Cross-border Acquisition Target Selection and Investor-protection

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Abstract

"*Cherry picking,"* foreign acquirers' tendency to select well-performing firms in emerging markets, is well-documented but little understood. I demonstrate that it is a general phenomenon caused by a gap in the strength of investor-protection between acquirer and target countries. An acquirer from a stronger investor-protection country values control premiums less than does a controlling shareholder in a weaker investor-protection country. To pay a lower control premium, the acquirer selects well-performing firms, which tend to self-select better governance and require lower control premiums. Examining U.S. cross-border acquisitions in 40 countries reveals that U.S. firms target well-performing firms in countries with weak investor-protection, but not in countries with strong investor-protection. In addition, I identify major corporate governance reforms (CGRs) in target countries, and employ a difference-in-difference approach based on variation in investor-protection, which is generated by the staggered passages of CGRs. I find that U.S. acquirers exhibit more willingness to target underperforming firms after a target country undertakes a CGR, which narrows the investor protection gap. Sarbanes-Oxley Act (SOX) has an opposite effect by increasing the investor protection gap: it leads U.S. acquirers' to pursue better performing firms, and this effect is greater for U.S. acquirers affected more by SOX. These findings imply that weak investor-protection of host countries works as a barrier against local firms most in need of managerial improvement from gaining access to well-governed foreign investors.

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I. Introduction

Acquisitions channel corporate assets to higher valued uses by reallocating controls from under- to well-performing firms. This well-accepted benefit of corporate acquisitions has been strongly supported by previous studies with data on U.S. domestic acquisitions. For instance, under-performing assets are more likely to be acquired (e.g., Maksimovic and Phillips, 2001; Liu, 2008)[2]; acquisitions of under-performing firms generate greater values for bidders, targets, and total synergistic gains (e.g., Lang, Stulz, and Walkling, 1989; Servaes, 1991)[3].

However, *"Cherry picking,"* the tendency of foreign acquirers to select well-performing firms in emerging markets is a well-documented phenomenon in the foreign direct investment (FDI) literature. Aitken and Harrison (1999) use panel data on Venezuelan plants and find that foreign equity participation is positively correlated with plants' pre-acquisition productivities. Sabirianova, Svejnar, and Terrell (2005) demonstrate a similar phenomenon with data on Eastern European firms. Some recent studies show that foreign investors invest less in poorly-governed firms in countries with weak legal investor-protection (Ferreira and Matos, 2008; Leuz, Lins and Warnock, 2008). Additionally, cherry picking is seldom observed for foreign acquisitions in industrialized countries, and seems to be a phenomenon unique to emerging markets (e.g., Bloom, Sadun, and Reenen, 2007; Haskel, Pereira, and Slaughter, 2007).

These phenomena raise several issues: why do foreign investors prefer well-performing firms? Why is cherry picking prevalent only in emerging markets, and not in industrialized countries? Does this mean that the market for corporate control does not function properly when it comes to cross-border acquisitions in emerging markets? If so, what is the culprit?

One of noticeable differences between emerging countries and industrialized countries is the strength of investor protection. In this paper, I argue that the gap in investor protection between the acquirer and target countries gives rise to this cherry picking phenomenon in emerging markets. The theoretical model starts with the notion that the controlling shareholder derives two streams of benefits from the firm: (1) cash flow rights; (2) private benefits through control rights (e.g., La Porta et al., 2002). Private benefits of control can be derived in various ways; tunneling companies' resources, paying abnormally high compensation, enjoying excessive perks, and so on. When an acquisition takes place, both cash flow and control rights are transferred, so the value

[2] Also, Bethel, Liebeskind, and Opler (1998) find that activist investors are more likely to purchase block shares in poorly-performing corporations.
[3] This basic finding is discussed in a great deal of prior empirical studies, including Lang, Poulsen, and Stulz (1995); Martin (1996); Loughran and Vijh (1997); Rau and Vermaelen (1998); Andrade, Mitchell, and Stafford (2001) and many others.

of both rights is included in the transaction price. The value of cash flow rights reflects the value of traded assets. Control rights are priced as control premiums at the value of the private benefits that the controlling shareholder derives from the firm (Dyck and Zingales, 2004).

