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Cyndi Man ZHANG

Singapore Management University, cyndizhang@smu.edu.sg

Henrich. R. GREVE

INSEAD

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Delayed Adoption of Rules: A Relational Theory of Firm Exposure and State Cooptation

Cyndi Man Zhang
Singapore Management University
Henrich R. Greve
INSEAD

The state creates and changes rules that coerce firms, but firms can delay or decouple responses to rule changes to manage the cost of demands. Theory of compliance to the state has not yet considered the degree to which the firm can delay adoption because of low exposure to rules and state links that allow cooptation, but both of these relations between state power and firm ability to counteract it can affect the adoption decision. This makes the response to state rule changes a more strategic outcome than the theory of coercive isomorphism implies. We develop a relational theory of delayed firm compliance to a state rule change that considers firm exposure due to discrepancy from the rule and firm cooptation of the state due to state links, and we test the theory by examining the adoption of the split-share structure reform, a state-mandated corporate governance reform among listed firms in China. We find that exposure and cooptation influenced the speed of adoption and the decoupling from reform intentions. We also found that their effects on firm response to coercion weaken when the new rule becomes institutionalized. Our theory of delayed compliance is also likely to apply to coercive pressure from other powerful organizations than the state.

Keywords: *resource dependence; power; state rule change; firm compliance; institutional theory*

Firms sometimes delay adoption of rules made by powerful actors such as the state and other rule-setting organizations in spite of the risks of slow adoption or noncompliance. Such

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Corresponding author: Cyndi Man Zhang, Lee Kong Chian School of Business, Singapore Management University, 50 Stamford Road, Singapore 178899, Singapore.

E-mail: cyndizhang@smu.edu.sg

cases of noncompliance are found in a range of industries and can be highly consequential for society at large. For example, compliance to pollution regulation is incomplete and highly dependent on a voluntary institution (ISO 14001) even in the presence of rules, facility inspections, and punishment (Delmas & Toffel, 2008; Potoski & Prakash, 2005). Bank adoption of the new U.S. Federal Reserve rules on capital buffers to prevent a repetition of the financial crisis has seen significant delays.¹ Delay in adoption of state rules is not only consequential for society but can also be detrimental for firms. For example, in 2014 major banks in Europe and the United States paid \$65 billion in fines for regulatory noncompliance, mainly for price-fixing schemes and mortgage-lending irregularities with a wide span of victims.² In China, the split-share structure reform made the stock market more efficient, but after a rapid 15 months of initial adoption the remaining one-fifth of the firms showed significant delays. In the face of strong enforcement and sanctions, most firms eventually comply with rules, but some show delayed and partial adoption. It is thus important and interesting to explore what factors lead firms to delay adoption of new rules.

The phenomenon of delayed and incomplete rule adoption has not been given sufficient attention in the literature. Institutional theory examines responses to rule changes through the theory of coercive isomorphism (DiMaggio & Powell, 1983), yet there has been very little follow-up to the finding that it took 37 years for civil service reform to spread to all municipalities in the states in which it became required by law (Tolbert & Zucker, 1983). This is a remarkably slow compliance by municipalities, who are supposed to follow the law, especially because they also have a duty to enforce it. Clearly, both public and private organizations delay adoption of state rules if they see them as too costly or risky (Ritchie & Melnyk, 2012). Organizations also decouple displays of compliance from actual behaviors by adopting structures and roles that match the rules and by making adaptations to fit the organization (Meyer & Rowan, 1977). This phenomenon is documented for practices that are adopted voluntarily, such as incentive schemes for executives (Westphal & Zajac, 1994), but it has seen little exploration in practices that are required by law or other forms of rules. The reason is partly that research on compliance to rules instituted through state coercion is a very small part of institutional theory, partly because it emphasizes isomorphism over delays in compliance (Heugens & Lander, 2009).

Because institutional theory sees coercive pressures from the state or other powerful organizations as isomorphic across firms, we lack theory that can explain why some firms but not all can have delayed or decoupled compliance with legal change or other rule changes. Such theory requires a focus on the relationship between state and firm and thus becomes a relational theory of rule adoption. Delayed adoption could also be explained by contextual factors, such as lack of rule knowledge, lack of rule clarity, or lack of resources to follow it, but such factors say less about interorganizational relations and the relation between the rule-making organization and the firm. The starting point of our theory is that coercive pressure is different from cognitive isomorphism because firms see coercive pressure as externally imposed rather than taken for granted (DiMaggio & Powell, 1983). As a result, firms respond more strategically to coercive institutional pressures than to cognitive ones (Oliver, 1991). This means that the theoretical focus shifts from examining the state as having a homogeneous effect on firms to a relational theory of the state and firm interacting to either force quick adoption of the rule or create opportunities for delayed adoption. Consistent with this relational view, key elements of the theory can be drawn from resource dependence theory,

which specifies how firms manage demands from powerful organizations in the environment and make heterogeneous rather than isomorphic responses (Pfeffer & Salancik, 1978; Wry, Cobb, & Aldrich, 2013).

The puzzle of delayed rule adoption can be analyzed by taking into account that firms may see the state as an actor in the environment that imposes resource-consuming demands and thus should be managed (Pfeffer & Salancik, 1978). Rule changes not only place resource demands but also alter the institutional environment in ways that complicate adaptation and create risks for the firm (Ritchie & Melnyk, 2012). Even firms that intend to comply fully may follow a strategy of delayed adoption to let other firms go first, face the greatest uncertainty, and provide failure and success examples from which they can learn. Delayed adoption as a strategic response is consistent with evidence that firms differ in the implementation of rules on toxic chemicals information release (Doshi, Dowell, & Toffel, 2013) and environmental site inspections (Berrone, Fosfuri, Gelabert, & Gomez-Mejia, 2013).

We examine whether firms delay or decouple compliance with coercive pressure to adopt rules mandating certain actions. We view state rule changes as a form of coercion that firms may follow but not necessarily immediately and fully. We develop theory specifying that the response is determined by two firm-state relations. The first relation that we examine is the firm exposure, where exposure is the degree of legal noncompliance as seen through the discrepancy between rule and current practice (e.g., Field, Lowry, & Shu, 2005; Shu, 2000). Greater exposure means having a greater difference between current practices and the practices that the new rules require. Exposed firms are more likely to be inspected for the compliance to the new rule and penalized as examples for others to follow, generating pressure to adopt. The second relation that we examine is that firms may have links to the state that allow cooptation, which is defined as ability to access internal information about the state and anticipate and shape rule enforcement (Pfeffer, 1972). This information enables firms to delay the adoption. These relations are central because they capture state influence on the firm and firm management of state influence, respectively. Finally, we examine the interrelation of these two firm-state relational factors with institutionalization: exposure and cooptation are important early in the institutionalization process but become less impactful as the rule becomes institutionalized and has been adopted by many firms.

Our main contribution is to provide a relational theory and evidence supporting the claim that rule adoption specifically and firm compliance to coercive isomorphism more generally are variable across firms and can be explained by seeing the firm and the source of coercion as a dyadic power balance. Our relational theory draws on (a) resource dependence theory for analysis of how a firms manage their relations with the rule-setting organization and its demands and whether the social structure provides the opportunity to do so and (b) institutional theory for analysis of how coercive pressures vary in strength over time. Our empirical evidence shows that delayed adoption is more likely when firms have low exposure and strong state links that allow cooptation and that these effects weaken as the rule is institutionalized. As a broader contribution, we hope that this work brings attention to varying firm responses to coercive rules, a part of institutional theory that has been neglected, even though it provides important implications for firms' strategic choices when adapting to their environments.

Our work also contributes to the debate on structure versus agency in institutional theory by shifting the focus back to a balanced view of the two forces. Influential work by DiMaggio

and Powell (1991) saw the examination of structure in the form of environmental influences on organizations as the central task of institutional theory, setting aside agency issues such as conflicts and interests as less important topics. Their view is consistent with later work that led to a lack of recognition regarding organizational influence in the adoption and adaptation of institutions [AQ: 1] (Hirsch & Lounsbury, 1997). Recent meta-analysis has shown the focus on isomorphism as dominant and organizational differences as less important, in part because this line of research has not been designed to explore differences (Heugens & Lander, 2009). Our study, instead, is designed to explore such differences by examining agency through the organizational sources of delays in compliance timing and degree, in a context with very strong state pressures toward isomorphism.

