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ESSAYS ON ANTI-CORRUPTION DISCLOSURE

Doctoral Thesis in Business and Management Sciences

Specialization in Accounting and Management Control

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Author's Biography

Renata Blanc was born in Coimbra, Portugal, but soon moved to Porto, where she presently lives. Renata finished her undergraduate studies in Economics in 1999 at FEP – School of Economics and Management and joined Arthur Andersen as an auditor and management consultant for a wide variety of industries. After five years working for Arthur Andersen (by then Deloitte) Renata decided to take an MBA followed by a Master Degree at Porto Business School.

After finishing these postgraduate studies, Renata joined a management consulting career at Porto Business School and started an academic career as Lecturer at FEP-School of Economics and Management, teaching in the fields of Accounting and Management Accounting, subjects that she still teaches today.

Since 2007, Renata coaches FEP and Porto Business School teams competing at several International Business Case competitions. In 2013 she received the Pierre Brunet Best Coach Award at the John Molson MBA International Case Competition (Montreal, Canada). These experiences at international business case competitions initiated Renata into new fields of teaching. In 2011 she created a Business Case Analysis course for the undergraduate and master levels and in 2012 she started lecturing in the field of Entrepreneurship.

Besides teaching at FEP, Renata is a Lecturer at Porto Business School where she teaches in the full-time Magellan MBA and in several executive education programs.

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List of Abbreviations

AC - Anti-corruption

AR – Annual Report

AT – Agency Theory

CEO – Chief Executive Officer

CG – Corporate Governance

CSD - Corporate Social Disclosure

CSR – Corporate Social Rsponsibility

CSER - Corporate Social and Environmental Research

CSR - Corporate Social Responsibility

GRI – Global Reporting Initiative

IGO – International Governmental Organization

NGO – Non-Governmental Organization

RDT – Resource Dependence Theory

SAT – Stakeholder-Agency Theory

SEC – Security and Exchanges Commission

SR – Sustainability Report

TI - Transparency International

UNGC - United Nations Global Compact

Abstract

This thesis is composed of three papers aimed at better understanding corporate anti-corruption disclosure (hereafter AC disclosure), a relevant, topical, and under-researched theme.

The first paper provides an examination of changes in compliance and the fight against corruption at Siemens A.G. over a period of 11 years during which a major corruption scandal occurred. Results, which are aligned with legitimacy and media agenda setting theories, show that Siemens engaged in substantive and symbolic disclosure strategies in response to increased levels of media attention. The second paper provides an analysis of the impact of board characteristics on AC disclosure in large multinational companies. Results support the arguments of stakeholder-agency and resource dependence theories in that firm with more board resources in terms of having higher levels of independence and diversity provide higher levels of AC disclosure. The third paper builds on prior studies of the market reaction of environmental events by analysing the investor response to the release of Transparency International's 2012 and 2014 "Transparency in Corporate Reporting: Assessing the World's Largest Companies" reports. Focusing on U.S companies, the study documents a significant negative market reaction to the first report release. Further, for both events, companies with better AC disclosure suffered significantly less negative market adjustments, providing evidence that investors are savvy to the regulatory cost exposures of the corruption issue.

At the theoretical level, this thesis shows that theories previously applied to mostly environmental-themed studies are useful in explaining AC disclosure. Empirically, the studies provide evidence allowing for a better understanding of AC disclosure practices, causes, and consequences. This thesis adds to the scarce literature on corporate AC disclosure and provides useful insights for stakeholders directly or indirectly influenced by the corporate fight against corruption.

Resumo

Esta tese, composta por três artigos, tem como principal objectivo proporcionar uma melhor compreensão acerca da divulgação de informação sobre anti-corrupção (DAC), um tema relevante, tempestivo e pouco tratado na literatura.

O primeiro artigo consiste numa análise das mudanças de divulgação de informação sobre *compliance* e anti-corrupção na Siemens ao longo de um período de onze anos durante o qual a empresa enfrentou um escândalo de corrupção. Os resultados, alinhados com a *legitimacy theory* e *media agenda setting theory*, indicam que a Siemens prosseguiu estratégias simbólicas e substantivas de divulgação de informação como resposta à atenção dedicada pelos media àquele evento. O segundo artigo consiste numa análise do impacto das características dos conselhos de administração (CA) sobre a DAC. Os resultados, alinhados com argumentos da *stakeholder agency theory* e da *resource dependence theory*, evidenciam que empresas cujo CA é caracterizado por maior independência e diversidade apresentam maior DAC. O terceiro artigo é uma extensão de investigação passada sobre a reação do mercado a eventos ambientais e consiste na análise da reação à divulgação dos relatórios "Transparency in Corporate Reporting: Assessing the World's Largest Companies", emitidos pela Transparência Internacional em 2012 e 2014. O estudo, centrado em empresas americanas, documenta uma reação negativa à divulgação do primeiro relatório. Adicionalmente verifica-se, para os dois anos, que empresas com maior DAC sofrem reações de mercado significativamente menos negativas, o que indicia sensibilidade dos investidores aos custos regulatórios associados a uma maior exposição a questões de corrupção.

Ao nível teórico, esta tese demonstra a aplicabilidade à DAC, de teorias previamente aplicadas à divulgação de matérias sociais e ambientais. Em termos empíricos, fornece evidência útil para uma melhor compreensão das práticas, causas e consequências da DAC. Esta tese acrescenta à escassa literatura sobre DAC e proporciona informação útil para *stakeholders* direta ou indiretamente influenciados pela luta corporativa contra a corrupção.

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To my mother Manuela,

CHAPTER 1

1. INTRODUCTION

1.1. Introduction

In the first decade of the 21st century, a wide range of corporate scandals opened the world's eyes to greed, corruption and business fraud (UNGC, 2015). Although in existence for a long time (Ashforth and Gibbs, 1990; Aguilera and Vadera, 2008), concern with corruption has had a dramatic ascendance over the past two decades and is becoming one of today's most pressing global and ethical problems (Sanyal and Samanta, 2004; Everett et al., 2006; UNGC, 2015) and a major social issue (Ashforth et al., 2008). Studies indicate that corruption is widespread in international business (Hauser and Hogenacker, 2014). According to the UNGC (2015, p.164) if corruption was an industry, it would be the third world's largest, corresponding to 5% of global GDP or to USD 3 trillion. Fighting corruption has become an integral part of any company's social responsibility (Branco and Delgado, 2012) and it is already considered one of the essential pillars of corporate social responsibility (CSR) (KPMG, 2013). There are many ways to fight corruption but transparency, which is defined by Vishwanath and Kaufmann (1999) as timely, reliable economic, social and political information which is accessible to all stakeholders, is considered one of the most important (Klitgaard, 1998; Halter et al., 2009). This thesis aims at a better understanding of transparency regarding corporate anti-corruption disclosure (hereafter AC disclosure) and on the causes and consequences of that type of social disclosure.

1.1.1. A brief overview of corruption

Corruption has many times been justified as a means to the greater goal of creation of economic value, as an unpleasant but necessary response to the weakness and venality of governments (Rose-Ackerman, 2002), as a way to avoid bureaucratic delays and to motivate bureaucrats to a more efficient work (Mauro, 1995), or as an instrument to create an opportunity for ensuring the legitimacy of firms entering foreign markets (Ahlstrom et al., 2008). Despite that positive view of corruption, there has been an intensified awareness among the general public about its negative consequences for economic and social development (Hauser and Hogenacker, 2014). According to Hills et al. (2009, p.2), corruption is a bottom line issue that affects companies' ability to compete through increased operational costs and greater exposure to legal and competitive risks. Further, corruption cheats disadvantaged populations by diverting

resources for critical services like education, clean water, and health care into the pockets of dishonest government officials. Besides causing huge development and economic costs, corruption erodes governance and trust, and provides fertile ground for social upheaval and extremism (UNGC, 2015, p. 38).

Corruption cannot be easily defined as it assumes myriad forms (Wang and Rosenau, 2001; Zarb, 2011). For many years, corruption was viewed almost exclusively as related to the behaviour of public officers, and existing definitions exhibited that public focus: "the abuse of public office for private gain" (World Bank, 1997); "acts in which the power of public office is used for personal gain in a manner that contravenes the rules of the game" (Jain, 2001); "illegal payments to a public agent to obtain a benefit that may or not be deserved in the absence of payoffs" (Rose-Ackerman, 1997); "the sale by government officials of government property for personal gain" (Shleifer and Vishny, 1993). Aligned with this view, much of the literature on corruption in the social sciences focuses on the public sector (Doh et al., 2003; Hodgson and Shuxia, 2007) with less attention directed to the private sector (Gopinath, 2008; Branco and Delgado, 2012). Although the private sector played an important role in the check of the arbitrary exercise of power by the government (Pleskovic and Stiglitz, 1997), it was rarely viewed as a source of analysis alone. This bias may be due to the utilitarian economical mainstream prejudice against state activity (Hodgson and Shuxia, 2007), or the common assumption of more efficient behaviour in the private sector with inherently fewer incentives for harmful conduct (Argandoña, 2003). Additionally, largely because of data limitations, research on corruption was mostly performed at the country as opposed to the firm level (Healy and Serafeim, 2015).

Corruption affects private and public organizations alike (Breit, 2010), so focusing exclusively on the public sector and at a country level provided only a limited perception of the phenomenon. Today, the definition of corruption has become more inclusive. For example, Transparency International (TI) defines corruption as "the use of entrusted power for private gain", a definition that includes both corporate and public corruption. In academic literature, the number of studies focusing on the private side of corruption has also been increasing (Aguilera and Vadera, 2008; Gopinath, 2008; Halter et al., 2009; Dion, 2010), but firm level studies still remain a relatively underexplored area of research (Gopinath, 2008; Hauser and Hogenacker, 2014; Jong and Ees, 2014;

Healy and Serafeim, 2015).

Hills et al. (2009) assert that corporations are the typical source of bribes, and accordingly, an important component in the corruption problem. Furthermore, Healy and Serafeim (2015) argue that it is at the company level where most corruption questions remain unanswered. The recent corporate scandals involving large multinational companies including Enron, Worldcom, Parmalat, and others (Hodgson and Shuxia, 2007; Choudhary, 2012) has brought to light corruption within organizations and provide additional evidence of why corruption should not be confined to the public or country levels (Hodgson and Shuxia, 2007).

1.1.2. Negative effects of corruption to corporations

There is a strong business case encouraging companies to fight corruption (Hess, 2009) because it may directly and indirectly affect firm profits. Several studies show that corruption has a negative impact on sales (Gaviria, 2002; World Bank, 2003), and that it may be associated with increased operational costs (Errath et al., 2005). Corruption also leads to costs associated with managerial misconduct resulting from the lower regulatory oversight typical in corrupted organizations (Jensen and Meckling, 1976). These costs include bribes, penalties, and fines (Argandoña, 2001; Doh et al., 2003). Furthermore, corruption is related to reputational, legal, and competitive risks (Hess, 2009). Companies that are engaged in unethical business practices are exposed to serious reputational risks and in many cases face negative consequences just from being accused of corruption-related infringements (Hills et al., 2009). Organizational corruption prevents companies from fulfilling its objectives (Hodgson and Shuxia, 2007), yet in many organizations it is still viewed as a short term competitive necessity (Hess, 2009).

Despite its negative impacts, implementing measures to deter corruption seems almost as difficult as providing a definition of the phenomenon (Zarb, 2011). Transparency regarding anti-corruption is considered by many one of the most important ways to fight corruption (Wilkinson, 2006; Halter et al., 2009; Transparency International, 2009; UNGC, 2009) and it is the focus of this thesis.

1.2. Corporate AC Disclosure, the research topic

Several institutions believe that the degree of reporting on anti-corruption can be a strong indicator of the quality and comprehensiveness of a company's efforts in addressing bribery and corruption (Transparency International, 2009; UNGC, 2009). According to Hess (2009), disclosure on corruption serves multiple goals: it helps to provide accountability with respect to performance; it raises public awareness and pressures other companies to adopt AC principles; it serves the goal of organizational learning by providing a deeper understanding of what works in the fight against corruption and which developments are most needed. Disclosure is a way to ensure that managers are held accountable to the public. Disclosure makes corrupting acts more risky and less attractive, cooperation more easy to sustain, and opportunistic rent seeking less likely (Kolstad and Wiig, 2009). It is expected that strengthening AC disclosure decreases the possibility of corruption events, but it also has a reverse side, such as opportunity costs in spending resources in informing the public and relevant stakeholders (Kolstad and Wiig, 2009, p. 525).

Despite the growing pressure of society and governments to increase transparency regarding anti-corruption (Halter et al., 2009) AC disclosure has received much less academic attention than other social responsibility issues such as the environment (Wilkinson, 2006). Justifications for the shortage of attention lie not only on a lack of perception about the importance of such disclosure but also on the secret, hidden nature of corruption which makes the issue sensitive for companies (ibid.). The few studies that have been performed tend to show that AC disclosure is still not satisfactory (Gordon and Wynhoven, 2003; Novethic, 2006; Transparency International, 2009; Branco and Delgado, 2012). Furthermore, most of the existing studies are non-academic and focus on companies' practices without examining the factors influencing it (Branco and Delgado, 2012). To date, only three academic studies (Islam and Mathews, 2009; Dissanayake et al., 2011; Healy and Serafeim, 2015) address practices and/or causes of corporate AC disclosure.

In this thesis, three papers are presented each providing different views of corporate AC disclosure practices, causes, and/or consequences. The first paper offers an analysis of the AC disclosure practices of Siemens AG, a large multinational

company, as a reaction to a major corruption scandal. The second study investigates how board characteristics influence the AC disclosure of large multinational firms. The third paper focuses on a sample of U.S firms and examines the market reaction to the first ever Transparency International firm level report on AC disclosure (and a subsequent update of that report). Detailed motivations for the research are presented in Section 1.3 and Section 1.4 provides a detailed analysis of the thesis structure.

1.3. Motivations for the research

Four main reasons motivated the decision to research AC disclosure at the firm level: the relevance and opportunity of the theme, the deemed interest for a wide range of stakeholders, the present dearth of research, and the increased call for studies about AC disclosure.

Relevance and opportunity of the theme

Though some authors advocate its advantages, the most widely accepted take on corruption is that it is a serious economic, social, political, and moral blight (Argandoña, 2007) with detrimental global effects (UNGC, 2015). Besides being a fascinating and motivating theme, corruption is in the spotlight. Corruption related scandals have risen significantly in the recent past (Wang and Rosenau, 2001) with strong impacts on businesses and society in general (UNGC, 2015). These significant past events have put corruption on the top of the agenda of companies, governments, NGO's and the general public (KPMG, 2011).

It is a theme with a wide stakeholder impact

Strong relationships with stakeholders can only be built if companies deliberately disclose the information stakeholders seek in order to provide reassurance that the firm is trustworthy (Bellver and Kaufmann, 2005, p.9). By providing a better understanding of AC disclosure, its causes, and its consequences, this thesis should prove useful to several key stakeholders.

Corporate disclosure, through regulated financial reports, voluntary communication, or information provided by external intermediaries, is critical for the functioning of capital markets because it helps mitigate existing information and incentive problems (Healy and Palepu, 2001). Corruption-related events may impact cash flows and risk (Lee and Ng, 2006; Hess, 2009), the two main aspects taken into consideration in investment decisions according to classical finance (Aaker and Jacobson, 1987). Additionally, there is a growing concern about the financial impacts of non-financial aspects of business such as corruption. Particularly over the past two decades, investors have increasingly included environmental, social, and governance factors as part of their financial analysis (UNGC, 2015). Hence, understanding the impact of corruption, a socially important issue, will likely be very important for current and potential shareholders.

AC disclosure is often dependent on the discretionary decision of managers, but social issues including corruption are increasingly present in corporate boardrooms (Elkington, 2006). Given their involvement in the decision process regarding what to divulge and when, managers and board members may also benefit from a better understanding of AC disclosure and of factors influencing the practice. If AC disclosure serves to increase learning, as suggested by Hess (2009), understanding how a leading multinational company like Siemens used AC disclosure to deal with a severe corruption-related scandal could provide meaningful insights to managers and board members. Additionally, if managers act as true agents of shareholders, then it may be important for them to understand the wealth effects of AC disclosure. Furthermore, managers today are themselves more exposed to risks, so their compliance and, I argue, disclosure efforts, are not just about protecting the business and its shareholders, but also about protecting themselves (EY, 2014). Understanding practices and incentives regarding AC disclosure is important to guide managers and board members through specific corruption-related events and through their discretionary decisions on the adequate levels of AC practices and disclosure.

Institutions fighting corruption may also benefit from AC disclosure studies because understanding companies' practices, motivations for AC disclosure, and the practice's consequences may help them to identify what works and what doesn't in the

fight against corruption. They can accordingly adjust their efforts to achieve greater success (Wilkinson, 2008).

Present dearth of empirical studies on firm level AC Disclosure

AC disclosure is considered one of the areas in the fight against corruption in need of more development (Hess, 2009). Whereas corporate social disclosure (CSD), in general, has received considerable attention (Frost et al., 2005; Coetzee and van Staden, 2011, p.3), most of the past CSD research focuses on environmental-related topics. Studies of the impact of specific environmental events on CSD (e.g., Patten, 1992; Jantadej and Kent, 1999; Deegan, Rankin and Voght, 2000; Savage, Rowlands and Cataldo, 2000; Cho, 2009) and on the market impacts of environmental CSD (e.g., Blacconiere and Northcut, 1997; Patten and Freedman, 2008; Flammer, 2013) are abundant. There is a consensus that only limited attention has been dedicated to other themes with the social arena (Islam and Mathews, 2009; Coetzee and van Staden, 2011).

Focusing more specifically on corruption, most of the past research is non-academic (Branco and Delgado, 2012), performed at the country level (Svensson, 2000), and focused on the relationship between AC and macro-economic aspects (Healy and Serafeim, 2015), such as growth (Mauro, 1995), economic freedom (Nwabuzor, 2005), political and civil freedom (Svensson, 2000; Svensson, 2005; Baughn et al., 2007), or foreign direct investment (Kwok and Tadesse, 2006). Despite the recent increase of attention regarding the organizational side of corruption (Branco and Delgado, 2012), the firm-level perspective remains a relatively underexplored area of research (Gopinath, 2008; Hauser and Hogenacker, 2014; Jong and Ees, 2014).

Within this domain, most existing studies provide theoretical approaches for a better understanding of corporate corruption (Anand et al., 2004; Argandoña, 2005; Aguilera and Vadera, 2008; Pinto et al., 2008; Jong and Ees, 2014) or relate to corporate corruption only with respect ethics (Zekos, 2004) or to firm performance (Cosenz and Noto, 2014). A few others examine corporate corruption and its relation to the profile of national institutions (Spencer and Gomez, 2011; Jeong and Weiner, 2012), to subsidiaries' practices such as employing a local partner in high corruption risk

countries (Spencer and Gomez, 2011), to companies' bargaining power (Svensson, 2003), and to financial market reactions (Rao and Hamilton, 1996).

