revisions towards the Shareholder Rights Protection 86
3.9.3 The Influences of Corporate Governance Code Revisions towards the Remuneration and Compensation Policy 91
3.10 The Other Variables that Influence the Effectiveness of Corporate Governance Code Revisions 96
3.11 Chapter Summary 97
3.12 Summary of Hypotheses 101

CHAPTER 4 DATA AND METHODOLOGY
4.1 Data 102
4.2 Measuring the Number of New Governance Practices Released in Corporate Governance Code Revisions 108
4.3 Regression Models 109
4.3.1 Baseline Model 109
4.3.2 Model Examining the Relationship between the Cumulative Number of Corporate Governance Code Revisions and Firm Value 110
4.3.3 Models Examining the Effect of Increasing the Number of New Governance Practices 112
4.3.4 Models Examining the Effect of Increasing Years of Compliance with the National Codes of Corporate Governance 114
4.3.5 Summary of the Function of the Main Models 114
4.4 Additional Tests 115
4.4.1 Decomposing Corporate Governance Score into Four Aspects of Governance Sub-score 115
4.4.2 Decomposing the Number of New Governance Practices into Four Aspect of Governance 116
4.5 Models for Sensitivity Tests 116
4.5.1 Controlling Corporate Governance Code Revision Regime Effect . 116

4.5.2 Controlling Country-Level Variables 117
4.5.3 Sample Selection Bias 119
4.5.4 Alternative Dependent Variable: Return on Equity 124
4.6 Robustness Tests 125
4.6.1 Examining the Effectiveness of Corporate Governance Code Revisions in the High and Low Corporate Governance Score Subsamples 125
4.6.2 Examining the Effectiveness of Corporate Governance Code Revisions in the High and Low Capital Market Pressure Subsamples 126
4.6.3 Subsample Analysis by Developed and Developing Economies 127
4.7 Panel Regression 127
4.8 Chapter Summary 130

CHAPTER 5 RESULTS AND DISCUSSION
5.1 Descriptive Statistics 132
5.1.1 Descriptive Statistics on Corporate Governance Code Revisions 132
5.1.2 Descriptive Statistics of the Control Variables 141
5.2 Regression Results of Baseline Model 147
5.3 The Moderating Effect of Corporate Governance Code Revisions to the Relationship between Corporate Governance Score and Firm Value 151
5.4 The Moderating Effect of Increasing Number of New Governance Practices 156
5.5 The Moderating Effect of Years of Compliance with the Codes of Corporate Governance 161
5.6 Sensitivity Analysis 165
5.6.1 Controlling Regime Effect of Corporate Governance Code Revisions 165
5.6.2 Incorporating Country-level Control Variables in Regressions 168
5.6.3 Tackling Sample Selection Bias 172
5.6.4 Alternative Dependent Variable: Return on Equity 174
5.7 Robustness Tests 177
5.7.1 The Influence of the High and Low Corporate Governance Score to the Effectiveness of Corporate Governance Code Revisions 177
5.7.2 The Influence of Capital Market Pressure to the Effectiveness of Corporate Governance Code Revisions 179
5.7.3 Additional Subsample Analysis by Developed and Developing Countries 182

5.8 Summary of Hypothesis Testing 188

CHAPTER 6 CONCLUSIONS
6.1 Introduction 190
6.2 Summary of the Findings 194
6.3 The Implications from Theoretical View 197
6.4 The Implications from Policy View 200
6.4 Limitation of the Study 202
6.5 Suggestions for the Future Studies 204

REFERENCES 206

APPENDICES

LIST OF TABLES

		Page
Table 2.1	The Attributes of Corporate Governance Covered in the Code of Corporate Governance	42
Table 2.2	The Total Number of Corporate Governance Codes Released by Individual Country and the Frequency of Code Revisions	49
Table 3.1	Previous Studies Investigating the Relationship between Corporate Governance Index and Firm Value	73
Table 4.1	Definitions of Variables	106
Table 4.2	Summary of the Function of Each Regression Models	115
Table 5.1	Descriptive Statistics of Corporate Governance Code Revisions	133
Table 5.2	Descriptive Statistics on the Cumulative Number of Corporate Governance Code Revisions and the Number of New Practices Released, by Countries	136
Table 5.3	Descriptive Statistics on the Number of Corporate Governance Code Revisions Occuring within Sample Period, by Countries	138
Table 5.4	The Number of New Practices on Four Aspects of Corporate Governance Practices Released in Each Corporate Governance Code Revision	139
Table 5.5	The Average Number of New Governance Practices Released in the Corporate Governance Code Revisions Occuring between 2007-2014	140
Table 5.6	Descriptive Statistics of Firms' Fundamental Variables	142
Table 5.7	Descriptive Statistics on Corporate Governance Variables	143
Table 5.8	Pearson Correlations	146
Table 5.9	Baseline Model Results	149
Table 5.10	Regression Results on the Relationship between Corporate Governance Score and Firm Value	151
Table 5.11	Regression Results on the Relationship between the Interaction Terms and Firm Value	153

Table 5.12	Regression Results on the Effects of Each Corporate Governance Code Revision towards the Relationship between Corporate Governance Score and Firm Value	155
Table 5.13	Regression Results on the Influence of the Number of New Practices Released towards the Effectiveness of Corporate Governance Code Revisions	159
Table 5.14	Regression Results Using Dummy Variable Representing the Number of New Practices Released towards the Effectiveness of Corporate Governance Code Revisions	160
Table 5.15	The Maximum Years of Compliance with the Codes of Corporate Governance by Firms in each Country	162
Table 5.16	Regression Results on the Relationship between the Number of New Practices Released and Firm Value, sub-sample by Years of Compliance	164
Table 5.17	Distribution of Corporate Governance Score across Years and Regimes of Corporate Governance Code Revisions	166
Table 5.18	Regression Results by Controlling the Regimes of Corporate Governance Code Revisions	167
Table 5.19	Regression Results after Controlling the Country-Specific Variables	171
Table 5.20	Regression Results using Two-Stage Sample Selection Bias Approach	174
Table 5.21	Regression Results using Alternative Dependent Variable, ROE	176
Table 5.22	Regression Results on the Influence of the Number of New Governance Practices Released, subsample by Two Range of Corporate Governance Score	178
Table 5.23	Subsample Regressions based on the Capital Market Pressure	181
Table 5.24	Subsample Regressions with the Developed Countries	184
Table 5.25	Subsample Regressions with the Developing Countries	186
Table 5.26	Summary of Hypothesis Testing	189