The controlling shareholder of an acquirer from a stronger investor-protection country derives less private benefits after the acquisition than does the incumbent controlling shareholder in a weak investor-protection country. Hence, the controlling shareholder of the acquirer values control premiums lower than does the incumbent controlling shareholder. Durnev and Kim (2005) show that although firms in weak investor-protection countries, on average, have weak corporate governance, well-performing firms have an incentive to self-select better governance, which means that their controlling shareholders drive less private benefits of control. As a result, well-performing target firms in weak investor-protection countries require lower control premiums, making them more attractive to acquirers from a strong investor-protection country. In other words, selecting well-performing firms in a weak investor-protection country can be viewed as a method to reduce the payment of control premiums. Thus, when the acquirer country has stronger investor-protection than does the target country, an acquirer tends to target well-performing firms. This tendency increases when this investor protection gap becomes greater.

These predictions are tested with data on U.S. cross-border acquisitions. Focusing only on U.S. cross-border acquisitions allows all country-level variation to come from the target side. In addition, the U.S. is the largest capital exporting country and has one of the strongest investor-protection and most efficient legal enforcement systems in the world.[4]

The empirical analysis begins with estimating a Probit model to examine the impact of firm performance on the likelihood of being a target of a U.S. acquirer. I construct a large sample of firms located in 36 countries from 1989 to 2005, including both target and non-target firms. I then separate this sample into strong and weak investor-protection countries, based on an investor-protection index that is a sum of *Anti-self-dealing* index (Djankov, La Porta, Lopez-de-Silanes, and Shleifer, 2008) and *Law-and-Order* index by International Country Risk (ICR). The results show that U.S. firms select well-performing firms in countries with weak investor-protection, but do not in countries with strong investor-protection.

[4] For example, the law and order index produced by the country risk rating agency International Country Risk (ICR) shows that the U.S. has a record of 10, which is the highest score.

Although this empirical approach is intuitively appealing, there is relatively little within country variation in legal environment indices, causing the results to be estimated mostly by cross-country variation. Cross-country variation in legal environment indices is related to many other county-level factors that may also affect foreign target selections. I circumvent this problem by exploiting the fact that over the past decade, many countries have enacted substantial corporate governance reforms (CGRs). These CGRs generate within country variation in investor protection. For each country, I check whether it has undertaken a CGR between 1990 and 2006 as an indicator for a change in investor protection. If a country has more than one CGR, I rely on the most influential CGR. This allows a difference-in-difference (D-I-D) approach to estimate how changes in investor protection affect the type of firms being targeted.

I firstly consider the impact of CGRs in target countries by comparing the pre-acquisition performance of target firms of acquisitions taken place before and after the CGR in a target country. To control for time effects occurring around the CGR legislation, I employ variation in investor-protection generated by the staggered passages of CGRs in target countries, and treat the acquisitions in countries that did not undertake CGRs in the same year as the control group.

Changes in investor protection gap can also arise if the acquirer country changes its investor protection. Thus, I examine the impact of Sarbanes Oxley Act of 2002 (SOX) on the type of firms being targeted. I compare the pre-acquisition performance of target firms of acquisitions taken place before and after SOX. To control for time effects occurring around SOX legislation, I employ the variation in the effect of SOX on U.S. acquirers, and treat the acquisitions by U.S. firms less affected by SOX as the control group of the acquisitions by U.S. firms more affected by SOX.

Using data on 969 U.S. cross-border acquisitions in 40 countries announced from January, 1, 1990 to December, 31, 2007, I find that U.S. acquirers exhibit more willingness to target under-performing firms after a target country undertakes a CGR, which narrows the investor protection gap by strengthening investor protection of the target country. Also, acquirers tend to pursue better-performing targets after SOX, which enlarges the investor protection gap by strengthening U.S. investor protection. Additionally, this effect is greater on the acquisitions by U.S. acquirers more affected by SOX. Overall, the gap in investor-protection between the countries where the acquirer and target are located has significant effects on cross-border acquisition target selections.