With respect to AC disclosure, most past studies consist of surveys produced by professional organizations such as PWC (2008), KPMG (2008), EY (2014) or Dow Jones (2015) and describe companies' practices, but not reasons for, or consequences of, AC disclosure. Most of these non-academic studies show that despite the improvement in companies attempts to address corruption (Dow Jones, 2015), reporting is still not satisfactory (Branco and Delgado, 2012). The limited academic investigations of AC disclosure include Islam et al. (Forthcoming) and Dissanayake et al. (2011), both of which analyse the disclosure practices of telecommunication companies and show an increase in AC disclosure as a consequence of corruption related events which received a significant amount of media attention. A thorough review of the CSR literature indicates that Healy and Serafeim (2005) is the only academic study to date examining the causes and consequences of AC disclosure. Their study provides evidence that firms' self-reported anti-corruption efforts are related to enforcement instruments, monitoring costs, industry and country corruption risks and to greater board independence. They also show that firms with higher AC disclosures have lower subsequent corruption allegations in the media.

Finally, despite the intense debate about whether firms are rewarded by the market for being socially responsible (e.g., Ruf et al., 2001; Patten, 2008; Guidry and Patten, 2010; Clacher and Hagendorff, 2012), relatively little effort has been directed at evaluating corruption and related events' implications in terms of financial performance at the firm-level (Cosenz and Noto, 2014; Donadelli et al., 2014).

Increased claim for AC Disclosure studies

There is a growing call for research into AC disclosure (Branco and Delgado, 2012). Some authors consider that corruption is still a neglected social issue among CSR priorities (Hills et al., 2009) and that CSR issues with a potentially large impact on market functioning, such as corruption, should get a more prominent place on the CSR agenda (Weyzig, 2009). Despite the popularity of the transparency concept, the link between corruption and transparency is far from being thoroughly explored (Kaufmann

and Bellver, 2005; Kolstad and Wiig, 2009). Studies decomposing the generic notion of transparency into specific components so as to provide useful tools for policy advise and interventions are almost non-existent (Kaufmann and Bellver, 2005). Regarding corruption, firm level studies are still at a formative stage, so there are many questions left to answer (Healy and Serafeim, 2015).

1.4. Thesis structure

With the intent to provide a better understanding of AC disclosure and of its causes and consequences, three papers were developed that are believed offer diversity across four main areas: research themes/perspective, data collection methods, methodological approach and theoretical background.

The first paper is presented in Section 2. This paper provides an examination the changes in compliance and AC disclosure practices at Siemens AG—a large German multinational corporation - over a period of 11 years during which a major corruption scandal occurred. Through a content analysis of the company's annual reports and sustainability reports from 2000 to 2011 and under the lens of legitimacy theory and media agenda setting theory, our findings suggest that Siemens changed its compliance and corruption disclosure practices to manage its legitimacy in the wake of the 2006 corruption scandal and in subsequent years. The strategies adopted by Siemens may be described as both symbolic and substantive (Dowling and Pfeffer, 1975; Ashforth and Gibbs, 1990). The implications of this study may be useful for several key societal stakeholders in that they provide additional arguments for the need for better regulations to ensure AC disclosure of relevant, reliable, and consistent corporate information about important social issues such as corruption.

The second paper, presented in Section 3, consists of a study regarding the influence of board characteristics on AC disclosure. Using used data provided by Transparency International about AC disclosure efforts by large multinational firms (Transparency International, 2012) and an ordinal regression this paper analyses the impact of board characteristics on AC disclosure by large multinational firms. The study also considers certain corporate characteristics and the business culture of the country of origin. Based on the analysis that combines stakeholder-agency theory and resource-dependence theory, we suggest that boards characterized by higher levels of

independence, knowledge, and diversity are more likely to present higher levels of AC disclosure than their counterparts. Our findings suggest to some extent that companies with better board resources provide higher levels of AC disclosure. More concretely, results show that boards with a higher proportion of independent members and with more diversity provide higher AC Disclosure. This information could be useful for boards to better understand how their own structure may influence AC disclosure, but even more so for regulators in the sense that it may be necessary to provide additional guidelines regarding board composition to ensure higher levels of AC disclosure.

The third paper, presented in Section 4, provides an analysis of the investor response to the release of TI's 2012 and 2014 "Transparency in Corporate Reporting: Assessing the World's Largest Companies" reports. These were TI's first firm-level reports, and given the organization's standing as a leading contributor to the fight against corruption, it is argued the reports could be expected to potentially increase regulatory cost exposures for affected firms. The study builds on prior U.S.-based studies of market reactions to environmental-related cost inducing events. Focusing on only U.S companies, evidence is provided indicating a significant negative market reaction to the first report release. The mean market response to the 2014 report release was not statistically significant. However, and consistent with the prior environmental-themed studies, we find that differences in political cost exposure, in this case, differences in AC disclosure ratings, appear to impact the market reactions. For each of the report releases, companies with better AC disclosure suffered significantly less negative market adjustments. This study thus provides evidence that investors are savvy to the political cost exposures of the corruption issue.

The three studies use differing theoretical backgrounds, data sources, and methods (see Table 1.1). It is believed that this diversity enriches this thesis and allows for a deeper understanding of the technical, methodological, and theoretical complexities of this specific aspect of CSD.

Table 1.1 - Comparison between the three essays presented in Sections 2 to 4.

	Paper 1 | Chapter 2 (a)	Paper 2 | Chapter 3 (b)	Paper 3 | Chapter 4	**Global Contribution**
Paper Title	"In Search of Disclosure Effects of the Siemens AG'S Corruption Scandal"	"Board characteristics and anti-corruption disclosure in large multinational companies"	"Market reactions to Transparency International Reports on corporate Anti-corruption disclosure"	Evidence presented in Paper 1 shows that Siemens A.G. used symbolic and substantive strategies in an attempt to manage its legitimacy when faced with a severe corruption scandal that raised considerable media attention. Paper 2 demonstrates that boards with better resources in terms of independence, diversity are likely to present higher levels of AC disclosure. Focusing on a sample of U.S companies, paper 3 provides evidence that investors negatively value exposure to potential regulatory costs arising from the release of TI's first firm-level corruption reports.
Purpose	Reaction to a major corruption related event through AC disclosure	Relation between board characteristics and AC disclosure	Financial markets negative reactions to two TI firm level reports in anticipation of increased regulatory costs	
Focus	Analyze company practices when facing a negative event	Analyze board characteristics as a possible cause for higher levels of AC disclosure:	Analyse market consequences of AC disclosure which may be incentives for different future levels of AC disclosure	
Theory	Legitimacy Theory; Media Agenda Setting Theory	Stakeholder Theory and Resource-Dependence Theory	Prior empirical studies on the effect of potential regulatory costs over financial markets	
Data Source	Financial and Sustainability Reports; Factiva Database	Annual Proxy Statements, Company Website; Osiris Database; TI Reports	DATASTREAM; Lexis Nexis Database; Transparency international Reports	
Method	Content Analysis	Ordinal logistic regression	Linear regression; Market model	

(a) Paper presented at French CSEAR Conference - Montpellier 2-3 May 2013; 36th EAA Annual Congress – Paris, 6-8 May 2013; Interdisciplinary Insights on Fraud and Corruption, Porto, 13-15 September, 2012. To be submitted to publication until end of 2015.

(b) Portuguese CSEAR Conference – Leiria, Portugal, 6-7 November 2014; Shadow Economy - Multiple Perspectives of the Shadow Economy, 13-15 September. 2014. Paper submitted to the Journal of Business Ethics.

CHAPTER 2

2. IN SEARCH OF THE DISCLOSURE EFFECTS OF THE SIEMENS A.G. CORRUPTION SCANDAL

IN SEARCH OF THE DISCLOSURE EFFECTS OF THE SIEMENS A.G. CORRUPTION SCANDAL

ABSTRACT

In this study, we examine the changes in disclosure practices at Siemens AG—a large German multinational corporation, on compliance and the fight against corruption over a period of 11 years during which the company faced a major corruption scandal. In 2006 the company was accused of paying an estimated amount of bribes of $1.4 billion (SEC, 2008). This particular scandal led to several other incidents of an identical nature as well as a number of additional investigations. As of 2011, the company paid to the American and German governments a total of $1.6 billion in fines (SEC, 2011). Through a content analysis of the company's annual reports, sustainability reports and corporate press releases from 2000 to 2011 and under the lens of legitimacy theory and media agenda setting theory, our findings suggest that Siemens changed its compliance and corruption disclosure practices to manage its legitimacy in the wake of the 2006 corruption scandal and in subsequent years. The strategies adopted by Siemens may be described as both symbolic and substantive (see Dowling and Pfeffer, 1975; Ashforth and Gibbs, 1990; Rodrigue et al., 2013). The implications emanating from this study seem therefore relevant for several key societal stakeholders in that they could at least provide additional arguments for the need of better regulations to ensure the disclosure of relevant, reliable and consistent corporate information about important social issues such as corruption—a serious economic, social, political and moral issue (Argandoña, 2007).

Keywords: corporate social responsibility; corruption; disclosure; legitimacy management; Siemens; substantive; symbolic; United Nations Global Compact

2.1. Introduction

This study examines the changes in corporate disclosure practices of a specific and under-researched area of corporate social responsibility (CSR), that of countering corruption. There seems to have a consensus that corruption is a cancer that destroys society (Rose-Ackerman, 2002) as it facilitates cheating disadvantaged populations by diverting resources for critical services like education, clean water, and health care into the pockets of dishonest government officials (Hills et al., 2009). Corruption is often also negative for business as it affects a company's ability to compete and brings operational costs such as those associated with a heightened legal risk (ibid.).

Disclosure on corruption issues serves multiple goals—it helps to hold managers and companies accountable concerning performance on its anti corruption efforts, raises public awareness, exhorts pressure towards the adoption of similar principles and procedures by other companies and is a means to understand what works in the combat against corruption and which developments are most needed (Hess, 2009).

Despite the importance of countering corruption, CSR research has traditionally been focusing on issues such as environmental protection, health and safety at work, and local community and consumer relations (Branco and Delgado, 2012). It was only in 2002 that this issue was considered by the Global Reporting Initiative in its Sustainability Reporting Guidelines (GRI, 2002), and only in June 2004 that the fight against corruption was added as the 10th principle of the United Nations Global Compact (UNGC, 2009).[1] This suggests that combating corruption in all its forms has only recently become an integral part of CSR policies.

Although several studies investigate the effects of specific events on corporate social disclosure (CSD) practices, most of this literature focuses on environmental, as opposed to social disclosure (Patten, 1992; Jantadej and Kent, 1999; Deegan et al., 2000; Savage et al., 2000; Cho, 2009). Exceptions include Coetzee and van Staden (2011) study of South African mining companies response to a mining accident and Islam and Mathews (2009) study of Grameen Bank changes in disclosure after severe

[1] The United Nations Global Compact and the Global Reporting Initiative are known to be the two of the most important CSR global movements.

criticism from the Wall Street Journal in 2001, both social events that received high public attention.

Similarly, while there is a wealth of non-academic investigations of anti-corruption disclosure, these rely mostly on companies' practices and place little emphasis on the factors explaining why this type of disclosure is produced (Gordon and Wynhoven, 2003; Novethic, 2006; KPMG, 2008; Transparency International, 2009; Transparency International, 2012). To the best of our knowledge, only three academic studies specifically examine the disclosure of corruption related matters, one related to factors influencing AC disclosure (Healy and Serafeim, 2015) and two related with the impact of bribery related events over disclosure (Dissanayake et al., 2011; Islam et al., Forthcoming). The latter studies will be addressed in more detailed in the literature review section.

Despite the scarcity of academic inquiries concerning AC disclosure, several institutions claim that the degree of reporting on corruption can be a strong indicator of the quality and comprehensiveness of a company's efforts in addressing bribery and corruption (Transparency International, 2009; UNGC, 2009). This paper addresses the existing gap in the literature.

In this study, we examine the changes in disclosure practices on compliance and the fight against corruption at Siemens A.G. (hereafter "Siemens") - a large German multinational corporation - over a period of 12 years (2000-2011) during which a major corruption scandal occurred. In 2006 the company was accused paying an estimated amount of bribes of $1.4 billion (SEC, 2008). This particular scandal led to several other incidents of an identical nature as well as a number of investigations that have yet to be finalized. As of 2011, the company paid to the American and German governments a total of $1.6 billion in fines (SEC, 2011). We conducted a content analysis of the company's annual reports and sustainability reports from 2000 to 2011 to specifically examine the changes in extensiveness and breadth of Siemens' corruption and compliance disclosure. Relying on arguments from legitimacy theory and media agenda setting theory, we find evidence that Siemens appeared to change its compliance and corruption disclosure practices to repair its legitimacy in the wake of the 2006 corruption scandal and in subsequent years with almost no evidence of legitimacy-

gaining strategies following another event that could have influenced Siemens AC disclosure: the issuance of the 10th principle of the United Nations Global Compact (of which Siemens is a member since 2003). The strategies adopted by Siemens may be described both as symbolic and substantive (see Dowling and Pfeffer, 1975; Ashforth and Gibbs, 1990; Rodrigue et al., 2013). We also find that disclosure trends differ across sustainability and annual reports relative to media attention directly following the 2006 corruption scandal. Annual reports show increased disclosure on corruption and compliance issues earlier than sustainability reports and these increases occur before the peak levels of media attention.

In the following section, we present the theoretical lens of our analysis. Section 2.3 provides some background information about the Siemens case and lays out the research methods. The analysis and the results are presented in section 2.4. We discuss our findings, limitations and implications, and conclude in the final section.

2.2. Theoretical framework

2.2.1. Legitimacy theory

Proponents of legitimacy theory argue that firms exist as a part of a broader system that determines whether the companies are legitimate and thus grants the license to operate within that system (Deegan, 2002). Legitimacy can be viewed as a social contract between the firm and society. The central issue is that society may revoke this contract if the company is perceived as falling short of public expectations (Dowling and Pfeffer, 1975; Deegan and Rankin, 1996). Evidence of such a rupture can be illustrated through stakeholders reducing or eliminating the supply of labor and financial capital to firms, or constituents lobbying the government for increased taxes, fines or laws to encourage the reduction of those actions which do not conform to the community's expectations (Dowling and Pfeffer, 1975; Deegan and Rankin, 1996). When an actual or potential disparity emerges between the two value systems—that of society and of the company, the entity's legitimacy is threatened (ibid.).

According to legitimacy theory, social disclosure is a tool utilized by companies to legitimize their behaviours vis-à-vis their stakeholder groups. The majority of studies that use legitimacy theory as a theoretical framework suggest that it provides an

explanatory basis for changes in disclosure (Patten, 1992; Deegan and Rankin, 1996; Buhr, 1998; O'Donovan, 2002; Branco and Rodrigues, 2008; Patriotta et al., 2011). Some, however, suggest that legitimacy theory cannot systematically explain social disclosures (Guthrie and Parker, 2006).

2.2.2. Media agenda setting theory

We bring in features of media agenda setting theory to complement legitimacy theory. Legitimacy theory posits that the extent of social disclosure is a function of public policy pressures faced by the company (Patten, 1992; Cho et al., 2010), so one can expect a positive relationship between media pressure and disclosure. Before companies employ deliberate legitimacy strategies, management must first have access to the nature and scope of the comments expressed by the public opinion which exist in the media (Cormier et al., 2005).

According to media agenda setting theory, the media drives, shapes and creates the public's agenda (McCombs and Shaw, 1972). This is primarily due to increased media attention, which helps trigger public awareness, and magnifies the issues under its attention so that they become a top concern (McCombs and Shaw, 1972; Brown and Deegan, 1998). Several authors (Patten, 2002a) use media agenda setting theory in conjunction with legitimacy theory (see Brown and Deegan, 1998; Deegan et al., 2000; Branco and Rodrigues, 2008; Aerts and Cormier, 2009; Elijido-Ten, 2011) with some providing evidence that increased environmental disclosure can be a result of higher media exposure (as in Brown and Deegan, 1998; Deegan et al., 2000; Cormier et al., 2005; Aerts and Cormier, 2009) and that disclosure is used as a means to reduce public policy pressure (Brown and Deegan, 1998; Patten, 2002a).

2.2.3. Reactions to legitimacy gaps

Companies use strategies to influence societal perceptions when legitimacy gaps emerge. External perceptions of legitimacy may change in the advent of threats due to specific events (Patten, 1991; Deegan and Rankin, 1996; Deegan et al., 2000) such as changes in the community's expectations (Lindbloom, 1994), changes in the composition and/or values of the public (O'Donovan, 2002) or the occurrence of incidents (Deegan et al., 2000). The specific strategy to adopt highly depends on

whether the company is trying to gain, maintain or repair legitimacy (O'Donovan, 2002). The primary difference between legitimacy gaining and repairing strategies is that the latter are reactive in response to a crisis, whereas the former are usually proactive, generally not in response to a crisis and ex ante (ibid.). Hence, for the purposes of this study, proactive refers to a more timely reaction in response to a situation whereas a reactive response occurs later.

Based on the work of Dowling and Pfeffer (1975), Ashforth and Gibbs (1990, p.178-181) presented a comprehensive list of possible substantive and symbolic reactions to threats to legitimacy. Symbolic strategies occur when the company does not make real changes but tries to portray itself as legitimate so as to meet society's expectations. Examples of such strategies are:

- espousing socially acceptable goals while pursuing less acceptable ones;
- denying or suppressing information about activities that may undermine legitimacy (see also Suchman, 1995);
- redefining means and ends by, for instance, identifying with symbols, values, or institutions that are highly legitimate (Dowling and Pfeffer, 1975);
- offering accounts or explanations, including excuses and justifications, as a way to minimize responsibility and reduce negative consequences for the company (see also Suchman, 1995);
- offering apologies and thus showing remorse about unacceptable behavior;
- performing ceremonial conformity by adopting practices with high visibility without actually making structural and procedural changes in the organization.

Savage et al. (2000) added the following three strategies based on their empirical work:

- admitting guilt and assuming responsibility for the facts that caused a negative impact on the company's legitimacy;
- creating misinterpretations or distortions by giving false impressions or accounts, or by providing misleading information whether intentional or not;
- evading, trivializing or skirting around the issue by, for instance, offering partial explanations, trivializing or not directly addressing the issue.

Suchman (1995) suggests that legitimacy repairing strategies may first consist of constructing a wall that allows the audience to separate past events from ongoing activities by using the equivalent to what the above authors referred to as symbolic legitimacy management. In the second stage, the focus may turn to engaging in real strategic restructuring. Other examples of substantive strategies are evidenced by Dowling and Pfeffer (1975) and Ashforth and Gibbs (1990, p. 178-181) and comprise:

- role performing and meeting its constituents' expectations;
- engaging in coercive isomorphism (DiMaggio and Powell, 1983) through conformity to values, norms and expectations of its constituents;
- altering resource dependencies;
- altering socially institutionalized practices so that they conform to companies practices.