LIST OF FIGURES

		Page
Figure 3.1	Research Framework	100
Figure 5.1	Boxplot showing the Data on the Cumulative Number of Corporate Governance Code Revisions	134
Figure 5.2	Boxplot Showing the Data on the Years of Compliance with the Revised Codes of Corporate Governance	134
Figure 5.3	Scatter Plot Showing the Cumulative Number of Corporate Governance Code Revisions against Years of Compliance	135

LIST OF ABBREVIATIONS

ASX	Australia Stock Exchange
CalPERS	California Public Employee's Retirement System
CEO	Chief executive director
CLSA	Credit Lyonnais Securities Asia
ECGI	European Corporate Governance Institute
ICGN	International Corporate Governance Network
IMR	Inverse Mill ratio
IRRC	Investor Responsibility Research Center
KCGI	Korean Corporate Governance Index
MCCG	Malaysian Code of Corporate Governance
NACD	National Association of Corporate Directors
OECD	Organisation for Economic Co-operation and Development
SOX	Sarbanes-Oxley Act

LIST OF TERMINOLOGIES

Terminology	**Descriptions**
Mandatory	Describes something which must be done, or which is demanded by law.
Code	A set of rules which are accepted as general principles, or a set of written rules which state how people in a particular organization or country should behave.
Norm	An accepted standard or a way of behaving or doing things that most people agree with.
Legitimate	To make something legal or acceptable

KEBERKESANAN ULANGKAJI KOD TADBIR URUS KORPORAT: BUKTI-BUKTI ANTARABANGSA

ABSTRAK

Dalam kesusasteraan, terdapat bukti-bukti terhad untuk menunjukkan keberkesanan ulangkaji kod tadbir urus korporat yang dilancarkan berterusan sejak awal. Dengan menggunakan data firma daripada 35 buah negara, kajian ini mendapati ulangkaji kod tadbir urus korporat yang berterusan mempengaruhi hubungan antara skor tadbir urus korporat and nilai firma dengan bersignifikan. Didapati kebanyakan negara yang terpilih dalam kajian ini telah menjalankan lebih daripada sekali ulangkaji kod tadbir urus disebabkan penggunaan data panel yang melingkungi tahun dari 2007 hingga 2014. Kajian ini menganalisasi ulangkaji kod tadbir urus korporat daripada tiga sudut pandangan, iaitu bilangan kumulasi ulangkaji kod tadbir urus, bilangan amalan baru yang diterbitkan pada ulangkaji tersebut, dan bilangan tahun untuk mematuhi amalan baru tersebut. Ujian tambahan dilakukan terhadap model regresi utama dengan membahagikan tadbir urus korporat kepada empat unsur, iaitu fungsi lembaga pengarah, struktur lembaga pengarah, polisi pampasan dan perlindungan hak pemegang saham. Ujian sensitif dijalankan dengan mengkaji kesan prestasi ekonomi negara, kualiti tadbir urus institusi, krisis kewangan 2008, bias pemilihan sampel, pengaruh regim ulangkaji kod tadbir urus, dan penggunaan pembolehubah bersandar alternatif terhadap keputusan utama yang didapati. Ujian keteguhan dijalankan dengan mengkaji kesan-kesan daripada tahap asal tadbir urus korporat dan tekanan pasaran modal terhadap keberkesanan ulangkaji kod tadbir urus. Lagi, keberkesanan ulangkaji kod tadbir urus di negara-negara telah membangun dan negara-negara sedang membangun dikaji secara berasingan. Keputusan utama kajian ini menunjukkan

bahawa bilangan kumulasi ulangkaji kod tadbir urus korporat memberi kesan positif yang signifikan terhadap hubungan antara skor tadbir urus korporat dan nilai firma. Peningkatan bilangan amalan baru tadbir urus korporat yang disebarkan daripada ulangkaji kod memberi kesan negatif yang signifikan kepada hubungan tersebut. Peninggian bilangan tahun untuk mematuhi amalan baru tadbir urus korporat merosotkan kesan negatif yang disebabkan oleh peningkatan bilangan amalam baru tadbir urus korporat. Keputusan ujian tambahan menunjukkan bahawa, kesan positif peningkatan kumulasi bilangan ulangkaji kod tadbir urus dipaparkan pada peningkatan skor fungsi lembaga pengarah, skor struktur lembaga pengarah, dan skor polisi pampasan. Kesan negatif peningkatan bilangan amalan baru tadbir urus korporat daripada ulangkaji kod dipaparkan pada amalan baru di bidang fungsi lembaga pengarah sahaja. Sebaliknya, peningkatan bilangan amalan baru di bidang struktur lembaga pengarah pada tahap sederhana memberi kesan positif yang signifikan kepada hubungan antara skor tadbir urus korporat dan nilai firma. Kesemua keputusan didapati tidak dipengaruhi oleh faktor-faktor yang dikaji di ujian sensitif. Keputusan daripada ujian keteguhan menunjukkan bahawa tahap asal tadbir urus korporat dan tekanan pasaran modal boleh menjejaskan penemuan utama kajian ini. Akhirnya, kajian ini mendapati penemuan utama kajian ini berdekatan dengan keputusan yang didapati dengan hanya menggunakan sampel daripada negara-negara telah membangun. Kesimpulannya, keputusan-keputusan kajian ini memberi implikasi dasar yang berguna kepada pembangunan kod tadbir urus korporat, dan juga menambahkan pandangan baru kepada teori-teori dalam kesusasteraan.

