Changing Corporate Governance in Response to Negative Media Reports

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Abstract

We study how organizations change their corporate governance in response to negative publicity in the media. We build on insights from the literature on interpersonal trust to theorize how organizations respond to different types of trust-damaging information. We suggest that organizations are likely to replace key individuals involved in the corporate governance process when trust-damaging information provides evidence of low integrity. In contrast, organizations are likely to make changes in how the governance process is organized when trust-damaging information provides evidence of low benevolence. We test our hypotheses by using data on publicly-traded Korean firms from 2006 to 2013. Our results provide general support for our argument about corporate governance changes that organizations initiate in response to different types of trust-damaging information. We also explore how foreign ownership and state ownership moderate organizational responses to trust-damaging information.

Keywords: *corporate governance, trust repair, organizational responses to negative publicity*

Introduction

How organizations respond to scandals that damage their reputation and undermine trust of stakeholders is an important topic attracting more and more research (Pfarrer et al., 2008; Desai, 2011; Zavyalova et al., 2012). Organizational responses to scandals often involve changes in corporate governance such as replacement of CEOs or board members (Arthaud-Day et al., 2006; Marcel & Cowen, 2014). Organizational misconduct that triggers scandals is often attributed to corporate governance failures and making changes in corporate governance is a natural response to such scandals. While empirical evidence about different types of organizational misconduct has been accumulated and different types of organizational responses have been explored (Greve, Palmer, & Pozner, 2010; Gomulya & Boeker, 2014; Wiersema & Zhang, 2013), each of these studies is usually focused on a particular type of misconduct and a particular type of response. Given that scandals are triggered by different types of misconduct and that different types of corporate governance changes potentially can be implemented as corrective responses, an important research question is "what kind of corporate governance changes are initiated after scandals provoked by different types of organizational misconduct?" Corporate governance is about relationships among managers, shareholders, and other stakeholders (Aoki, 2001; Hitt et al., 2013). Trust plays an important role in these relationships and thus we choose to answer our research question by drawing on theories developed in research on trust repair (Bachmann, Gillespie, & Priem, 2015; Gillespie & Dietz, 2009).

While some prior studies describe responses to media reports about organizational misconduct in terms of impression management (e.g., McDonnell & King, 2013; Zavyalova et al., 2012), we consider these responses from the trust repair perspective acknowledging that attempts to repair trust have important symbolic components but can also involve substantive

changes in how organizations operate (Eberl, Geiger, & Ablander, 2015; Gillespie, Dietz, & Lockey, 2014). We believe that some insights generated in research on interpersonal trust can be fruitfully applied in the analysis of corporate governance changes that organizations initiate in response to different types of negative publicity.

In this paper, we shed light on two notable changes in a firm's corporate governance: the replacement of individuals involved in the governance process and the adoption of new governance structures. We relate these corporate governance changes to two distinct trust-repair approaches described in the literature on interpersonal trust – one trust-repair approach is focused on dispositional factors contributing to trust-damaging behavior while the other approach is focused on situational factors. We theorize what corporate governance changes organizations are likely to initiate depending on the nature of trust-damaging information (indicating the lack of integrity or the lack of benevolence) and how these choices are affected by preferences of different types of shareholders.

In our empirical analysis, we trace trust-damaging information reported by Korean newspapers and corporate governance changes in publicly-traded Korean firms from 2006 to 2013. We use conceptual models developed in research on trust to understand which corporate governance changes organizations choose to initiate in response to different types of negative publicity.

Literature Review

Trust in organizations is susceptible to damages (Bachmann & Inkpen, 2011; Gillespie & Dietz, 2009; Kramer & Lewicki, 2010; Mayer, Davis, & Schoorman, 1995; Searle et al., 2011). Trust can be breached when an organization behaves in a way that contradicts the stakeholders' expectations and these breaches will eliminate the benefits of trusting relationships with

stakeholders (Dirks, Lewicki, & Zaheer, 2009; Kim et al., 2004; Tomlinson & Mayer, 2009). Various events could lead to diminished trust including scandals, irregularities in financial reporting, mistreatment of employees, etc. If reputation and trustworthiness of an organization are damaged, it will face difficulties in obtaining needed resources or support from its stakeholders (Rhee & Valdez, 2009). A number of prior studies have considered how companies are trying to repair trust after their misconduct has been exposed. For example, researchers have studied how organizations are trying to restore confidence of investors after financial restatements (Gomulya & Boeker, 2014; 2016) or after being accused of some other types of organizational misconduct (Connelly et al., 2016).

Dirks et al. (2009) point out that challenges of repairing relationships have been described using different conceptual frameworks. Researchers have described organizational responses to scandals in terms of repairing trust, reputation, and legitimacy (Gillespie, Dietz, & Lockey, 2014; Gomulya & Boeker, 2014; Pfarrer et al., 2008). Several studies describe actions taken by organizations after the disclosure of reputation-damaging information as impression management (e.g., McDonnell & King, 2013; Westphal & Graebner, 2010; Zavyalova et al., 2012). Impression management is often associated with superficial organizational changes, while trust repair is often associated with substantive organizational changes. However, this simplified distinction leads to one-sided interpretations of both impression management and trust repair. There is no reason why impression management cannot include substantive actions as long as they are sufficiently visible and thus can impress the audience (e.g., Durand & Vergne, 2015). Similarly, there is no reason why trust repair cannot involve symbolic actions that have limited practical implications but send a strong signal to stakeholders (e.g., Eberl, Geiger, & Ablander, 2015). If the audience does not perceive these signals as misleading, then such signaling can help

organizations to engender trust. Correspondingly, instead of presenting trust repair as an alternative to impression management, we consider impression management as an important part of the trust-repair process. For effective trust repair, it is important for organizations not only to make some changes in how they operate, but also to communicate these changes or to make them visible for the audience whose trust needs to be repaired.

Researchers have pointed out that trust plays an important role in corporate governance and that corporate governance affects trust of shareholders and other stakeholders (Child & Rodrigues, 2004; Farber, 2005; Gillespie et al., 2012; Puranam & Vanneste, 2009; Schnakenberg & Tomlinson, 2016). If corporate governance can engender trust of stakeholders, it is reasonable to expect that negative consequences of revealing trust-damaging information potentially can be alleviated by making modifications to a firm's governance. Recent studies have demonstrated that organizations often replace top executives and board members after stock option backdating (Wiersema & Zhang, 2013), disclosures of financial fraud (Marcel & Cowen, 2014), and announcements of financial restatements (Arthaud-Day et al., 2006). Firms affected by scandals that can be attributed to governance failure also can respond by introducing new governance structures and procedures (Gillespie et al., 2012). While it has been acknowledged that corporate scandals are a common reason why corporate governance practices attract attention (Ocasio & Joseph, 2005), researchers still need to explore how corporate scandals trigger the adoption of "best governance practices." Given that a number of potential corporate governance changes can be implemented in response to negative publicity, it is important to understand which corporate governance changes would be appropriate as a response to different types of trust-damaging information.

Theory Development

Research on trust in management, sociology, and political science demonstrates that we can trust not only in other individuals, but also in teams, organizations, governments, and various social institutions (Dirks, Lewicki, & Zaheer, 2009; Bachmann, Gillespie, & Priem, 2015). Recently scholars began to synthesize research on trust in individuals, groups, and organizations (Fulmer & Gelfand, 2012) and to explore whether trust in organizations is based on the same mechanisms as trust in individuals. Is it meaningful to talk about organizational integrity and benevolence the same way as we talk about integrity and benevolence of individuals? We agree with researchers who argue that the critical question is not whether an organization can have what we usually think of as personality characteristics, the critical question is whether organizations are perceived as having such characteristics (Gillespie & Dietz, 2009). If an organization exhibits behavior that might be expected from a person with integrity and benevolence, we tend to attribute these personality characteristics to the organization.