According to Zyglidopoulos (2001), accidents and discrete one-time undesirable or unfortunate events that happen unexpectedly in the life of corporations and cause damage to any number or kind of stakeholders may particularly damage a company's reputation. Damage to companies reputation may happen because: (1) stakeholders react emotionally to accidents, or evaluate them as events which provide relevant information about the company's business and their stakes in it and (2) accidents trigger investigations and thus increased social concern and public attention. Furthermore, factors such as the severity of the accident and the extent of damages are expected to play an important role in the level of impact on the company's reputation (ibid.). We argue that events under investigations can be particularly harmful as they may reveal even more embarrassing facts. Regarding Siemens 2006 corruption scandal, the company was under investigation in a number of different countries, involved several stakeholders (employees, management and suppliers for instance) and received significant media attention. We can then expect this event to be particularly harmful to the company reputation.

Previous literature on the impact of events on company's legitimacy and disclosure is focused mainly on environmental incidents or events (Patten, 1992; Deegan et al., 2000; Branco et al., 2008; Coetzee and van Staden, 2011). To our knowledge only two studies addressed the impact of corruption related events on

corporate disclosure (Dissanayake et al., 2011; Islam et al., Forthcoming). Islam et. al (Forthcoming) analyzed anti-bribery disclosure of two Chinese multinational companies – China Mobile and ZTE – as a consequence of increased global concern over the issue of bribery in the telecommunication industry. Dissanayake et al. (2011) performed an exploratory analysis of the extent of anti-bribery disclosure at Alcatel-Lucent and Siemens A.G., over a period of 15 years, in response to incidents of corporate bribery and under the influence of media pressure and increased International Governmental Organization (IGO's) anti-bribery activity. Both studies concluded for an increase in corporate disclosure in reaction to a legitimacy-threatening event and under increased media pressure. Despite also focusing on Siemens disclosure practices, our study substantially differs from that of Dissanayake et al. (2011) in terms of scope of analysis, research methods and theoretical lenses.

2.3. Background and research methods

2.3.1. Background

In November 2006, Munich public prosecutors conducted searches at the company and employees' private homes in an attempt to discover evidence concerning suspicions of public corruption including embezzlement, bribery, money laundering and tax evasion. As a result, the company incurred a fine of 201€ million in October 2007. According to the court's final disposition, former manager of the communications group colluded with others and bribed foreign public officials for the purpose of obtaining contracts on behalf of the company in Russia, Nigeria and Libya, which totaled 77 cases during the period from 2001 to 2004 (Siemens, 2008, p.275). Investigations by the Munich public prosecutor continued throughout 2006 and involved several companies from the Siemens group in several geographical areas—Germany, Greece, Switzerland, Liechtenstein and Italy. Some of the cases, which led to these investigations dated back to 2004 and 2005. In 2007 new corruption allegations appeared, involving Siemens companies in China, Hungary, Indonesia, Nigeria, Norway and the United States. In December 2008, legal proceedings against the company's Supervisory and Managing Board from the Munich legal prosecutor in Germany and the United States were terminated with the imposition of an additional fine of 395€ million.

Several other anticorruption investigations continued or started after 2009 in Russia, Austria, Brazil, Greece and Afghanistan, among other countries. Most of these legal proceedings were related to events that occurred before 2006 but were only uncovered after the 2006 scandal or as a result of its investigation. Hence, the post-event period considered in this study is not exempt from corruption-related situations.

To fully comprehend the problem, we analyzed the annual reports, stand-alone sustainability reports and corporate press releases issued by Siemens from 2000 to 2011, period of 6 years before and after the event.

When reviewing Siemens reports in the years previous to 2006 we realized that another corruption related event had occurred, which might have an impact on disclosure: the issuance of the United Nations Global Compact (UNGC) 10th principle on the fight against corruption, in 2004. The UNGC is "an international voluntary network-based initiative consisting of participants from companies, NGOs, governments, academic institutions and other stakeholder groups" (Runhaar and Lafferty, 2009, p.481). Until 2004 the UNGC was focused on nine principles concerning Human Rights, Labor and Environment. In June 2004, a 10th principle on anticorruption was issued stating that "businesses should work against all forms of corruption, including extortion and bribery" (UNGC, 2009). Given that this event was also related to corruption and that it might have influenced Siemens disclosure in the pre-event period we included it in our analysis.

To obtain a comprehensive understanding of the problem, we analyzed the annual reports, stand-alone sustainability reports issued by Siemens based on the following timeline:

- 2000 to 2003: pre-event period 1 (Period 1);
- 2004 to 2005: pre-event period 2, consisting on year when the UNGC issued its 10th principle on anticorruption and the subsequent year (Period 2);
- 2006 to 2008: time period from when the first corruption scandal emerged to its last fine settlement (Period 3); and
- 2009 to 2011: post-event period during which the company kept undergoing through corruption related situations.

For the event and pre-event periods we also analysed Siemens corporate press releases. Analysing pre- and post-event periods is a widely used procedure (Patten, 1992), which allows for an analysis of the increase in disclosure over time, and more specifically disclosure in reaction to specific events (see Deegan et al., 2000; Branco et al., 2008; Cho, 2009).

2.3.2. Content analysis

We use content analysis—a method commonly applied in CSR reporting research (Gray et al., 1995; Coetzee and van Staden, 2011) to examine the annual reports, stand-alone sustainability reports and corporate press releases available on Siemens' website. We measured disclosure extensiveness with the number of sentences[2] (e.g. Hackston and Milne, 1996; Buhr, 1998; Deegan et al., 2000; Deegan et al., 2002; Branco et al., 2008) related to compliance and corruption while breadth was measured through disclosure indexes (e.g. Gul and Leung, 2004; Haniffa and Cooke, 2005; Branco and Rodrigues, 2008; Prado-Lorenzo et al., 2009). Disclosure scores were computed by assigning a score of "1" if a particular category was disclosed and "0" otherwise. Consistent with Branco and Rodrigues (2008) and Cho and Patten (2007), we made the assumption that each item of disclosure was equally relevant and added the disclosure scores rather than weighting them. We also supplemented the quantitative analysis with qualitative data from the reports.

Given that compliance and corruption disclosure item scoring grids have not been used in prior studies, we developed our own specific disclosure index based on, and adapted from, established related sources. The starting point was the "Reporting Elements for the 10th principle" to which we added additional elements and sub-elements from the following sources: (1) the Novethic (2006) study, (2) (Transparency International, 2009) and (Transparency International, 2012) and studies and (3) the GRI's key performance indicators (GRI, 2002). Table 2.1 presents the final Disclosure Index used to analyze the content of Siemens' annual reports and stand-alone sustainability reports from 2000 to 2011. The Index is composed of 5 Categories:

[2] While the number of words or the number or percentages of pages (Gray et al., 1995) are also both widely used in CSD research, Hackston and Milne (1996) suggest that sentence counts are preferable because they convey a better meaning and may generate fewer errors (Milne and Adler, 1998).

commitment and policy, risk management, implementation, monitoring and key performance indications. The index maximum score is 33.

Table 2.1 Disclosure Index Composition and Scores

CATEGORY	SCORE	ELEMENT	SUB-ELEMENT (where relevant)
COMMITMENT & POLICY	**1**	Commitment compliance/anti-corruption	Public commitment to fight corruption
RISK MANAGEMENT	**3**	Risk Management Activities	Carrying out risk assessment Policies/rules for high-risk areas Risks according to stakeholders
IMPLEMENTATION	**13**	Internal organization	Corporate structure Programmes, processes, Code of Conduct, rules,...
		Employees	Communication on the commitment to all employees Existing training Incentive related scheme Other processes employee oriented amnesty programs inquiries, conferences) Existence of communication/reporting channels and follow-up mechanisms Consequences of non-compliance
		Suppliers and Business Partners	Communication on the commitment towards S and BP Existing training Actions/intruments to encourage business partners to implement commitments Existence of communication/reporting channels and follow-up mechanisms Consequences of non-compliance
MONITORING	**5**	Monitoring Activities	Management review and monitoring Practices on dealing with incidents Public legal cases External review of programs Existing control system
KEY PERFORMANCE INDICATORS	**11**	Employee related	Training Incentive System Other instruments used for compliance (amnesty requests, surveys, etc.) Consequences of non-compliance
		Suppliers and Business Partners	Intruments to encourage business partners to implement commitments Consequences of non-compliance
		Structure, inputs and outputs	Corporate structure Communication - questions, inquirires Communication - reported incidents Compliance cases Other compliance KPI's (surveys, internal control related, etc.)
TOTAL SCORE	**33**		

2.3.3. Media attention

Media attention (or exposure) is traditionally measured by counting the number of media press releases or reports in specific newspapers (Branco and Rodrigues, 2008) or in media databases (Brown and Deegan, 1998; Coetzee and van Staden, 2011) through a keyword search. We used FACTIVA database and measured media attention by the number of headline news for the words (1) “Siemens” and “Compliance and (2) “Siemens” and “Corruption”.

2.3.4. Reliability and validity of analysis

Reliability may be achieved by ensuring stability, reproducibility and accuracy of data (Milne and Adler, 1998). Stability means ensuring intra-observer reliability, the degree to which the same coder analyses the same data set over time. According to (Milne and Adler, 1998), a learning cycle of 20 reports need to be carried out before more elaborated sub-category analysis could be reliably performed on the coded output of less experienced coders. To ensure reliability we analyzed the 12 reports (2000-2011) three times, to a total of 36 reports. To guarantee reproducibility (inter-coder agreement) and validity of analysis the reports were examined and categorized by another researcher. Discrepancies in coding were analyzed and differences solved. Regarding accuracy - accessing coder performance - we followed Guthrie and Mathews (1985), and based our methods in prior research. Additionally, the disclosure index was built against previous studies from well-recognized organizations.

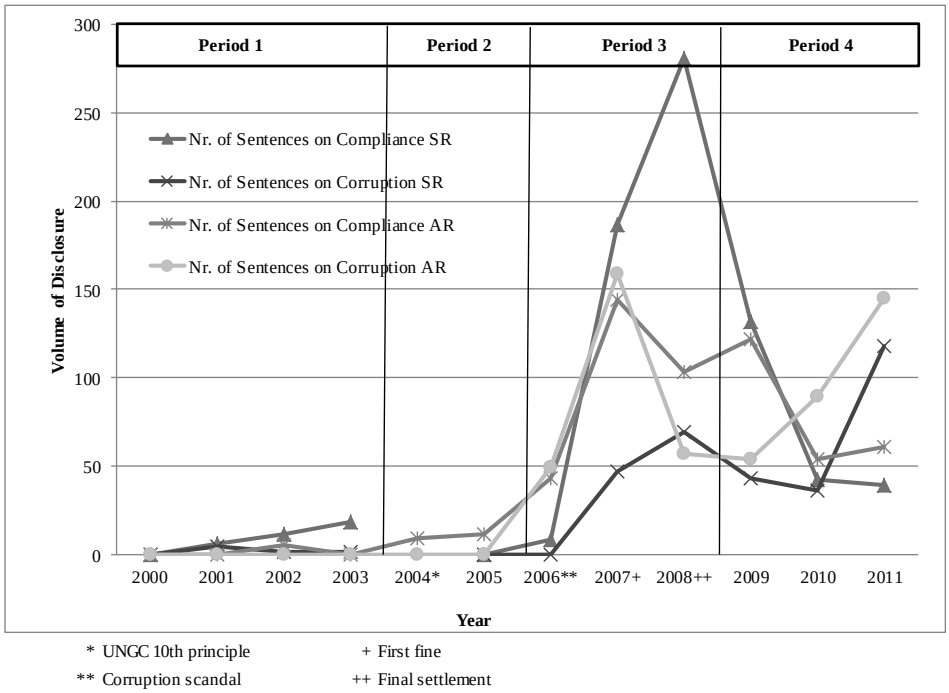
2.4. Analysis and Results

2.4.1. Impact of events on disclosure extensiveness

PRE-EVENT PERIOD - Periods 1 and 2 – 2000 to 2005

As shown in Figure 2.1 the content analysis of the company's annual and sustainability reports indicates that the lowest amount of disclosures was recorded in the 2000-2003 pre-event period. Results also suggest that the issuance of the UNGC's 10th principle on anticorruption had only a marginal effect on disclosure. According to legitimacy theory, we would have expected an increase in the volume of disclosure under the assumption that the company could make use of this event to gain legitimacy. Contrary to our expectations, however, we only note a slight increase of disclosure in the annual report with regards general compliance and no increase in disclosure specifically on corruption that year and the following. Interestingly, and in contrast to all periods within the scope of our analysis, the company did not have its stand-alone sustainability report available online in 2004. This finding in itself could provide evidence of another disclosure strategy—base level disclosure (Cho, 2009).

Figure 2.1. Disclosure volume on compliance and corruption, 2000-2011



EVENT PERIOD - Period 3 – 2006 to 2008

As expected, results document a significant change in Siemens' disclosure patterns in 2006 as shown in Figure 1. The volume of compliance and corruption disclosure included in both annual and sustainability reports exhibits a highly significant increase with the advent of the 2006 corruption scandal. These results are consistent with the company implementing a strategy to repair its legitimacy in the wake of the worldwide corruption scandal. Our findings are consistent with past studies showing a significant increase in disclosure after the occurrence of a legitimacy-threatening incident (Branco et al., 2008; Cho, 2009; Islam and Mathews, 2009; Eweje and Wu, 2010; Coetzee and van Staden, 2011; Patriotta et al., 2011). Results also indicate that the increase in disclosure volume was even more significant for the years subsequent to the scandal (i.e., 2007 and 2008)—this is consistent with Deegan and Rankin (1996), who report a significant increase in positive disclosure after the successful trial of 20 companies prosecuted by the New South Wales and Victorian Environmental Protection Industries, and Deegan et al. (2000), who show a higher increase in disclosure in the year following specific environmental incidents concerning a small sample of Australian firms. Similar to studies such as Cho (2009), our investigation analyzes both

annual and sustainability reports and we note different trends across these media. These include:

- annual report disclosures for the year of the corruption scandal (i.e., 2006) are far more extensive than those included in the stand-alone sustainability report;
- peaks and general increases in disclosure extensiveness occurred at different moments in annual reports and sustainability reports. More concretely, peaks and increases in disclosure volume in sustainability reports exhibit a one-year lag when compared to annual reports;
- peaks in disclosure extensiveness during the 3-year time period occurred for the annual report in 2007 which is the year when the company had its first condemnation and for the sustainability report in 2008 when the 2006 corruption case ended following the first settlement.

These results thus suggest that from 2006 to 2008 Siemens disclosed information earlier in its annual report compared to its sustainability report. Furthermore, peaks in disclosure extensiveness in the 2007 annual report, but not in the 2008 sustainability report, indicate that the company was more concerned in disclosing information about the first confirmation of guilt in its annual report while it would provide information about the process and termination of the corruption scandal case in its sustainability report. The lagging results for the sustainability report may indicate a more reactive strategy while a more proactive disclosure strategy may have been used for the annual report. The immensity of the final and its impact in the annual financial statements may also explain why the results peaked first in the company annual report. Our results contrast with the findings of Frost et al. (2005) who performed a (non-academic) study on CSD trends in Australian firms and concluded that issues related both to non-compliance and specifically to corruption and bribery had a higher presence in sustainability reports than they were in annual reports. Depending on the year, annual reports had more compliance and corruption disclosures than the sustainability report.

POST EVENT PERIOD - Period 4 – 2009-2011

Prior studies show evidence of significant decreases in disclosure in post-event periods (e.g. Cho, 2009). According to De Villiers and van Staden (2006), reductions in disclosure may occur for instance when societal suspicions or concerns reduce or disappear; when the strategy turns from (re)gaining to maintaining legitimacy; when it is perceived that reducing disclosure will reduce the importance of the issue; when disclosure is perceived as useless (O'Dwyer, 2003); or when managers perceive a theme to be sensitive (Solomon and Lewis, 2002).

Figure 2.1 shows an inconsistent evolution of disclosure in the post-event period (2009-2011). As expected, the extensiveness of sustainability report disclosure on compliance decreased significantly in the year following the 2008 settlement. On the contrary, and against our expectations, there is again an increase in the extensiveness of corruption related disclosure after 2009. While we acknowledge that the 2006 likely raised other corruption-related concerns from 2009 to 2011, we conjecture that increases in disclosure are associated with possible new corruption-related situations, especially in 2011 when specific corruption-related disclosure substantially increased. We conduct further analyses below to explore the potential influence of the media.

COMPARISON BETWEEN BEFORE AND AFTER 2006, THE YEAR OF THE FIRST CORRUPTION SCANDAL

Consistent with prior studies such as Islam and Mathews (2009) we used non-parametric tests to whether differences in the mean volume of disclosures between Periods 1 and 2 and Periods 3 and 4 exhibit statistical significance. The periods before and after the UN 10th principle were not analyzed due to its marginal impact on disclosures. As presented in Table 2.2, the difference in the number of sentences on compliance in the sustainability report ($p < .05$), the number of sentences on corruption in the sustainability report ($p < .05$), the number of sentences on compliance in the annual report ($p < .05$), and the number of sentences on corruption in the annual report ($p < .05$), all differ significantly across the two periods.

Table 2.2. Comparison of the mean volume of disclosure between before and after 2006, the year of the first corruption scandal

Type of disclosure	Mean volume of disclosure (six-year average) before corruption scandal (Periods 1 and 2)*	Mean volume of disclosure (six-year average) during and after corruption scandal (Periods 3 and 4)	*Z* Stat.	*p*-value (one-tailed)
Nr. of Sentences on Compliance SR	7.000000*	114.833333	-2.2874	0.0111
Nr. of Sentences on Corruption SR	1.200000*	52.166667	-1.9392	0.0262
Nr. of Sentences on Compliance AR	4.166667	87.833333	-2.8220	0.0024
Nr. of Sentences on Corruption AR	0.000000	92.166667	-2.9912	0.0014

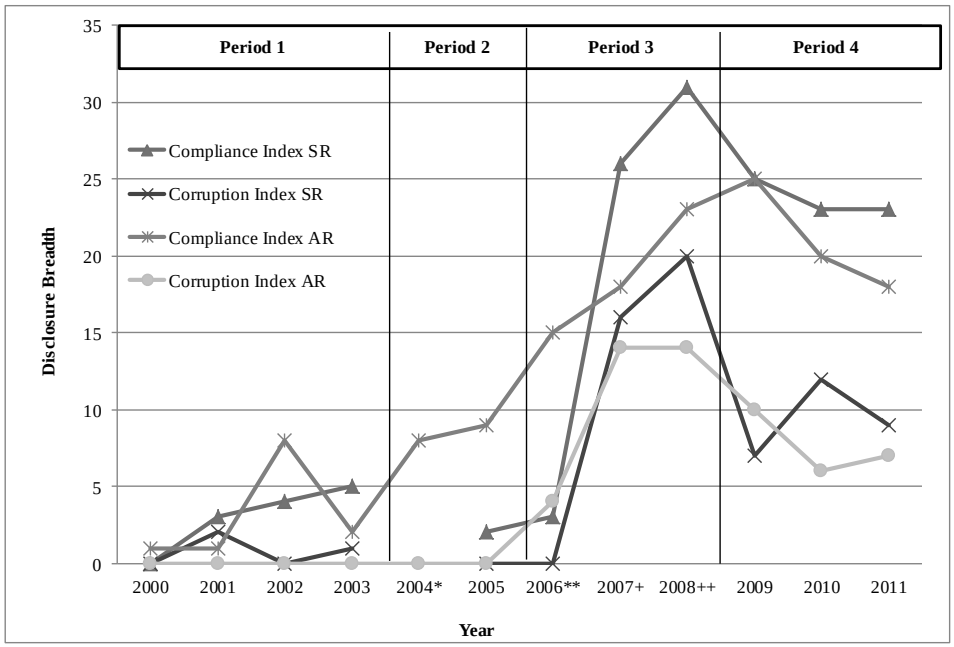
*For the items indicated above, they represent 5-year averages due to the lack of a 2004 SR

2.4.2. Impact of events on disclosure breadth

Figure 2.2 and Table 2.3 provide details on the evolution of Siemens' disclosure breadth over time.