We examine state coercion, which has often been found to produce rapid policy adoption by firms (Greve, Palmer, & Pozner, 2010). A key state policy domain is corporate governance in the form of laws that determine what publicly traded corporations can do, who controls them, and how control is exercised (Blair, 1995). [AQ: 2] We examine rule adoption through analysis of a corporate governance reform, the split-share stock ownership structure reform by listed firms in China between 2005 and 2012. This context highlights the theory's ability to predict delayed or decoupled responses to rule changes because some firms delayed adoption of the reform even though delayed adoption risks sanction due to the state mandate. The delays are in part motivated by knowledge of the internal disputes in the state about the rule change, the potential repeal of the rule, and market uncertainty. Also, firms have strong interests in corporate governance, and it will be costly for them to make changes to it. Therefore, they have incentives to delay compliance of the new rules to reduce cost and uncertainty. The cost and uncertainty of change in corporate governance can involve conflicts between the firm and the state. The onus is on the firm to resolve the conflict by crafting the compliance strategy, which will be done differently depending on the firm exposure, state cooptation, and rule institutionalization.

Coercion as a Relation

We consider state coercion as a relation between a focal firm and the state in which the coercive pressure to adopt rule change differs among firms as a result of the power balance between firm and state (Casciaro & Piskorski, 2005; Pfeffer & Salancik, 1978). The firm exposure to the rule change increases the likelihood of adoption, while the firm cooptation through state links helps it manage the power relation and gain discretion to allow delayed compliance. The firm-state relational factors of exposure and cooptation vary among firms and affect how the firm responds because they give firms different ability to manage the pressure (Oliver, 1991; Pfeffer, 1973). Both affect the firm differently at different stages of institutionalization, with the firm-state relation being more important when fewer prior adoptions have been made. As a result, predicting firm responses to coercion—especially early on—requires relational theory on how well the state is positioned to influence a firm and how well the firm is positioned to manage the state influence.

Firm Exposure

Coercive pressures take the form of demands from powerful organizations or legal changes from states. We summarize these under the rubric of rule changes and note one important feature of rule changes: They invariably expose some firms more than others

because greater discrepancy between the current practice and the new rule imply that the rule design or enforcement could be targeted to these firms. The exposure of the firm can easily be compared across firms. As a result, the state can explicitly put more pressure on firms with more exposure, and managers can assess the exposure and preempt the state pressure through early adoption if the firm is highly exposed. Following state rules is a foundation of a positive relationship, whereas not complying with rules (reflected in a big discrepancy between practice and rule) will create tension between the firm and the state that can result in pressure applied to the firm. This makes the firm exposure an important firm-state relation.

In our context, we knew from informants that the state did apply pressure, but interestingly it was an executive whose firm deviated greatly from the new rule who made an interpretive link from the firm behavior to the pressure: “Ever since the announcement of the reform, our provincial government and SASAC [State-owned Assets Supervision and Administration Commission] has held monthly mobilization meetings for all of us, the executives from prominent listed firms, to ‘encourage’ us to adopt the reform as soon as possible. Of course it is in fact ‘enforcing’ us. I feel quite pressured because our firm has a huge portion of nontradable shares. I believe the government will keep holding frequent meetings like this until firms like us have all adopted.”³ The executive explicitly linked the high pressure to the firm’s wide discrepancy from the new rule even though the state had mobilization meetings with all large firms with nontradable shares, thus enforcing the same rule on all the subjected firms.

The exposure influences firm assessments of the coercive pressure, which in turn drives the firm to adopt practices that follow the new rules. A highly exposed firm with wide discrepancy from the new rule is disadvantaged in its relation to the state and hence likely to be a potential target of fines or other penalties, whereas a less exposed firm is in a safer position in its relation to the state and likely to avoid sanctions. The logic behind such assessments is that a state enforcement agency will direct punitive action against the firms least in compliance with the new rules because enforcement is most effective when directed at prominent noncompliant actors (Lott, 1996; Yiu, Xu, & Wan, 2014). The exposure will also attract stakeholder attention (King & Soule, 2007; Rowley & Moldoveanu, 2003) and make firms visible exemplars (Wry, Lounsbury, & Glynn, 2011) and easy targets of inspection for conformity. Hence, the greater a firm’s exposure to a rule change, the greater is the pressure to change. Coercive pressures may also expose firm misalignment with emerging rules and trigger internal questioning of existing practices that do not match the new rules (Edelman, 1992). Thus, firms with great exposure to a rule change will have a narrow range of actions possible and are pushed to adopt the new rules rapidly. Conversely, low firm exposure means less likelihood of punitive action or stakeholder pressure and, hence, greater ability to delay adoption.

The effect of exposure on rule compliance has been neglected in research so far (though see Berrone et al., 2013), but there is some predecessor theoretical and empirical work. Exposure is related to the process of enactment in resource dependence theory (Pfeffer & Salancik, 1978), where the decision makers of a firm seek to understand environmental demands through monitoring active influence attempts, such as lawsuits or boycotts, and seeking to anticipate potential influence attempts arising from strong discrepancy with what external actors would like the firm to do (Banaszak-Holl, Mitchell, Baum, & Berta, 2006; Karpoff, Lee, & Vendrzyk, 1999; King, 2008). Decision makers may disagree on the importance of compliance, but even when there is disagreement, firm exposure to a state rule becomes important because it is a strong argument in favor of rapid adoption (Briscoe, Chin, & Hambrick, 2014; Briscoe & Safford, 2008; Delmas & Toffel, 2008; Jonsson & Regnar,

2009). High exposure thus creates urgency in the rule adoption, and conversely, low exposure allows delayed adoption:

Hypothesis 1a: A firm with low exposure is more likely to delay new rule adoption.

Low exposure also enables decoupling. When regulations are ambiguous, they offer firms wide latitude to construct the meaning of compliance in a way that alleviates the conflict between environmental demands and managerial interests (Edelman, 1992). Firms decouple by displaying visible symbols of compliance to show their attention to regulations while choosing behaviors with an actual compliance lower than the symbolic one (Meyer & Rowan, 1977). Decoupling lets firms appear to comply with regulations and norms pertaining to their structure and operation rather than follow the full intent of the rules (Scott, 2001; Tilcsik, 2010; Westphal & Zajac, 1994). In our context, *decoupling* meant complying with the letter of a law intended to increase transparency but in a firm-specific and nontransparent way. Decoupling not only allows easier continuation of operations but can also reduce internal opposition against a new rule (Raaijmakers, Vermeulen, Meeus, & Zietsma, 2015). However, because exposure from the wide discrepancy from the new rule can attract state attention to the firm-state relation, decoupling the adoption from the new rule is risky. The difficulty again arises from two sources. Internally, decision makers favoring full compliance can argue that the high exposure makes full compliance necessary due to the regulatory attention that the firm is likely to receive. Externally, increased regulatory attention is a likely consequence of exposure, which also focuses decision maker attention on the potential cost of enforcement action (Delmas & Montes-Sancho, 2010). Exposed firms thus have fewer options also with respect to decoupling. Firms with low exposure, however, have more leeway because of the lower state attention, giving them greater ability to choose the preferred option of decoupled adoption:

Hypothesis 1b: A firm with low exposure is more likely to decouple the rule adoption.

State Cooptation

Another firm-state relation is a firm's cooptation with the state through state links. Cooptation is defined as the ability to access internal information about the state and anticipate and shape rule enforcement (following Pfeffer, 1972). Firms that have state links can gain information on the legal changes, such as the content and expected level of enforcement, and try to influence them (Peng & Heath, 1996; Peng & Luo, 2000; Ritchie & Melnyk, 2012). These actions allow a broader range of actions, as when lobbying for exceptions is successful or provides knowledge of exceptions that other firms have obtained (Silverstein & Hohler, 2010). However, cooptation is a bilateral exchange, so the firm receiving favors implies an obligation to follow state instructions faithfully.

Combining these arguments, scholars have hypothesized that firms that are well connected to the state may receive more coercive pressures for institutional change, so they will respond to change quickly. Conversely, firms that are less connected to the state may be less aware of institutional expectations (Galaskiewicz & Wasserman, 1989) and less receptive to pressure (Westphal & Zajac, 2001; Zuckerman, 1999). This theory suggests that ties to the state predict swift compliance; however, evidence on this proposition is weak (e.g., Sutton & Dobbin, 1996). One important limitation of this argument is that it is based on the assumption

that the state has reached internal agreement about the effectiveness of the new rule and is determined to enforce compliance, so firms with state links will not exploit their information advantage before adoption. However, in practice that assumption is often not satisfied in rule changes. The state can mandate a rule but later withdraw it due to doubts about its effectiveness, and the state can mandate a rule and later adjust it in response to adverse consequences. Because rule instability is a possibility, firms with a state link do not necessarily comply quickly to a rule change. There is already empirical evidence of state ties causing weaker rule enforcement (Karpoff et al., 1999), so the simple idea of quick compliance through state connections is incomplete.