Trust repair in interpersonal relationships has been studied for decades (Heider, 1958; Sitkin & Roth, 1993; Kim et al., 2004). Scholars studying how trust is damaged and repaired in interpersonal relationships have developed useful theoretical frameworks for analysis of these processes. In our study, we consider individuals as subjects of trust and organizations as objects of trust (Fulmer & Gelfand, 2012; Janowicz & Noorderhaven, 2006). We follow researchers who applied theories of interpersonal trust to understand trust in organizations (Gillespie & Dietz, 2009). We use this approach to understand better how external stakeholders are likely to interpret negative media reports about companies and how these companies change their corporate governance to repair stakeholders' trust. Repairing trust through changing corporate governance is a relatively new research topic. Corporate governance practices visible to external stakeholders

send signals about organizational trustworthiness and we can use theories of trust to understand how companies try to improve their perceived trustworthiness by changing corporate governance practices (Gillespie et al., 2012).

Theories from research about interpersonal trust can help us identify factors that determine the choice of particular corporate governance interventions triggered by different types of trust-damaging information. We draw from interpersonal trust studies that make a distinction between situational and dispositional factors affecting behavior (Heider, 1958; Dirks et al., 2011). We build on the idea that behavior is determined by dispositional and situational forces and, correspondingly, trust can be repaired through changing dispositional or situational forces (Dirks et al., 2011). To clarify this distinction with an example, consider a hypothetical situation of engaging in a business transaction with a company. After negative experience of interacting with a person representing this company, we are reluctant to continue doing business with this company because our trust in the company has been damaged. This company can attempt to restore our trust by changing dispositional factors (i.e., replacing this company representative) or by changing situational factors (i.e., changing how company representatives interact with clients).

How can these two trust-repair approaches be implemented in the context of corporate governance? Dispositional factors tend to persist at the individual level but they can be changed at the organizational level by replacing key individuals involved in the corporate governance process. Key governance decisions are made by CEOs and board members; therefore, we can change how the company is governed by replacing CEO and /or board members of this company. Volkswagen CEO was replaced after the company had experienced the diesel emissions scandal. Since this scandal had occurred as a result of intentional manipulation, key decision makers had

to bear the responsibility. Changing situational factors implies changing how the governance process is organized. This approach can be implemented by adopting new structures and procedures for making governance decisions. This is how companies and regulators often respond to demands to improve corporate governance in the aftermath of corporate governance scandals. Sometimes new governance structures and procedures are required by mandatory regulation (e.g., Sarbanes Oxley Act); sometimes companies choose to adopt "best governance practices" on a voluntary basis (Tuschke & Sanders, 2003). The adoption of these structures and procedures is intended to enhance the diligence of the governance process and to demonstrate this enhanced diligence (Eberl, Geiger, & Ablander, 2015). For example, Nike faced a lot of criticism after publications about the terrible working environment and child labor in their Asian subcontracting factories. After a series of unsuccessful responses, Nike announced the creation of a corporate responsibility committee on the board to institutionalize the firm's responsible behavior and to regain public's trust in the company (Paine, 2014).

To understand why organizations can be considered as non-trustworthy, we draw on insights about dimensions of trustworthiness originally developed in research about interpersonal trust (Mayer et al., 1995). Scholars of interpersonal trust consider three distinct dimensions of trustworthiness: integrity, benevolence, and ability (Dirks et al., 2011). Correspondingly, trust in interpersonal relationships can be compromised if perceived integrity, benevolence, and ability of trusted individuals becomes suspect. Similarly, trust of stakeholders in organizations will be damaged by information that can be interpreted as evidence of low integrity, low benevolence, or low ability (Gillespie & Dietz, 2009). Media reports that reveal problems with integrity or benevolence do not appear frequently, but when such reports appear, they tend to make serious accusations that cause scandals. In contrast, media reports that provide information that can be

interpreted as evidence of ability, appear frequently and may indicate more or less serious problems with organizational abilities. As a result, publications with evidence of low ability are too frequent and in most cases are not important enough to constitute an "event." We were mostly interested in publications revealing sensitive information likely to trigger some organizational responses and thus we decided to focus on evidence of low integrity and low benevolence. These dimensions of trustworthiness are particularly important in the context of corporate governance – while problems with ability are often resolved at the level of operational units that need to perform better, problems with integrity and benevolence usually have to be resolved at the corporate level and this often implies changes in corporate governance.

Some trust-damaging events in organizations can be attributed to the lack of integrity while other trust-damaging events can be attributed to the lack of benevolence. Correspondingly, organizations potentially can repair trust if they make corporate governance changes that should translate into changes in perceived integrity and benevolence. Gillespie and Dietz define integrity as consistent adherence to "moral principles and a code of conduct" and benevolence as "genuine care and concern for the well-being of stakeholders" (2009, p. 128). In other words, integrity is about care for general moral principles or formal rules of behavior, while benevolence is about care for specific stakeholders. In the context of corporate governance, our focus is on perceived integrity and benevolence of top executives and board members – whether they consistently make decisions in accordance with certain moral principles and rules of business conduct and whether they take into account interests of various stakeholders in making these decisions. Motivations and intentions of executives and board members are non-transparent for external observers, who make judgements about integrity and benevolence based on behavioral indicators. Since we are concerned with perceived integrity and benevolence, we also

focus on observable behavioral indicators of integrity and benevolence rather than on underlying motives and intentions of individuals involved in the corporate governance process.

We argue that the organizational choice of a trust-repairing approach will depend on whether trust-damaging events are interpreted as evidence of low integrity or low benevolence (Figure 1). If trust-damaging events are likely to be interpreted as evidence of low integrity, then organizations need to choose a response that will reassure stakeholders that the problem of low integrity has been resolved. In this situation, replacing key individuals involved in the governance process (a dispositional response) would be a preferred solution - by replacing individuals in charge of corporate governance, organizations can quickly and radically change dispositional factors affecting governance outcomes. In contrast, when trust-damaging events are interpreted as the evidence of low benevolence – in other words, as evidence of dismissing interests of certain stakeholders – then organizations are likely to focus on changing how the governance process is organized to ensure the diligence of the governance process. Thus, to repair trust when a low level of benevolence is suspected, organizations are likely to adopt new governance structures and procedures (a situational response) that should prevent negligence in making governance decisions.

INSERT FIGURE 1 ABOUT HERE

Hypotheses

Responses to Different Types of Trust-Damaging Information

Organizations are likely to choose different trust-repair tactics in response to different types of trust-damaging information. We consider the disclosure of information about organizational corruption and about mistreatment of business stakeholders. Organizational corruption refers to

unfair or illegal actions that break formal rules or informal norms in the pursuit of personal or organizational gain and include accounting fraud, bribing, tunneling of resources, etc. (Aguilera & Vadera, 2008; Pfarrer et al., 2008). Mistreatment of business stakeholders refers to an organization's improper or unlawful use of superior power or position in the relationships with important business stakeholders, such as employees or suppliers.

Information about organizational corruption – accounting irregularities, bribery, financial fraud, or other instances when organizational actions break established rules or principles - is likely to be interpreted as evidence of low integrity. When organizational integrity is threatened, organizations are likely to respond by replacing key decision makers. By replacing people in charge, the focal organization demonstrates that the source of compromised integrity has been eliminated. Replacing key decision makers also should prevent instances of organizational corruption in future assuming that newly appointed individuals uphold high standards of organizational integrity.