THE EFFECTIVENESS OF CORPORATE GOVERNANCE CODE REVISIONS: THE INTERNATIONAL EVIDENCE

ABSTRACT

The literature lacks empirical evidence to show the effectiveness of progressive revisions on the national codes of corporate governance. Using firm-level data from 35 countries, this study shows that progressive corporate governance code revisions have significantly moderated the relationship between corporate governance score and firm value. Majority of the countries selected in this study has at least more than one code revision covered as the use of a panel data covering the years from 2007 to 2014. In detail, this study assesses corporate governance code revisions from three perspectives, i.e. the cumulative number of corporate governance code revisions, the number of new governance practices released in each revision, and the years of compliance with the codes. Additional tests are conducted by running the main regression model on four sub-aspects of corporate governance, i.e. board function, board structure, compensation policy and shareholder rights protection. Sensitivity tests are conducted to examine if the effects of countries' economic performance, institutional governance quality, the 2008 financial crisis, sample selection bias, regime effect of corporate governance code revisions, and the alternative dependent variables are able to affect the main findings. Robustness tests regarding the influence of firms' internal corporate governance standard in existence and the influence of capital market pressure to the effectiveness of corporate governance code revisions have been conducted. Also, the effectiveness of corporate governance code revisions in developed and developing countries are examined. This study shows that the cumulative number of corporate governance code revisions has a significant positive

moderating effect to the relationship with corporate governance score and firm value. Instead, increasing the number of new governance practices released from corporate governance code revisions has a significant negative moderating effect to the relationship. The negative moderating effect is deteriorated following the increased years of compliance with the codes of corporate governance. The additional tests reveal that, the positive moderating effect brought by the cumulative number of corporate governance code revisions are driven by the improved board function score, board structure score, and compensation score. Meanwhile, the negative moderating effect brought by increasing the number of new governance practices is significantly driven by the increased new board function practices only. However, we find that, increasing the number of new board structure practices in a moderate level has a significant positive moderating effect to the relationship between corporate governance score and firm value. In sum, the findings are not influenced by all the other factors tested in the sensitivity tests. Robustness tests reveal that firms' internal corporate governance standard in existence, and the capital market pressure have affected the main results of this study. Lastly, this study finds that the main results obtained in this study are further corroborated only when using the sample from developed countries only. In summary, the findings of this study have provided the useful policy implications to the corporate governance code development, and have added new theoretical insights to the body of knowledge in the related literature.

CHAPTER 1

INTRODUCTION

1.1 Background of the Study

International non-regulatory organizations such as the Organisation for Economic Co-operation and Development (OECD), Pan-European, Commonwealth, and International Corporate Governance Network (ICGN) has shaped the world's corporate governance by providing governments and regulators around the world with effective policy instruments in evaluating and strengthening the legal, regulatory and institutional framework of corporate governance of individual countries (Cuomo, Mallin and Zattoni, 2016). One of the important contribution of these organisations to the world's corporate governance development is the release of the transnational codes and principles of corporate governance such as the *OECD Principles of Corporate Governance, the International Corporate Governance Network (ICGN) Statement of Global Corporate Governance Principles* which have provided important guidance to the development of the world's corporate governance.

The transnational codes and principles of corporate governance released provide a common corporate governance guidance to the publicly listed firms around the world. Gradually, as the compliance with the codes of corporate governance has become legitimized, the recommendations on corporate governance practices are more widely incorporated into the publicly listed firms around the world. However, due to the argument that the common corporate governance guidance provided by the transnational codes and principles of corporate governance is not a good fit to each country's local institutional and organisation norms, it has been further modified by the local policy makers. Thus, this has given rise to individual national codes of corporate governance. The code issuers of each country may be different, some may be the government, the stock exchange, or the professional associations. Nevertheless, all of the national codes share the similar objective, which is promoting good governance practices to the firms.

The *OECD Principles of Corporate Governance* acts as the popular common guidance to the world's corporations in corporate governance. The Principles bears the responsibility of being the main reference point in guiding the development of the world's corporate governance. In order to adapt to the changes in market structure, the dynamic market expectation on new governance practices, and the essence for keeping the corporations updated regarding the most appropriate practices of good governance, the Principles has been revised three times since the first issue in 1999. The latest revision of the Principles was conducted during the G20/OECD Corporate Governance Forum on 10th April 2015 at Istanbul, Turkey, and the finalized revision of Principles was then presented to the G20 Finance Ministers and Central Bank Governors in September 2015 during a meeting (OECD, 2015).

The revision of the transnational codes and principles of corporate governance may drive a major reform to the world's corporate governance. The policy makers of individual country too, need to stay connect with the new governance practices by revising their national codes of corporate governance. Besides conforming to the new transnational codes, revision of the national codes of corporate governance may sometimes need to be revised even more, if local authorities find that the existing corporate governance guidance is ineffective or inappropriate to the local firms. Usually, surveys, forums, as well as discussion with experts may be carried out in the process of revising the national codes of corporate governance.

The effectiveness of corporate governance code revisions in individual country depends on how well the code issuers adapt the common guidance to the local institutional and organization norms. Local firms that blindly follow the common guidance might not reap any benefit from the practices. Instead, this action may backfire because complying with the inappropriate governance practices increases the cost of compliance borne by the firms. Based on this argument, it is therefore worthwhile to research on the effectiveness of corporate governance code revisions.