In practice, the state does not necessarily reach internal agreement about the effectiveness of a new rule due to its uncertain impact. Different internal and external stakeholders of the state will have divergent perspectives on the rule-setting process so that disagreement and disputes occur, as in any political governance system (March & Olsen, 1989). If the uncertainty of rule enforcement is high due to internal state dispute, firms with strong state links will use their connections with the state as a device of cooptation (Pfeffer & Salancik, 1978) to reduce compliance with state initiatives deemed to be risky. Specifically, firms with state links hold information advantages on current debates, possible future rule changes, and planned enforcement (Hillman, Zardkoohi, & Bierman, 1999; Hinthorne, 1996; Karpoff et al., 1999) that enable them to make a better strategic response to coercive pressures (Getz, 1993). For example, their direct links provide firsthand information about the political struggle within the state and transfer knowledge of whether the dispute can be resolved and which camp is dominant. Cooptation reduces the uncertainty of the effects of the coercive pressures and allows actions that reduce their burden (Hillman, 2005; Levitsky & Murillo, 2009).

Flow of personnel between state and firm results in formation of coalitional ties to build personal networks of influence (Peng, 2003; Peng & Luo, 2000). Close connection to the state allows firms to make a more informed interpretation of the rationale behind the imposed practice. Thus, cooptation lets firms collect information from the state and reduce their risk of delayed compliance (Silverstein & Hohler, 2010). Also, as firms monitor the policy risk and accumulate inside information about the state's intent to enforce the rule change, they are able to delay their responses until the policy becomes definite and early adopters show positive outcomes of compliance. During the delay, their ties to the state make it easy to find arguments to support their delayed responses because they know what reasons they can give to justify being slow (J. Li & Qian, 2013). They will also have direct supporters in the state because a cooptation link becomes a durable relation, generating a motivation to support the firm and an expectation that this support will be reciprocated (Pfeffer & Salancik, 1978).

This opportunity to delay to learn more about the consequence of the policy change can be risky if connected firms have high exposure. However, these firms also have some negotiating ability because the cooptation allows them to bargain for exceptions to the rule. Similar to the "too big to fail" argument in banking, they can plead difficulties from being too big, too complex, and too important to change while requesting greater institutional privileges and greater access to alternative bases for attracting resources. As a firm executive noted, "if firms like us trigger a stock market drop during the reform, it would be a disaster for the people up there in the state. Through our informal interaction, they have been explicit to us that we need to make sure all types of shareholders are taken care of. But, as a result, they have to be patient with us because we are not going to do this quickly. It is also for their own sake if they do not want to see quick but failed adopters." Such rationales and the ability to plead directly help firms

overcome the deterrence of the state because they protect the firms from state sanctions for noncompliance (Greenwood & Suddaby, 2006; Kostova, Roth, & Dacin, 2008). Therefore, firms with state links have a better chance of retaining the status quo in the face of coercive change and negotiating a delay (Guillen, 2000; Hillman & Hitt, 1999). Confronted with a policy that is debated in the state, firms with state links that see the rule as costly have the opportunity and capability to delay their response. This reasoning leads to the following:

Hypothesis 2a: A firm with state links is more likely to delay rule adoption.

The cooptation advantages obtained through state links also affect decoupling. It is a central insight of cooptation theory that the relation is bilateral: the firm has increased ability to predict and control the actions of the coopted organization (here, the state), but in return the cooptation obliges the firm to follow direct and often detailed influence from the state (Pfeffer & Salancik, 1978). Here the theory makes a clear distinction between the outcomes that would be most beneficial for the firm and the outcomes that can be achieved because cooptation involves exchange of favors. This sets in motion a process that reduces the likelihood that a firm with state links will decouple its adoption of the rule. The ability to influence the state is not sustainable over time if the influence is too one-sided, because cooptation is an implicit exchange of favors among individuals in the network linking the state and corporate actors (Peng & Luo, 2000). The firm gains the favor of learning more about the flexibility of the rule, and it returns the favor by adopting the original proposed rule rather than a decoupled version that could be seen as an implicit rejection of the rule. Thus, firms use state links for cooptation, and they maintain these links through a faithful adoption of the original rule. This trade-off is beneficial to firms because adoption affects many stakeholders, creating a highly uncertain environment that firms prefer to avoid, even at the cost of staying with the original rule. It is acceptable to the state if the favor of delaying adoption extended to only a few firms and to only a certain extent for these firms, so the momentum of rule adoption is not weakened. These arguments lead to the following:

Hypothesis 2b: A firm with state links is less likely to decouple the rule adoption.

It is useful to point out that Hypothesis 2a has a plausible counterhypothesis and thus is an important empirical question. First, if state links mean that the firm is capable of influencing the rule change, it will be more likely to accept it and thus be an early adopter (opposite of Hypothesis 2a) of the standard rule (same as Hypothesis 2b). Second, if cooptation lets the firms get information about impending changes earlier, they will be able to prepare for the change earlier and more effectively (opposite of Hypothesis 2a). We specify Hypothesis 2a rather than the counterhypothesis because the main reason to delay adoption was fear of an adverse market reaction and following policy reversal, which would be difficult to overcome through influencing the rule change or gaining information about the rule content early. The contrast between these arguments makes Hypothesis 2a an important empirical question.

Institutionalization

The impact of the two firm-state relational factors on a firm's adoption strategy facing coercive pressure is likely to change over time. A classic prediction on the adoption of institutions is that any firm-level characteristics that initially predict adoption will become less

influential later on, as institutionalization of the new practice causes mimetic adoptions to become more important (DiMaggio & Powell, 1983; Tolbert & Zucker, 1983). The logic behind this prediction is that the pressures to make firms comply are not objectively assessed but rather discovered and enacted by firm decision makers (Pfeffer & Salancik, 1978). If the firm has great exposure, the potential for enforcement actions means that early adoption is beneficial regardless of whether other organizations also adopt early. When most other firms have adopted, the exposure becomes less important for the decision because the coercive pressure from the state is supplemented with mimetic pressure from other firms that already comply, reducing the potential for further delay. This makes the degree of institutionalization important for understanding the effect of the firm-state relation on coercive pressures.

The same logic can be applied to the effect of cooptation. From the firm point of view, state links bring particular advantage and value when the choice of whether to adopt still seems open, leaving firms with a state link the option of late adoption to let other firms comply first and expose the risk of adoption. However, as the new rule is institutionalized, the situation changes in two ways. First, the state's tolerance for delayed adoption gets reduced as the policy gains stability and there are fewer noncompliant firms that can become targets of rule enforcement. Second, the value of delay is reduced because many prior adoptions can already be observed and their effects assessed. Thus, the effect of state links on the speed of compliance is weaker when many other firms have adopted.

From the state point of view, cooptation could have different usage early and late in the institutionalization process. Recall that the cooptation is bilateral, with the firm exerting influence on the state but with the state also having the opportunity to directly influence specific firms. Because the state is interested in prominent firms complying with the rule change quickly, to encourage other firms to adopt the new rule, it may select some firms as early adopters and instruct the state-linked board members of those firms to support adoption. To focus on firm cooptation of the state, we do not hypothesize this effect, but our empirical investigation is designed to allow detection of it.

The prediction of greater influence of firm characteristics initially has been examined and supported (e.g., Scott, 2001). **[AQ: 3]** However, the original study making this prediction tested it only for the population of organizations in which there was no state rule requiring adoption of the practice, and it made no test for the population in which adoption resulted from a state rule change with coercive pressure (Tolbert & Zucker, 1983). This is an omission for the theory of coercive isomorphism because state rule changes also have firms that are more or less willing to adopt early on, as argued already, but these sources of willingness or resistance are likely to change as more firms adopt the new rule. Thus, exposure and cooptation predict compliance with state rule changes less well when many other firms have adopted:

Hypothesis 3a: Firm exposure has a lower effect on the rate of adoption when many other firms have adopted the new rule.

Hypothesis 3b: State links have a lower effect on the rate of adoption when many other firms have adopted the new rule.