Replacement of senior executives and board members after trust-damaging events demonstrates that particular individuals receive punishment for the occurrence of these events. This response corresponds to trust repair through "penance" described in the literature about interpersonal trust as a trust-repair approach focused on changing dispositional factors affecting behavior (Bottom et al., 2002; Gillespie et al., 2012; Tomlinson & Mayer, 2009, Dirks et al., 2011). The replacement of key decision makers changes dispositional characteristics of individuals involved in the governance process. This response attributes responsibility for organizational corruption to senior executives and board members. Even when executives and board members are not directly involved in corrupt practices, they are still considered liable because one of their primary responsibilities is to create an organizational environment that

should prevent corruption. This argument is supported by the findings demonstrating that top executives and board members often step down when financial fraud is revealed (e.g. Arthaud-Day et al., 2006; Marcel & Cowen, 2014; Wiersema & Zhang, 2013). Building on the above reasoning and prior findings we hypothesize the following:

Hypothesis 1: The disclosure of information about organizational corruption is positively associated with the replacement of individuals involved in the governance process.

Mistreatment of business stakeholders - such as mistreatment of employees or abuse of suppliers – may have less damaging consequences for organizational reputation compared with instances of organizational corruption but still might be perceived negatively even by those stakeholders who were not directly affected by abusive practices. While organizational corruption is usually associated with a transgression of certain norms or policies (Pfaffer et al., 2008), mistreatment of stakeholders is associated with the lack of organizational policies protecting these stakeholders (Theodorakopoulos, Ram, & Kakabadse, 2015). If instances of stakeholder mistreatment are consistent with existing organizational policies, they would not be interpreted as evidence of low integrity (an organization stays true to its policies). Instead, stakeholder mistreatment is likely to be interpreted as evidence of low benevolence – low concern about needs of these stakeholders.

Making changes in how the governance process is organized is another response to negative events that can be interpreted as a failure of governance. This response corresponds to an alternative trust-repair approach described in the literature about interpersonal trust as “structural perspective” (Dirks et al., 2009) or “regulation” (Gillespie & Dietz, 2009); the latter understood broadly as “a system to assure future trustworthy behavior and limit future transgressions” (Dirks et al, 2011: 89). Imposing structural constraints can take various forms such as introducing new

rules, policies, or structures (Sitkin & Roth, 1993; Gillespie & Dietz, 2009). This trust-repair strategy aims to change situational factors that affect decisions and behavior of a trustee. In particular, the adoption of new governance structures can change situational factors affecting how governance decisions are made. New governance structures impose structural constraints on future conduct and are supposed to prevent the reoccurrence of trust-damaging events in future. Such structural solutions can be initiated by an organization itself or by external regulatory agencies if the loss of trust appears to be a systematic problem affecting many organizations. For example, a major breach of trust happened as a result of the financial crisis of 2008 and scholars considered regulation as one of the key mechanisms for restoring trust in the financial system (Gillespie et al., 2012).

As argued above, in response to trust-damaging information that can be interpreted as evidence of low benevolence, organizations are likely to change how the governance process is organized. In particular, they may introduce new formal rules, structures, or policies to ensure the diligence of the governance process. For example, a global apparel firm could decide to accept independent external monitoring of the firm's subcontractors after experiencing a labor-related problem (Lamin & Zaheer, 2012). By adopting new formal structures and procedures, an organization demonstrates an increased level of formal monitoring of its future actions (Pfeffer, 1981; Suchman, 1995). Changes in how the governance process is organized do not always result in making decisions more favorable to vulnerable stakeholders; however, a more rigorous governance process demonstrates that due diligence is done when governance decisions are made.

Hypothesis 2: The disclosure of information about mistreatment of business stakeholders is positively associated with changes in how the governance process is organized.

Moderating Role of Ownership

Various contingency factors can come into play when organizations choose their responses to trust-damaging information. Even when organizations face the same type of negative publicity, their responses may vary depending on the organization-specific characteristics and other contingency factors. We focus on the presence of particular owners because owners have direct impact on important governance decisions, such as CEO replacement (Zeitoun & Pamini, 2017). To this end, we examine moderating effects of foreign and state shareholders since these shareholder groups have unique strategic preferences (Johnson & Greening 1999).

Foreign investors may play an important corporate governance role (Ahmadjian & Robbins, 2005; Park & Kim, 2008; Yoshikawa & Gedajlovic, 2002). Existing studies provide evidence that foreign shareholders pay special attention to corporate governance and CSR (Ferreira & Matos, 2008; Oh, Chang, & Martynov, 2011; Chen et al., 2017). Leuz, Lins, and Warnock (2009) argue that weak corporate governance and low transparency have an adverse effect on foreign investments. Foreign investors tend to be more sensitive to potential risks and agency costs than domestic investors because foreign investors have fewer opportunities to obtain relevant information and to exercise monitoring over management, especially through informal channels. Using the same logic, we expect that foreign investors would be more sensitive to information about organizational misconduct because it signals problems with corporate governance and high investment risks.

The presence of foreign shareholders will put additional pressure on organizations to respond to trust-damaging information because foreign shareholders are likely to exit if organizational trustworthiness is not restored. Foreign investors, especially in emerging economies, have a reputation of buying and selling stocks frequently (David et al., 2006), being

more vigilant and risk-averse than domestic ones. Therefore, we expect that firms with foreign shareholders have especially strong incentives to respond to trust-damaging information with corporate governance changes described in Hypotheses 1 and 2.

Hypothesis 3a: Foreign ownership positively moderates the relationship between the disclosure of information about organizational corruption and the replacement of individuals involved in the governance process.

Hypothesis 3b: Foreign ownership positively moderates the relationship between the disclosure of information about business stakeholder mistreatment and changes in how the governance process is organized.

Partial state ownership of publicly traded companies is common in most emerging economies. State ownership is often considered as a risk factor for private investors because of possible negative implications of state intervention in strategic decision-making (Musacchio & Lazzarini, 2014). However, some studies report that investors and customers favor companies with state ownership because state ownership is considered as an indicator that these companies have access to resources controlled by the state and may receive some support from the state when facing difficult situations (Ramirez & Tan, 2004; Spicer & Okhmatovskiy, 2015). This access to state resources and ability to rely on state support in crisis situations imply lower dependence on private investors and less concern about market reaction to news about the company. The state often holds shares of companies to pursue goals of long-term economic development and thus state investments represent the source of patient capital, especially in emerging economies (Musacchio & Lazzarini, 2014). While companies with partial state ownership are negatively affected by the disclosure of information about organizational corruption or about mistreatment of business stakeholders, their need to respond to this

information in order to repair trust is less urgent. This argument is supported by studies of CEO turnover in China demonstrating that state-owned companies are reluctant to replace CEOs when corporate fraud is discovered (Cumming, Hou, & Lee, 2011; Chen et al., 2016). Correspondingly, we expect negative moderating effects of state ownership on corporate governance changes initiated when organizational corruption or mistreatment of business stakeholders are revealed. Figure 2 provides a graphical summary of all our hypotheses.

Hypothesis 4a: State ownership negatively moderates the relationship between the disclosure of information about organizational corruption and the replacement of individuals involved in the governance process.

Hypothesis 4b: State ownership negatively moderates the relationship between the disclosure of information about business stakeholder mistreatment and changes in how the governance process is organized.