1.2 Motivation of the Study

The literature has shown that there is a significant relationship between corporate governance and firm value. According to agency theory, improving the standard of corporate governance can reduce the cost of agency, which will then increase firm value. A national code of corporate governance acts as an important guide to the firms' corporate governance settings. In order to quickly advance the development of corporate governance, many regulatory and non-regulatory bodies such as the government, the stock exchange, and professional associations have taken the initiative to facilitate the development of the national code of corporate governance. These parties assist in many ways in revising the national code of corporate governance from time to time so that the firms are continuously updated with the best practices of governance. For example, in Malaysia, the Security Commission Malaysia released the first national code of corporate governance (namely the *Malaysia Code of Corporate Governance*) in 2000, and the Code has been revised twice in 2007 and 2012 respectively. In Germany, the Government Commission on the German Corporate Governance Code has revised and released the national code of corporate governance namely *German Corporate Governance Code* several times. In Hungary, the Budapest Stock Exchange has also revised and released the national code of corporate governance in the year 2007, 2008 and 2012 after the first issue of the code in the year 2002. There are also other codes of corporate governance that only target a specific group of players in the market. Such codes include the *Principles for Responsible Institutional Investors, or Japan's Stewardship Code* which was released by the Financial Services Agency, and the *Corporate Governance Code for Collective Investment Schemes and Management Companies* which was released by Irish Funds Industry Association. In sum, the intervention of both the governing and non-governing bodies have largely driven the reforms of corporate governance (Zalewska, 2014), through their roles in improving the corporate governance system (Kim and Lu, 2013).

Corporate governance code revisions are essential in order to update the firms regarding the best governance practices that are parallel with the changing market expectation. The changing market expectation on new corporate ethos may be due to the shift in financial market structure, such as the increased in blockholders and institutional investors (Schmeling, 2007). This group of investors have high financial literacy skills and their increasing presence may require better corporate governance standard. For example, in the *King II Report* released in 2002 in South Africa, it has documented that institutional investors require additional measurements to enable them to judge stewardship, performance, conformance, and sustainability on a common basis (King II Report, 2002). In addition, an increasing number of foreign investors due to the advance in financial technology development may place a greater pressure on policy makers with respect to upgrading the local firms' corporate governance so that it is comparable to the international requirements. Hence, corporate governance code revisions are essential so that the local firms can keep updated about the new practices of governance with accordance to the constant change in market expectations.

Corporate governance code revisions are prevalent in many countries. For example, in the United Kingdom, the first code of corporate governance, *The Cadbury Report* was released in 1992. *The Cadbury Code* was then replaced by a newer issue in year 2003, namely *The Combined Code*. It was then revised again in the year 2006, 2008 and 2009 respectively. In order to meet the changing environment due to the new Listing Regime, which was introduced in 2010, the U.K. Financial Reporting Council released a new code of corporate governance namely *The UK Corporate Governance Code* in the year 2010. It was then revised in 2012 and 2014. In Singapore, the Singapore Ministry of Finance has revised the *Code of Corporate Governance* in the year 2005, four years after the first issue; the Code was then revised again in the year 2012. In developing country such as Malaysia, the first release of *Malaysian Code on Corporate Governance* was in the year 2000; the Code was then revised in 2007 and 2012 respectively. In Thailand, the Stock Exchange of Thailand released the first code of corporate governance, namely *The SET Code of Best Practices for Directors of Listed Companies* in the year 1998, and made a series of revisions in the year 1999, 2002, 2006, and 2012 respectively.

The national code of corporate governance, for example, in Malaysia, has shown the evolution in the aim of corporate governance required by the changing market expectation through corporate governance code revisions. In the release of the revised code of corporate governance in the year 2012 (i.e. the MCCG 2012), the new recommendations in the revised code has informed the firms with regard to the creation of a corporate governance model that promotes sustainable growth, imitating the trend in the major markets (Elkington, 1998). Also, the MCCG 2012 recommends an additional responsibility of the board of directors regarding monitoring the adoption of sustainable strategic decision making in a firm. The example has shown that corporate governance code revisions are essential to promote the practices of governance which is parallel with the current market expectation.

Corporate governance code revisions also aim to increase the degree of acceptance by the majority of the firms. For example, in the U.S., the first release of the code of corporate governance namely *Cadbury Report* in 1992 recommends the U.S. firms to send shareholders a brief summary of points raised at the annual general meeting (Financial Reporting Council and London Stock Exchange, 1992, p48). However, the cost of such practice, either by a separate mailing or included in the next financial report circulated to shareholders, will be borne entirely by the firms. The cost is considered high especially for the minority shareholders. Hence, the appropriateness of the new practice to the U.S. firms has raised a doubt. In the revised code namely the *Hampel Report* released in 1998, the recommendation has been amended. The new recommendation in the *Hampel Report* suggests that the firms will sent the summary of points raised at the annual general meeting only when it is requested by the shareholders, as a matter of the best practice (Hampel Report, 1998). In general, corporate governance code revisions are desirable in order to correct the inappropriate recommendations on governance practices, while taking into account the changing legal institutional structure, as well as the new expectations from the shareholders and stakeholders on the role of corporate governance (Belgian Corporate Governance Committee, 2009).

In fact, the most fundamental aim of corporate governance code revisions is to reduce the agency cost and to increase the firm value for shareholders. In reviewing the code of corporate governance from France released in 2002, namely *Promoting Better Corporate Governance in Listed Companies*, the Code documents that the aim of the revision is not merely to improve moral imperative, but also serves as a key driver for economic growth, while considering for business competence and the performance of the financial market. Similarly, the largest American public pension fund called the California Public Employee's Retirement System (CalPERS), highlights that corporate governance is value relevant, but it does not aim to change the political or social environment (CalPERS, 1999). There are several supportive cases that can provide proofs regarding the importance of associating corporate governance code revisions to firm value. First, corporate scandals such as the case of Bernie Ebbers, the CEO of WorldCom, who allows a $11 billion accounting fraud to occur, results in the loss of $180 billion of shareholder value when the stock prices plummeted (BBCNews, 2005). Second, the case of Kenneth Lay and Jeffrey Skilling, the former CEOs of Enron, are both convicted of fraud and conspiracy that eventually led to the bankruptcy of Enron (The New York Times, 2006). Both cases have shown the close relationship between corporate governance and firm value. Therefore, in order to assess the effectiveness of corporate governance code revisions, firm value should be emphasized. Consistently, Aguilera and Cuervo-Cazurra (2009) highlight the need to investigate the impact of releasing new codes of corporate governance towards the economic value of the firms.