This study makes contributions to the literatures of law and finance, international capital flow, and market for corporate control. This paper contributes to the growing literature on law and finance by demonstrating how the "*gap*" in investor-protection between countries affects real economic activities. Previous studies in the literature mainly focus on cross-country variation in legal environments. These studies show that weaker legal protection of minority shareholders is associated with less developed stock markets (La Porta, Lopez-de-Silanes, Shleifer, and Vishny, 1997); lower corporate valuation (La Porta, Lopez-de-Silanes, Shleifer, and Vishny, 2002); higher concentration of ownership and control (La Porta, Lopez-de-Silanes, and Shleifer, 1999); more private benefits of control (Dyck and Zingales, 2004; Nenova, 2003); lower likelihood of restructuring when firms suffer a sharp deterioration in operating performance (Atanassov and Kim, 2007); and, a lower volume of M&A activities (Rossi and Volpin, 2004) and foreign capital inflows (e.g., Gelos and Wei, 2005; Alfaro et al., 2008). This paper provides insights into how the distance in investor protection between countries affects cross-border investment target selections.

In the FDI literature, previous studies have paid considerable attention to why capital does not flow from rich to poor countries as much as it should; namely: the "Lucas Paradox."[5] The results of this study add a new explanation for the Lucas Paradox. The gap in investor protection between poor and rich countries acts as a barrier against the foreign capital flows to under-performing firms in weak investor protection countries.

Target selections are channels through which corporate assets and control are reallocated to their higher valued uses through the market for corporate control. The results of this paper illustrate that weak local investor-protection is a major hindrance against the proper functioning of the cross border acquisition market. It works as a barrier preventing local firms most in need of managerial improvement from gaining access to well-governed foreign investors.

The paper proceeds as follows. A theoretical model is presented in Section II. Section III presents empirical analyses of how the relation between the likelihood of being a target and firm performance is affected by local investor-protection. Section IV conducts an empirical analysis using a difference in difference approach employing the staggered passages of corporate governance reforms by different countries. A summary is provided in Section V

[5] Suggested answers to "Lucas Paradox" include departures from purchasing power parity, information asymmetries between domestic and foreign investors, hedging of human capital or other non-traded assets, home bias, over-optimism of domestic investors toward home assets, and weak local legal environments (e.g., Lewis, 1999; Karolyi and Stulz (2002); Gelos and Wei, 2005; Alfaro et al., 2008).

II Theoretical Framework

This paper focuses only on acquisitions of public listed firms. For simplicity, I focus only on the firm-level heterogeneity in corporate governance of target firms, and treat corporate governance of acquirers identical given legal environment of the acquirer country. I also assume no information asymmetry between acquirers and target, but allow for asymmetry of information between the controlling shareholder and minority shareholders. This information asymmetry can be reduced by better disclosure regulations and corporate governance.

The controlling shareholder derives two streams of benefits from the firm: cash flow rights and the private benefits of control. When an acquisition takes place, both cash flow and control rights are transferred from the controlling shareholder of the target to the acquirer. Hence, the value of cash flow and control rights would be both included in the price of the transaction. The value of cash flow rights reflect the value of traded assets. Control rights are priced as control premiums with the value of the private benefits of control the incumbent controlling shareholder derives before the acquisition (Dyck and Zingales, 2004). The controlling shareholder of the acquirer obtains the benefits from both cash flow rights and the private benefits of control after the acquisition.

The modeling framework is similar to La Porta (2002) and Durnev and Kim (2005). The controlling shareholder has exogenously determined cash flow rights, α[6], and the profitability of the firm (i.e. the rate of return of investments), ($\pi>0$). For simplicity, firm's capital assets are normalized, and hence π represents cash flow rights per unit of investment.

The controlling shareholder may divert d percent of the firm to herself before distributing the rest as dividends. The cost of diversion is $(1/2)C(\pi d)^2$.[7] Assume $C>0$, where C is the cost of diversion and indicates stronger investor-protection. The cost of diversion is convex in d and π. The marginal cost of diversion increases with the size of diversion.[8] The controlling shareholder of a firm maximizes the following objective function by choosing d,