Figure 2.2 documents a relatively low level of disclosure breadth in both the annual and sustainability report concerning compliance and the absence of disclosure with regards to corruption in the year of the scandal. However, we observe significant increases in disclosure breadth subsequent to the 2006 corruption scandal. While the issuance of the UNGC 10th principle does not appear to have a significant impact on the breadth of disclosure items, we report a significant increase in both reports the years following the corruption scandal. The breadth of corruption and compliance disclosure increased after 2006, achieved its peak in 2008 during the year of the final settlement, and decreased thereafter with the exceptions of compliance disclosure, which actually increased in the 2009 annual report and corruption disclosure which also increased in the 2010 SR.

Figure 2.2. Disclosure breadth on compliance and corruption in SR and AR, 2000-2011



* UNGC 10th principle + First fine

** Corruption scandal ++ Final settlement

Table 2.3 shows detailed evidence on the different scores per category included in the disclosure indexes on compliance and corruption. For most categories the peak of disclosure occurred in 2007 and 2008 regarding both compliance and corruption. The peaks in disclosure shown in pictures 2.1, 2.2 and in table 2.3 are an evidence that Siemens used AC disclosures to repair its legitimacy after the 2006 corruption scandal and the years of settlement of the 2007 and 2008 fines.

Table 2.3. Disclosure variety on compliance and corruption in SR and AR

Source	INDEX Categories/Year	MAX	DISCLOSURE INDEX: COMPLIANCE												CORRUPTION											
			00	01	02	03	04	05	06	07	08	09	10	11	00	01	02	03	04	05	06	07	08	09	10	11
SR	Commitment and Policy	1	0	1	1	1	-	0	1	1	1	1	1	1	0	0	0	1	-	0	0	1	1	1	1	1
	Risk Exposure	3	0	0	0	0	-	0	0	3	3	2	2	2	0	0	0	0	-	0	0	1	2	0	1	0
	Implementation	13	0	2	3	4	-	2	2	12	12	11	11	10	0	2	0	0	-	0	0	7	10	4	6	6
	Monitoring	5	0	0	0	0	-	0	0	5	5	5	5	5	0	0	0	0	-	0	0	4	5	2	2	2
	KPI's	11	0	0	0	0	-	0	0	5	10	6	4	5	0	0	0	0	-	0	0	3	2	0	2	0
	Total Index SR	33	0	3	4	5	-	2	3	26	31	25	23	23	0	2	0	1	-	0	0	16	20	7	12	9
AR	Commitment and Policy	1	0	0	1	1	1	1	1	1	1	1	1	1	0	0	0	0	0	0	1	1	1	1	1	1
	Risk Exposure	3	1	1	1	1	1	1	1	1	1	1	2	2	0	0	0	0	0	0	0	1	2	2	1	2
	Implementation	13	0	0	5	0	5	6	9	10	11	13	10	9	0	0	0	0	0	0	0	8	7	5	3	3
	Monitoring	5	0	0	1	0	1	1	4	5	4	4	5	4	0	0	0	0	0	0	3	4	4	2	1	1
	KPI's	11	0	0	0	0	0	0	0	1	6	6	2	2	0	0	0	0	0	0	0	0	0	0	0	0
	Total Index AR	33	1	1	8	2	8	9	15	18	23	25	20	18	0	0	0	0	0	0	4	14	14	10	6	7

Legend: squared cells represent peaks in disclosure and shadowed cells represent the first year of disclosure

It is relevant to note that the company started disclaiming its commitment and existing policies to compliance many years before the 2006 corruption scandal and even before the issuance of the UNGC 10th principle on the fight against. Table 2.3 results show that it is only after the corruption scandal that the company openly disclosed its clear and specific commitment to the fight against corruption to its constituents. It also started to provide a broader range of information with regards to its internal formal structure; its exact practices of engaging employees and suppliers in implementing compliance rules with techniques such as training or incentive schemes; and its compliance monitoring activities and key performance indicators (see Appendix 4.1 for more details). The variety of instruments used to fight corruption followed the same pattern as the volume of disclosure—it increases in 2007, achieves its peak in 2008 and decreases thereafter. Following the scandal, the company created watchdogs and monitors in the figure of an "Ask Us" and "Tell Us" helpdesk for reporting incidents, changed the procedures of approval for business consultant agreements with some items fading out or disappearing in the following years as it is the case with the "Approve it" and "Improve it" functions which were disclosed only in 2008s (Table 2.4). We believe this could be an evidence of an attempt to engage in mere ceremonial conformity (Pfeffer, 1981).

Table 2.4. Anti-corruption instruments

	2000- 2006	2007	2008	2009-2010
Communication Mechanisms				
Compliance officer at Business Unit	x	-	-	-
Ombudsman	x	x	x	x
Ask Us helpdesk	-	x	x	x
Tell Us helpdesk	-	x	x	x
"Find It"	-	-	x	-
"Approve It"	-	-	x	-
"Improve It"	-	-	x	-
Incentive related scheme for employers	-	-	x	x
Processes to encourage business partners				
Acceptance of the code of conduct for Business Sup	-	x	x	x
Supplier audits	-	x	x	x
Supplier qualification process	-	x	x	x
Supplier evaluation based on country risk	-	-	x	-
Business Partner Compliance Due Diligence Tool	-	-	x	-

Our results are aligned with Lindbloom (1994) and Gray et al. (1995) who claim that one possible reaction from an organization when faced with a legitimacy threatening event is to invest in changing itself and educating and informing the relevant publics about the actual changes in actual behavior in order to meet its constituents' expectations. As Suchman (1995) notes, although being a sign of change and instability, this type of strategy may at the same time be effective in containing the damage. Assuming that the company did implement the additional measures that it reports, and not only talked about it, that would be an evidence of substantive legitimacy repairing strategy.

CHANGE IN COMPANY DISCOURSE OVER TIME

According to Suchman (1995), legitimacy repairing strategies may at first consist in constructing a wall that allows the audience to separate past events from ongoing activities. We found evidence in Siemens discourse suggesting that it was engaging in such symbolic legitimacy techniques following the 2006 scandal. The company admitted the occurrence of the event while at the same time detaching itself from the problem by attributing the guilt to employees and showing its commitment to solving the problem, as we can see in this extract of Siemens' 2006 annual report:

> *"Unfortunately, it has now become clear that our compliance measures are not yet sufficient. Several former and current Company employees are under investigation regarding allegations of embezzlement, bribery and tax evasion. Siemens is doing everything in its power to facilitate the full and speedy clarification of this matter and has taken appropriate and immediate countermeasures. In this connection, we've also engaged independent experts to detect any concrete violations, identify flaws in Siemens regulatory system, structures and processes and eliminate these shortcomings entirely without exception (p. 12)".*

Showing remorse about unacceptable behavior is a symbolic legitimacy management strategy (Dowling and Pfeffer, 1975; Ashforth and Gibbs, 1990). As Ashforth and Gibbs (1990, p. 181) refer, apologies may serve: (1) to convey managements understanding and concern regarding the event, (2) garner sympathy from constituents, (3) reaffirm at least the appearance of managerial control and,

implicitly, that management has learned from the event and (4) maintain some managerial credibility.

In the 2007 corporate responsibility report the company already assumes responsibility although not yet admitting guilt:

> "*The fact that our Company made mistakes here in the past is a painful realization. We've taken many steps to uncover misconduct and to heighten all employees' awareness for lawful, ethically irreproachable behavior (p.3)."*

Up to the end of 2008 the Company was convicted to pay a fine of € 1 billion. In that year there was a clear admission of guilt as is visible in the 2008 sustainability report:

> *"Our three basic values are nothing new. Problems in the past arose simply because these values were not applied systematically. And this means they were not promulgated or internalized to a sufficient degree. In addition, a framework capable of anchoring these values was often lacking… A good reputation is a company's greatest capital. In the past we endangered this reputation, as we did not succeed in anchoring compliance throughout the company as an integral part of our corporate responsibility. Compliance was not sufficiently integrated in our business practices, contrary to the existing internal regulations (p. 48, 60)."*

We also found evidence of Siemens identifying with reputed institutions and showing commitment towards stakeholders needs and goals which are also example of symbolic legitimacy management (Dowling and Pfeffer, 1975; Ashforth and Gibbs, 1990; Suchman, 1995). After 2006, Siemens disclosed the creation of a number of new compliance and anticorruption programs and adherence to relevant initiatives[3], as we can see from this extract of Siemens' 2008 sustainability report:

[3] Such programs and initiatives included a compliance committee; a mandate for a new Chief of Compliance Officer; a new managing board position for legal and compliance matters; a reinforcement of supplier and business partner audit, qualification, risk identification and measurement procedures; supplier conferences with an emphasis on compliance and the Siemens Compliance Program; the Code of Conduct for Business Suppliers; intensive training for employees both on general compliance and specifically on corruption to incentive related schemes; watchdogs and monitors in the form of an ombudsman; a "Tell Us" helpdesk for reporting incidents; and the Siemens Integrity Initiative.

"Our policy of collective action includes participating in initiatives and organizations for combating corruption. One example is our involvement in a World Bank Institute collective action working group. We are also an active member of the working group for the tenth principle (anti-corruption) of the UN Global Compact and of the Commission on Anti-Corruption of the International Chamber of Commerce (ICC). A pilot process is currently underway to implement the results (p. 68)."

Since 2006 the company disclosed its increasing participation in anticorruption initiatives throughout the world and its membership in additional anticorruption institutions and movements such as the UNGC or Transparency International (before 2006), the World Economic Forum Partnering Against Corruption Initiative (since 2007), the Commission on Anti-Corruption of the International Chamber of Commerce (since 2008), the Anti-Corruption and Compliance Declaration (since 2009), the Coalition for Transparent Business in the Czech Republic, and the United Nations Anti-Corruption Convention. Siemens also reported an increased effort to dialogue with its stakeholders (e.g., the Siemens Materiality Portfolio included in its annual report since 2007).

Besides the symbolic strategies, and consistent with Suchman (1995), after a first phase of detachment to the problem the company went a step forward and offered more than normalizing accounts. The company made progress in showing it was taking all the necessary measures to remedy the problem, as seen in the following excerpt from the 2008 sustainability report:

"Compliance violations must not occur at Siemens again. For this reason we will continue to develop our Compliance Program along its present lines. The simplification and further integration of our compliance processes will be a main focus of our work. As part of our Collective Action Initiative, we intend to cooperate with other stakeholders in driving our activities to combat corruption (p. 148)."

Changes in discourse are again visible in 2009, the year after the settlement. Once again the Company did not ignore the issue, instead made a reference to it but presented it part of a past situation, which offered as an opportunity for improvement. In the 2009 annual report the CEO conveys this positive message to its stakeholders:

> *"We're relieved that the German and U.S. authorities investigating the allegations of bribery against Siemens have concluded their proceedings, and we're proud that the Company is now an international benchmark in the area of compliance. For us, these developments are both a confirmation of our efforts and an incentive to remain vigilant, professional and highly focused in all our activities (p. 13)."*

Overall, the analysis of Siemens' annual and sustainability reports in the years following the 2006 corruption scandal reveal a mixed strategy—symbolic strategies such as admitting guilt, associating with symbols and institutions, and performing ceremonial conformity; and, substantive strategies such as make actual changes in its methods of operations, tracking outputs in the form of key performance indicators, and altering resource dependencies.

2.4.3. Effect of public pressure on disclosure volume

Several past studies suggest that increased media attention, a potential proxy for social and political pressure, leads companies to increase disclosure in their annual reports (Bansal, 2005; Cormier et al., 2005). In a recent study, Elijido-Ten (2011) concluded that the influence of media coverage on annual report disclosure, particularly related to environmental issues, is higher for negative and "unobtrusive" events. We believe that this is also the case for compliance and corruption. For the Siemens case, our results (shown in Figure 2.3 and 2.4) indicate that disclosure on corruption and compliance in sustainability reports follows the evolution of our proxy for public attention, which is in line with media agenda setting theory and previous literature suggesting that increased media attention leads to increased disclosure. In contrast to annual reports, peaks in sustainability report disclosures were systematically found to be one year after the peaks in media attention. This reinforces one of our previous findings that annual report disclosures seem to be more responsive than sustainability report disclosures. A possible explanation is that Siemens anticipated different informational

needs from the stakeholders targeted by each type of report. For instance, annual report readers could be more demanding and sensitive to this type of event given that corruption scandals can have some material impacts on the company's financial statements and possible impacts on their own wealth. The company may disclose information in a more responsive manner while facing media pressure as it could consider the annual report audience better informed, hence feel "pressure" from this stakeholder group at an earlier stage and not so much as a consequence of higher media influence.

Figure 2.3. Media attention and corruption disclosure volume in SR and AR

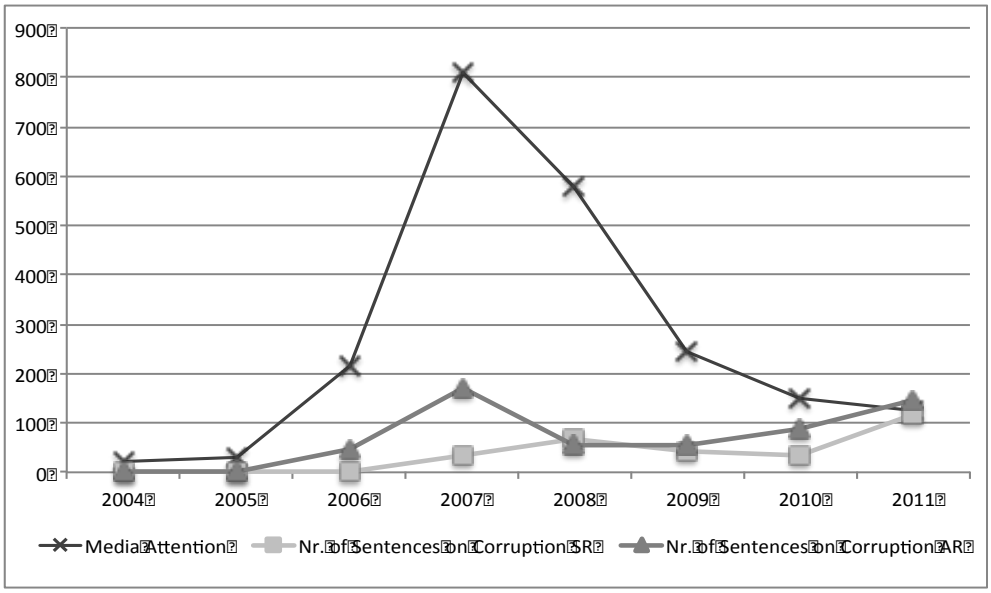
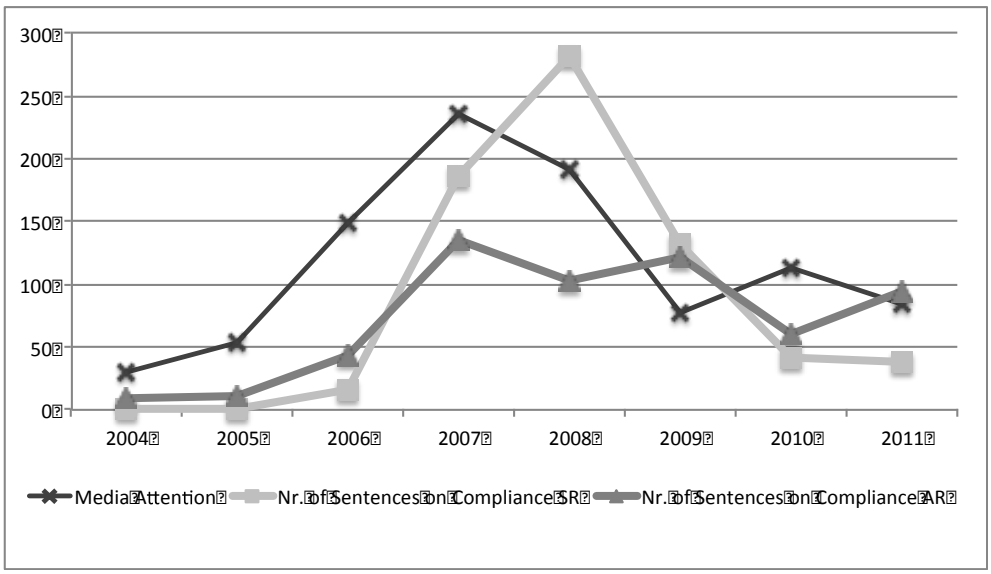


Figure 2.4. Media attention and compliance disclosure volume in SR and AR



When comparing the number of corporate issued press releases dedicated to the issues of compliance and corruption with media attention dedicated to the theme of "Siemens corruption", we find evidence that corporate press releases and media attention follow similar trends. When media attention increases the number of corporate press releases generally increases as well. After 2007 both corporate press releases decrease as well as media attention. Details are provided in Table 2.5.

Table 2.5. Media attention and corporate press releases on compliance and corruption

	2004	2005	2006	2007	2008	2009	2010	2011
Media Attention	22	29	215	812	533	217	125	116
Press releases related to Compliance	0	0	1	17	7	6	5	1
Press releases related to Corruption	0	0	1	9	6	5	2	1

Note: There are no press releases online before the corruption related event; squared cells represent peaks of disclosure

2.5. Discussion and conclusions

Consistent with prior research (e.g. Patten, 1992; Deegan and Rankin, 1996; Cho, 2009; Islam and Mathews, 2009; Eweje and Wu, 2010), our findings suggest that Siemens AG engaged in legitimacy repairing strategies by increasing disclosure when faced with an event threatening its legitimacy—the occurrence of the 2006 corruption scandal. We find no evidence concerning legitimacy gaining strategies associated with the issuance of the UNCG 10th principle on anticorruption. The results of this study are aligned with past evidence since post-event disclosure clearly outcasts pre-event disclosures (De Villiers and van Staden, 2006; Cho, 2009).