INSERT FIGURE 2 ABOUT HERE

Methods

Empirical Context

We test our arguments with data on Korean companies. This context fits well with the focus of our study. South Korea was ranked 40th (out of 102 countries) in the Corruption Perceptions Index issued by Transparency International in 2014. Korea's rapid economic development was accompanied by corporate scandals; for example, the chairman of Samsung Group was charged with financial wrongdoing in 2008 and his son, the vice chairman, was charged with bribery and sentenced in 2017. Anecdotal evidence demonstrates that some Korean companies changed their corporate governance structures in response to negative publicity. Namyang Dairy Products Ltd.,

one of the largest dairy product suppliers in Korea, faced widespread public criticism for its abuse of retailers by using its supreme status. The company was accused of pressuring retail owners to buy excessive inventory for the purpose of shifting its inventory burden to the retail stores. Namyang's CEO, Woong Kim, publicly apologized for its behavior and promised to establish the "coexistence committee" comprised of both executives and retail store representatives to prevent the reoccurrence of the same malfeasance. Similarly, Hyundai Motors decided to set up a new board committee that consisted of independent directors in order to represent shareholders' rights in major business decision-makings. This decision was made in response to criticism and requests by shareholders (particularly, by foreign institutional investors) following Hyundai Motors' controversial purchase of a land site in Seoul.

The Korean context also provides opportunities to consider complex effects of state ownership and foreign investors. After the Asian Financial Crisis in the late 1990s, Korea rapidly globalized its economy by opening its market to foreigners and foreign investors became a major source of influence on Korean firms' strategies (Park & Kim, 2008). Even after opening the market for foreign investors, the Korean government continues to exercise strong influence on business through regulation and through ownership of shares held by state-affiliated investors.

Data and Variables

Our sample consists of 110 publicly traded Korean firms observed between 2006 and 2013. This sample includes the largest firms from Korea Composite Stock Index (KOSPI) 200. The total asset of our sample firms corresponds to 93 percent of KOSPI 200. By focusing on the largest publicly-traded firms, we were able to obtain comprehensive accounting and corporate governance data.

In order to trace trust-damaging information, we used eight major Korean newspapers - three general newspapers (Donga Ilbo, Hankyoreh, and Hankook Ilbo) and five business newspapers (Maeil Business Newspaper, Korean Economic Daily, Seoul Economic Daily, Financial Times, and Herald Business) that cover business-related issues extensively. Considering the possibility that the tone of newspapers varies depending on their political orientation, we chose general newspapers that have liberal (Hankyoreh), neutral (Hankook Ilbo), and conservative (Donga Ilbo) political orientations. We accessed the content of these newspapers using Korean Integrated News Database System (KINDS) operated by Korea Press Foundation. Accounting and ownership information was obtained from the KIS-Value III database. Data on CEO turnover were collected through the KocoInfo database and board committee adoption data were collected from firms' annual reports. The data on business group affiliations was obtained from the Financial Supervisory Service in Korea.

Dependent variables. We used two sets of dependent variables. First, we measured the replacement of key individuals involved in governance by using two variables, namely *CEO replacement* and *executive replacement*. *CEO replacement* was coded as "1" if the CEO in year t is different from year t-1; otherwise, this variable took the value of "0". *Executive replacement* was measured as a percentage of newly elected executive board members. Top executives of Korean firms usually sit on the board as inside directors and they are much more involved in the governance process than outside directors. Executives sitting on the board of directors are legally responsible for corporate actions and thus can be considered as key executives of the firm.[1]

[1] Since we are focusing on executive board members, we can avoid the ambiguity faced by studies that look at the turnover of non-executive board members (Marcel & Cowen, 2014); while non-executive directors may voluntarily leave the board of the firm implicated in a media scandal, the replacement of executive board members is usually initiated by the firm.

Second, we operationalized changes in how the governance process is organized as *establishment of new governance structures.* This variable captures the adoption of new board committees (the difference between the number of board committees in year *t* and year *t*-1). There were 591 replacements of CEOs and executives during our observation period, 95 new board committees were created during this period.

Independent variables. Our independent variables capture reporting of different types of trust-damaging events by the media. We searched the content of eight major Korean newspapers and identified instances of organizational corruption and mistreatment of business stakeholders to generate the corresponding variables. In choosing relevant events from these newspapers, we searched for articles that contained names of our sample companies and made the initial judgment whether these articles addressed adverse events of our interests. If an article passed this initial screening, then one of the author read the article to code a negative event that the company had experienced. To include only significant events, we coded a negative event only when it was mentioned by at least two newspapers (in most cases, these negative events were mentioned by more than two newspapers). In coding negative media reports, we focused on instances of organizational corruption and mistreatment of business stakeholders to generate the corresponding variables.[2] *Organizational corruption* variable captures whether the focal firm was accused of breaking the law or violating established rules of business conduct as evidenced by instances of accounting fraud, bribing, tunneling, etc. *Mistreatment of business stakeholders* variable captures whether the focal firm was accused of exploiting its superior power or position

[2] From the content of the articles, it was quite easy to identify instances of organizational corruption and mistreatment of stakeholders. To check the reliability of our coding, we used an extra coder (also a native Korean speaker) to code a subset of negative media reports (14% of all the analyzed reports). The level of inter-coder agreement for this subset was very high (91.35 percent agreement for organizational corruption and 94.23 percent agreement for mistreatment of stakeholders), reflecting minimal ambiguity of the coding process.

in the relationship with employees, suppliers, or customers (intervening in supplier firms' human resource matters, unjust dismissal of employees, etc.). Appendix A provides examples of negative media reports about Korean companies.

We also use two moderating variables in this study. *Foreign ownership* was measured as a percentage of voting shares held by foreign investors. *State ownership* was measured as a percentage of voting shares owned by the government and government-affiliated investors.

Control variables. We control for profitability as measured by return on equity (*ROE*) calculated as operating profit divided by total equity. We include *family ownership* in our models as it may have a significant effect on firms' decisions (Chua, Chrisman, & Sharma, 1999; Hautz, Mayer, & Stadler, 2013). If a firm heavily relies on debt, it is prone to be influenced by creditors and this may affect its corporate governance. To control for this potential effect, we include *leverage* operationalized as the firm's debt to equity ratio. Corporate governance processes are affected by *firm size* that we measure as a natural log of the total number of employees in a given year. Large firms tend to be more visible and attract more scrutiny (Okhmatovskiy & David, 2012), but their resources may give them a buffer against shocks induced by corporate scandals. We used a binary variable for *business group affiliation* to code whether the focal firm was affiliated with one of the thirty largest Korean business groups. We also control for *penalty* imposed by two regulatory authorities, namely the Fair Trade Commission (FTC) and the Financial Supervisory Service (FSS). These two governmental agencies monitor, supervise, and penalize organizations for various wrongdoings including accounting fraud, collusion, monopoly power abuse, etc. Change of controlling owner(s) is often associated with the replacement of top managers and with the establishment of new governance structures. To capture this effect, we include *change of controlling owner* variable indicating whether the controlling owner has

changed from time *t*-1 to time *t*. *Cross-listing* may affect corporate governance by bonding the firm by the rules of (often more demanding) foreign stock markets. This variable captures whether the focal firm has its stocks listed at foreign stock exchanges in a given year. We also include year dummies and industry dummies in all our models. We applied one-year time lag for all independent and control variables to make sure that firms' responsive actions are taken after the publication of negative media reports.

Even though our observation window covers eight years (from 2006 to 2013), due to one-year time lag between our covariates and dependent variables, the data matrix used in our analysis covers seven years. From 110 firms included in our sample, 16 were publicly listed after 2006 and do not have data for the early years of our observation period, thereby reducing our dataset from 770 to 723 firm-year observations. With 15 variables used in our analysis, this yields 10,845 data entries. When certain data were not available in the primary source, we used companies' annual reports to obtain the missing data. As a result, we have unbalanced but complete panel data for the firms from our sample.