The Split-Share Structure Reform in China

We examine these hypotheses using a context and a rule change that make the tension between state coercion and firm action particularly strong: the split-share stock ownership

structure reform in China. Stock ownership reform is an important rule change because ownership and control are central features of firms and because changes can be controversial for the state and costly for firms. Prior to 2005, listed firms in China had a split-share structure in which ownership shares were partially nontradable. Nontradable shares are a special class of shares giving the shareholders the same ownership rights (e.g., to vote or to receive a dividend) as holders of tradable shares, but trading of these shares was restricted. A typical Chinese listed firm had three major categories of ownership (Qi, Wu, & Zhang, 2000 [AQ: 4]): (a) state shares owned by the central or provincial government agencies (SASACs), as well as state-owned enterprises (SOEs) wholly owned by the state; (b) legal person shares owned by various domestic institutions comprising SOEs (partially owned by the state), private industrial firms, and nonbank financial institutions; and (c) ordinary shares owned by individual investors and private institutional investors. Of these, state shares and legal person shares constituted nontradable shares. Since incorporation, every listed firm's equity had nontradable shares. Up to 2004, they could be transacted only through negotiations among designated parties, if approved by the regulatory authorities.

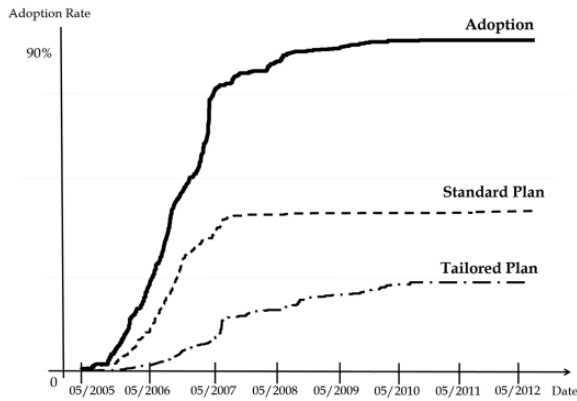
The split-share structure constituted a unique governance structure of Chinese listed firms, hindering the healthy growth and maturity of the financial market. Following the shift in economic logic from state socialism⁴ to market capitalism (Greve & Zhang, 2016), the central government saw it as an obstacle to economic growth and mandated conversion of nontradable shares into tradable shares, which started May 9, 2005. The strength of the state pressure is clearly illustrated by the speed of the initial adoption, with 80% adoption reached in 15 months. The adoption also neared completeness: by the end of 2012, 96% of all firms that were subject to the reform had completed or initiated the adoption of the reform. The significant delays in adoption speed after reaching a high adoption rate shows that some firms resisted the state pressure (Figure 1). This is thus a good case for examining how some firms delay compliance despite strong coercive pressure. The split-share structure reform was a legal mandate motivated by important and urgent national policy goals, so although policy enforcement can be adapted to the economic conditions of each province, it was the type of rule change for which the central Chinese government applies close firm inspection and regulatory enforcement through frequent mobilization meetings in every province (Estrin & Prevezer, 2011). Most adoptions followed the standard plan endorsed by regulators, but a minority instead initiated a tailored plan. Such variance in choosing whether to comply with the state-prescribed conversion method allows examination of factors influencing decoupling from the original regulatory intent.

Background of the Split-Share Structure Reform

The split-share structure reform was a key continuation of China's economic transition from a centrally planned redistributive economy to a market economy, which had already started remaking its economic institutions at the time of the reform (Nee, 1992). The opening of the Shanghai and Shenzhen stock exchanges in 1990 and 1991 signaled the regime's resolve to shift from the prevailing economic logic of state socialism to one of market capitalism, with a focus on increased self-reliance for individuals and reduced financial demands on the state by relaxing government control of the market, partially privatizing SOEs and promoting the national stock exchange (G. Jiang, Yue, & Zhao, 2009).

A major issue of the stock market in China is that each nontradable share had a low price when the listed firm was incorporated, but the price of each tradable share was much higher.

Figure 1
Diffusion of the Split-Share Structure Reform, 2005-2012



Nevertheless, each share has the same voting right, though at different prices. The nontradable shareholders were typically the initial (often state or SOE) founder of the listed firm. Therefore, tradable shareholders needed to pay more for each share of equity and still had little power in a firm's decision making, while the nontradable shareholders were the key decision makers of the firm and were much less susceptible to stock value fluctuations.

The split-share structure and the many nontradable shares were blamed for the slump in China's stock exchange through the 2001-2005 period (B. B. Jiang, Laurenceson, & Tang, 2008), with a total decline in market capitalization of >50%, and were regarded as a long-term hurdle to the development of domestic financial market institutions. A range of adverse effects were identified (Liao, Liu, & Wang, 2014): First, the conflict of interest between shareholders (i.e., tradable vs. nontradable) was severe, which led to strategy inconsistencies (Chen & Young, 2010). Second, holders of tradable shares were typically small, diverse in background, and dispersed in location. The lack of incentive and knowledge among nontradable shareholders (AQ: 5) to participate in firm decision making resulted in limited supervision of management decisions, a problem particularly salient to firms under long-standing state control (Shleifer, 1998). Third, the small public float for listed companies on the stock market made shares relatively illiquid, volatile, and vulnerable to market manipulation and insider trading. Fourth, the market inefficiencies induced many valuable Chinese companies to list overseas, inhibiting domestic investors' access to high-performing local companies. Overall, the split-share structure was thought to undermine market institutions and hold back China's economic reform.

Reform Process

On April 29, 2005, the China Securities Regulatory Commission (CSRC), a central governmental agency equivalent to the Stock Exchange Commission in the United States, announced that all nontradable shares should be converted to tradable shares. Two decisions had to be made by nontradable shareholders of listed firms: (a) when to adopt the reform and (b) how to compensate tradable shareholders on their diluted share value given the increase

in liquid shares after conversion. In each firm, nontradable shareholders had to file a request to the board of directors and have the reform proposal audited externally. The board publicized the reform proposal, if approved, and set the agenda for a shareholders' meeting to proceed with the negotiation with tradable shareholders. The date of the announcement was considered to be the firm's reform adoption time. The conversion of stock was done on the implementation day after both the nontradable and tradable shareholders approved the compensation method by voting.

The official implementation details of the reform⁵ specified that methods of compensation for the tradable shareholders would be determined by structured private negotiations between nontradable and tradable shareholders. The CSRC advocated the standard plan of compensation, whereby nontradable shareholders issued a negotiated consideration ratio of bonus shares to compensate tradable shareholders. This method was transparent and regarded as the most legitimate implementation of the reform, both because of its regulatory approval and because it left less room for concealed benefits to one of the negotiating parties. A minority of firms instead adopted a set of alternative methods, the tailored plan, which involved internal asset and debt reconfiguration, offering call or put warrants, guaranteeing stock buybacks at preset prices, paying cash, transferring assets, or writing off debts. Although this method formally adhered to the rules, it was decoupled because it reflected firm control rather than the state goal of isomorphic procedures. The resulting compensation schemes varied by firm conditions and negotiating power and had less transparent economic and control consequences (Wu, Zheng, Lin, Li, & Wu, 2006).

Reform Controversy

Before 2005, the CSRC had already recognized the defects of the split-share structure and debated whether and how to convert nontradable shares into tradable shares. The CSRC had launched an attempt to convert nontradable shares in 2001, but it led to negative stock market reactions and was finally abandoned (Cooper, 2008; Liao et al., 2014). The aborted reform, the underperformance of listed firms, and a general lack of confidence in market institutions combined to generate uncertainty among government and market players. Drawing from these lessons, from 2001 onward, the CSRC issued a series of corporate laws to provide greater protection for minority investors and started a new wave of the reform.

Despite this preparation, the split-share structure reform had been controversial, with prolonged discussion in the central government that included debates on the effectiveness of the reform and whether and how to implement it. Substantial resistance typically arose to any format of economic transition and market reform involving further privatization and looser state control, especially among the communist party officials, government bureaucrats, and SOEs (Xu, Lu, & Gu, 2014). Opponents continued to refer to the earlier failed attempt to release the nontradable shares to the market to emphasize the uncertainty about the outcomes of the reform (Liao et al., 2014). There was sufficient knowledge about the debate within the state to give firms reason to believe that the rule change might be repealed.