In addition, we find evidence supporting slight differences in disclosure strategies between the two main sources of content analysis—the annual report and stand-alone sustainability report. Concerning the latter, findings are consistent with previous studies in that the peaks of disclosure breadth and extensiveness occur in the year following the event (e.g. Deegan and Rankin, 1996; Deegan et al., 2000). Moreover, changes in disclosure on compliance and corruption appear to follow the

same trend as increases in media attention. This is consistent with media agenda setting theory and legitimacy theory, since as a general rule a company's disclosure changes in reaction to increased public pressure. Concerning the annual report, results suggest that during the 2006-2008 period peaks in disclosure breadth and extensiveness occurred a year earlier than in the SR and before the heightened media attention. One potential explanation for this difference of timing in the peaks of reporting is that the company may assume that annual report readers constitute a different audience than the sustainability readers and that the former have different and more demanding informational needs at least in terms of the timeliness of the reporting. We could assume that sustainability reports are more targeted to general stakeholders such as the community, consumers, employees, and certain types of investors as opposed to annual reports, which are more financial and technical in nature target a better informed and more demanding public such as shareholders, banks, tax authorities, and financial analysts. Such an assumption combined with the idea that the company may perceive social information as useful for investment decisions can potentially explain the occurrence of earlier peaks of information disclosure in the annual report when compared to the sustainability report. Our results contribute to previous research, which presented mixed findings. For example, Milne and Chan (1999) find that CSD had little impact on the decisions made over investment funds while Deegan and Rankin (1997) conclude on the materiality of environmental disclosures for shareholder decision making along with individuals inside the organization but not for analysts or stockbrokers. Teoh and Shiu (1990) conclude that general CSD was not relevant for institutional investors decision-making although it has potential to increase its relevance if presented in a quantified, financial form focusing on product improvement or fair business practices. Hence, additional research in this area appears warranted.

Concerning the specific legitimacy repairing strategies used by the company, we our analyses indicates that in the presence of a corruption-related threatening event Siemens AG followed a mix of symbolic and substantive strategies (as suggested by Dowling and Pfeffer, 1975; Ashforth and Gibbs, 1990; Savage et al., 2000). After the 2006 scandal, the company became associated with several ethical institutions and created its own anticorruption global initiatives, which can be perceived as symbolic strategies. At the same time the company implemented new processes, codes and

procedures while reinforcing existing structures and creating new ones, such as watchdogs and monitors, strengthening its monitoring practices and implementing key performance indicators to evaluate its anticorruption and compliance performance which are more substantive in nature.

Like all studies, ours is subject to several limitations. First, it does not allow for any generalization given the unique case and context that we examine. Second, it is limited to the extent that public company information is made available only online in the form of corporate reports and press releases. Third, to our knowledge the legislation did not change during the time period we tested so we assume that the changes were due to the event and not to legislation.

Despite these limitations, however, this study contributes to existing research in several ways. It first brings additional evidence to the scarce research body on the social dimension of CSD. Results are relevant contributions to legitimacy theory and media agenda setting theory. Additionally, the specific results of this study document the strategic changes in Siemens AG's disclosure breadth and extensiveness, when faced with specific threats to its legitimacy. The findings in this paper provide additional arguments for the need of better legislation/regulation or at least mandatory standards to ensure that companies disclose relevant, reliable and consistent information about important social issues such as corruption—a serious economic, social, political and moral issue (Argandoña, 2007). Therefore, we believe this study is relevant for several key societal stakeholders such as governments, corporate governance institutions, NGOs and CSR promoters such as the UNGC.

Finally, this study uncovered several issues for further investigation. Additional research could be conducted concerning the impact of corruption related events in other companies in different contexts. The present work also revealed the need for more research concerning factors influencing disclosure on corruption. Although studies have considered the materiality and importance of social disclosure in the annual report for its users (e.g. Campbell et al., 2003), a lack of research exists concerning differences in informational needs of the users of CSD in both the annual and sustainability report, or possible differences in pressure generated by those different constituents. Finally, additional research could ask the question of how disclosures related to corruption differ

from environmental disclosures. In particular, is corruption a more socially taboo topic than environmental concerns, and do the trends between these corporate social disclosures differ in a significant way?

Appendix 2.1

Disclosure variety on Compliance and Corruption in SIEMENS AG Sustainability Reports

	SUSTAINABILITY REPORTS																							
	COMPLIANCE												CORRUPTION											
	00	01	02	03	04	05	06	07	08	09	10	11	00	01	02	03	04	05	06	07	08	09	10	11
INDEX TOTAL SCORE	0	3	4	5	-	2	3	26	31	25	23	23	0	2	0	1	##	0	0	16	20	7	12	9
COMMITMENT AND POLICY	0	1	1	1	-	0	1	1	1	1	1	1	0	0	0	1	0	0	0	1	1	1	1	1
Commitment to integrity/ compliance / fight corruption		1	1	1			1	1	1	1	1	1				1				1	1	1	1	1
RISK EXPOSURE	0	0	0	0	-	0	0	3	3	2	2	2	0	0	0	0	0	0	0	1	2	0	1	0
Carrying out risk assessment								1	1	1	1	1									1		1	
Policies/rules for high-risk areas								1	1												1			
Risks according to stakeholders								1	1	1	1	1								1				
IMPLEMENTATION	0	2	3	4	-	2	2	12	12	11	11	10	0	2	0	0	-	0	0	7	10	4	6	6
Internal organization:	0	1	1	1	-	1	1	2	2	2	2	2	0	1	0	0	-	0	0	2	2	2	2	1
Corporate structure								1	1	1	1	1								1	1	1	1	
Programmes, processes, code of conduct, rules, etc.		1	1	1	-	1	1	1	1	1	1	1		1						1	1	1	1	1
Employees:	0	0	1	2	-	0	0	6	6	6	4	4	0	1	0	0	-	0	0	4	6	1	2	2
Communication on the commitment to all employees			1	1				1	1	1	1	1		1						1	1		1	1
Existing training								1	1	1	1	1								1	1		1	1
Incentive related scheme								1	1	1											1			
Other processes employee oriented								1	1	1	1										1			
Existence of communication/reporting channels				1				1	1	1	1	1								1	1			
Consequences of non-compliance								1	1	1		1								1	1	1		
Suppliers and Busness Partners:	0	1	1	1	-	1	1	4	4	3	5	4	0	0	0	0	-	0	0	1	2	1	2	3
Communication on the commitment towards S and BP		1	1	1		1	1	1	1	1	1	1								1	1			1
Existing training											1	1												1
Actions/intruments to encourage business partners								1	1	1	1	1									1	1	1	1
Existence of communication/reporting channels								1	1		1													
Consequences of non-compliance								1	1	1	1	1											1	
MONITORING	0	0	0	0	-	0	0	5	5	5	5	5	0	0	0	0	-	0	0	4	5	2	2	2
Review of monitoring and improvement results								1	1	1	1	1									1			
Practices concerning dealing with incidents								1	1	1	1	1								1	1	1	1	1
Public legal cases regarding corruption/non compliance								1	1	1	1	1								1	1	1	1	
External review of programs								1	1	1	1	1								1	1			1
Existing control system								1	1	1	1	1								1	1			
KEY PERFORMANCE INDICATORS	0	0	0	0	-	0	0	5	10	6	4	5	0	0	0	0	-	0	0	3	2	0	2	0
Employees:	0	0	0	0	-	0	0	2	4	3	1		0	0	0	0	-	0	0	2	1	0	0	0
Training								1	1	1	1									1				
Incentive System									1	1														
Other instruments used									1															
Consequences of non-compliance								1	1	1										1	1			
Suppliers and Busness Partners:	0	0	0	0	-	0	0	1	2	0	2	1	0	0	0	0	-	0	0	0	0	0	2	0
Intruments to encourage business partners								1	1		1	1											1	
Consequences of non-compliance									1		1												1	
Structure, inputs and outputs:	0	0	0	0	-	0	0	2	4	3	1	4	0	0	0	0	-	0	0	1	1	0	0	0
Corporate structure									1	1														
Communication - questions, inquirires								1	1	1	1	1												
Communication - reported incidents									1			1								1				
Compliance/corruption cases								1	1	1		1									1			
Other compliance KPI's												1												

Note: cells are shadowed in the first year of disclosure.

Appendix 2.2

Disclosure variety on Compliance and Corruption in SIEMENS AG in Annual Reports

	ANNUAL REPORTS																							
	COMPLIANCE												CORRUPTION											
	00	01	02	03	04	05	06	07	08	09	10	11	00	01	02	03	04	05	06	07	08	09	10	11
INDEX TOTAL SCORE	1	1	8	2	8	9	15	18	23	25	20	18	0	0	0	0	0	0	4	14	14	10	6	7
COMMITMENT AND POLICY	0	0	1	1	1	1	1	1	1	1	1	1	0	0	0	0	0	0	1	1	1	1	1	1
Commitment to integrity/ compliance / fight corruption			1	1	1	1	1	1	1	1	1	1							1	1	1	1	1	1
RISK EXPOSURE	1	1	1	1	1	1	1	1	1	1	2	2	0	0	0	0	0	0	0	1	2	2	1	2
Carrying out risk assessment	1	1	1	1	1	1	1	1	1	1	1	1								1	1	1	1	1
Policies/rules for high-risk areas											1	1									1	1		1
Risks according to stakeholders																								
IMPLEMENTATION	0	0	5	0	5	6	9	10	11	13	10	9	0	0	0	0	0	0	0	8	7	5	3	3
Internal organization:	0	0	2	0	2	2	2	2	2	2	2	2	0	0	0	0	0	0	0	2	2	2	1	2
Corporate structure			1		1	1	1	1	1	1	1	1								1	1	1		1
Programmes, processes, code of conduct, rules, etc.			1		1	1	1	1	1	1	1	1								1	1	1	1	1
Employees:	0	0	2	0	2	2	4	5	6	6	5	5	0	0	0	0	-	0	0	5	5	2	2	1
Communication on the commitment to all employees			1		1	1	1	1	1	1	1	1								1	1	1	1	1
Existing training							1	1	1	1	1	1								1	1	1	1	
Incentive related scheme									1	1	1													
Other processes employee oriented							1	1	1	1	1	1								1	1			
Existence of communication/reporting channels			1		1	1	1	1	1	1	1	1								1	1			
Consequences of non-compliance								1	1	1		1								1	1			
Suppliers and Busness Partners:	0	0	1	0	1	2	3	3	3	5	3	2	0	0	0	0	0	0	0	1	0	1	0	0
Communication on the commitment towards S and BP						1	1	1	1	1	1	1								1		1		
Existing training										1														
Actions/intruments to encourage business partners							1	1	1	1	1													
Existence of communication/reporting channels			1	0	1	1	1	1	1	1	1	1												
Consequences of non-compliance										1														
MONITORING	0	0	1	0	1	1	4	5	4	4	5	4	0	0	0	0	0	0	3	4	4	2	1	1
Review of monitoring and improvement results								1	1	1	1	1									1			
Practices concerning dealing with incidents							1	1	1	1	1	1							1	1	1	1	1	1
Public legal cases regarding corruption/non compliance							1	1	1		1								1	1				
External review of programs							1	1		1	1	1							1	1	1			
Existing control system			1		1	1	1	1	1	1	1	1								1	1	1		
KEY PERFORMANCE INDICATORS	0	0	0	0	0	0	0	1	6	6	2	2	0	0	0	0	0	0	0	0	0	0	0	0
Employees:	0	0	0	0	0	0	0	1	2	1	1		0	0	0	0	0	0	0	0	0	0	0	0
Training								1	1	1	1													
Incentive System																								
Other instruments used									1															
Consequences of non-compliance												1												
Suppliers and Busness Partners:	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Intruments to encourage business partners																								
Consequences of non-compliance																								
Structure, inputs and outputs:	0	0	0	0	0	0	0	0	4	5	1	2	0	0	0	0	0	0	0	0	0	0	0	0
Corporate structure									1	1														
Communication - questions, inquirires									1	1	1	1												
Communication - reported incidents									1	1		1												
Compliance/corruption cases										1														
Other compliance KPI's									1	1														

CHAPTER 3

3. BOARD CHARACTERISTICS AND ANTI-CORRUPTION DISCLOSURE IN LARGE MULTINATIONAL COMPANIES

BOARD CHARACTERISTICS AND ANTI-CORRUPTION DISCLOSURE IN LARGE MULTINATIONAL COMPANIES

ABSTRACT

This paper analyses the impact of board characteristics on anti-corruption disclosure (AC disclosure) by large multinational firms. Based on a lens of analysis that combines stakeholder-agency theory and resource-dependence theory, we suggest that boards characterized by higher levels of independence, knowledge and diversity are more likely to present higher levels of AC disclosure than their counterparts. Using Transparency International (TI) ratings of disclosures on anti-corruption efforts by large multinational firms and an ordinal regression analysis, our findings suggest that, at least to some extent, companies with more resources in terms of board characteristics provide higher levels of AC disclosure. These results suggest that a theoretical framework combining stakeholder and resource-dependence theories may help to understand corporate AC disclosure.

Keywords: Board; corporate social responsibility; anti-corruption disclosure; corporate governance.

3.1. Introduction

Corruption is a serious economic, social, political and moral blight affecting society as a whole and companies in particular (Argandoña, 2007). It is generally viewed as a social menace, a way to cheat disadvantaged populations by diverting resources away from critical services like education, clean water, and health care (Hills et al., 2009). From the corporate perspective, corruption's detrimental effects are associated with increased operational costs through the company value chain, as well as significant legal and competitive risks (ibid.).

Although it was for many years a neglected issue amongst corporate social responsibility (CSR) priorities (ibid.), the idea that corruption is a cancer that destroys business and society is now widely accepted and companies are expected to adhere to the worldwide efforts to combat corruption. Accordingly, anti-corruption efforts are now an integral part of almost all companies' CSR agenda.

Both Transparency International (2009) and the UNGC (2009) argue that the degree of anti-corruption disclosure (hereafter AC disclosure) can be a strong indicator of the quality and comprehensiveness of a company's efforts in addressing corruption, an important mean to help understand what works in the fight against corruption, and a way to provide accountability with respect to performance on that field and to pressure other similar companies to adopt anti-corruption principles (Hess, 2009). Moreover, it is in this area of social disclosure that further developments are most needed (ibid.).

Despite the global call for research on the subject of anti-corruption, few academic studies examine AC disclosure (e.g. Dissanayake et al., 2011; Healy and Serafeim, 2015; Islam et al., Forthcoming) and only Healy and Serafeim (2015) examine factors influencing AC disclosure. Further, while Healy and Serafeim (2015) include a few governance variables in their analysis of AC disclosure, no studies to date thoroughly explore the role of board characteristics with respect to differences in reporting on corruption related issues. Our paper contributes to extant literature by analyzing the impact of board characteristics on AC disclosure.

Incorporating insights from stakeholder agency-theory and resource dependence theory, we use an ordinal regression analysis to explore the relations between board characteristics and AC disclosure for a sample of 91 large multi-national firms [drawn

from TI (2012)]. Results suggest that a theoretical framework combining stakeholder-agency and resource-dependence theories appear to provide an explanatory basis for AC disclosure as we document that companies that have specific board and firm characteristics provide higher levels of AC disclosure.

The remainder of the paper is organized as follows. The next section provides a brief background and an analysis of related literature. Section 3.3 presents the theoretical lens of analysis adopted and develops the hypotheses. Section 3.4 describes the research method. In Section 3.5 the main findings are reported. Finally, in section 3.6, the findings are discussed and some conclusive remarks are offered.

3.2. Background and related literature

Most current studies on corruption do not focus on understanding corporate disclosure practices, but rather relate the phenomenon of corruption to the social and cultural dimensions of countries (Davis and Ruhe, 2003; Jing and Graham, 2008), to human development and economic freedom (Sanyal and Samanta, 2004), to country institutional frameworks and the level of competition (Venard and Hanafi, 2008), to investment and growth (Mauro, 1995), to GDP and innovation (Shleifer and Vishny, 1993). At the firm level, recent studies show a positive relation between corruption and having local partners in high-risk industries (Spencer and Gomez, 2011) or foreign direct investment (Kwok and Tadesse, 2006). The limited studies examining corporate disclosure on the fight against corruption focus on companies' practices with little emphasis on the factors explaining this type of social disclosure (Gordon and Wynhoven, 2003; Novethic, 2006; Transparency International, 2009; Transparency International, 2012; Dow Jones, 2015).

According to Adams (2002), past research relates corporate social disclosure (CSD) to three main types of factors: corporate characteristics (including size, leverage, profitability and industry), general contextual factors (such as the stakeholder context) and internal context (governance aspects such as chair characteristics or the existence of a CSR committee). Our study focuses on the internal corporate governance context, namely the characteristics of the board of directors, while also controlling for the effects of corporate characteristics and contextual factors.

Some authors posit that corporate governance and CSR concepts should be integrated as good corporate governance provides the foundations for good CSR (Aguilera et al. 2006). Whereas traditionally corporate governance was mostly related to questions such as what business is for, social issues including corruption are increasingly present in corporate boardrooms (Elkington, 2006). Given that disclosure policies emanate from the board of directors, sustainability disclosures may be a function of board characteristics (Michelon and Parbonetti, 2012).

There is as wealth of literature regarding corporate governance and the awareness that companies' decisions related to CSR (Jamali et al., 2008) and to CSD (Ingley, 2008) are core board responsibilities. Notwithstanding, research on how board characteristics affect CSD is relatively scarce (Adams, 2002; Haniffa and Cooke, 2005; Michelon and Parbonetti, 2012; Mallin et al., 2013). Research on the impact of board characteristics on the disclosure regarding anti-corruption efforts is even more limited (Healy and Serafeim, 2015). To our knowledge only Healy and Serafeim (2015) have yet analyzed factors influencing AC disclosure. In their study, those authors included two variables related to board characteristics: proportion of independent board members and existence of a CSR Committee. Results showed that board members independence has a positive and statistically significant relation with AC disclosure and that CEO duality was not statistically significant at explaining AC disclosure.

3.3. Theoretical framework

We adopt a multi-theoretical approach to explain AC disclosure based on stakeholder-agency theory (SAT) and resource dependence theory (RDT). SAT draws on agency theory but incorporates insights from stakeholder theory. Unlike agency theory, SAT acknowledges short-medium run market inefficiencies and views the firm as a nexus of implicit and explicit contracts between managers and all stakeholders (Hill and Jones, 1992). According to SAT, a firm is viewed as a "multilateral set of relationships amongst stakeholders" instead of as a "bilateral relationship between shareholders and managers" (Prior et al., 2008, p.162). Other stakeholder groups besides shareholders exert influence on critical decisions by managers. There are stakeholders who contribute with critical resources to the firm and have the power to provide or withhold resources effectively, thus having some influence on the

management decisions. Such stakeholders "supply the firm with resources on the implicit (tacit) understanding that their claims on the organizations will be recognized" (Hill and Jones, 1992, p.140). Amongst these claims one can count shareholder claims for return on investment, employee claims for higher wages, consumer claims for higher quality and/or lower prices, supplier claims for lower prices and/or more stable ordering patterns. SAT focuses on the agency relationship between managers and all stakeholders, and highlights the importance of having that relationship monitored by governance structures (Hill and Jones 1992). According to SAT, the board of directors is not only responsible for safeguarding the interests of its company's stakeholders (ibid.), but it must also ensure a balance between satisfying the interests of the different stakeholders and for being accountable towards them. Accordingly, we expect differences in board composition to relate to differences in AC disclosure.