The previous studies also show evidence that every single aspect of corporate governance significantly affect firm value. For example, Yermack (1996), Black and Kim (2012), and Ooi, Hooy and Ahmad Puad (2015) show a significant link between the board structure and firm value; Nenova (2003) and Chi (2005) show a significant link between the shareholder rights and firm value; Mehran (1995) and Palia (2001) show a significant link between the compensation policy and firm performance as well as firm value. The link between corporate governance and firm value can be explained by agency theory in such a way that the cost of agency will be greatly reduced when corporate governance functions optimally in maximizing shareholder value as well as firm value. Therefore, the national codes of corporate governance have always provided recommendations on the best practices of governance from all possible aspects to the firms, including the practices on board structure and board function, remuneration or compensation, and the shareholder rights protection.

With the exception of the U.S., the majority of the national codes of corporate governance are not the hard laws, but they are rather the soft laws which allow for voluntarily compliance. In other words, the majority of the national codes of corporate governance are not mandated by laws. With non-mandatory codes of corporate governance, it has several advantages. First, the non-mandatory codes are flexible to amend. Second, the non-mandatory codes can be easily revised based on the market mechanism for evaluation in case of deviances without to have undergoing the complicated legal processes. Similarly, the *OECD Principles of Corporate Governance* emphasizes the importance of issuing a non-mandatory code of corporate governance with the aim to fill the weaknesses of the rigid corporate governance legal systems. The benefits of not mandating the codes of corporate governance have been highlighted in some national codes of corporate governance. For example, *The 2009*

Belgian Code on Corporate Governance released by Belgian Corporate Governance Committee highlights that the Code provides higher flexibility than hard law due to the continuous changes in business practices and the needs of corporate stakeholders. The Belgian Code even documents that policy makers can swiftly anticipate such changes and formulate recommendations for appropriate actions under non-mandatory implementation of the Code (Belgian Corporate Governance Committee, 2009).

The comply-or-explain and freedom with accountability principles form the foundations of non-mandatory compliance. It means that, the firms can choose to adopt the corporate governance practice recommendations that are suitable and appropriate for them only. However, even though the firms have the flexibility to comply with some recommendations but not all, but the firms also face pressure which is exerted by the investors upon requiring them to justify for the non-compliance. That is why the codes of corporate governance are considered as a soft law to the firms (Aguilera and Cuervo-Cazurra, 2004; 2009). The investors' pressure put on the firms is critical to ensure that the firms do not simply incorporating the recommendations in the codes for the sake of meeting the market expectation. Understanding that there is no such thing as a one-size-fit-all compliance, the recent issue of the *OECD Principles of Corporate Governance* emphasizes that the principle of voluntarily compliance is effective to improve the standard of corporate governance. On the other hand, a rigid corporate governance law will restrict the firms in adopting the best corporate governance structure innovatively when its governing structure is not suitable to fit to the new governance practices. In such case, firm value cannot be optimized because the firms are forced under the legal law to comply with the new practices which may not be suitable to their governance settings.

Under non-mandatory national codes of corporate governance, Goncharov et al. (2006) consistently show that investors in the market played an important disciplinary role in monitoring firms' compliance with the recommendations in the codes of corporate governance. Investors may penalize the firms for unreasonable non-compliance through lowering the valuation of the firms' stock prices. Therefore, it creates a capital market pressure for the firms to comply with the code of corporate governance. This may increase the competition between firms in advertising their compliance to the investors as a way to increase their stock valuation. As such, the investors should be intelligent in evaluating whether the firms have adopted the recommendations on corporate governance in a wise manner that can optimize the firms' corporate governance functioning.

Research regarding the issues of the codes of corporate governance is relatively new in the literature, but it is increasingly gaining the attention of scholars (Cuomo et al., 2016). The reason why the research on the codes of corporate governance is immature is because the interval between the release of the initial version of the national codes of corporate governance until the present day is relatively short. This is because dissemination of transnational codes of corporate governance to the world has only started to gain momentum after year 2004, which is the timeline after the dotcom bubble and various high profile corporate scandals like Enron, Worldcom and Parmalat. The turbulence in financial markets only triggers the introduction of national codes of corporate governance in many countries. Within a short interval of time since the first issue of the codes in the majority countries, corporate governance code revisions may have only happened two to three times. Hence, the data on corporate governance code revisions is not sufficient to initiate researches prior to this. However, Aguilera and Cuervo-Cazurra (2004) and a recent study by Cuomo et al. (2016) have suggested the potential area of study on the codes of corporate governance. The recent empirical study conducted by Fauver et al. (2017) on board reforms due to the corporate governance code revision may give an impetus to the future studies looking into this area of research.

Due to the lack of data on corporate governance code revisions in the earlier years, the majority of the previous studies tend to look into the effect from the release of a code of corporate governance to the firms, but those studies could not highlight the effect of continuously releasing several revised codes of corporate governance to the firms. The studies by Chen et al. (2011), Dahya, McConnell, and Travolas (2002) and Dedman (2002) show that the degree of compliance with a specific code of corporate governance brings significant changes in the governance practices such as board structure, CEO turnover, and earnings management. Another group of scholars (including Goncharov et al. (2006), Talaulicar and Werder (2008), and Reddy, Locke and Scrimgeour (2010)) shows that the degree of compliance with a specific code of corporate governance is significantly related to firm value or firm performance. Nonetheless, the literature has little evidence to prove the effect of progressive corporate governance code revisions on firms.