The goal of institutionalizing a fully tradable shareholding structure reflected the state's interest in refining stock market institutions and improving firms' financial efficiency. However, at the beginning of this reform, many officials in the public sector and state-appointed agents who represented state shares in firms strongly objected (Cooper, 2008; Hua, 2010). They insisted that China's economy was not yet ready for this rapid reduction of state

control over the financial market, and the listed firms were not prepared for a fully liquid governance structure. One state official recalled, “We thought that reform was a strong signal of further selling off crucial national asset to private sectors. We had many meetings and discussions about it, and people were anxious and confused facing this radical decision by the CSRC. Honestly, we were not sure whether the central government has thought this through.” The quote illustrates well how the clear and publicly announced requirement came against a background of conflict within the state. Firms with state links would be able to understand the conflict better and assess its consequences for the timing and form of adoption.

Adoption Risk

Since the start of the split-share structure reform, firms faced the decision of when and how to adopt the reform, and they needed to strategically evaluate the costs and benefits of being quick or slow to respond to the state mandate. If they adopted the reform quickly, they might experience a stock price drop, and stock price drops in multiple firms could result in a repeal of the rule, judging from the previous experience of the failed reform. The benefit of being an early adopter was that the CSRC would reward firms with priority access to state-controlled resources, such as bank loans. The sanctions against slow adopters were not fully spelled out, but they were blocked from raising capital through secondary offerings (Cooper, 2008), and the state could also withhold other crucial resources. Thus, the rule change led to certain risks of noncompliance but uncertainty about who would be hit and the strength of the penalties.

Data and Methodology

Data Sources

The China Stock Market and Accounting Research database and the WIND database are the main data sources for the study. The database covers the ownership structure and financial performance of all listed firms in China to date since 1992 as well as data on board members and top management teams, including board members’ curriculum vitae. It has been widely used in finance (D. Li, Moshirian, Nguyen, & Tan, 2007; Lin & Su, 2008) and economics research (Rousseau & Xiao, 2008). The WIND database provides detailed information on firm adoptions of the split-share structure reform, including the date of the announcement of reform proposal by the board of directors, the attendance rate and voting outcome of the shareholding meetings about the reform plan, and the negotiated compensation method of the reform.

The quantitative study was supplemented with eight interviews with key insiders—government officials at SASACs, institutional investors, and senior managers in two prominent listed firms to draw inferences about the rationales for the adoption of the reform. These interviews were conducted after the theory development and were done to check that the reform adoption was driven mainly by the factors treated in the theory above. Because of the complex ties between the state and firms through ownership, personnel exchange, and regulation, it was useful to follow a grounded theory approach to let insiders describe their decision making to allow mapping of statements matching the theory, as well as any statements suggesting routes of influence outside the theory. The interviews allowed us to check that the relational factors that we developed were indeed the main drivers of adoption.

Estimation Method and Dependent Variables

The data comprised 1,356 firms that were subject to the reform since 2005. We conducted event history analysis of the adoption time and logit analysis of the choice of adoption plan. The adoption time is operationalized as the duration from the April 29, 2005, announcement of the split-share reform requirement to the date of the firm's announcement of its adoption of a split-share unification proposal, as this date indicates agreement among the key stakeholders on this change. The adoption plan is operationalized as the choice of the standard plan or the tailored plan. In the analysis of the plan choice, the data were the plan choices by the firms that successfully completed the reform. After missing data deletions, we had data for 1,354 firms in the event history analysis and 1,286 adoptions in the adoption plan analysis.

Because the research question focused on the firm's intention to adopt the new rule, the announcement of the submission of the proposal for an adoption was coded as an event, irrespective of whether the reform proposal passed or failed at the shareholder meeting. Because adoption would remove a need for readoption and because a vote against adoption would be likely to significantly change the decision-making process, a firm that has proposed adoption generated no more observations in the subsequent periods. Only four proposals failed to win support at the shareholding meeting.

In a continuous-time event history model of adoption time, the controls for the influence of time are important. The most flexible control was applied through the Cox proportional hazards model (Cox, 1972). Unlike parametric event history models, such as the exponential or Gompertz model, the Cox model lets the effect of time on the hazard rate vary freely per the data. This flexibility makes the Cox model a particularly safe choice when time effects have a shape not well captured by other models. We can obtain the same results using the exponential model with time interval controls, so the choice of the Cox model is for caution only. The Cox time axis was historical time, and tied event times were handled by the exact partial-likelihood method to get the most accurate estimates.

Independent Variables

Exposure

We measured exposure as the proportion of nontradable shares because this shows the discrepancy between current practice and the new rule. The proportion of nontradable shares varies across firms, owing to differences in the initial equity and subsequent movement of shares from nontradable to tradable status and hence reflecting a firm's discrepancy between its current share structure and the fully tradable shareholding structure required by the reform.

State links

Two separate but related measures are used to measure the state links of the firm. The first is a direct measure of cooptation through capturing the movement of individuals from state positions to the board of the firm, and it equals the proportion of board members with a current or past position in a government agency. Preliminary testing comparing this variable with a variable counting only agencies with direct supervision of firms showed that the more inclusive variable used here had better explanatory power.

Alternatively, cooptation can be captured through the firm association with the state hierarchy. Every listed firm in China with state shares reports to the respective controlling state agency across national, provincial, and local hierarchical levels. At each level, the SASACs have the right to appoint and supervise key agents to listed firms to assert the right of the state's shareholding. Firms associated with central government and the central SASAC are connected to the highest level of the state: they often belong to crucial industries that operate nationally and have closer relationships with central policy makers (Walder, 1995). Listed firms monitored by provincial governments and SASACs are connected locally to a lower state hierarchy, which pressures them to follow state rules because they are, in turn, under pressure from the central state. Such firms have weaker links with the rule-setting central state and thus are less able to gain information and seek influence. Firms that are not directly monitored by any level of SASACs have the weakest linkage with the state. The variable is given the value of 1 for firms without a state tie, 2 for firms with a provincial tie, and 3 for a firm associated with the central government.

These two variables trace cooptation well because of the systematic way in which the state uses personnel movement to monitor firms while giving firms the converse ability to influence the state through the contacts of the same individuals. We enter the variables as main effects and as interactions with the number of past adoptions to test the effect of institutionalization. In a preliminary analysis, we entered the proportion of state ownership, instead of board members with state experience, and found similar results. We thus found that state cooptation can be captured either indirectly through the state ownership or directly through individuals with state background. We retain state ownership share as a control variable.

Control variables

We control for the age of listed firms, which captures how long the firm had been operating in the old governance system. A firm's size can influence risk-taking behavior and was controlled through the log of the firm total assets (Audia & Greve, 2006). We control for industry effects by including 12 major industry category dummies (13 industries with 1 as the baseline) and 30 region dummies (31 in total with 1 as the baseline). We added a dummy variable indicating whether the firm's stocks were included in the China Securities Index (CSI 300). CSI 300 is a stock market index that consists of 300 stocks listed on the Shanghai or Shenzhen stock exchange. The firms in the index are usually chosen to reflect the price fluctuation and performance of China's stock market, which could affect their decisions on the adoption of the split-share structure reform given the stock index impact.

We also considered the impact of a firm's growth opportunities on the reform adoption decisions, using the market-to-book ratio to capture this effect. We included the debt-to-equity ratio to capture the potential impact of a firm's financial leverage on reform adoption decisions. Also, firms make decisions to change according to their past performance (Greve, 1998). Recent studies of firms' responses to institutional changes show that sustaining and achieving economic gain is of equal importance with obtaining social legitimacy as a rationale for practice adoption decisions (Kennedy & Fiss, 2009). Thus, a 1-year lagged performance measure is entered to control for firms' economic motivation. We selected return on assets (ROA) as the performance measure because it has been widely used as a performance measure that can be compared across industries (Shinkle, 2012). Greater overseas sales can also affect the reform adoption decision because firms with overseas presence may seek to

have a market-oriented governance structure, so we included the proportion of sales overseas. The decision to initiate a reform can be influenced by the change in the upper echelons (Hambrick & Mason, 1984; Wiersema & Bantel, 1992), especially the succession of the chairman of the board or the CEO. Thus, the analysis has a dummy variable indicating if the firm has changed its board chairman or CEO in the previous year.

We included variables describing board characteristics that could influence the knowledge of and preference for the reformed ownership structure. The board of directors is the correct decision-making group for reincorporating in accordance with the new rule, as they make the decision and mediate the negotiations that follow. The first is the average age of the board members, which is a proxy for total experience. The rest are all proportions of board members with a specific characteristic and thus capture its prevalence in the board. We have the proportions of members with graduate degrees (master or PhD), independent directors, top management team members, and members who get some salary or payment from the firm (firms can pay board members even if they are not top management team members). Also, we have the proportion of board members with a finance role in the corporation and the proportion of board members who own shares in the corporation. Expectations for these control variables are not completely clear, because they depend on how the board members assess the consequences of the reform, but independent board members and top management team members often have divergent interests. Board members with a finance role or with stock ownership are more familiar with the stock market and less so with the state and can be expected to view exposure to the new state rule as a potential threat that deserves attention.