Beyond the arguments supported by SAT, we rely on RDT to better understand how specific differences in board composition might be expected to influence AC disclosure. RDT focuses on the effects of the environment on organizations. It assumes that organizations engage in exchanges and transactions of resources with other entities to ensure the supply of resources that are vital to its survival (Pfeffer and Salancik, 1978). As posited by RDT, boards bring important resources to the firm by providing expertise, advice and counsel (Hillman and Dalziel, 2003), channels for communicating information with external organizations, and preferential access to commitments or support from outside members (Pfeffer and Salancik, 1978). Members with experience and a wide range of networks add value and enhance the advisory function, while enhancing legitimacy and contributing to firm reputation (Hillman and Dalziel, 2003). Mallin et al. (2013) contend that the advisory role of the board is also a measure of stakeholder orientation in the sense that board member resources will be used to implement stakeholder-oriented strategies.

Prado-Lorenzo et al. (2009) argue that the strength of the board of directors is strictly connected to independence and diversity, while Amran et al. (2014) assert that specific knowledge is also beneficial. Accordingly, we focus on these factors. We investigate the impact on of five board characteristics found to influence CSD in previous literature: two measuring independence (CEO duality and proportion of independent board members); two measuring diversity (proportion of community

influentials and proportion of women on the board); and one measuring the impact of specialized social-related knowledge which we consider to be an important intangible regarding the specific type of social disclosure (existence of a CSR committee).

Independence.

CEO Duality. This variable is relevant because corporate disclosure policies are influenced by corporate politics and by CEOs' attitudes (Gibbins et al., 1990). The CEO duality discussion identifies a possible conflict regarding the accumulation of the CEO and Chairman functions. The CEO is a representative of the top management and the chairman is a guarantee that the management is performing according to shareholders' interests (Kesner and Johnson, 1990). Combining the function of CEO and Chairman would, under an AT perspective, increase the risk that the CEO would adopt strategies that favor personal interests even if they are detrimental to the company (Jensen and Meckling, 1976). The separation between the duties of CEO and Chairman of the board allegedly contributes to preventing the pursuit of personal rather than company interests (ibid.). Increased separation of duties could reduce the advantages associated with withholding information, increasing the monitoring effectiveness of the board and consequently ensuring higher levels of transparency, thus increasing the levels of disclosure. Past research shows evidence of both negative (Ballou et al., 2006; Barako et al., 2006; Lattemann et al., 2009) and null (Ho and Shun Wong, 2001; Haniffa and Cooke, 2002; Ntim and Soobaroyen, 2013) impact of duality on voluntary disclosure. Regarding AC disclosure we hypothesize:

H1: Firms with CEO duality will have a lower AC disclosure.

Proportion of Independent Board Members. Dominance of independent board members is viewed by SAT proponents as a governance instrument to enhance the monitoring role of the board (Fama and Jensen, 1983), decrease managerial discretion and opportunistic behavior (Jensen and Meckling, 1976; Gibbins et al., 1990) and ensure higher effectiveness (Haniffa and Cooke, 2005). According to RDT, independents are viewed as a source of additional transparency of information due to their independence condition (Kesner and Johnson, 1990) and breadth of expertise (Fama and Jensen, 1983). Past research is not consensual on the influence of

independent board members on social disclosure. Khan et al. (2013) and Ntim and Soobaroyen (2013) provide evidence of significantly higher levels of voluntary disclosure by firms with a higher proportion of non-executives (that are not necessarily independent). On the contrary, Eng and Mak (2003) and Haniffa and Cooke (2002) concluded that an increase of non-executive directors actually reduced voluntary disclosure in listed Singaporean and Malayan firms, while Ho and Shun Wong (2001), found no evidence to support that a higher number of independents led to a higher extent of disclosure. Regarding anti-corruption, Healy and Serafeim (2015) concluded for a positive significant effect of board independence over AC disclosure. We suggest that a higher percentage of independents on the board reduces the benefits of withholding information, leading to increased disclosure regarding anti-corruption practices:

H2: Firms with a higher percentage of Independent Board Members have higher AC disclosure.

Diversity.

Diversity is often defined as the variety, traits (Prado-Lorenzo et al., 2009) or resources brought by board members, or the different set of attributes, characteristics and expertise brought by the individual members to the board process and decision making (Van der Walt and Ingley, 2003). Diversity brings heterogeneity to the board, enhanced networks and ties, contributes to a greater capacity to understand and solve problems, and to increased reputation (Bear et al., 2010) while also legitimizing a company's actions (Hillman et al., 2000). Promoting diversity in the boardroom is likely to impact positively on the voluntary provision of holistic information and thus improves stakeholder engagement (Frias-Aceituno et al., 2013). Studies linking board diversity and CSR disclosure are rare (Baracko et. al, 2006; Hannifa and Cooke, 2005; Khan, 2010) and seem to confirm a positive relationship between diversity and CSD (Rao and Tilt, 2013). To our knowledge no study has yet analyzed the impact of diversity on AC disclosure. To analyze the impact of diversity on AC disclosure we use two measures: gender and the proportion of community influential board members.

Proportion of Community Influentials. According to Michelon and Parbonetti (2012), the existence of board members who are community influential individuals impacts sustainability. Community influential members have networks composed of academic experts, scientific resources, legal, investment and commercial banking networks (Bear et al. 2010). In addition, they have ties to government agencies, community groups and non-profit organizations (Hillman et al. 2000) and provide access to academic experts, scientific resources, legal, investment and banking networks (Bear et al. 2010). Networks represent increased knowledge and they are sources of advice, expertise, and connections that enhance the company relationship with its stakeholders. In general, networks "enable [a] forum for discussion, direct attention to new practices, and facilitate the transmission of information and normative". Diversity helps the board to better understand its environment and brings increased capacity to understand and solve problems (Bear et al. 2010), while also legitimizing a company's actions (Hillman et al. 2000). Following Hillman et al. (2000), Markarian and Parbonetti (2007) and Michelon and Parbonetti (2012) we classify independent directors as being community influential when they are retired politicians, academics, or members of social and non-profit organizations. We expect that an increased proportion of community influential individuals will increase transparency and consequently disclosure. We state this hypothesis as:

H3: Companies with a higher proportion of community influential members have higher AC disclosure.

Gender. Research regarding board diversity mostly focuses on gender (Van der Walt and Ingley, 2003; Rao and Tilt, 2013). The discussion centers on whether women and men bring different resources to the company because of inherently different views of the world or approaches to problems. Some authors contend that women are on average less selfish and more ethically driven (Eckel and Grossman, 1998). According to Rao and Tilt (2013) most past literature provides evidence of a positive relationship between a higher women representation in the board of directors and CSR. Past studies suggest that female gender positively influences CSR strategy (Fernandez-Feijoo et al., 2012), reporting (Rao et al., 2012; Fernandez-Feijoo et al., 2014), corporate reputation (Brammer et al., 2009) and corporate social performance (Boulouta, 2013). Additionally, boards with higher women representation were shown to be more

sensitive to CSR (Williams, 2003) and to achieve higher CSR strength ratings (Bear et al., 2010). Also, women directors were found to be more philanthropically driven compared to more economically driven male directors either globally (Ibrahim and Angelidis, 1994; Eckel and Grossman, 1998; Williams, 2003) and in specific areas like community and the arts (Williams, 2003). Among the few exceptions to that positive relation are for instance the studies of Bear et al. (2010) that found no relation between the presence of women on the board and environmental social disclosure or Khan (2010) who found no significant relationship between having woman in the board and CSR reporting. Regarding AC disclosure, we hypothesize:

H4: Firms with higher percentage of female board members will have a higher AC disclosure.

Knowledge

CSR Committee. The establishment of a CSR committee is viewed as a capital resource for an organization (Amran et al., 2014, p.222). The presence of a CSR representative on the board could bring increased knowledge and awareness on the importance of global CSR and more specifically about the CSR issue under study – that of the fight against corruption. Having a CSR representative on the board may be a resource used by the company to ensure institutional legitimacy and may act as a substitute for increased disclosure, or on the contrary act as a resource that could make boards more sensitive to CSR issues, consequently increasing transparency and leading to increased disclosure. Specific knowledge of the board has been the subject of research in the past through studies about diversity provided by education and the past track of board members. Regarding the impact of specific committees on disclosure, Kent and Monem (2008) found a positive relation between the existence of an environmental committee and triple bottom line reporting in Australia, whereas Michelon and Parbonetti (2012) only found weak evidence of the relation between the presence of a CSR Committee or Director on social disclosure. Following RDT, and regarding AC disclosure, we hypothesize that:

H5: Firms with CSR representatives on the Board have higher AC disclosure.

3.4. Research design

Our initial sample consisted of the 105 publicly listed companies included in the Transparency International Report "Transparency in Corporate Reporting: Accessing the World Largest Companies" (TI 2012). We excluded 14 companies for which we could not gather data regarding the independent variables[4], resulting in a final sample of 91 firms (Table 3.1). Country distribution reflects a comparatively high number of observations in the United Kingdom (13) and United States of America (39). Regarding industry, observations are concentrated over four main industry types, namely consumer goods and services (N=16), healthcare (N=10), oil and gas (N=14) and technology (N=10).

Table 3.1. Sample by country and industry

Country	**Total**	**Country**	**Total**	**Industry**	**Total**
Australia	3	Japan	4	Basic Materials	3
Belgium	1	Korea	1	Consumer Goods & Services	16
Brazil	1	Luxembourg	1	Healthcare	10
Canada	2	Mexico	1	Industrials	5
China	4	Netherlands	1	Oil & Gas	14
France	6	Norway	1	Technology	10
Hong Kong	1	Spain	2	Telecommunications	7
India	2	Switzerland	3	Utilities	3
Israel	1	UK	13		
Italy	2	USA	39		
Totals			91		91

Our dependent variable is based on the Anti-Corruption Index as provided by TI (2012). Using documents or information publicly available on the global websites of the

[4] We excluded 14 companies from Germany (8), Brazil (2), China (1), Japan (1), Russia (1) and Saudi Arabia (1) for which we could not gather information regarding board independence or CEO duality.

companies included in the sample, TI (2012) developed a weighted index including thirteen categories (seven related to companies' policies, five to internal practices and one to monitoring activities). We adapted the index provided by TI by un-weighting the index and attributing a score of "1" if a particular category was disclosed or "0" if no disclosure was detected. The final adapted AC disclosure index amounted to a maximum of 13 points.

We used the ordinal logistic regression to test the relationships between the dependent and the independent variables. The model used is as follows:

DUAL INDEP CI + GENDER CSR STAKE INDRISK

UNGC SIZE PROFIT

Independent variables and data sources are listed in Table 3.2.

Table 3.2. Summary if independent variables

Variable	Definition	Measure	Source
DUAL	CEO Duality	1 if the CEO is Chairman, 0 if otherwise	Annual Report, Proxy Statements Website
INDEP	Proportion of Independents	Ratio of independent board members to board size	
CI	Proportion of Community Influentials	Ratio of Community Influentials to board size	
GENDER	Percentage of Women	Ratio of women on board to board size	
CSR	CSR Committee on the Board	1 if there is a CSR Committee member on the board; 0 otherwise	
STAKE	Stakeholder Orientation	Construct as used by Dhaliwal et al. (2012)	
INDRISK	Pertaining to a Risk Industry	1 if the Company operates in a corruption-risk industry (as defined by TI), 0 otherwise	OSIRIS Database
UNGC	Pertaining to UNGC	1 if UNGC Signatory, 0otherwise	UNGC
SIZE	Company size	Log (Total Assets of the Firm)	OSIRIS Database
PROFIT	Company profitability	ROE (Profit/Loss to Total Equity)	

The main independent variables used in the model pertain to the board characteristics as discussed above. We also include several control variables to capture other factors that are likely to influence AC disclosure. First, a country's stakeholder orientation is considered. The influence of the various stakeholders over managerial decisions, such as on AC disclosure, is likely to be greater in countries with higher stakeholder orientation where constituents may pressure the company towards increased transparency leading to increased disclosure (Van der Laan Smith et al., 2005; Kolk and Perego, 2010; Dhaliwal et al., 2012; Dhaliwal et al., 2014). We use the Dhaliwal et al. (2012) country stakeholder orientation measure (STAKE), which comprises information regarding: (1) countries environment in protecting stakeholders regarding employment, social security, collective bargaining and human rights laws; (2) the existence of CSR related laws in each country; (3) the country level of public awareness regarding CSR issues; (4) countries relative rankings regarding sustainable development, ethical practices, social responsibility of leaders and corporate responsibility competitiveness.

Second, we control for association with the United Nations Global Compact (UNGC). Engaging in associations with symbols of legitimacy may be a way for a company to ensure legitimacy (Lindblom, 1994) and achieve enhanced reputation, and we argue that adherence to the UNGC might serve this purpose. Further, UNGC signatories have more publicly available information in terms of policy and management systems related to anti-corruption than other companies (TI, 2009). Hence, we include a one/zero indicator variable to identify companies that are UNGC signatories.

Third, prior evidence suggests that companies from higher corruption risk sectors disclose more on their anti-corruption practices (Gordon and Wynhoven, 2003; Novethic, 2006; Healy and Serafeim, 2015). Following Healy and Serafeim (2015), we use TI (2009) classifications of differences in industry risk of corruption. Firms in the Oil & Gas operations, Basic Materials, Aerospace & Defence, Capital Goods, Construction, Telecommunication Services and Utilities are considered as being of higher risk of corruption. A one/zero indicator is used to account for companies pertaining/not pertaining to industries at a higher risk of corruption.

Finally, we include controls for size and profitability. Size has persistently been found to be a factor influencing CSD. Larger corporations are expected to have higher disclosure because they have a bigger effect on community and face the pressure of larger stakeholder groups (Belkaoui and Karpik, 1989; Patten, 1991; Patten, 1992; Gray et al., 1995; Hackston and Milne, 1996). More profitable companies are deemed to have increased resources available for CSD (Hackston and Milne, 1996) and also increased sensitivity and knowledge regarding CSR (Belkaoui and Karpik, 1989), both leading to potentially higher levels of AC disclosure.

3.5. Main findings

Descriptive statistics for dependent and independent variables are shown in Table 3.3. Our independent variable, AC disclosure, has an average value of nine out of 13, which suggests a relatively high level of disclosure by the companies in our sample. Regarding independence, board seats of the majority of companies are occupied by independents (68%) and 46% of the companies have the same person performing CEO and Chairman functions. In terms of diversity, on average, 51% of board members are community influentials and 18% are women. Slightly more than one third of our sample companies had CSR committees represented on the board. Approximately 29% of the companies analyzed are from risk industries and 47% were enlisted in the UNGC in our year of analysis.

Table 3.3. Descriptive statistics

Variables	Mean	Minimum	Maximum	SD
Dependent variable				
Anti-Corruption Disclosure	9	0.00	13.00	3.24
Continuous independent variables				
INDEP (%)	0.68	0.00	1.00	0.24
CI (%)	0.51	0.00	1.00	0.25
GEND (%)	0.18	0.00	0.43	0.11
STAKE	-0.49	-2.73	2.62	1.22
SIZE (Log Assets)	8.23	6.40	9.40	5.89
PROFIT (ROE %)	86.56	-8.12	5476.86	571.65
Dichotomous independent variables	**Yes**	**No**		
DUAL	46%	54%		
CSR	32%	68%		
IND_RISK	29%	71%		
UNGC	47%	53%		

Table 3.4 provides Pearson correlations for our continuous independent variables. As indicated in the table, the correlation coefficients between variables is not high, suggesting that multicollinearity is unlikely to be a problem[5].

[5] As a rule-of-thumb, multicollinearity in regression analysis is considered harmful only when it exceeds 0.8 (Gujarati, 1995).

Table 3.4. Pearson correlation matrix for the continuous independent variables

	INDEP	**CI**	**GEND**	**STAKE**	**SIZE**	**ROE**
INDEP	1					
CI	0.437**	1				
GEND	0.381**	0.273**	1			
STAKE	-0.063	-0.167	0.041	1		
SIZE	0.018	0.110	0.065	0.255*	1	
ROE	0.055	-0.073	0.000	-0.092	-0.124	1

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

Results of the regression analysis are provided in Table 3.5. The explanatory power of the model is relatively high based on the Nagerlkerke R^2 of 37.3%. With the exception of size, the coefficients of all control variables are in the hypothesized directions, and stakeholder orientation, industry risk, and size (although signed opposite from expectations) are statistically significant. The unexpected finding with regard to firm size is potentially a function of TI's focus on only the very largest multinational firms in the world. Importantly, we find at least some evidence that board characteristics, as hypothesized, appear to influence AC disclosure. The positive and significant association for the proportion of independents confirms our expectation that companies with more independent board members have increased disclosure regarding their anti-corruption practices (Hypothesis 2). Similarly, we find support for Hypotheses 3 and 4 in that our diversity variables, measured by gender and the proportion of community influential members on the board, are both positively and significantly (at $p < .10$, or better) related to AC disclosure. However, while both the CEO duality and CSR variables are signed as expected, neither is statistically significant at conventional levels. As such our findings do not support Hypotheses 1 or 5.

Table 3.5. Results from Ordinal Regression

	Coefficient	Sig.		Coefficient	Sig.
LOCATION					
INDEP (%)	2.745	0.005	STAKE	0.404	0.042
CI (%)	2.143	0.021	IND_RISK = 0.00	-0.962	0.036
GEND (%)	3.473	0.087	UNGC = 0.00	-0.669	0.121
DUAL	-0.206	0.631	SIZE (Log Assets)	-0.909	0.011
CSR= 0.00	-0.364	0.401	PROFIT (ROE %)	0.000	0.356
Model Statistics					
X^2	41.903		Sig.	0.000	
Two log likelihood	381.360		Nagelkerke R^2	0.373	

3.6. Discussion and concluding comments

In this study, we examined the impact of board characteristics on AC disclosure. Using a frame of analysis combining stakeholder-agency and resource dependence theories, we find that certain board characteristics appear to explain differences in AC disclosure by the large multinational companies included in our sample.

We document a significant positive association between overall board member independence and AC disclosure, suggesting that stronger boards may implement additional monitoring and advisory mechanisms to reduce the asymmetry of information between the preparers of information and stakeholders (Rhodes, 2010), consequently presenting higher AC disclosure. This result is also in line with past studies suggesting that boards with a higher proportion of outside members are more concerned with reputation and sustainability (Ibrahim and Angelidis 1995; Post et al. 2011) and with Healy and Serafeim (2015), who also found a positive significant relation between board independence and AC disclosure. It is important to highlight, as Healy and Serafeim (2015) also refer, that it is difficult to evaluate whether boards with

increased independence actually have stronger anti-corruption efforts or they just have improved disclosures.