[6] Here, $a<1$. This study focuses only on acquisitions of listed firms, and for listed firms it impossible for any shareholder to completely own the firm.
[7] The cost of diversion is only borne by the controlling shareholder (La Porta et al., 2002). This diversion cost function is a special case of the diversion cost function in the Durnev and Kim (2005) model, in which the cost of diversion is defined as $C(\pi d)^s$, where $s>1$. For simplicity, I assume $s=2$. This difference does not change any main prediction of the model.
[8] A plausible story could be that firms with greater profitability tend to attract more outside investor interest and to be under greater public scrutiny, and consequently, diversion costs increase as firms have greater profitability. Another plausible story is that if the controlling shareholder of a well-performing

$$Max\ \alpha\pi + d(1-\alpha)\pi - (1/2)C(\pi d)^2 \qquad (1)$$

In equation (1), $\alpha\pi$ represents the value of her cash flow rights, $d(1-\alpha)\pi$ represents the value of diversion and $(1/2)C(\pi d)^2$ is a diversion cost. The sum of the second and third term represents the net private benefits of control that she consumes, denoted as *PB*.

Differentiating (1) with respect to *d* and setting it equal to, we obtain the optimal level of diversion,

$$d^*=Min[((1-\alpha)/\pi C),1] \qquad (2)$$

Since the controlling shareholder can not steal more than 100 percent of the cash flows of the firm, I ignore the case when $d^*=1$ in the following discussion. Differentiating (2) with respect to *C* and π, we obtain that other things being equal, a controlling shareholder may self-select better corporate governance and consume fewer private benefits of control, when the firm is in a stronger investor-protection country (La Porta et al., 2002), $\partial d^*/\partial C<0$, or when the firm is more profitable (Durnev and Kim, 2005), $\partial d^*/\partial \pi<0$.

Suppose that C_A and C_T represent investor-protection of the acquirer and target country respectively. PB^*_A and PB_T^* represents the private benefits of control enjoyed by the acquiring firms' controlling shareholder after the acquisition and that enjoyed by the incumbent controlling shareholder, respectively.[9] Also, suppose that the acquirer purchases all α percent shares from the target. Then, the sum of $\alpha\pi$ and PB_T^* is equal to the reservation price of the incumbent controlling shareholder (Barclay and Holderness, 1989; Dyck and Zingales, 2004). The sum of $\alpha\pi$ and PB_A^* represents the potential total benefits that the acquiring firm's controlling shareholder obtains after the acquisition. The rate of return of the acquiring firm's controlling shareholder is, [10]

$$R = ((\alpha\pi+PB_A^*) - (\alpha\pi+PB_T^*))/(\alpha\pi+ PB_T^*) \qquad (3)$$

By selecting different firms, the acquisition will generate different level of the rate of return to the controlling shareholder of the target. After substituting PB_A^* and PB_T^* into *R*, [11] an interesting results is obtained by taking

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firm self-selects good governance (i.e. divert less), she may benefit more from greater firm value, but it is not true for the controlling shareholder of a under-performing firm (Durnev and Kim, 2005).

[9] PB^*_A and PB_T^* can be obtained by plugging in d_A^* and d_T^* into $d(1-\alpha)\pi - (1/2)C(\pi d)^2$, respectively.

[10] Here, I do not consider the change in profitability of the firm, π after the acquisition through post-acquisition restructuring. Also, any transaction costs are ignored.

[11] $R = ((\alpha\pi+PB_A^*) - (\alpha\pi+PB_T^*))/(\alpha\pi+ PB_T^*)=((1-\alpha)^2/2C_A - (1-\alpha)^2/2C_T) /(\alpha\pi+(1-\alpha)^2/2C_T)$

derivative of R with respect to π. The partial derivate, $\partial R/\partial \pi$,[12] suggests that the impact of the pre-acquisition performance of the firm on the rate of return is positive only when acquirer country has stronger investor-protection than does the target country,

$$\partial R/\partial \pi > 0 \text{ if } C_A > C_T$$
$$\partial R/\partial \pi = 0 \text{ if } C_A = C_T$$
$$\partial R/\partial \pi < 0 \text{ if } C_A < C_T \quad (4)$$

When the controlling shareholder of an acquirer selects acquisition targets, she will choose the firm which can generate greater rate of return for her. Thus, the following relation is obtained,

$$\partial Prob(Target=1)/\partial \pi > 0 \text{ if } C_A > C_T \quad (5)$$

Prediciton1: Other factors remaining equal, when the acquirer country has stronger investor-protection than does the target country, the acquirer tends to target well-performing firms.