Analytic approach. To analyze the panel data that contain multiple observations for every firm, we use the generalized estimating equations (GEE) approach (Liang & Zeger, 1986). This method has been used in prior studies with panel data (e.g., Chartergee & Hambrick, 2007; Quigley & Hambrick, 2012) to account for the correlation of error terms arising from repeated observation of the same firms. We also tried alternative analytic approaches to check the robustness of our results. In particular, we tried a random-effects generalized least squares (GLS) regression model (the random-effects model was chosen over the fixed-effects model based on the Hausman test) and seemingly unrelated regression (SUR) analysis that controls for cross-equation contemporaneous correlations (Zellner, 1962). Furthermore, we used a generalized

method of moments (GMM) approach (Arellano & Bond, 1991) to account for potential endogeneity by using lagged dependent and independent variables as instruments (Betschinger, 2015). GMM estimators address unknown heteroscedasticity and potential autocorrelation (Alessandri & Seth, 2014), but the downside of this approach is that using lagged variables as instruments reduces the number of observations included in the analysis. The results obtained with these robustness checks replicate the relationships between independent and dependent variables revealed in the reported GEE models.

Results

Table 1 presents descriptive statistics for our sample. Table 2 presents the results of GEE regressions estimating the effects of our covariates on *CEO replacement,* Table 3 presents the results of GEE regressions for *executive replacement,* and Table 4 presents the results of GEE regressions estimating the effect of our covariates on *establishment of new governance structures*. In Tables 2-4, the first model includes all control variables. According to Model 1 of Table 2, organizational size and business group affiliation are positively associated with CEO replacement ($p<.05$). In addition, family ownership shows negative impact on CEO replacement while the impact size was marginally significant ($p<.10$). Model 1 of Table 3 shows that family ownership and leverage are negatively related to executive replacement, but organizational size is positively associated with executive replacement. In the same model, foreign ownership, one of our moderating variables, shows negative direct impact on executive replacement. Model 1 of Table 4 shows that organizational size is positively associated with establishment of new governance structures ($p<.001$), while ROE, cross-listing, change of controlling owner, and business group affiliation are negatively associated with establishment of new governance structures ($p<.05$). In addition, leverage shows significant negative impact ($p<.001$), while

family ownership shows marginally significant positive impact (*p*<.10) on the establishment of new governance structures. In Model 2 of Table 2 we include our two independent variables – organizational corruption and mistreatment of business stakeholders. As predicted by Hypothesis 1, the disclosure of information about organizational corruption is positively associated with CEO replacement (*p*<.01). We also tested the relationship between organizational corruption and executive replacement - the result in Model 2 of Table 3 yields support for Hypothesis 1 as well (*p*<.01). Both results confirm our Hypothesis 1 that disclosure of information on organizational corruption is associated with the replacement of key decision-makers. According to Model 2 of Table 4, media reports about mistreatment of business stakeholders are positively and significantly related to the establishment of new governance structures (*p*<.01), supporting Hypothesis 2. In sum, we have found that organizational corruption is associated with the replacement of key personnel (CEO and top executives), while stakeholder mistreatment is associated with the establishment of new governance structures. As presented in all models, no impact has been found between organizational corruption and the establishment of new governance structures or between stakeholder mistreatment and the replacement of key personnel.

INSERT TABLES 1 - 4 ABOUT HERE

We furthermore tested the moderating effects of foreign and state ownership. While Model 3 of Table 2 shows that foreign ownership does not have a significant effect on the relationship between organizational corruption and CEO replacement, Model 3 of Table 3 yields support for our prediction that foreign ownership positively moderates the relationship between organizational corruption and executive replacement (*p*<.01), providing partial support for

Hypothesis 3a. Although a firm experiencing negative publicity regarding organizational corruption tends to replace its CEO and other executives, foreign ownership strengthens this tendency only for the broadly defined *executive replacement*. In Model 4 of Tables 2 and 3, state ownership has significant negative moderating effect on the relationship between corruption and CEO replacement / executive replacement ($p<.05$). These results provide support for our Hypotheses 4a: state ownership weakens the impact of organizational corruption on the replacement of individuals involved in the governance process. Interaction plots in Appendix B illustrate the effects of organizational corruption and foreign / state ownership on CEO and executive replacement.

According to Model 3 of Table 4, Hypothesis 3b that foreign ownership strengthens the relationship between mistreatment of business stakeholders and establishment of new governance structures does not receive support. Model 4 of Table 4 demonstrates that, similar to the case of foreign ownership, the moderating effect of state ownership is non-significant and thus Hypothesis 4b is not supported.

Discussion

Our findings provide general support for the argument that after a disclosure of organizational corruption, firms tend to replace key individuals involved in the governance process. We also find that after a disclosure of business stakeholder mistreatment, firms change how the governance process is organized by adopting new governance structures.

The absence of certain relationships also tells us something interesting. The lack of statistically significant relationships between organizational corruption and new governance structures suggests that new governance structures are perceived as having limited effectiveness in preventing future instances of corruption. We also find that a disclosure of stakeholder

mistreatment is not associated with replacing key decision-makers involved in the governance process. Apparently, organizations consider the replacement of key decision-makers as a too radical response to media reports about disrespecting interests of certain stakeholders. These results reveal that organizations try to restore damaged trust by initiating corporate governance changes that correspond to the nature of negative events reported by the media.

In addition, our results show that foreign ownership is likely to strengthen and state ownership weakens the relationship between negative media reports and the replacement of individuals making governance decisions. We find that the positive moderating effect of foreign ownership is significant only for *executive replacement* but not for *CEO replacement.* It is possible that the effect of foreign ownership is weakened by the language barrier in access to the Korean media, but it is less likely to be an issue for institutional investors, especially, if they have offices in Korea. Another possible explanation for this finding is that in making critical decisions about CEO replacement, controlling shareholders are less likely to take into account the position of foreign investors. At the same time, the moderating effects of state ownership are significant for both *CEO replacement* and *executive replacement*, thus demonstrating strong influence of state ownership. Ownership variables do not have significant moderating effects on the establishment of new governance structures and one possible interpretation of this result is that the firm's treatment of other stakeholders is not considered as a matter of high importance by state shareholders and foreign shareholders.

Our analysis continues the stream of studies that apply theories developed in research about interpersonal trust to analyze trust in organizations (Gillespie & Dietz, 2009; Kramer & Lewicki, 2010; Bachmann et al., 2015). In particular, we bring the trust perspective into corporate governance research to analyze changes in governance initiated by companies in response to

negative media reports. Recently, a number of studies considered corporate governance changes triggered by negative publicity as a process of reputation repair or impression management (Westphal & Graebner, 2010; Gomulya & Boeker, 2014; Gangloff, Connelly, & Shook, 2016). These approaches imply that corporate governance changes initiated by organizations are mostly ceremonial and frequently decoupled from substantive changes (Westphal & Zajac, 1998; 2001). In contrast, the trust perspective accommodates the possibility that organizations make substantive changes and at the same time try to make these changes visible in order to restore trust of stakeholders. Corporate governance changes that we analyze in our study are directed both internally (to change how the organization is governed) and externally (to change how the organization is perceived). The reorganization of the governance process as well as the replacement of individuals involved in this process are likely to have material consequences and also to be visible to stakeholders – both conditions are important for effective trust repair.