Results also support our expectations that diversity on the board will lead to greater AC disclosure. Consistent with Michelon and Parbonetti (2012), we find that higher levels of community influentials on the board are associated with higher disclosure levels. Similarly, we document that a greater representation of women on boards of directors is significantly associated with higher AC disclosure (although only at a 90% confidence interval), a finding consistent with other prior studies of board composition on aspects of social disclosure (e.g., Williams, 2003; Mallin et al. 2013).

In contrast to expectations, but aligned with Healy and Serafeim (2015), our results show that CEO duality is not statistically significant at conventional levels. Similarly, the presence of a CSR committee on the board was also not statistically significant at explaining AC disclosure.

In general, the findings that certain differences in board characteristics are associated with higher levels of AC disclosure suggest that exploring CSD practices through a combined lens of SAT and RDT is warranted. Boards are argued to be important tools for maintaining stakeholder relations and the resources that diversity and expertise bring appear to help in explaining disclosure choices. Extending this reasoning to examinations of other types of corporate information provision could thus prove interesting. While our investigation adds to the limited body of research concerning the impact of corporate governance on CSD, we more importantly shed light on the under-researched topic of corporate anti-corruption practices. Understanding what motivates AC disclosure is essential because corporate disclosure of efforts to combat corruption can further enforce activities while opening the dialogue to other stakeholders who can then pressure the firm, access its efforts and distribute knowledge of best practices (Osuji, 2011).

Like all studies, ours is subject to limitations. First, we focus on a relatively small number of multinational companies and the degree to which our findings generalize to broader samples is not addressed. Thus, extending our analysis to a larger sample that is richer in terms of size, industry, and country of origin would appear to be warranted. A further limitation is that our reliance on the TI disclosure ratings means

that we are analyzing disclosure that particular organization deems as relevant. Alternative disclosure schemes focusing more heavily on anti-corruption performance metrics could potentially also prove interesting. Finally, we note that our study examines AC disclosure at one particular point in time. Examining whether adaptations in board characteristics lead to changes in AC disclosure or other aspects of anti-corruption performance would strengthen the basic findings document here.

CHAPTER 4

4. MARKET REACTIONS TO TRANSPARENCY INTERNATIONAL REPORTS ON CORPORATE ANTI-CORRUPTION DISCLOSURE

MARKET REACTIONS TO TRANSPARENCY INTERNATIONAL REPORTS ON CORPORATE ANTI-CORRUPTION DISCLOSURE

ABSTRACT

In this paper, we examine the investor response to the issuance of Transparency International's (TI) 2012 and 2014 "Transparency in Corporate Reporting: Assessing the World's Largest Companies" reports. Building on prior studies of political cost-inducing events in the environmental domain, we anticipate a negative market reaction, although we argue that the adjustment will be less severe for firms rated as having better anti-corruption disclosure. Focusing on a sample of U.S companies to control for country-level effects and to allow for comparison with the prior environmental-themed studies, we document a significantly negative market reaction to the first TI report issuance. Although also negative, the market reaction to the 2014 report was not statistically significant. However, we also document that, as expected, market adjustments differ significantly across sub-groups based on anti-corruption disclosure in both time periods. These results hold controlling for other factors potentially influencing investor perceptions of exposure to the report issuances. In general, our results are consistent with the prior studies and suggest the market is savvy to political cost exposures arising from non-environmental events.

Keywords: AC disclosure, Transparency International; Regulatory Costs

4.1. Introduction

Corruption has become one of today's most pressing global and ethical problems (Sanyal and Samanta, 2004; Everett et al., 2006) and a major social issue (Ashforth et al., 2008). Studies indicate that corruption is widespread in international business (Hauser and Hogenacker, 2014) and has severe economic and social consequences. And while several organizations are well known for contributing to the fight against corruption, perhaps foremost among those is Transparency International (TI). Wang and Rosenau (2001), Andersson and Heywood (2009), and others note that the organization has used a series of indices and publications to bring attention to the issue of corruption. Until 2012, the TI efforts focused only on country-level performance and information. However, in that year, the organization released its first firm-level report under the name "Transparency in Corporate Reporting: Assessing the World's Largest Companies" (Transparency International, 2012) and followed that up with a second release in 2014. In this study, we analyze the investor reaction to the issuance of these firm-level TI reports.

A number of prior studies document significant negative market reactions for U.S. companies following events potentially increasing political cost exposure (e.g. Hill and Schneeweis, 1983; Blaconniere and Patten, 1994; Blacconiere and Northcut, 1997), although these relate almost exclusively to issues in the environmental domain[6]. We extend this vein of research by focusing on a corporate social issue, corruption, that we argue might also induce increased exposures for affected companies. Further, because the prior studies indicate that differences in political cost exposure relate to differences in market response across firms, we explore whether having better anti-corruption disclosure (hereafter AC disclosure) as evaluated by TI in their reports serves to reduce negative market reactions for companies included in the releases.

Using a sample of U.S. companies to reduce potential country-level effects and to allow for comparison with the prior environmental-themed studies, we find a negative and statistically significant average market reaction to the issuance of the 2012 TI report. We also document that companies rated as better AC disclosers suffered

[6] An exception is Dowdell et al. (1992) investigation of the market reaction to a series of deaths due to product tampering in the pharmaceutical industry.

significantly less negative reactions, although other potential regulatory cost exposure variables were not significant. In contrast, while the mean market response to the issuance of TI's 2014 report is not statistically significant overall, AC disclosure, controlling for the other regulatory cost exposures, is again positively related to market changes. These results are consistent with the findings of the prior investigations into environmental-related events, and suggest that investors are equally as savvy to potential political cost exposures in other corporate social responsibility areas of concern.

Our paper is organized as follows: In the next section we provide background on corruption and TI, followed by a literature review and the development of our hypotheses. We then present our methods and results, followed by our conclusion section.

4.2. Relevant literature and development of hypotheses

In this study, we are interested in the on-going issue of corporate corruption. Hess and Ford (2008, p.312) argue, for example, that bribery remains "a common business practice," and according to Wang and Rosenau (2001) companies world-wide pay out more than $80 billion on bribes each year. Evidence from KPMG Forensics' *Integrity Survey 2013* indicates that issues with money laundering and other illicit activities are also widespread within the corporate world (KPMG Forensic, 2013). The issue of corruption has received increasing attention from both the media and academic investigators over the past two decades (Andersson and Heywood, 2009), although much of the latter tends to focus on macroeconomic aggregates such as output, consumption, and physical capital (Donadelli et al., 2014). Andersson and Heywood (2009, p.747) argue that TI has been the most influential organization in terms of "sharpening the focus on corruption."

Established in 1993, TI employs a variety of tools in its work to curb corruption. For example, the organization has established alliances with worldwide institutions such as the Office of Economic Development and the World Bank, and it has also published documents such as "Business Principles for Countering Bribery" and the "Corruption Fight Toolkit" to offer advice and suggestions on reducing corruption practices (Wang and Rosenau, 2001). Perhaps most importantly, at the country level TI has published an

annual "Corruption Perceptions Index" since 1995, ranking countries in terms of their perceived levels of corruption (Andersson and Heywood, 2009). The intent of the organization, according to Wang and Rosenau (2001), is to employ what is often referred to as *politics of shame* to heighten public awareness of corruption issues.

Until 2012, TI issued no formal reports singling out the corruption issues associated with specific firms, but in July of that year released its first-ever "Transparency in Corporate Reporting: Assessing the World's Largest Companies." The report, and a follow-up issued in November of 2014, rated the companies on the disclosure of their efforts to combat corruption. TI argues that company reporting on anti-corruption efforts can allow stakeholders to better monitor firms' activities, which in turn may provide incentives for companies to reduce corruption practices. However, because the reports, for the first time, single out companies for their efforts with respect to the issue of corruption, we believe their issuance may serve to increase the likelihood that firms included in the reports may face greater social and political pressures with respect to their corruption exposures. If investors believe this is true, it could be expected to lead to market valuation impacts for the companies.

4.3. Prior studies of political cost exposure

A number of academic investigations explore how investors respond to events that potentially increase the social and political cost exposure of affected firms. The earliest of these, Hill and Schneeweis (1983) and Bowen et al. (1983), both examine the market reaction following the near nuclear meltdown at General Public Utility's (GPU) Three Mile Island power plant in 1979. Focusing on U.S. utility companies other than GPU, both studies find significant negative market reactions for intra-industry firms with nuclear power-based facilities, with the latter study showing more negative reactions for firms with higher dependence on nuclear power.[7] As the market prices for utilities without nuclear capacity were virtually unchanged, both sets of authors attribute the primary findings to investor concerns with potential regulatory cost increases associated with nuclear power generation. In a somewhat similar study, Blaconniere and Patten (1994) investigate the intra-industry market reaction following Union

[7] Hill and Schneeweis (1983) use monthly returns whereas Bowen et al. (1983) rely on daily returns. The studies also differ in the way they break out the nuclear power capacity of their respective samples.

Carbide's chemical leak in Bhopal, India in 1984. Also relying on a sample of only U.S. companies, Blacconiere and Patten document a significant negative market adjustment for their portfolio of firms over the five trading-day period following the disaster. In cross sectional analysis, the authors also show that individual company market reactions were negatively associated with firms' levels of chemical sales as a ratio of overall revenues, and positively related to levels of prior environmental disclosure. Blacconiere and Patten thus argue that, consistent with the studies of Three Mile Island, it was regulatory cost exposure that drove the market reaction. Also examining a catastrophic environmental event, Patten and Nance (1998) analyzed the market reaction of U. S. petroleum companies (other than Exxon) following the 1989 *Exxon Valdez* oil spill off the coast of Alaska. In contrast to the prior studies, Patten and Nance report increased market returns, on average, for this particular event. However, using cross sectional tests, they show that abnormal returns were negatively related to both firm size and having petroleum operations in Alaska, and positively associated with levels of prior environmental disclosure. Patten and Nance (1998) thus claim regulatory cost concerns significantly influenced the market reactions even though the returns were positive overall.

Focusing on legislative environmental events as opposed to environmental disasters, two additional studies also present evidence that investors negatively value exposure to potential regulatory cost exposures. The first of these, Blacconiere and Northcut (1997), determine the overall market reaction to a series of events related to the passage of the Superfund Amendments and Reauthorization Act of 1986. Blacconiere and Northcut report negative cumulative abnormal returns, on average, for their sample of U.S. firms with chemical operations, and further find that reactions are more negative for firms with larger Superfund exposures while, consistent with Blacconiere and Patten (1994) and Patten and Nance (1998), companies with higher levels of environmental disclosure suffered less negative market effects. Finally, Freedman and Patten (2004) report an overall positive market reaction surrounding the first President Bush's unexpected call for changes to the Clean Air Act in June of 1989, but also document that companies with higher levels of airborne toxic releases suffered more negative adjustments while differences in the reaction were positively related to levels of prior environmental disclosure.

4.4. Hypothesis development

In contrast to events of an environmental nature, we focus in this study on the TI release of reports with company-level assessments related to the issue of corruption. As noted above, TI is recognized as a major force in the battle against corruption, and as such, we argue that investors could see the reports as increasing social and political exposures for affected firms. For example, knowing that TI is evaluating, and making publicly available, company efforts with respect to corruption efforts could lead investors to believe firms will need to incur additional costs to improve those efforts, communicate the changes, and participate in any political debate arising from TI's efforts. Based on the results of the prior environmental-related studies, we would therefore anticipate a negative market response to the issuance of the TI reports, and we formally state this hypothesis as:

H1: The market reaction to the issuance of TI firm-level reports will be negative.

While, on average, we anticipate negative market responses to the issuance of the TI reports, prior research also suggests that the reaction will vary across social and political cost exposure. A primary focus of the TI firm-level reports relates to the information companies are already providing regarding their effort to address corporate corruption. As such, we believe that investors will assess less exposure risk to firms rated as having better AC disclosure by TI, and will thus anticipate lower levels of cost exposure for these firms. We state this second hypothesis as:

H2: Companies with better AC disclosure will suffer less negative market reactions to the issuance of TI firm level reports.

4.5. Methods

4.5.1. Sample

We draw our sample from the 2012 and 2014 Transparency International reports on corporate transparency and anti-corruption reporting. However, in order to control

for potential differences in regional perceptions toward corporate corruption[8] and to allow for comparison with prior research into the market reaction to potential regulatory cost increases, we limit our analysis to only the U.S.-based firms included in the reports. We also used the LexisNexis database to search for potentially confounding events surrounding the dates of the TI report releases for each of the U.S. companies included in the reports to assure that any market adjustments were not a function of other news. Our final sample consists of 39 companies in 2012 and 43 firms from 2014. As TI focused only on the largest multi-national firms in the world for its ratings, our sample companies are large (e.g., average market value of $123 billion in 2012), and they represent seven (eight) different industry sectors in 2012 (2014). Appendix 4.1 identifies the sample firms for each of the two periods of our analysis.

4.5.2. Market Reaction

Following Brown and Warner (1985) and others, we use standard event study methods to determine the investor response to the TI report releases. Under this approach, we first identify the sensitivity of each firm's stock movements to changes in the overall market by estimating the standard market model[9] stated as:

where t is the time index, i is the security, is the error term associated with security i at the moment t, is the market return of security i in day t, is the return of the market portfolio (measured in our study by the S&P 500) and are the parameters of the market model. We collect daily stock return data from DATASTREAM, and we estimate the model over a 200 trading day period culminating two days before the release date of each of the reports (10 July 2012 and 4 November 2014).

[8] Regional perceptions regarding corruption may differ across countries. The U.S. has had a particularly strong intervention in the fight against corruption. Since the approval of the Foreign Corrupt Practices Act in 1977 several measures have been taken regarding the fight against corruption. The U.S. has played an important role in the fight against international corruption through leading and/or participating in initiatives such as the Inter-American Convention Against Corruption and the OECD Anti-Bribery Convention (through the International Anti-bribery Act) both in 1997, the United Nations Convention against corruption and the adoption of the National Strategy to Internationalize Efforts Against Kleptocracy in 2004 or the Dodd-Frank Act in 2008. More recent developments include the approval of the first Anti-Corruption Act in Florida State in 2014. (www.ussoecd.usmission.gov; www.transparency-usa.org)

[9] Market model methods have been extensively used to estimate abnormal returns (Dowdell et al., 1992; Blaconniere and Patten, 1994; Blacconiere and Northcut, 1997; Patten and Nance, 1998).

For each day of the test period, we calculate the abnormal return as a company's actual return minus the expected return based on the parameter estimates from the market model regressions and overall market returns for the date:

and then identify cumulative abnormal returns (CARs) by summing abnormal returns over the four-day period from trading dates -1 through +2. We use these returns to test our first hypothesis.

4.5.3. Impact of anti-corruption disclosure

To test Hypothesis 2, we first partition the sample for each issuance at the mean AC score for the period and use a standard *t*-test of means to identify the significance of the differences. We expect the average market reactions to be less negative for companies in the better reporting classification for each of the test periods. However, because other factors might be expected to also impact investor perceptions of the regulatory cost risk arising from the TI report releases, we also estimate the following model to control for these potential effects:

where,

= cumulative abnormal return for firm i over the event window t

= scores 1 if AC score of firm i is above average for period t, and 0 otherwise

= scores 1 if firm i is from a high corruption risk industry, and 0 otherwise

= the natural log of firm i's total assets for period t

= scores 1 if firm i had any corruption-related news articles for period t, and 0 otherwise.

Our primary test variable, "AC Code", is again based on the AC disclosure scores assigned by TI, and we classify firms with scores above the mean for the sample in each period as 1, and zero otherwise. We expect this variable to be positively related to the CARs.

We include our first control variable, industry risk ("IndRisk"), to designate companies operating in sectors argued to be at more risk for corruption. Healy and Serafeim (2015), for example, claim that companies in industries having more interactions with governments relative to the sale of goods or services likely face greater corruption risks. Both Donadelli et al. (2014) and Donadelli and Persha (2014) document a more negative relation between corruption and performance for firms in corruption sensitive industries. If investors believe the release of the TI reports would increase exposure for companies with greater corruption risk, we would anticipate more negative market reactions for these firms. We rely on TI's 2009 "Bribe Payers Index" to identify corruption risks across industries, and based on that report, we classify firms in the Oil & Gas Operations, Basic Materials, Aerospace & Defense, Capital Goods, Construction, Telecommunication services, and Utilities industries as being of higher risk. We use a one/zero indicator variable to designate the high risk firms.

Our second control variable, firm size, has been used extensively in corporate disclosure research as a proxy for political costs, but its expected relation to the market reaction in this case is not clear cut. If investors anticipate larger companies to be more visible and, as such, more exposed to potential regulatory costs (e.g. Watts and Zimmerman, 1978; Hagerman and Zmijewski, 1979; Blaconniere and Patten, 1994; Blacconiere and Northcut, 1997), we would anticipate firm size to be negatively related to the CARs surrounding the issuance of the TI reports. Alternatively, however, investors could believe that larger firms have more resources at their disposal to fight corruption and/or have better anti-corruption practices already in place. If so, investors might see these companies as being less exposed to the potential regulatory costs, leading to a more positive market adjustment. We measure "Size" as the natural logarithm of assets[10] for each sample firm in the year of the respective report release, and we make no predictions as to the direction of the relation.

Finally, we also include a control for the media exposure our sample companies faced with respect to corruption issues in the year prior to the release of each of the TI reports. A number of CSR-related studies (e.g. Brown and Deegan, 1998; Patten, 2002a; Aerts and Cormier, 2009) argue that media coverage appears to lead to greater

[10] As a sensitivity test, we also estimate our model using the log of firm sales. Results, not presented here, are qualitatively similar to those using the assets measure.

social and political exposure, and as such, we anticipate that investors will react more negatively to the TI report issuance for companies facing such exposure. Again using the LexisNexis database, we searched for articles related to corruption, bribery, money laundering, whistle blowing, and scandal for each of the sample companies for the one year period prior to each of the TI report release dates.[11] We code our control variable ("MediaExp") one for any company with a corruption-related article in the media in the year prior to the relevant report, and zero otherwise.

4.6. Results

Table 4.1 provides descriptive statistics on the primary variables used in our analysis. Average AC disclosure scores were quite similar across the two periods (74.17 in 2012 and 74.00 in 2014) and ranged from 27 to 92 in 2012 and 35 to 96 in 2014. Descriptive statistics in Table 4.1 also show that 17.9% and 18.6% of our sample companies operated in high corruption risk industries in 2012 and 2014, respectively. Regarding media exposure, 35.9% of the 2012 sample companies and 34.5% of the 2014 sample companies had at least one corruption related news article published about them in the year previous to the TI report release.

Table 4.1. Descriptive Statistics

Variables	N	Min.	Max.	Mean	Std. Dev.
AC Disclosure Score 2012	39	27	92	74.17	13.911
AC Disclosure Score 2014	43	35	96	74.00	14.599
Log Assets 2012	39	7.52	9.38	8.14	0.4986
Log Assets 2014	43	7.40	9.36	8.09	0.5132
Sample Frequencies		2012		2014	
Industry Risk		7		8	
		(17.9%)		(18.6%)	
Media exposure		14		15	
		(35.9%)		(34.5%)	

[11] Following Gilley et al. (2000), our search was performed over the following media sources: The Wall Street Journal, USA Today, The Washington Post and Financial Times.