The insight is that other factors being equal, a controlling shareholder consumes less private benefits of control when the firm is in a stronger investor-protection country $\partial d^*/\partial C<0$. As a result, the gap in investor-protection between the acquirer and target country may cause disagreement on the valuation of control rights. Well-performing firms can self-select better corporate governance, $\partial d^*/\partial \pi<0$, and hence consume fewer private benefits of control relative to the operating cash flows. As a result, a well-performing firm is more attractive to an acquirer from a strong investor-protection regime, since it can generate greater rate of return for the controlling shareholder of the acquirer.

The impact of firm performance on the likelihood of being a target may vary across legal regimes of the acquirer and target country, which can be seen by taking the derivative of equation (5) with respect to C_A and C_T respectively,[13]

[12] $\partial R/\partial \pi = -(((1-\alpha)^2/2C_A - (1-\alpha)^2/2C_T))\,\alpha)/(\alpha\pi+(1-\alpha)^2/2C_T)^2 = ((1-\alpha)^2(1/2C_T - 1/2C_A)\,\alpha)/(\alpha\pi+(1-\alpha)^2/2C_T)^2$

[13] $\partial^2 R/\partial\pi\partial C_A = (1/2C_A^2)\alpha(1-\alpha)^2)/(\alpha\pi+(1-\alpha)^2/2C_T)^2$; $\partial^2 R/\partial\pi\partial C_T = (-\alpha(1-\alpha)^2(1/2C_T^2))/(\alpha\pi+(1-\alpha)^2/2C_T)^2 + (1/2C_T - 1/2C_A)((\alpha(1-\alpha)^4(1/2C_T^2))/(\alpha\pi+(1-\alpha)^2/2C_T)^3)$

$\partial^2 Prob(Target=1)/(\partial\pi\partial C_T) < 0$ *if* $C_A > C_T$ (6a)

$\partial^2 Prob(Target=1)/(\partial\pi\partial C_A) > 0$ *if* $C_A > C_T$ (6b)

Equation (6a) shows that the sensitivity of the likelihood of being a target to firm performance decreases as investor-protection of the target country rises. Equation (6b) shows that the sensitivity of the likelihood of being a target to firm performance increases as investor-protection of the acquirer country rises. Thus, the following predictions are obtained.

Prediction 2a: The tendency to select well-performing target firms becomes weaker when investor-protection of the target country becomes stronger.
Prediction 2b: The tendency to select well-performing target firms becomes stronger when investor-protection of the acquirer country becomes stronger.

The insight is that control rights are valued greater for the incumbent controlling shareholder in a weaker investor-protection target country and, hence, well-performing target firms become more attractive for acquirers from a strong investor-protection country. In contrast, control rights are valued lower for the acquiring firm's controlling shareholder from a country with stronger investor-protection and hence well-performing target firms in weak investor-protection countries become more attractive.

In sum, when the acquirer country has stronger investor-protection than does the target country, firms with better performance are more attractive to the acquirer. This gap may lead to greater disagreements on the valuation of control rights, and hence, to stronger tendency to select well-performing firms. This prediction also can be applied to the block share acquisitions, which do not involve complete transfers of control rights. A block share acquisition by a foreign acquirer from a strong investor-protection country can also increase the costs of diversion for the remaining incumbent controlling shareholders because of additional monitoring from their foreign block shareholders. As a result, such loss of private benefits of control for the incumbent management will also be priced as control premiums in the acquisition.

III. Investor-protection and Target Selections

A. Empirical Methodologies

I use two empirical approaches to test the hypotheses. The first is to estimate how the likelihood of becoming a target of U.S. acquirers in related to potential target firms performance using a Probit model. The second is to

use a difference-in-difference approach using changes in regulations on corporate governance reforms that have taken in a staggered fashion in the sample countries. In this section, I briefly describe the following Probit model. The dependent variable is a binary choice variable *(*$Target_{ijct}$*)*, equal to one if the firm receives a bid from a U.S. firm in year *t* and zero otherwise,

$$Target_{ijct} = 1, \text{ if } Target^{*}_{ijct} > 0$$
$$= 0, \text{ Otherwise} \qquad (7)$$