In research on corporate governance, the concept of trust does not figure prominently yet, even though in some other fields (e.g., in the literature on contracts), the concept of trust and theories of trust are used very frequently. When the concept of trust is used in the corporate governance literature, it is usually to describe an alternative to close monitoring of (presumably, opportunistic) management prescribed by the agency theory (e.g., Larcker & Tayan, 2013). Our focus, however, is on trust in the relationships of the firm with its external stakeholders, including its existing and potential shareholders. Corporate governance plays an important trust-generating function in these relationships. Firms cannot function without trust of investors and other stakeholders - unless a sufficient degree of trust is present, these stakeholders would be reluctant to provide the inputs needed by the firm (capital, labor, demand for products, etc.). Certification and audit by independent external parties have been described as trust-generating

mechanisms (Zucker, 1986; Bachmann & Inkpen, 2011); we suggest that internal corporate governance mechanisms, such as the board of directors, also generate trust of stakeholders. Shareholders would be reluctant to invest their money if corporate governance mechanisms were absent or dysfunctional; in contrast, when effective corporate governance mechanisms are in place, shareholders are more likely to trust their savings to the firm even when these shareholders are not involved in the governance process. Sometimes these trust-generating mechanisms are abused by firms to mislead external stakeholders (e.g., getting certifications without rigorous examinations or using rubber-stamp boards of directors). If these abuses become common, the corresponding trust-generating mechanisms may be discredited, but these mechanisms are abused precisely because they potentially can generate trust.

Acknowledging the importance of this trust-generating function implies that we need to evaluate the effectiveness of corporate governance not only in monitoring and incentive alignment, but also in sending reassuring signals to external stakeholders. Correspondingly, we need to study when it is particularly important for firms to signal the diligence of their corporate governance, which signals would be most relevant in different situations, and what makes these signals effective in generating stakeholders' trust. With this study, we make the first steps in exploring the trust-generating function of corporate governance and also delineate the areas for further research on this topic.

Recently, several studies have considered media as a corporate governance mechanism (Bednar, 2012; Aguilera et al., 2015). We contribute to the analysis of the role that media play in corporate governance by demonstrating that media reports act as a trigger for corporate governance changes. This empirical regularity shows the strong impact of media but also makes us suspect that organizations initiate expected changes without evaluating whether these would

be the most effective solutions. In particular, the replacement of executives after media reports about organizational corruption might be positively perceived by investors and other stakeholders, but this response may not be the most effective solution if corrupt behavior is encouraged by strong pressures on executives. In this case, more systemic changes in how the company is operated and governed are needed to ensure that newly appointed executives do not end up engaging in corrupt practices.

While our study is explicitly focused on corporate governance, the analysis of organizational changes as efforts to repair trust of stakeholders would also be relevant in other contexts – for example, in studies of CSR initiatives. We believe that our conceptual framework can be applied across various domains where it is important for organizations to maintain trust of stakeholders.

The current paper has some limitations that suggest avenues for future research. First, we focus on the factors predicting the choice of responses to trust-damaging information and do not consider consequences of these organizational responses. It would be important to examine in future research how stakeholders' perceptions of organizational trustworthiness are impacted by these responses. In particular, we encourage conducting survey studies that can directly ask questions about respondents' perception of organizational integrity and benevolence to identify how these perceptions are affected by changes in how organizations are governed. Second, we focus on substantive organizational responses to trust-damaging information and do not consider communicative tactics (e.g. apology, denial, excuse, and reticence) in our analysis. Prior studies have demonstrated the effectiveness of communication when facing negative events that threaten organizational legitimacy (e.g., Elsbach, 1994). Studying combinations of communicative responses with corporate governance changes could be a potentially interesting avenue for future research. Third, our analysis has been focused on how organizations change themselves to regain

trust of stakeholders. However, organizations may also take actions intended to reduce damage done to certain stakeholders or to provide some compensation for this damage (Dirks et al., 2009). Tracing both corporate governance changes and corrective actions that should benefit certain stakeholders can provide a more comprehensive picture of how organizations respond to trust-damaging information. Finally, we expect that social context will affect the choice of organizational responses to negative publicity. Prior research suggests that organizations are under less pressure to take corrective actions when transgressions are more common, such as in emerging markets. It is also possible that the variation in responses to trust-damaging information is decreasing over time as certain responses are institutionalized and become standard. Future research may explore how transgressions and corrective actions of peer organizations may affect the trust-repair responses chosen by the focal organization. The effect of context can be further explored in cross-national studies that would consider whether in different countries organizations tend to initiate different corporate governance changes as responses to trust-damaging information.

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Table 1. Descriptive Statistics and Correlations

		Mean	SD	1	2	3	4	5	6	7
1.	CEO Replacement	.34	.48	1						
2.	Executive Replacement	.21	.26	.26***	1					
3.	Establishment of New Governance Structures	.12	.49	.02	.02	1				
4.	Organizational Corruption	.10	.30	.06	-.02	-.03	1			
5.	Mistreatment of Business Stakeholders	.12	.33	.05	.01	-.01	.12***	1		
6.	Foreign Ownership	26.03	17.41	-.02	-.03	.00	.03	.11***	1	
7.	State Ownership	6.13	12.04	.02	.15***	.02	.03	.01	-.15***	1
8.	ROE	.25	3.47	.05	-.02	.21***	.00	.09**	-.01	-.01
9.	Family Ownership	28.05	20.01	-.04	-.15**	.00	-.01	.00	-.36**	-.41***
10.	Leverage	176.66	247.44	.04	.07*	-.01	.01	-.12***	-.26***	-.08*
11.	Employee [ln]	7.87	1.68	.09*	.08*	.02	.10**	.24***	-0.05	.00
12.	Business Group Affiliation	.77	.42	.09**	-.03	-.10**	.14***	.03	-0.18***	-.19***
13.	Penalty	.28	.45	.04	.00	.04	.04	.06	0.11**	.02
14.	Change of Controlling Owner	.05	.21	.09**	.15***	.02	.06	.08*	-0.02	.03
15.	Cross-listing	.22	.42	.05	.05	-.03	.08*	.18***	0.11***	0.18***

*** p<0.001, ** p<0.01, * p<0.05, † p<0.1. N=110. K=10,845

Table 1. Descriptive Statistics and Correlations (Continued)

		8	9	10	11	12	13	14	15
8.	ROE	1							
9.	Family Ownership	.04	1						
10.	Leverage	-.02	-.08*	1					
11.	Employee [ln]	.01	-.08*	-.19***	1				
12.	Business Group Affiliation	-.07	.38***	-.06	.30***	1			
13.	Penalty	.06	-.07*	.06	.00	.02	1		
14.	Change of Controlling Owner	.01	-.07*	-.02	.03	-.06	.03	1	
15.	Cross-listing	-.02	.26***	-.05	.33***	.03	.12***	.03	1

*** p<0.001, ** p<0.01, * p<0.05, † p<0.1. N=110. K=10,845

Table 2. Results of GEE Regression Analysis with CEO Replacement as Dependent Variable