Table 4.2 identifies the mean market reactions for our sample companies across the two event periods. As highlighted in the table, the mean CAR for the 2012 report release was -1.01 percent, and this is statistically significant at p = .009, one-tailed. Although also negative (-0.46 percent), the average market response to the release of the 2014 report is not statistically significant at conventional levels. Further, a review of individual company CARs revealed one observation that fell more than three standard deviations from the mean. Excluding this outlier observation (a CAR of – 10.83 percent), average abnormal returns were reduced to -0.22 percent, which again, is not statistically significant at conventional levels[12]. Overall, these results indicate that only the initial report release led to significant downward adjustments, on average, to sample company market value.

Table 4.2. Mean CARs

Year of Report	Mean Car	*t*-statistic	Significance
2012	-1.01%	-2.743	0.009
2014 – overall	-0.46%	-1.234	0.224
2014 – no outlier	-0.22%	-0.747	0.460

Results for tests for differences in the mean reactions across better and worse AC disclosers, presented in Table 4.3, indicate that in both periods, companies with better AC disclosure suffered less negative mean market reactions than firms with lower disclosure ratings. Our independent test of means, summarized in Panel A of the table, shows that the difference in CARs in 2012 is statistically significant (p = .019, one-tailed) based on a mean market reaction of -1.88% for the worse disclosers in comparison to an average CAR of only -0.04% for the firms with better disclosure ratings. For 2014, the companies rated as worse disclosers reflected a mean CAR of -0.67%, whereas the better disclosers' average decline was only 0.30%. As noted in Panel B of Table 3 this difference in returns is not statistically significant. However, when the outlier observation is removed, the mean CAR for the better disclosing

[12] Mean CARs over a slightly shorter three day (-1,1) time frame were -0.67% in 2012, -0.22% in 2014 considering the entire sample and - 0.27% in 2014 when excluding the outlier observation.

companies improves to a positive 0.16 percent, and is significantly different from the average for the worse disclosure group, although only at p = .083, one-tailed (see Panel C of Table 4.3).

Table 4.3. Differences in mean CARs across AC disclosure

Panel A – 2012				
Category	N	Mean CAR	t-statistic	Significance[a]
Better AC Disclosers[b]	23	-0.04%		
Worse AC Disclosers	16	-1.88%	2.165	.019
Panel B – 2014 – Overall				
Category				
Better AC Disclosers[b]	24	-0.30%		
Worse AC Disclosers	19	-0.67%	0.507	.308
Panel B – 2014 – No Outlier				
Category				
Better AC Disclosers[b]	23	0.16%		
Worse AC Disclosers	19	-0.67%	1.416	.083

[a] Significance levels are one-tailed.

[b] Disclosure groups are separated at the mean disclosure score for the respective year.

Table 4.4 (2012) and Table 4.5 (2014) report the results of our regression analysis controlling for other impact factors. As indicated in Table 4.4, AC code is the only explanatory variable significantly associated with 2012 CARs, suggesting that the other potential impact factors did not influence investor concerns at the time of the first TI release. Overall, the model explains only a modest 6.3 percent of the variation in the market reactions. In contrast, results of the regression analysis for the 2014 CARs[13] (Table 4.5) indicate the model explains 27.7% of the variation in the observations. Further, in addition to AC code (significant at p = .027, one-tailed), all the three control

[13] We exclude the outlier value for this estimation.

variables are also statistically significant (at p = .005 or better). One possible explanation for the difference in the relation for the control variables in the second analysis is that investors became savvier to the threats of corruption exposures following the issuance of the first report. More importantly, the results of the regression analyses controlling for other factors provide additional support for the argument that investors interpret better AC disclosure as leading to reduced exposure to the potential regulatory cost threats arising from the issuance of the TI reports.

Table 4.4. Regression results for tests of the relation between 2012 CARs and AC Disclosure, controlling for other factors.

Sample size is 39.

Adj. R^2 = .063	F-statistic = 1.636		Significance of F-stat = .188	
Variable	Predicted Relation	Parameter estimate	t-statistic	Significance of t-statistic[a]
Constant	None	-0.117	-1.583	.123
AC Code	(+)	0.017	2.221	.033
IndRisk	(-)	-0.005	0.484	.632
Size	None	0.012	1.292	.205
MediaExp	(-)	-0.005	-0.530	.600

[a] Significance levels are one-tailed for the AC CODE, IndRisk, and MediaExp variables.

Table 4.5. Regression results for tests of the relation between 2014 CARs and AC Disclosure, controlling for other factors.

Sample size is 42[14]

Adj. R^2 = .277	F-statistic = 4.928		Significance of F-stat = .003	
Variable	Predicted Relation	Parameter estimate	t-statistic	Significance of t-statistic[a]
Constant	None	-0.140	-1.583	.005
AC Code	(+)	0.012	2.221	.027
IndRisk	(-)	-0.022	-3.005	.003
Size	None	0.017	2.953	.005
MediaExp	(-)	-0.018	-3.018	.003

[a] Significance levels are one-tailed for the AC CODE, IndRisk, and MediaExp variables.

Further Analysis

In addition to the AC scores provided in each of the TI reports, the organization also includes an overall transparency score, based partly on the anti-corruption disclosures, and partly on other factors. It is necessary, therefore, to assure that the differences in market reaction we document are not due to the transparency ratings rather than the AC disclosure. Because the two metrics are highly correlated (Pearson product-moment correlation of 0.616 in 2012 and 0.772 in 2014), including the measure as an additional variable in the regression models is problematic. Instead, we re-run our tests using the transparency scores rather than the AC scores to differentiate our sample and find no statistically significant differences in mean CARs across better and worse transparency score groups for either 2012 or 2014.[15] Similarly, regression results using the transparency score code instead of AC code yield no statistically significant relations for the replacement variable (and other variable relations remain qualitatively

[14] One observation was withdrawn from the initial sample due to being a strong outlier.
[15] This holds for 2014 with or without including the outlier observation.

unchanged). These additional tests add further credence to our claims that it is the difference in AC disclosure driving differences in the market reaction.

We also concede that, for the 2014 analysis, investors could focus on the change in AC scores themselves relative to 2012 as opposed to the levels. We first address this issue by calculating the change in AC scores for the sample companies with observations from both periods, and including this metric as an additional control variable in the regression analysis. Results indicate the change in score variable, although positively signed, is not significant at conventional levels. Further, with the change in score measure included, all of the additional explanatory variables remain statistically significant at $p < .05$. Finally, because the change in score metric is significantly correlated with the AC code variable (Pearson product-moment correlation of 0.371, $p = .020$), we also estimate the regression replacing AC code with the changes measure, and find the association with CARs is not statistically significant at conventional levels. Thus, our primary results do not appear to be influenced by the changes in AC scores.

4.7. Conclusion

A number of prior studies provide evidence that investors react negatively to environmental-related events that potentially increase the political and social cost exposure of affected firms (e.g., Blacconiere and Patten, 1994; Blacconiere and Notrthcut, 1997; Bowen et al., 1983). We extend this stream of research by exploring the market reaction to a non-environmental action with potential regulatory cost exposure threats – the issuance of TI's first-ever corporate-level reports related to corruption. TI is widely recognized as the premier organization engaged in the fight against corruption, and as such, we anticipate that investors might assume the release of the company-level reports will lead firms included to incur future costs to improve their anti-corruption efforts, communicate those actions, and/or participate in social and political debate regarding the issue. Using event study methods and focusing on only the U.S. companies included in the two reports, we find evidence consistent with the prior environmental-based studies. The average market reaction to the release of the first TI report was negative and statistically significant. Further, the market response was significantly less negative for firms rated by TI as having better than average anti-

corruption disclosure, a factor we argue signals lower levels of exposure to the regulatory cost threats. Although the mean CAR surrounding the release of the second report is not statistically significant, we document that better AC disclosure is again significantly and positively related to differences in the reaction, controlling for other impact factors. Thus, it appears that the market is savvy to political cost exposures within the social, as well as, the environmental domain.

While our results shed light on investor perceptions of regulatory cost threats, they also suggest that TI's strategy could prove beneficial in the fight against corruption. As noted by Wang and Rosenau (2001), TI's politics of shame center on raising attention to the issue of corruption, and the negative investor response to that attention would appear likely to induce management at impacted firms to address their corruption exposures. To the extent that this in turn leads to improvements in the anti-corruption efforts, the TI strategy would seem to be effective. However, in that TI has made the choice to focus largely on the AC disclosure of the firms it evaluates, a less promising outcome is also possible. Considerable research in the environmental disclosure domain documents a negative relation between corporate environmental performance and environmental disclosure (e.g. Patten, 2002b; Cho and Patten, 2007; Aerts and Cormier, 2009; Cho et al., 2012). Worse performers appear to use disclosure to reduce the exposures to social and political pressure arising from the poorer performance. Accordingly, rather than actually improving anti-corruption programs and efforts, corporations might instead choose to only change their disclosure, an act that would likely yield far fewer benefits in the fight against corruption. Which scenario plays out can only be determined by future investigation.

As with all studies, ours is subject to limitations. We limit our analysis to a restricted sample of U.S. companies, and as such cannot generalize how our results would hold across firms in other countries where attitudes toward corruption issues, as well as concerns with regulatory cost exposures may differ. Our reliance on market model methods means that we treat shareholders as a uniform group of investors with homogeneous beliefs about the value of social and political exposures and the role of disclosure in reducing those impacts. Cornell and Shapiro (1987) argue that prices responses to new information likely depends on the firm's net organizational capital and on the nature of its stakeholders, and as such it would be interesting to explore if, and

how, the differences in stakeholder power influence market reactions in the regulatory cost setting. Finally, our investigation is limited to the impact of the TI firm-level reports on shareholders only. Certainly, other stakeholder groups would likely respond to the assessments provided by TI, and exploring both what those reactions are, and how they impact corporate response could prove likewise enlightening.

APPENDIX 4.1

SAMPLE COMPANIES 2012	SAMPLE COMPANIES 2014
3M	3M
ABBOTT LABORATORIES	ABBOTT LABORATORIES
AMAZON.COM	AMAZON.COM
AMGEN	AMGEN
APPLE	APPLE
AT&T	AT&T
BANK OF AMERICA	BANK OF AMERICA
BERKSHIRE HATHAWAY 'A'	BERKSHIRE HATHAWAY 'A'
CHEVRON	CHEVRON
CISCO SYSTEMS	CISCO SYSTEMS
CITIGROUP	CITIGROUP
COCA COLA	COCA COLA
CONOCOPHILLIPS	CONOCOPHILLIPS
EXXON MOBIL	EXXON MOBIL
GENERAL ELECTRIC	GENERAL ELECTRIC
GOLDMAN SACHS GP.	GOLDMAN SACHS GP.
GOOGLE 'A'	GOOGLE 'A'
HEWLETT-PACKARD	HEWLETT-PACKARD
HOME DEPOT	HOME DEPOT
INTEL	INTEL
INTERNATIONAL BUS.MCHS.	INTERNATIONAL BUS.MCHS.
JOHNSON & JOHNSON	JOHNSON & JOHNSON
JP MORGAN CHASE & CO.	JP MORGAN CHASE & CO.
MCDONALDS	MCDONALDS
MERCK & COMPANY	MERCK & COMPANY
MICROSOFT	MICROSOFT
OCCIDENTAL PTL.	OCCIDENTAL PTL.
ORACLE	ORACLE
PEPSICO	PEPSICO
PFIZER	PFIZER
PHILIP MORRIS INTL.	PHILIP MORRIS INTL.
PROCTER & GAMBLE	PROCTER & GAMBLE
QUALCOMM	QUALCOMM
UNITED PARCEL SER.'B'	UNITED PARCEL SER.'B'
UNITED TECHNOLOGIES	UNITED TECHNOLOGIES
VERIZON COMMUNICATIONS	VERIZON COMMUNICATIONS
VISA 'A'	VISA 'A'
WAL MART STORES	WAL MART STORES
WALT DISNEY	WALT DISNEY
-	COMCAST 'A'
-	GILEAD SCIENCES
-	NEWS 'A'
-	WELLS FARGO & CO

CHAPTER 5

5. CONCLUSIONS

5.1. Conclusions

This thesis focuses in investigating anti-corruption (AC) disclosure practices, possible drivers of this type of social disclosure and consequences arising from it.

The first paper (presented in Section 2) explores how Siemens A.G – a large multinational company – used disclosure as a reaction to an external event. The study analyzes the trends in Siemens' disclosures on compliance and AC over a period of eleven years (2000-2011), during which the company was found to have paid bribes of around $1.4 billion and consequently ordered to pay a total of $1.6 billion in related fines. Results document a significant increase in the volume and breadth of compliance and AC disclosure in annual and sustainability reports starting in the year when the first corruption scandal occurred (2006). Additionally evidence shows that disclosure increased again the following year (when the first fine was charged against the company), and peaked in 2008, the year of the final settlement. Analysis of the disclosure across this period indicates attempts at both substantive and symbolic legitimation. For example, although Siemens had claimed in prior reporting to be engaged in the fight against corruption, it was only following the scandal that the company included specific disclosure of new compliance and anti-corruption procedures such as creating training programs, monitors, and watchdogs. Post-event disclosure of a symbolic nature included, for example, references to the company's association with the United Nations Global Compact (UNGC). Finally, the study also provides evidence showing that increased media attention concerning Siemens' corruption scandal led to increased AC disclosure. Overall, the results indicate that legitimacy theory and media agenda setting theory, both of which have been shown to explain environmental disclosure, appear also to apply to the AC disclosure setting.

The second paper, presented in Section 3, addresses board characteristics as a factor influencing AC disclosure and uses a frame of analysis combining stakeholder-agency (SAT) and resource dependence (RDT) theories. Results show that certain board characteristics appeared to explain differences in AC disclosure by large multinational companies. Consistent with SAT, our results show that companies with a higher proportion of independent board members disclose more on their AC practices. Aligned with RDT, results also show that the proportion of community influential board members (academics, government members, or NGO's board members) is positively

and significantly related to levels of AC disclosure and though not very strongly, so does gender. In contrast to our expectations, neither the existence of a CSR Committee on the board nor being a signatory to the UNGC, were statistically significant in explaining differences in AC disclosure at conventional levels.

Paper three examines investors response to the issuance of Transparency International's (TI) 2012 and 2014 "Transparency in Corporate Reporting: Assessing the World's Largest Companies" reports (see Section 4). Building on prior studies of political cost-inducing events in the environmental domain, we anticipated a negative market reaction to the issuance of TI reports, although we argue that the adjustment will be less severe for firms rated as having better AC disclosure. Focusing on a sample of U.S companies to control for country-level effects and to allow for comparison with the prior environmental-themed studies, document a significantly negative market reaction to the first TI report issuance. Although also negative, the market reaction to the 2014 report was not statistically significant. However, we also document that, as expected, market adjustments differ significantly across sub-groups based on AC disclosure in both time periods. These results hold controlling for other factors potentially influencing investor perceptions of exposure to the report issuances. In general, our results are consistent with the prior studies and suggest the market is savvy to political cost exposures arising from non-environmental events.

5.2. Theoretical and managerial implications

The three papers presented in this thesis are deemed to provide relevant empirical and theoretical contributions regarding AC disclosure, factors influencing the practice, and possible consequences arising from it.

First, the three papers presented in the thesis provide empirical evidence regarding corporate anti-corruption disclosure, which is consensually considered a topical (KPMG, 2013; Donadelli et al., 2014; Transparency International, 2014; UNGC, 2015) and under-researched theme (Branco and Delgado, 2012; Donadelli et al., 2014) in CSR. Furthermore, two of the studies, Papers 1 and 3, extend the abundant prior literature examining, largely, environmental events and disclosure, and the results indicate consistency with the findings of those prior studies.

Second, the results of the three papers are likely to be relevant for several key corporate stakeholders:

- Governmental and non-governmental organizations involved in the fight against corruption could use the results to argue for increased regulation to ensure that adequate levels of this important type of social disclosure are not totally dependent on manager's discretionary decisions.
- The studies should allow managers to enrich their understanding of AC disclosure practices, causes, and consequences. For example, the evidence in Paper 1 on how Siemens A.G. used substantive and symbolic legitimacy management strategies when faced with a corruption–related scandal could assist managers in dealing with their own social exposures. Further, because AC-related decisions are more and more being emanated by the board of directors, results of Paper 2 could help managers understand how specific board characteristics may be influencing their own board's perception (and requests) regarding anti-corruption. Finally, the results of paper 3 can provide managers with a better understanding of how investors view both political cost exposures and the potential for tools such as good AC disclosure to address the concerns.
- The results of the studies may also allow investors to gain a better perspective of AC disclosure practices, influences, and consequences, which may help them to better use that information in their investment decisions.

Third, the papers provide a significant theoretical contribution in that they appear to validate the explanatory power of specific theories to explain a range of social disclosure beyond the environmental domain. More specifically, legitimacy and media agenda setting theory proved useful in explaining Siemens' AC disclosure practices as a reaction to a corruption related event, while the relation between certain aspects of board characteristics and AC disclosure were consistent with the arguments of stakeholder agency theory combined with resource dependence theory.

5.3. Limitations and future research

As with all research, the studies comprising this thesis are subject to limitations. Because Paper 1 is a case study and Papers 2 and 3 rely on relatively small samples, how well the results generalize to larger populations cannot be determined. Further, all

of the sample companies included in the studies are very large multi-national firms, and while corruption risks are likely high for these companies, they also exist for firms of all sizes. Examining whether the causes and consequences of AC disclosure hold across other samples would therefore be potentially enlightening. Further, and again an issue of generalizability, Paper 3 examines only the U.S. investor response to the release of TI's firm-level reports. And while there is the belief that that was important in order to control for potential differences in country-level attitudes toward corruption and to allow for meaningful comparison with prior studies, exploring whether investors in other regions of the world similarly appear to value negatively the exposure to corruption-related risks would make for an interesting extension of Paper 3.

A second broad limitation related to both Paper 2 and Paper 3 is their reliance on the TI assessments of AC disclosure. One of the strengths of the body of environmental disclosure research is the existence of a broad set of alternative disclosure schemes that have been used in assessing differences in the extent and quality of information being provided. When theoretical claims such as those under legitimacy theory are shown to hold in studies with alternative disclosure metrics, the validity of the arguments is strengthened. No such variety exists to date in AC disclosure work, and as such, development and testing using alternative metrics would be valuable.

Finally, while the studies in this thesis shed light on AC disclosure, its causes, and its consequences, an unexplored question is whether AC disclosure actually leads to positive social benefits. While TI, the UNGC, and other organizations clearly believe that better disclosure can help lead to reduced corruption activities, that link is not explored in this thesis. Unfortunately, as evidenced in much environmental-themed research, an alternative possibility is that companies may use AC disclosure as a way of reducing their exposure to the social and political pressures arising from corruption exposures, and as such, rather than leading to better corruption performance, the disclosure may instead allow practices themselves to go unchanged. Future research needs to carefully explore, therefore, how AC disclosure actually relates to companies' AC practices.

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