$Target^{*}_{ijct}$ is a continuous latent variable that determines whether a firm *i* in country *c* becomes an acquisition target in year *t*. $Target^{*}_{ijct}$ is determined by the following specification.

$$Target^{*}_{ijct} = \alpha_{jt} + \alpha_c + \theta Perform_{ic,t-1} + \lambda Z_{ijc,t-1} + e_{ijct} \qquad (8)$$

where $Perform_{ic,t-1}$ is a measure of firm performance based on either operating earnings or sales growth, and α_{jt} is year-varying industry fixed effects (defined as one-digit SIC), α_c is country fixed effects, $Z_{ijc,t-1}$ are control variables, and e_{ijct} is the error term. The model is estimated with robust standard errors. I split the sample into two sub-samples by the median of strengthen of investor protection (*IP)*. In the below-*IP* sample, θ is expected to be positive, but not for the above-*IP* sample. This means that when investor-protection of target countries is significantly weaker than that of the U.S., acquirer country, an acquirer tends to target well-performing firms.

B. Variables

B.1. Investor-protection Index

The measure of investor-protection incorporates both *de jure* and *de facto* aspects of regulations. The *Anti-self-dealing* index in Djankov, La Porta, Lopez-de-Silanes, and Shleifer (2008) measures *de jure* minority shareholder protection against controlling shareholders' actions that may hurt shareholder value. This index is country-specific and time invariant. The *Law-and-Order* index produced by the country risk rating agency, International Country Risk (ICR), measures the effectiveness of the enforcement of formal rules. This index is updated monthly, and I take yearly averages. Investor-protection index, *IP* is defined as the sum of the normalized *Anti-self-dealing* index and *Law-and-Order* index with equal weight.[14] It measures the overall quality of investor-protection of a country, and higher value of *IP* indicates stronger investor-protection in the country. Table 1 shows *IP* for 36 countries under study along with each country's average GDP per Capita during the sample period. Singapore and New Zealand have the highest *IPs* (0.98 and 0.98); Mexico and Brazil have the lowest

[14] Durnev and Kim (2005) employ the same method to combine *de jure* and *de facto* regulations of investor-protection.

IPs (0.31 and 0.39). The pair-wise correlation between *IP* and average GDP per Capita of each target country from 1989 to 2005 is 0.29 and significant at 1% level.

B.2. Firm Performance Variables

Firm performance is measured by the growth rate of operating earnings before interest, taxes, depreciation, and amortization divided by total assets *(EBITDA/TA_Gr)*, and the growth rate of sales divided by total assets *(SALES/TA_Gr)*. These measures of performance are less affected by accounting rules and earnings management. In addition, Durnev and Kim (2005) show that they are positively related to the quality of firm-level corporate governance.

I use the growth rate of performance, instead of performance level for two reasons. The first one is to eliminate the impact of data coverage bias. Worldscope covers more firms in industrialized countries than in emerging markets. WorldScope tend to cover larger and better-performing firms in emerging markets, whereas it tends to cover more broad range of firms in industrialized countries, making the size and performance of firms in industrialized countries more diverse. The second one is that a recent study (Liu, 2008) using data on U.S. acquisitions show that changes in performance, rather than performance level, are related to the likelihood of being acquired. To reduce the impact of outliers, both *EBITDA/TA_Gr* and *SALES/TA_Gr* are winsorized at the 1 and 99 percentile.

B.3. Control Variables

At the firm level, I control for firm size (*Firm Size*), market-to-book ratio (*MB*), leverage (*Leverage*), and liquidity (*Liquidity*), which are well-documented predictors of acquisition targets (e.g., Palepu, 1986). *Firm Size* is measured by the logged book value of total assets. *MB* is measured by the ratio of the market value of common equity to the book value of equity. *Leverage* is measured as the total debt (long term + short term debt) divided by the book value of total assets. *Liquidity* is measured as the ratio of current assets to current liabilities. Firms with negative *MBs* and leverage greater than one are dropped from the sample.