Variable	Model 1	Model 2	Model 3	Model 4
Organizational		0.76**	0.55	0.93**
Corruption		(0.26)	(0.56)	(0.30)
Mistreatment of		0.21	0.19	0.20
Business Stakeholders		(0.24)	(0.23)	(0.24)
Organizational Corruption			-0.01	
× Foreign Ownership			(0.02)	
Organizational Corruption				-0.03*
× State Ownership				(0.01)
ROE	0.01	0.00	0.00	0.00
	(0.01)	(0.01)	(0.01)	(0.01)
Foreign Ownership	-0.00	-0.00	-0.00	-0.00
	(0.01)	(0.01)	(0.01)	(0.01)
State Ownership	-0.00	-0.01	-0.01	-0.00
	(0.01)	(0.01)	(0.01)	(0.01)
Family Ownership	-0.01†	-0.01†	-0.01†	-0.01†
	(0.01)	(0.01)	(0.01)	(0.01)
Leverage	-0.00	-0.00	-0.00	-0.00
	(0.00)	(0.00)	(0.00)	(0.00)
Employee [*ln*]	0.15*	0.13*	0.12*	0.13*
	(0.07)	(0.06)	(0.06)	(0.06)
Business Group Affiliation	0.55*	0.45†	0.45†	0.47*
	(0.26)	(0.25)	(0.25)	(0.26)
Penalty	0.01	-0.03	-0.03	-0.01
	(0.17)	(0.18)	(0.18)	(0.18)
Change of Controlling	1.22	1.02	1.06	1.15
Owner	(1.20)	(1.21)	(1.21)	(1.25)
Cross-listing	0.09	0.06	0.06	0.06
	(0.23)	(0.23)	(0.23)	(0.22)
Year Dummy	Yes	Yes	Yes	Yes
Industry Dummy	Yes	Yes	Yes	Yes
Number of Observations	723	723	723	723
Number of Groups	110	110	110	110
Wald $\chi 2$	45.33**	49.50**	50.40**	50.91**

Standard errors are shown in parentheses. *** p<0.001, ** p<0.01, * p<0.05, † p<0.1

Table 3. Results of GEE Regression Analysis with Executive Replacement as Dependent Variable

Variable	**Model 1**	**Model 2**	**Model 3**	**Model 4**
Organizational		0.39**	-0.20	0.57***
Corruption		(0.12)	(0.21)	(0.13)
Mistreatment of		0.10	0.08	0.11
Business Stakeholders		(0.15)	(0.15)	(0.15)
Organizational Corruption			0.02**	
× Foreign Ownership			(0.01)	
Organizational Corruption				-0.02*
× State Ownership				(0.01)
ROE	-0.01	-0.01	-0.02	-0.01
	(0.05)	(0.05)	(0.05)	(0.04)
Foreign Ownership	-0.01**	-0.01**	-0.01***	-0.01**
	(0.00)	(0.00)	(0.00)	(0.00)
State Ownership	-0.00	-0.00	-0.00	0.00
	(0.00)	(0.00)	(0.00)	(0.00)
Family Ownership	-0.01***	-0.01***	-0.01***	-0.01***
	(0.00)	(0.00)	(0.00)	(0.00)
Leverage	-0.00**	-0.00**	-0.00**	-0.00**
	(0.00)	(0.00)	(0.00)	(0.00)
Employee [*ln*]	0.11**	0.11**	0.09*	0.11**
	(0.04)	(0.04)	(0.04)	(0.04)
Business Group Affiliation	0.03	-0.05	-0.06	-0.02
	(0.16)	(0.17)	(0.16)	(0.18)
Penalty	0.04	0.05	0.06	0.06
	(0.10)	(0.09)	(0.09)	(0.09)
Change of Controlling	-0.65	-0.78	-0.86	-0.70
Owner	(0.54)	(0.54)	(0.62)	(0.60)
Cross-listing	-0.10	-0.13	-0.09	-0.13
	(0.13)	(0.14)	(0.13)	(0.13)
Year Dummy	Yes	Yes	Yes	Yes
Industry Dummy	Yes	Yes	Yes	Yes
Number of Observations	723	723	723	723
Number of Groups	110	110	110	110
Wald $\chi 2$	145.80***	153.53***	195.16***	194.67***

Standard errors are shown in parentheses. *** p<0.001, ** p<0.01, * p<0.05, † p<0.1

Table 4. Results of GEE Regression Analysis with Establishment of New Governance Structures as Dependent Variable

Variable	**Model 1**	**Model 2**	**Model 3**	**Model 4**
Organizational		0.02	-0.01	0.01
Corruption		(0.05)	(0.10)	(0.05)
Mistreatment of		0.20**	0.20**	0.20**
Business Stakeholders		(0.07)	(0.07)	(0.07)
Mistreatment of Business Stakeholders			0.00	
× Foreign Ownership			(0.00)	
Mistreatment of Business Stakeholders				0.00
× State Ownership				(0.00)
ROE	-0.00*	-0.00**	-0.00**	-0.00**
	(0.00)	(0.00)	(0.00)	(0.00)
Foreign Ownership	-0.00	-0.00	-0.00	-0.00
	(0.00)	(0.00)	(0.00)	(0.00)
State Ownership	0.00	0.00	0.00	0.00
	(0.00)	(0.00)	(0.00)	(0.00)
Family Ownership	0.00†	0.00	0.00	0.00
	(0.00)	(0.00)	(0.00)	(0.00)
Leverage	-0.00***	-0.00***	-0.00***	-0.00***
	(0.00)	(0.00)	(0.00)	(0.00)
Employee [*ln*]	0.06***	0.04**	0.04**	0.04**
	(0.01)	(0.13)	(0.01)	(0.01)
Business Group Affiliation	-0.16*	-0.14*	-0.15*	-0.15*
	(0.07)	(0.06)	(0.06)	(0.06)
Penalty	-0.05	-0.06†	-0.06†	-0.06†
	(0.03)	(0.03)	(0.03)	(0.03)
Change of Controlling Owner	-0.10*	-0.11*	-0.10*	-0.12*
	(0.04)	(0.05)	(0.05)	(0.05)
Cross-listing	-0.10*	-0.12**	-0.12**	-0.12**
	(0.04)	(0.04)	(0.04)	(0.04)
Year Dummy	Yes	Yes	Yes	Yes
Industry Dummy	Yes	Yes	Yes	Yes
Number of Observations	722	722	722	722
Number of Groups	110	110	110	110
Wald $\chi 2$	73.12***	73.59***	77.84***	77.17***

Standard errors are shown in parentheses. *** p<0.001, ** p<0.01, * p<0.05, † p<0.1

