

Woidtke, T. (with Y. Yeh). (2005). Commitment or Entrenchment?: Controlling Shareholders and Board Composition. *Journal of Banking and Finance*, 29, 1857-1885.

### **Abstract**

This paper examines the determinants of board composition and firm valuation as a function of board composition in Taiwan – a country that features relatively weak protection for investors, firms with controlling shareholders, and pyramidal groups. The results suggest that there is poor governance when the board is dominated by members who are affiliated with the controlling family but good governance when the board is dominated by members who are not affiliated with the controlling family. In particular board affiliation is higher when negative entrenchment effects – measured by (1) divergence in control and cash flow rights, (2) family control, and (3) same CEO and Chairman – are strong and lower when positive incentive effects, measured by cash flow rights, are strong. Moreover, relative firm value is negatively related to board affiliation in family-controlled firms. Thus, the proportion of directors represented by a controlling family appears to be a reasonable proxy for the quality of corporate governance at the firm level when investor protection is relatively weak and it is difficult to determine the degree of separation between ownership and control.