To control for financial crises, an indicator, *Crisis1*, is included in the regressions. It is equal to one for the observations during financial crisis. Specifically, it is equal to one if a firm-year observation has any of the following country-year combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995. Financial crises may affect acquisitions, if crises invoke

more fire-sale markets. Aguiar and Gopinath (2005) find that financial crises often change M&A patterns in emerging markets.[15]

I also control for four additional country level variables, which might be related to foreign acquisition decisions. The first is macroeconomic condition, which is measured as GDP per Capita (*GDPPA*). Firms in low income countries may be more capital constrained, making it easier for U.S. firms to acquirer them. *GDPPA* is denominated in 2000 US dollars, taken from the World Development Indicators (WDI) for all countries except Taiwan; for Taiwan, it is taken from Global Insights.

Second is country openness, measured as FDI net inflows as percent of GDP *(Inward FDI/GDP)*. It is easier for U.S. firms to acquire firms in a country more open to FDI. And because of this, the competition among acquirers will be greater, giving local firms more bargain power (Bradley, Desai, and Kim, 1988). *Inword FDI/GDP* is an annual country level variable, taken from the WDI for all countries except Taiwan; for Taiwan, it is taken from Global Insights.

The third is the regulatory environment of restructuring, measured as an index, *Restructure Reg*. Lu (2008b) demonstrates that regulations making restructuring costly reduce the probability of takeovers of under-performing firms. *Restructure Reg* index includes three components: labor market regulations, regulations of closing a business, and the enforceability of contract. The labor law is taken from Botero, Djankov, La Porta, Lopez-de-Silanes, and Shleifer (2004); regulations of closing a business is taken from the World Bank Doing Business Indicator; the enforceability of contracts is taken from Djankov, La Porta, Lopez-de-Silanes, and Shleifer (2003). The details of constructing *Restructure Reg* can be found in Appendix 1. Higher value of *Restructure Reg* index indicates regulations making restructuring more costly.

The fourth is merger-related anti-trust regulations, measured as an index, *Anti Trust Reg*, taken from Hylton and Deng (2007). Market power is an important motivation of acquisitions (Kim and Singal, 2003). Weaker anti-trust regulation may make it easier to acquire large and well-performing firms. *Anti Trust Reg* is a time invariant and country-specific variable.

[15] Aguiar and Gopinath (2005) find that the nature of M&As during a crisis contradicts productivity-based explanations of a crisis, they find that the number of foreign M&As in East Asia increased by 88% between 1996 and the crisis year of 1998. IMF bail-out packages to Thailand, Korea, and Indonesia following the East Asian crisis imposed additional conditions to allow foreign competition in the market for corporate acquisitions.

Finally, I include year-varying industry- fixed effects (defined as one-digit SIC code)[16] and country fixed effects to control for time trends, industry characteristics and related regulations, industry merger waves, and other country factors (e.g. macro economic conditions) that may affect both firm performance and target selections. Summary statistics of all firm level variables for the full, target, and non-target samples are presented in Panel A, B, and C of Table 2, respectively.

C. Simple Construction

This paper focuses only on target selections of U.S. cross-border acquisitions. The acquisition screening criteria are as follows.

a. Acquirers have to be U.S. firms and targets have to be non-U.S. firms. To remove noise arising from "round-tripping capital," firms' nationalities are defined by the nationalities of their ultimate parents. "Round-tripping capital" describes the origination of capital in a country (usually a developing country) for routing to another place, before re-entering this country as FDI inflows.[17] In practice, round-tripping capital is always associated with special purposes, such as tax evasion (Fisman and Wei, 2004).

b. Acquisitions are announced between January 1, 1990 and December 31, 2006. I start with 1990s, because many emerging economics had restrictions against foreign acquisitions. Prior to 1990s, and many of them opened up domestic stock markets to foreign portfolio investors during the 1980s (Kim and Singal, 2000).[18]

c. Both acquirer and target are publicly listed firms. The controlling shareholder of a public listed firm does not own 100 percent of the firm, making control premiums relevant to determine acquisition prices. In addition, this allows access more reliable information on deal and firm characteristics. For U.S. acquirers, firm level data are primarily obtained from COMPUSTAT or SDC. For international targets, data are taken from different sources including SDC, DataStream, WorldScope and Bloomberg.

d. Acquirers do not own any shares of the target before the acquisition, and purchase more than 5% target shares. In the acquisition literature, 5% often is used as the definition of block acquisitions (e.g., Bethel et al., 1998). We also restrict the sample to acquisitions of at least 10% or 20% of target shares transactions, and the results are robust.