With that, this study is motivated to investigate the effectiveness of progressive corporate governance code revisions. As previous studies and the national codes of corporate governance highlighted the importance of associating corporate governance with the economic value of firms, thus, this study intends to assess the effectiveness of corporate governance code revisions by looking at how code revisions affect the relationship between corporate governance and firm value. This research could provide a new insight at how continuous revising the codes of corporate governance affects the firms' corporate governance practices in generating higher value to the firms. Hence, this study fills the gap in the literature on this research issue.

1.3 Problem Statement

"*£2bn wiped off Tesco's value as profit overstating scandal sends shares sliding – as it happened*" – the scandal of Tesco in year 2014 following the discovery that its profits has been artificially inflated by £250 million (Wearden, 2014). This incident of Tesco revealed the weaknesses of corporate governance in the organization. The head of its Digital Transformation Training, Antony Welfare, pointed out the weaknesses of Tesco's corporate governance from two perspectives: (1) the failure of the chairman and non-executive directors to monitor false reporting; (2) the failure of the chief executive officer (CEO) and chief financial officer to sense the unusual reporting prior to its disclosure (Antony Welfare, 2014). The misconducts of the board of directors and CEO revealed the weaknesses of the corporate governance system.

Besides that, Forbes - an America business magazine owned by Forbes Inc., has also been embroiled in a scandal in 2011. Dubbed as the top corporate governance news of 2011, there were criticisms on Rupert Murdoch's management style, its dominancy in controlling over director's election, and other matters pertaining to shareholder vote. Corporate governance scandals also happen in East Asian countries. For example, the criticism on Olympus – a Japanese camera-maker, on the failure of its board of directors to effectively provide independent oversights on behalf of its shareholders, contributed towards the payment of advisory fees of more than a third of the value of the deal to two financial companies (Nathaniel, 2011). Other than that, there are also the shocking corporate scandals such as corporate collapse (e.g. Enron), undue profit boosting (e.g. WorldCom), managerial corporate looting (e.g. Tyco), audit fraud (e.g Arthur Andersen) has also happened in the U.S. - the world's largest economy and a country with a well-developed legal system.

In response to these corporate governance scandals, the U.S. government has stepped-in to be involved in the development of corporate governance system. For example, the U.S. president implemented the Sarbanes-Oxley Act and made it a law in August 2002. The Act aims to strengthen the corporate governance system and minimize corporate failures. Intervention of the U.S. government has led to an advancement in the development of corporate governance. Following the corporate governance reformation due to the intervention of third parties, the national codes of corporate governance have been released in parallel with the international corporate governance code and principles. As the majority of the national codes of corporate governance are not mandated by law, it aims to compensate the weaknesses of a rigid legal corporate governance framework. Non-mandatory compliance with the codes of corporate governance raises the doubt on the effectiveness of releasing the codes of corporate governance to substantively improve the standard of corporate governance. The doubt is even significant when numerous corporate governance scandals have been occurred.

This study raises a doubt on the effectiveness of releasing the national codes of corporate governance by questioning the appropriateness of the new recommendations added in the revised code of corporate governance. In fact, corporate governance code revisions should improve the quality of recommendations on governance practices which are able to fit to the majority of the local publicly listed firms' governing settings. It is unknown whether code issuers take into consideration of the capability of the local firms in complying with the governance practice recommendations. Local firms may face issues regarding cost of compliance, and the inadequate facilities to complement to the new governance practices; these issues may hamper the incorporation of the new practices into the local firms. For example, due to inappropriate recommendations on new governance practices, firms in the U.S. complain that the cost of compliance outweighs the benefits; the recommendations on certification of financial statements by the chief executive officer and chief financial officer, as well as the expectation on internal control assessments have raised the average estimated cost of first-year implementation for large firms by $35 million. The Sarbanes-Oxley Act may be a costly example on how the many are paying for the mistake of the few. The example showed that the revision of the national codes of corporate governance need to take into account the capability of the firms in the market in adopting the new practices, as well as its cost of compliance - which may include transaction costs associated with greater disclosure such as the cost of changing company charters, restructuring, nominating committees and disseminating financial information to increase corporate transparency. High cost of compliance may lead to a decrease in shareholders' value (Chhaochharia and Laeven, 2009).

There is a recommendation in the German corporate governance code regarding the installation of webcast during shareholder meetings, and the process of nomination of the board of committees. However, this recommendation is less applicable to small-sized firms because it increases the financial burden of the firms complying with it (Werder et al., 2005). Nonetheless, if firms choose to not complying with the recommendation, they may also face lower stock valuation by investors who might prefer the other firms that have complied with the recommendations. This creates an unhealthy environment for the firms because the firms have to compete with each others for obtaining good valuation from the investors through complying with the recommendations on corporate governance practices even when the recommendations are unsuitable to the organization. This does not only depart from the principle of comply-and-explain, but also increases the incentive for symbolic compliance through box-ticking approach in order to avoid penalization by the investors for non-compliance.

The lack of empirical evidence raises the question regarding the efforts of progressive corporate governance code revisions are able to substantively improve the standard of corporate governance. By reviewing several national codes of corporate governance, this study finds that, prior to the release of the revised codes, usually, the issuers will set-up a committee to review and identify the weaknesses of the previous recommendations through several ways like surveys and group discussions with the professionals. In fact, the teams involved in the revision process may conduct in-depth survey with the firms to identify the weaknesses of the previous recommendations. After that, there will be a survey in order to introduce new recommendations on governance practices that will be widely accepted by the local firms. Nonetheless, due to limited empirical evidence as shown in the literature, it is not known whether the effort of revising the code of corporate governance has been performed in the right manner which could improve the degree of compliance with the recommendations in the code of corporate governance.