According to the theory on herd behavior, firms tend to mimetically adopt a practice if others have adopted it. They believe that the decisions of others are rational such that their adoptions imply positive information about the practice (Greve, 1996). In the adoption analysis, the Cox model controls for this effect because it fully controls for temporal changes in the hazard rate. In the binary outcome logit model, the same issue is addressed by controlling for the number of prior adoptions using the standard plan.

Results

Adoption Likelihood

Descriptive statistics and correlations for the Cox model of the adoption of split-share reform are shown in Table 1. The table shows low correlations, including the two measures of state links. In Table 2, the modeling starts with only control variables in Model 1, followed by all hypothesis-testing variables with either the board proportion holding a state position or the state hierarchy indicating the state link. Models 2 and 3 show that exposure has a positive and significant coefficient, indicating that it makes delayed adoption less likely, as predicted by Hypothesis 1a. Firms that diverge more from the coercive state's intended practices appear to be influenced by exposure and to adopt more rapidly. Both measures of state links—proportion of board members with state positions in Model 2 and state hierarchy in Model 3—show negative and significant coefficients, in support of Hypothesis 2a, although state position is only marginally significant. Thus, the state links provide cooptation that allows firms to delay adoption of the coercive but controversial split-share structure reform.

The effects of control variables remain similar across all the models. The older the firm, the less likely it will be to adopt the reform, whereas the bigger the firm, the more likely it

Table 1
Descriptive Statistics and Correlation Coefficients [AQ: 6]

Variables	M	SD	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19			
1. Age	7.75	3.44																						
2. Size	21.15	1.07	-01																					
3. CSI 300	0.15	0.36	-04	.41																				
4. Debt to equity	2.01	18.88	.01	.04	.05																			
5. Market to book	1.08	0.87	.06	-.43	-.03	-.05																		
6. ROA	-0.00	0.14	-.13	.24	.13	-.02	.00																	
7. Ratio overseas sales	0.08	0.18	-.06	.02	-.03	-.01	-.04	.01																
8. Proportion state share	0.35	0.26	.16	.26	.12	.02	-.09	.15	.15															
9. Change in chair/CEO	0.34	0.47	.05	-.10	-.06	-.01	-.00	-.13	-.03	-.01														
10. Board average age	47.95	3.94	.01	.32	.16	.02	-.07	.09	.06	.23	-.10													
11. Board graduate degree	0.16	0.23	.04	.11	.05	-.01	.01	.07	.02	.00	-.04	-.11												
12. Board independent	0.34	0.05	-.02	.00	-.02	-.00	-.00	-.01	.03	-.10	.02	-.01	.04											
13. Board TMT member	0.20	0.12	-.02	-.02	-.02	-.03	-.01	-.04	.04	-.05	-.12	-.12	.02	.41										
14. Board paid by company	0.35	0.19	-.05	.02	-.03	.03	-.06	-.04	.02	-.12	-.10	-.10	.03	.22	-.07									
15. Board finance role	0.02	0.05	-.01	-.02	-.03	-.02	.01	-.00	.03	.01	-.03	-.07	-.02	.04	.02	.03								
16. Board shareholders	0.16	0.20	.07	.17	.06	.00	-.09	.06	-.04	.02	-.17	.17	-.01	.07	-.06	.19	.18							
17. Exposure	0.60	0.11	-.36	-.08	-.02	-.01	.14	.08	-.03	.31	.04	-.03	-.03	-.02	-.07	-.16	-.16							
18. Board state position	0.44	0.24	.01	.17	.10	.02	.03	.07	.03	.24	.00	.25	.23	-.07	-.05	-.07	-.03	.05						
19. State hierarchy	1.79	0.74	-.05	.23	.10	-.00	-.06	.12	.04	.50	.01	.20	.04	-.08	-.08	-.13	-.19	.04	.07	.20				
20. Prior adoptions	581.1	341.0	.30	-.17	-.08	.03	.03	-.26	-.02	-.07	.12	-.01	-.09	.01	-.04	-.02	-.08	-.13	-.13	-.08	-.01			

Note: The data comprise 1,354 firms and 2,269 firm-year observations. ROA = return on assets; TMT = top management team.

Table 2
Results for Cox Model of Split Share Reform Adoption

Variables	Model 1	Model 2	Model 3
Industry fixed effects	Yes	Yes	Yes
Province fixed effects	Yes	Yes	Yes
Age	-0.07** (0.01)	-0.06** (0.01)	-0.06** (0.01)
Size	0.12** (0.04)	0.13** (0.04)	0.13** (0.04)
CSI 300	0.06 (0.10)	0.06 (0.10)	0.06 (0.10)
Debt to equity	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
Market to book	-0.02 (0.05)	-0.01 (0.05)	-0.01 (0.05)
Return on assets	3.22** (0.37)	3.30** (0.37)	3.30** (0.37)
Proportion overseas sales	0.28 (0.21)	0.31 (0.21)	0.32 (0.21)
Proportion state shares	-0.17 (0.13)	-0.29* (0.14)	-0.13 (0.15)
Change in chair or CEO	-0.06 (0.06)	-0.07 (0.06)	-0.06 (0.06)
Board average age	-0.00 (0.01)	-0.01 (0.01)	-0.01 (0.01)
Board proportion graduate degree	0.14 (0.14)	0.24+ (0.14)	0.20 (0.13)
Board proportion independent directors	0.53 (0.61)	0.51 (0.61)	0.52 (0.61)
Board proportion top management team members	0.41 (0.30)	0.32 (0.30)	0.31 (0.30)
Board proportion paid by company	0.16 (0.19)	0.22 (0.19)	0.17 (0.19)
Board proportion finance role	-1.31+ (0.70)	-1.20+ (0.70)	-1.32+ (0.71)
Board proportion shareholders	0.57** (0.16)	0.62** (0.16)	0.64** (0.16)
Exposure		1.12** (0.31)	1.02** (0.31)
Board proportion state position		-0.25+ (0.14)	
State hierarchy			-0.16** (0.05)
Likelihood ratio, χ^2 (df)	394.41** (60)	410.09** (62)	417.87** (62)
Likelihood ratio vs. Model 1		12.19**	19.97**

Note: Standard errors are in parentheses. Two-sided z tests for coefficients.

+ $p < .1$. * $p < .05$. ** $p < .01$.

will be to adopt the reform. None of the CSI 300 dummy variables, debt-to-equity ratio, and market-to-book ratio had a significant impact on a firm's adoption speed, indicating that a

firm's response to a coercive change is not related to the stock market even though the reform is about stock transaction rights. ROA in the previous year is positively related to the adoption decision, so high-performing firms are more likely to adopt the reform. The effect of ROA can be interpreted to mean that high performance increases exposure as well, leading to earlier adoption. This is a post hoc interpretation, however, so we cannot be sure, and unreported additional analyses showed that ROA was a main effect that did not interact with the other hypothesis-testing variables. The board proportion variables show that boards with many shareholding directors are significantly more likely to adopt, suggesting that they are indeed more concerned about noncompliance with state rules leading to potential penalties.

Table 3 has additional models that test the hypotheses on how the effect of firm exposure and state cooptation is influenced by the degree of institutionalization. Again, we test the two measures of state links separately. Model 4 enters the interaction of exposure and the number of prior adopters over time, showing that the interaction effect has a significant coefficient estimate that is negative, opposite of the main effect of exposure. This supports Hypothesis 3a that the effect of exposure is stronger initially. Model 5 and 6 each test the effect of one of the state link cooptation variables and show interesting effects. The positive and significant signs of state cooptation main effects in Model 5 and Model 6 and the negative and significant effects of their interactions with prior adoptions show that state cooptation also initially increases the adoption rate. However, this effect declines and then reverses as this rule becomes institutionalized, and for most of the period, firms with state links had a lower rate of new rule adoption.