Figure 1. Threats to Trustworthiness and Trust-Repair Approaches

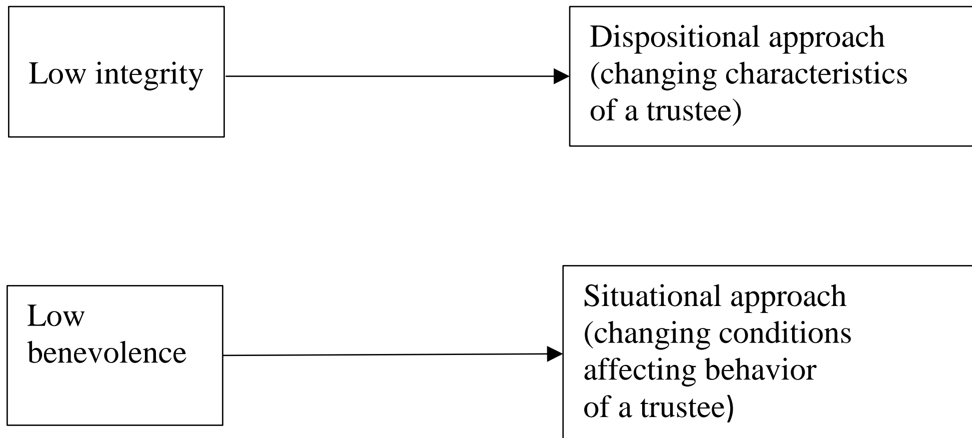
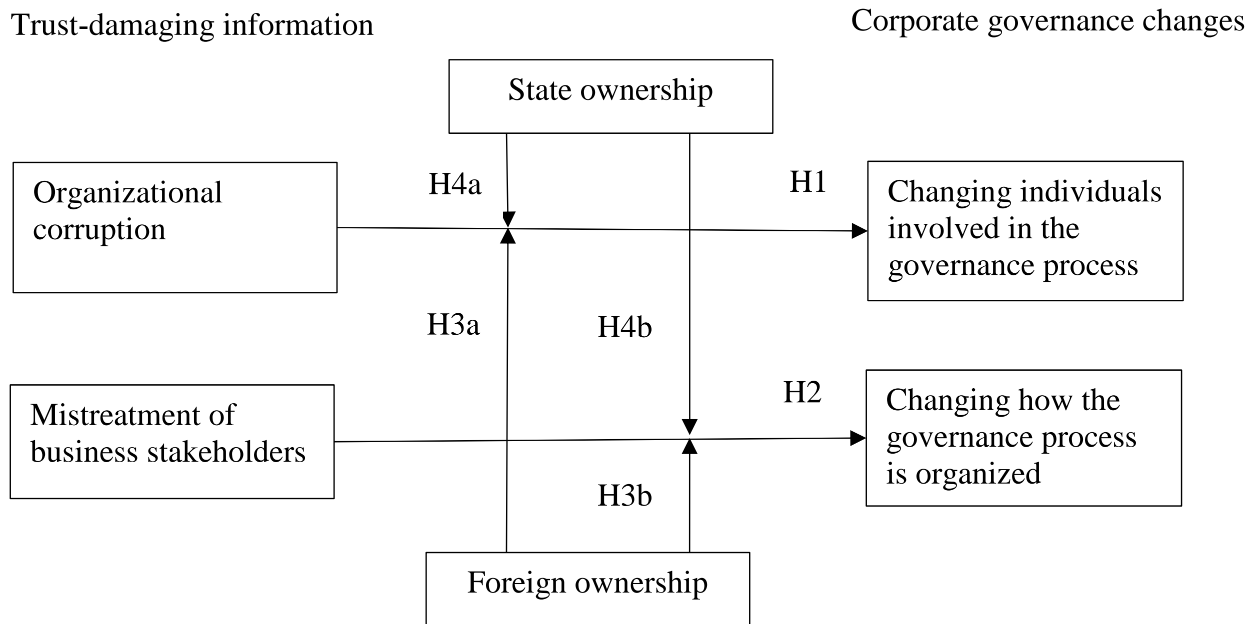


Figure 2. Trust-Damaging Information and Corporate Governance Changes

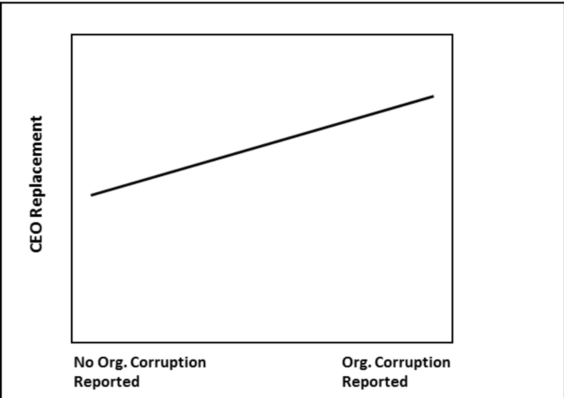


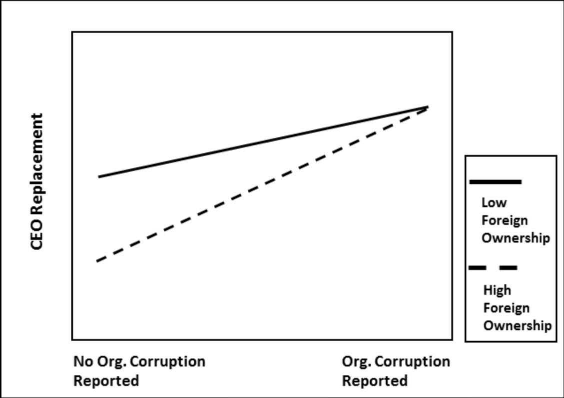
Appendix A. Examples of Negative Media Reports

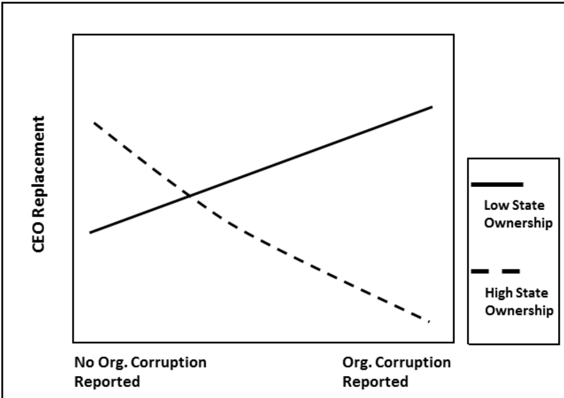
Organizational Corruption	Mistreatment of Business Stakeholders
The prosecution enforced search and seizer of Hyundai Kia Motors Group to investigate illegal fundraising and bribing high-rank public officials. The company also lobbied high-rank officials to gain construction consent of its building. (Hankyoreh, Mar. 31, 2006)	Fair Trade Commission fined Hyundai Motors Company $200 million for forcing its dealers to achieve a high sales target. (Kyunghyang Shinmun, Jan. 8, 2008)
An attorney Mr. Yong Chul Kim, a whistle-blower who had worked for Samsung Group as a chief of legal team, disclosed Samsung C&T's illegal fundraising of $200 million that involved its foreign subsidiaries and accounting fraud. (Hankyoreh, Nov. 26, 2007)	Naver Corporation, the largest internet content provider and web-surfing engine in South Korea, is accused of fabricating its retrieval ranking thus misleading users and business partners. (Kyunghyang Shinmun, Sept. 14, 2012)
The CEO of Korea Express company, a logistics company affiliated to Kumho Group, was arrested on a warrant for embezzling $10 million of the company's fund. The prosecution investigated whether the embezzled money was used to bribe politicians or high-ranking public officials. (Asia Business Daily, Sep. 29, 2009)	E-Mart Company has kept watch on its employees' union establishment activities in order to obstruct them. According to the internal documents, the company organized a response team to monitor and to obstruct the establishment of a union by inducing employees not to join the union. (Hankyoreh, Jan. 20, 2013)
Choi Tae-won, the chairman of SK Corporation, was accused of embezzlement of $40 million to cover up personal trading losses. (Donga.com Dec. 17, 2011)	An employee of Namyang Dairy Products Company abused a shop owner by requesting to accept excessive inventory burden and the low-selling products that the shop owner did not order from the company. (Kyunghyang Shinmun, May 6, 2013)
The prosecution enforced search and seizer of Shinsegae Group to investigate the illegal support of affiliated companies by the top management team. The company was accused by civil associations for its illegal support of affiliated companies and Fair Trade Commission fined the company. (Hankyoreh, Nov. 29, 2012)	POSCO Corporation, the largest steel-making company in South Korea, pressured its employees to change their affiliation to the company's outsourced supplier. The employees filed lawsuits and claimed that the company deceived them to persuade employees to change jobs. (Hankyoreh, Jun. 5, 2013)
Lee Jay Hyun, the CEO of CJ Group, was arrested on a warrant for tax evasion and embezzlement of $200 million. (Kyunghyang Shinmun Jul. 1, 2013)	Nongshim Company, a food and beverage company, exerted pressures on its agencies to meet the unrealistic sales target. The contract between Nongshim and agencies was an extreme case of one-sided bargain, exclusively beneficial to Nongshim. (Hankyoreh, Jun. 26, 2013)

Appendix B. The Effect of Organizational Corruption and Foreign / State Ownership on CEO Replacement and Executive Replacement

Dependent Variable: CEO Replacement







Dependent Variable: Executive Replacement