The news on corporate scandals raises another possibility that the past corporate governance code revisions do not have a balanced development on every single aspect of corporate governance, and hence, causes corporate governance issues to remain unsolved. It may be the situation of where the issuers merely focus on updating the board function and board structure, but less emphasizing on improving the recommendations on executive compensations, as well as the other aspects of governance. If the focus of corporate governance code revisions only falls on the specific area of governance, it may be less effective to enhance the firms' overall standard of corporate governance.

For non-mandatory codes of corporate governance, investors in the market play an important role to ensure that firms comply with the governance recommendations in the codes of corporate governance. However, if the market has limited investors with high financial literacy skills, then the investors may have failed in its monitoring role towards the firms' practices of governance whether are parallel with the recommendations in the codes of corporate governance. Hence, due to limited evidence in the literature, the capability of the investors to pinpoint whether the firms comply substantively with the code are questionable. Besides that, the investors could be very tolerant towards the firms that generate a good return of investment but failed in complying with the code of corporate governance. This may hamper the incorporation of the best practices of governance to the firms.

Zattoni and Cuomo (2008) gives the notion that the incorporation of new governance practices was more than driven by legitimation reasons rather than driven by the initiation of the firms in the matter of compliance. Zattoni and Cuomo (2008) raises the concern regarding the lack interest of the firms to restructure its existing corporate governance practices. The firms may tend to comply symbolically with the code only to fulfill the market expectations. In other words, firms may comply with the new governance practices through box-ticking rather than adopting the practices in the substance form. This is shown by the study of Ananchotikul, Kouwenberg and Phunnarungsi (2010) that provide evidence regarding symbolic compliance with the Thai code of corporate governance. Therefore, measuring the degree of compliance is not sufficient to show the effectiveness of a corporate governance code revision. Even, due to the compliance with the national codes of corporate governance is not mandated by laws, the firms can find the other alternatives to justify to shareholders. This prevents the firms to be penalized by the investors if the investors do not investigate whether the justification is reasonable.

In sum, the incessant corporate scandals indicate that there are loopholes in the corporate governance system. The doubt on the effectiveness of corporate governance code revisions is an issue that should be looked with concern. The lack empirical evidence in the literature has failed to prove that the world's code issuers are working in the correct manner in revising the recommendations in the codes of corporate governance. Also, the literature could not provide any view on whether progressive corporate governance code revisions are able to substantively improve the firms' corporate governance. The problem on the capability of investors to detect the firms' symbolic compliance may be a serious concern in implementing the non-mandatory code of corporate governance. All these problems regarding corporate governance code revisions may raise the doubt to the effectiveness of corporate governance code revisions.

1.4 Research Questions

(1) Do the cumulative number of corporate governance code revisions significantly moderate the relationship between corporate governance score and firm value?

(2) Do the number of new practices released in each corporate governance code revision significantly moderate the relationship between corporate governance score and firm value?

(3) Do the years of compliance with a code of corporate governance significantly moderates the influence of the number of new practices on the relationship between corporate governance score and firm value?

1.5 Objectives

Overall, this study aims to investigate the moderating effect of corporate governance code revisions towards the relationship between corporate governance score and firm value. The specific objectives of this study are:

(1) To investigate the moderating effect of the cumulative number of corporate governance code revisions towards the relationship between corporate governance score and firm value.

(2) To investigate the moderating effect of increasing the number of new governance practices released in each corporate governance code revision towards the relationship between corporate governance score and firm value.

(3) To investigate the moderating effect of the years of compliance on the influence of increasing the number of new governance practices towards the relationship between corporate governance score and firm value.

1.6 Significance of the Study

The importance of investigating the effectiveness of corporate governance code revisions is supported by the increasing number of national codes of corporate governance in the world. The European Corporate Governance Institute (ECGI) shows that the number of national codes of corporate governance has increased from a total of 72 issues by 24 countries in year 1999 (Aguilera and Cuervo-Cazurra, 2004) to a total of 189 issues by 63 countries in 2008 (Zattoni and Cuomo, 2008). This study further updates the statistics; this study finds that the number of countries issuing the national codes of corporate governance has increased to nearly 100 up to the year 2015. The increasingly high number of countries releasing the national codes of corporate governance has caught the attention of scholars to look into this research area. As documented by Aguilera and Cuervo-Cazurra (2009), the *Journal of Corporate Governance: An International Review* has recently published 14 articles that are related to the issues of the national codes of corporate governance and a total of 59 articles mentioned about "governance code" in the abstract of their respective manuscripts.

The governance practices recommended by each national code of corporate governance may not be exactly similar because the recommendations need to fit to the local institutional norms and organization cultures. However, the majority of the national codes of corporate governance share identical scopes of governance (Gregory, 2000; 2001), such as in the aspects of board structure and board function, shareholder rights protection, and the executive compensation policy. Among the shared scopes of corporate governance, the practices recommended to the local firms in individual countries are different. Hence, there could be a limitation of studying only a single country sample in research because the findings could not be generalized. As such, it motivates the present study to look into the cross-country sample which is rarely investigated by the previous studies, while controlling for country-specific effect in the analysis.

This study investigates the effectiveness of corporate governance code revisions by associating the effect of corporate governance code revisions to market-based firm value. Tobin's Q is chosen in the analysis as it is less biased if compared to the stock prices. Associating corporate governance code revisions with firm value will reveal how investors value the firms based on their compliance with the codes of corporate governance.

Instead of testing the direct effect of corporate governance code revisions on firm value, this study tends to show how corporate governance code revisions affect firms' corporate governance practices, which will subsequently impact firm value. In other words, this study shows whether corporate governance code revisions are able to moderate the relationship between corporate governance score and firm value. The corporate governance score is collected from ASSET4ESG database. The regression models of this study are constructed to examine the interaction effect of corporate governance code revisions with corporate governance score. This is different from the regression model constructed by Fauver et al. (2017) which only tests the direct relationship between the corporate governance reforms and firm value, without looking into the changes of corporate governance practices of the firms in the reforms. Hence, the findings generated from the present study could add to the body of literature on corporate governance code revisions.