Although the declining effect over time supports Hypothesis 3b, the new result of a positive initial effect was not hypothesized and instead suggests a more differentiated pattern of compliance. It appears that some firms with cooptation opportunities were unable to use them; instead, the state link was actually used for influence in the reverse direction, from state to firm, making these firms exemplars of early adoption. Examination of the early-adopting firms strongly suggests that some firms with state links were specifically chosen because they were prominent firms in strategic industries. For example, among the first adopters, Citic Securities is a member of the "national team" of stock brokers that the Chinese government uses when it seeks to influence the stock market, for example, after the June 2015 stock market crash. Yangtze Power operates the giant Three Gorges Dam and had a 75% state-linked board, including a chair who was party committee secretary (one of the top 200 party members). These firms had extraordinarily strong state links. However, once they led an initial wave of adoptions, the state's objective of visible compliance was met, and for the rest of the state-linked firms, cooptation instead was in the hypothesized direction from firm to state, with the effect of delaying compliance.

Finally, Model 7 is a supplementary analysis that uses the variables on board proportions to examine whether the concern for legitimacy changes over time. It does so by adding interactions of board proportions of members who are particularly concerned with the state as a potential threat with prior adoptions. The findings show that board members in a finance role and board members who are shareholders initially increase the rate of adoption (main effects), but their influence declines as the number of prior adoptions increases (interactions).

Adoption Plan

The descriptive statistics and correlations for the logit model of the standard adoption plan are omitted for brevity, as they are very similar to those in Table 1. In Table 4, Model 1

Table 3
Results for Cox Model of Split Share Reform Adoption

Variables	Model 4	Model 5	Model 6	Model 7
Industry fixed effects	Yes	Yes	Yes	Yes
Province fixed effects	Yes	Yes	Yes	Yes
Age	-0.03** (0.01)	-0.04** (0.01)	-0.04** (0.01)	-0.05** (0.01)
Size	0.05 (0.04)	0.09* (0.04)	0.11** (0.04)	0.13** (0.04)
CSI 300	0.01 (0.10)	0.03 (0.10)	-0.02 (0.10)	0.04 (0.10)
Debt to equity	0.00 (0.00)	0.00* (0.00)	0.00* (0.00)	0.00* (0.00)
Market to book	-0.06 (0.05)	-0.05 (0.05)	-0.07 (0.05)	0.00 (0.05)
Return on assets	2.32** (0.32)	3.22** (0.35)	2.92** (0.35)	3.04** (0.36)
Proportion overseas sales	-0.03 (0.21)	0.19 (0.22)	0.13 (0.21)	0.30 (0.21)
Proportion state shares	-0.09 (0.14)	-0.39** (0.14)	-0.42** (0.15)	-0.17 (0.14)
Change in chair or CEO	0.00 (0.06)	-0.15* (0.06)	-0.06 (0.06)	-0.07 (0.06)
Board average age	-0.02** (0.01)	-0.00 (0.01)	-0.00 (0.00)	0.00 (0.01)
Board proportion graduate degree	0.12 (0.13)	0.26* (0.13)	0.12 (0.13)	0.19 (0.14)
Board proportion independent directors	1.22* (0.63)	0.60 (0.62)	1.09* (0.64)	0.13 (0.61)
Board proportion top management team members	0.46 (0.29)	0.37 (0.30)	0.65* (0.30)	0.56* (0.30)
Board proportion paid by company	0.01 (0.19)	-0.07 (0.19)	0.06 (0.19)	0.04 (0.19)
Board proportion finance role	-0.70 (0.71)	-1.06 (0.69)	-0.90 (0.71)	8.28** (1.39)
Board proportion shareholders	0.53** (0.16)	0.54** (0.16)	0.60** (0.16)	4.56** (0.30)
Exposure	12.09** (0.42)	1.01** (0.31)	1.28** (0.31)	0.59* (0.31)
Board proportion state position		6.72** (0.27)		-0.13 (0.13)
State hierarchy			2.31** (0.08)	
Exposure × prior adoptions	-0.01** (0.00)			
Board proportion state position × prior adoptions		-0.91**		
State hierarchy × prior adoptions			(0.032)	
Board proportion finance role × prior adoptions			-0.33** (0.01)	-1.34** (0.17)
Board proportion shareholders × prior adoptions				-0.66** (0.05)
Likelihood ratio, χ^2 (df)	1,294.79** (62)	1,305.99** (63)	726.57** (64)	1,650.02** (63)
Log-likelihood	-7,300.36	-7,323.36	-7,613.07	-7,151.34
Likelihood ratio vs. Model 1	912.27**	923.77**	344.35**	1267.80**

Note: Standard errors are in parentheses. Two-sided z tests for coefficients. Prior adoptions are not entered as a main effect in this model, because it is fully collinear with the Cox model controls for time dependence.

* $p < .1$. ** $p < .05$. *** $p < .01$.

Table 4
Results for Logit Model of Adoption of Standard Plan

Variables	Model 1	Model 2	Model 3
Industry fixed effects	Yes	Yes	Yes
Region fixed effects	Yes	Yes	Yes
Age	-0.05 ⁺ (0.03)	-0.02 (0.03)	-0.02 (0.03)
Size	-0.07 (0.10)	-0.05 (0.10)	-0.08 (0.10)
CSI 300	-0.83** (0.24)	-0.81** (0.25)	-0.81** (0.24)
Debt to equity	-0.00 (0.00)	-0.00 (0.00)	-0.00 (0.00)
Market to book	-0.30** (0.09)	-0.34** (0.09)	-0.34** (0.09)
Return on assets	-0.40 (0.67)	-0.26 (0.67)	-0.36 (0.68)
Number of prior adoptions of standard plan	-0.0004** (0.00)	-0.0005** (0.00)	-0.0004** (0.00)
Proportion overseas sales	0.52 (0.59)	0.57 (0.60)	0.45 (0.60)
Proportion state shares	0.61 ⁺ (0.35)	0.16 (0.38)	-0.23 (0.41)
Change in chair or CEO	-0.20 (0.17)	-0.23 (0.17)	-0.25 (0.17)
Board average age	-0.03 (0.02)	-0.04 (0.02)	-0.03 (0.02)
Board proportion graduate degree	-0.28 (0.33)	-0.34 (0.35)	-0.28 (0.34)
Board proportion independent directors	-1.76 (1.67)	-1.77 (1.68)	-1.75 (1.67)
Board proportion top management team members	0.47 (0.81)	0.39 (0.82)	0.43 (0.82)
Board proportion paid by company	0.33 (0.51)	0.55 (0.51)	0.72 (0.52)
Board proportion finance role	-2.45 (1.84)	-2.33 (1.86)	-2.31 (1.86)
Board proportion shareholders	0.87 ⁺ (0.47)	1.06* (0.48)	1.06* (0.48)
Exposure		2.42** (0.82)	2.782** (0.83)
Board proportion state position		0.33 (0.37)	
State hierarchy			0.36** (0.13)
Likelihood ratio, χ^2	160.41**	173.97**	180.79**
Likelihood ratio vs. Model 1		13.56**	20.36**

Note: Standard errors are in parentheses. Two-sided z tests for coefficients.

⁺ $p < .1$. * $p < .05$. ** $p < .01$.

contains all control variables, and Models 2 and 3 show that the exposure has a positive and significant effect on the likelihood of the standard plan adoption, consistent with Hypothesis 1b. Firms that have a wide discrepancy with the new rule show caution and use the standard adoption approach, as predicted. Model 2 shows no effect of board members with state positions, but Model 3 shows that the measure of state hierarchy has a positive and significant effect on the likelihood of the standard plan, consistent with Hypothesis 2b. Compared with unconnected firms, firms that have links with the state that can be used for cooptation appear more likely to adopt the standard practice, about which they have better information and on which they may also have had some influence. Figure 1 shows clearly that the adoption of the standard plan was most frequent early on, while the adoption of the tailored plan was initially less frequent but lasted longer. This suggests that early adopters experienced the greatest pressure to conform to a state-prescribed plan.

The control variables show that firms in the CSI 300 were less responsive to the standard of coercive change and, surprisingly, firms became less likely to adopt the standard plan when it became more common. A high market-to-book ratio also led to less likelihood of adopting the standard plan. Other control variables do not yield significant results, highlighting the central role of the theoretical variables in predicting this outcome.