The is a void in the existing literature regarding the effectiveness of progressive effects of corporate governance code revisions. The present literature only reveals the degree of compliance with a code of corporate governance that is released at one point in time, but there is limited evidence to show the progressive effectiveness of corporate governance code revisions. Hence, this study fills the research gap by investigating the effect of progressive corporate governance code revisions using time series data. In this stream of research, the concern raised by Zattoni and Cuomo (2008) regarding symbolic compliance should be taken into account. However, the majority of the investors may not be able to detect symbolic compliance in the short interval of time because they are not involving in the management of the firms. Hence, utilizing time series data that covers more than one corporate governance code revision occurs within the sample period of this study may generate the findings that can add to the body of the literature. The rationale is that, time series data can reveal the overall effect of corporate governance code revisions on firm value that may be negative instead of expecting the effect is positive. With that, this study examines the effect of cumulative number of corporate governance code revisions on the relationship between corporate governance score and firm value. The cumulative number of corporate governance code revisions is able to reflect the historical activity of corporate governance code revisions until the present day. Also, the cumulative number of corporate governance code revisions are able to reveal the effect of progressive corporate governance code revisions on firm value throught the regressions.

In the corporate governance code revisions, besides of the matter of compliance, the new governance practices are similarly important in driving the effectiveness of corporate governance code revisions. Rather than assessing the content of the new governance practices released from corporate governance code revisions, this study examines the quantity of new governance practices released in each corporate governance code revision to the relationship between corporate governance score and firm value. In fact, the quantity of new governance practices can affect the overall effectiveness of corporate governance code revisions. The rationale is that, the quantity of new governance practices released may have direct relationship with the cost of compliance, because an increasing number of new governance practices raises the cost of compliance. Incurring a high cost of compliance due to numerous new governance practices released may increase the incentive of symbolic compliance. In such cases, the number of new governance practices are investigated.

Given the cost of compliance is a concern in non-mandatory codes of corporate governance, it is also critical to measure the average cost of compliance per year besides the total cost of compliance incurred for adopting the new governance practices. The rationale is that, releasing numerous new governance practices at one time may incur a lower cost of compliance per year (when averaged) because it is usually done by the countries that do not frequently revise the national code of corporate governance. In other words, when dividing the number of years of compliance with the number of new governance practices released, the average cost of compliance may not be high. Thus, instead of only examining the number of new governance practices, inclusion of the number of years which allows for firms to compliance with the new practices are also critical. In fact, there are some countries that revise their national codes of corporate governance every one or two years, while certain countries revise their national codes less frequently, and some countries have no constant interval in their code revision. The heterogeneity of the years of compliance create the value of research.

In summary, this study shows several significance. First, the research gap in the literature is filled through revealing the effectiveness of progressive corporate governance code revisions. This study focuses on the effect of a series of corporate governance code revisions rather that a specific code revision. Second, this study uses the world sample to generalize the findings. Third, this study do not test the direct effect of corporate governance code revisions towards firm value, but this study looks into the effect of corporate governance code revisions to the firms' corporate governance practices which subsequently affect firm value. Fourth, this study investigates the effectiveness of corporate governance code revisions from three new perspectives, i.e. the cumulative number of code revisions, the number of new practices released in each revision, and the years of compliance with each revised code of corporate governance. These are the significance of this study that adds value to the literature as well as policy makers.

1.7 Contribution of the Study

This study contributes to the literature by showing the overall effectiveness of corporate governance code revisions to the changes of the firms' corporate governance practices which subsequently affect firm value. The findings of this study are able to reveal whether corporate governance code revisions that cause a change in the firms' governance practices is substantive or symbolic. If the increased of corporate governance score following the corporate governance code revisions does not improve firm value, it should indicate the suspicious regarding symbolic compliance. The findings are able to show whether firms tend to symbolically comply with the code only to fulfill the market expectation, but intend to retain the loopholes in corporate governance to safeguard the benefit of the decision makers in the firms rather than sharing the benefit to all of the stakeholders in fairly mood, or vice versa. Hence, the findings are able to add to the body of literature regarding the response of the firms when confronting with the need to restructure the internal governance mechanism. The findings could also provide useful implication to justify whether agency theory or institutional theory is predominant in this context. This may also give a policy implication on whether implementing non-mandatory codes of corporate governance is a wise decision by the policy makers.

The main findings of this study could justify institutional theory regarding the emphasis on legitimacy with respect to the issue of low degree of compliance with the non-mandatory codes of corporate governance. Amid the limited empirical studies on corporate governance code revisions, this study provides the evidence to state the importance of institutional theory in explaining the development of non-mandatory codes of corporate governance. The support for institutional theory may highlight the importance of forming a norm in corporate governance institutional setting. The norm can exert pressure to the firms that fail in complying with the code of corporate governance. Because limited studies provide empirical evidence to highlight the importance of legitimacy in the matter of compliance with the codes, this study adds value to the literature in supporting the standpoint of the institutional theory.

The effectiveness of corporate governance code revisions can justify for the importance of soft laws in pressuring firms for complying with the non-mandatory codes of corporate governance. The findings will be able to signal the important role played by the investors in monitoring the firms' compliance with the codes of corporate governance. The findings may shed light the additional role played by the investors in penalizing the firms for the failure of compliance through stock price valuation (Goncharov et al, 2006). For example, investors should give lower valuation to the firms that have failed in complying with the recommendations on corporate governance without a reasonable justification. Investors should intellingently invest in the firms which possesses a sound corporate governance system only, rather than investing in the firms which possesses a poor corporate governance system. This creates a strong pressure to the firms with weak governance because they may have less accessibility to external financing. Hence, the investors play a significant role in creating a healthy competition for the firms in the financial market.