Discussion and Conclusion

We introduce a relational view of firm reactions to coercive pressures and argue that this view is necessary because firms see coercive institutional pressures as imposed by a powerful actor rather than as taken-for-granted practices. As a result, relational theory of how the firm reacts through adoption timing and potential decoupling can best predict behaviors. Following this view, we propose theoretically and show empirically that the heterogeneity in firm responses to state-initiated coercive institutional change can be explained by the relation between the state and the firm. The first relation is firm exposure, or discrepancy between current practices and new rules, which invokes pressure to adopt the rule and leads to quicker and less decoupled adoption. The second relation is cooptation, obtained through state links, which provides access to internal state information and leads to delayed and less decoupled adoption. The analyses showed that the effect of these two firm-state relations on the speed and degree of adoption were strongly supported. The power balance of exposure and cooptation shows the benefit of a resource dependence argument that considers both power and counterpower (Pfeffer & Salancik, 1978).

Our study takes a fresh look at the structure-versus-agency debate in institutional theory (e.g., DiMaggio & Powell, 1991; Hirsch & Lounsbury, 1997) through raising the question of when firms will delay and decouple in response to coercive institutional pressures from the state. This entails closer examination of the relation between the firm and the state through taking four steps. The first is to draw attention to state coercion as a mechanism of change that has been understudied (Mizruchi & Fein, 1999); particularly, the well-known phenomenon of slow rule adoption by some organizations has not been explained well (Tolbert & Zucker, 1983). The second step is to see this as strategic action, as firm decision makers are fully aware that rules are imposed and carry costs, benefits, and risk of noncompliance or decoupled compliance (Oliver, 1991; Pfeffer & Salancik, 1978; Wry et al., 2013). The third step is to develop a relational theory explaining why rule adoption specifically and firm compliance to coercive isomorphism more generally are variable across firms and can be

explained by examining the dyadic power balance between the firm and the source of coercion. An important part of the theory is the firm exposure to state coercive pressure as a result of the discrepancy between its current practice and the new rules, which in turn reduces the ability to delay rule adoption (Pfeffer & Salancik, 1978). The theory also considers how cooptation of the state gives informational advantages allowing delay of adoption but is also an exchange relation with the state, causing adoption to be faithful rather than decoupled. Finally, exposure and cooptation are firm characteristics that, just as in mimetic isomorphism, have greater explanatory power early on, before the new rule has become institutionalized and seen as necessary for all firms.

This study shows that coercive pressure needs to be studied more. It is not as automatic as the term *coercive* implies; in fact, one can observe the puzzle of delayed and decoupled compliance by firms under state pressure. Adoption is not a direct result of regulatory change but a strategic action in which the firm appears to make cost-benefit assessments (e.g., Fremeth & Shaver, 2014; Ritchie & Melnyk, 2012). It is natural that the interests of its main decision makers affect the outcome, as seen through the control variable of board member stock ownership, but it is a notable demonstration of the firm cost-benefit assessment that adoption is affected by exposure and ability to coopt the state. Clearly, state rules set parameters for firm actions, but they do not determine them (Greve & Zhang, 2016). Given the extent and legitimacy of the state power as compared with other powerful organizations, this finding opens for a renewed look at how firms act to manage the demands of powerful actors in the environment (Pfeffer & Salancik, 1978). Future studies examining other organizations than the state would be interesting, such as large-assembly or service-providing firms that place demands on their suppliers.

This study adds to the debate about how public policies mandate or encourage change within business organizations (Kochan, Guillen, Hunter, & O'Mahony, 2009). The institutional and political context of China—where government officials intervene in firm decisions—provides a good context for scrutinizing the impact of firm-state relationships on firm strategies exactly because delayed adoption is surprising. Our findings indicate that state rule changes do not imply rapid and full compliance. Identifying such behavior deepens our understanding of the links between corporate and national governance and how such interactions can lead to unequal treatment of firms. In particular, the slower adoption of the split-share structure reform by firms with state links shows that state agents may use their political influence to delay state reforms. Future studies on how cooptation is made possible and what effects it has would be very valuable.

In these data, the firm advantage derived from cooptation kept shares nontradable longer, maintaining an ownership structure with complications for capital market transactions such as mergers and acquisitions and refinancing. Firms adopt new rules at different times, with greater risk and cost for the less-connected firms that adopt early (Ritchie & Melnyk, 2012). This matters because coercive pressures are used for a reason: Firms would not adopt on their own because it is not in their interest to comply, at least as the interest is defined by the top decision makers. In this case, the resistance against state pressures was partly for political reasons related to state control, partly for risk concerns that turned out to be unfounded. For other rule changes, the resistance may be related to costs that are imposed on firms to fulfill societal goals, such as reduced pollution or greater employee benefits. The firm ability to delay adoption through state links forces the less-connected firms to take on greater costs and risk, possibly even the risk of adopting rules that will be revoked by the state when the

consequences are better known. State links thus give the benefit of letting other firms do the trials of new rules. The existence of such benefits from state links also means that firms engage in competition to obtain them, which will affect firm-state relations.

The relational theory and findings developed here have implications for other theories as well. One important implication is for the resource-based view of the firm, which now has a significant research record with a focus on how firms develop and maintain distinct capabilities (Barney, 1991; Barney, Wright, & Ketchen, 2001). State ties that yield cooptation capabilities are clearly within the scope of the resource-based view and match its development to examine how firms manage their relation to institutional environments (Barney et al., 2001). Also, this work illustrates how firms can resist coercive pressures through either low exposure or high cooptation capabilities. This shows clearly the potential for firms to maintain institutional logics against pressures (Greenwood, Raynard, Kodeih, Micelotta, & Lounsbury, 2011), such as those that would result from state coercion or public rankings (Rowley, Shipilov, & Greve, 2016).

Future research opportunities on responses to rule pressures are abundant. It would be valuable to have more research, not just on how individual firms respond, but also on how these responses shape important collective outcomes, such as industrial development and state policy implementation. At the level of firm adoption, key tasks would be to replicate the findings on exposure and cooptation as drivers of adoption speed and decoupling. Because the theory applies to other sources and destinations of coercive pressure than the state versus firms, research extending the findings to other contexts will be valuable. A relational theory of responses to coercive pressures should apply when their source is another firm or a social movement. Investigating such processes could uncover mechanisms other than exposure and cooptation, as well as additional sources of exposure and decoupling than what we studied here. Specifically, exposure can be from media or social movement attention, not just the actual discrepancy from the new rules; likewise, cooptation can be through behaviors such as endorsement, not just through network ties. **FAQ: 7** Each mechanism is suitable for much additional research.

It would also be promising to extend the theoretical lens in two directions. A firm-centered approach would be to examine additional firm characteristics, especially top management team characteristics, that influence the timing and form of adoption. We would expect findings that resonate with coalitional views of the firm (Cyert & March, 1963), such as managers responding more favorably to changes matching their backgrounds. For a change as in our study, for example, training in Western management techniques could lead to increased willingness to adopt early. The other direction of an environmental approach would look not only at the dyadic relation between a firm and the state but also at firm networks and their effect on policy formulation and implementation (Barley, 2010). We already had an interesting finding through the discovery that firms became less likely to adopt the standard plan as it became more common, suggesting that the tailored plan, preferred by many firms, was easier to adopt in an environment with many prior adoptions that did not use a decoupled approach, possibly because decoupling is harder to detect late in an institutionalization process.

Firm responses to coercive pressures are an interesting topic of research because they are less isomorphic than commonly assumed, in large part because firm responses to coercion have a strategic element. As a result, relational theory examining how the source and destination of the coercive pressure interrelate can produce valuable insights into the timing and form of compliance and can reveal late compliance and partial compliance even in contexts

that are commonly believed to involve a high degree of regulation and firm compliance. The relational theory of firm responses to state coercion developed here proved effective in predicting firm responses to a significant rule change in the Chinese market reform and clearly has potential for much additional work in other contexts. Although we are several steps away from it, rich theory and evidence on how firm networks, state-firm dyads, and firm characteristics jointly determine responses to coercive pressures are within reach.

Notes

1. "Big Banks Struggle to Pass Fed's 'Stress Tests,'" *Wall Street Journal*, March 11, 2015.
2. "For Banks, 2014 Was a Year of Big Penalties," *Wall Street Journal*, December 30 1994.
3. All quotes are from interviews done by one of the authors and are translated from Mandarin.
4. Under the state socialism logic (Szelenyi, 1978), **IAQ: B** goods and services are channeled through firms to the state, which allocates resources back to firms and distributes output to consumers. Firms serve political and social objectives through a hierarchy of government control at the local, provincial, regional, and national levels. This differs from the market capitalism firm that interacts with a market and is governed and valued by shareholders.
5. "Measures on Administration of Split-Share Structure Reform of Listed Companies," published by China Securities Regulatory Commission, May 9, 2005.

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