[16] When restricting the sample to weak investor-protection countries, the size of the sample is very small. As a result, to save the degrees of freedom, the industry dummies are defined as one-digit SIC code.

[17] In some developing countries (e.g., China), round-tripping capital is a popular phenomenon. For example, Prasad and Wei (2005) estimate that round-tripping capital represents as much as one-third of Chinese FDI.

[18] For example, in the early 1990s, Latin American countries began actively seeking foreign investments in their newly privatized industries. In a number of East Asian countries, however, prohibitions on foreign investors gaining a controlling share of local firms continued until the mid-1990s.

Because this paper focuses on target selections, not transaction outcomes, I do not distinguish whether acquisitions are complete or incomplete. Nor do I distinguish whether acquisitions are friendly or hostile, because Schwert (2000) finds that economic differences between friendly and hostile takeovers are indistinguishable. Under a strong view of managerial entrenchment, managers may wish to avoid all changes of corporate control, even those that appear in the press as "friendly."

To construct a sample of firms in foreign countries that are targets and non-targets of U.S. acquirers, I merge data from WorldScope with SDC Thompson's International M&A database. WorldScope provides panel data of listed firms located in more than 80 countries and covers both target and non-target firms. SDC covers information on public and private M&As taken place in more than 200 countries.[19] The sample construction procedures are as follows:

1. Firms in WorldScope receiving bids from U.S. acquirers in a given year are manually identified with information from SDC.
2. Target firms identified by SDC but not covered by WorldScope are also included, if there is at least one country-industry-year firm[20] observation in WoldScope that can be used as a non-target matched sample, where industry is defined by two-digit SIC code, and the year is identified to be the year prior to the acquisition announcement year.
3. Firm-year observations of target firms are excluded from the sample following a successful acquisition.
4. Target and non-target firms are matched by country, year, and industry (defined as the first two-digit SIC code).

These two sample construction procedures yield a large cross-country firm-level panel dataset including both target and non-target firms. The full sample covers 8424 firm-year observations with firms located in 36 countries during 1989 to 2005.[21] The target sample includes 481 firm-year observations and accounts for 5.7% of the full sample; the non-target sample includes 7943 firm-year observations, and accounts 94.3% of the full sample. As a robustness check, I exclude 1956 firm-year observations in regulated industries (i.e., financial services [SIC codes: 6000-6999] and utility [SIC codes: 4911-4931]). The results do not change.

[19] SDC collects information from English and foreign language news, SEC filings and the filings from the international counterparts, trade publications, newswire reports, the proprietary surveys of investment banks, law firms, and other advisory firms. All transaction characteristics are double-checked with Factiva and synopsis. When deal information is different from that described in Factiva and synopsis, it is changed with the content of Factiva and synopsis.

[21] The sample period is one year before the period of acquisition sample, because the information of target firms is taken in one year prior to the acquisition announcement.

Table 1 shows country distribution for target and non-target firms by U.S. acquirers. The number of observations varies across countries due to differences in the coverage of data by SDC and WorldScope. Industrialized countries generally have more observations than do emerging market countries. The U.K. (2721) and Canada (1280) have the two largest numbers of observations; Czech Republic (2) and Poland (3) have the two lowest numbers of observations. The pair-wise correlation in the number of observations between the target and non-target sample of each country (i.e. Column (3) and (5)) is 0.87. This means that the target and non-target sample are roughly even distributed cross countries.

D. Results

Table 3 reports the results of the Probit regressions. Firm performance is measured by *EBITDA/TA_Gr* in Column (1), (2), (5) and (6), and *SALES/TA_Gr* in Column (3), (4), (7) and (8). The results are similar for these two measures of firm performance. The coefficients of both *EBITDA/TA_Gr* and *SALES/TA_Gr* are positive and significant for the below-median-*IP* sample presented in Column (1), (3), (5) and (7). In contrast, their coefficients are negative and insignificant for the above-median-*IP* sample presented in Column (2), (4), (6) and (8). Together, these findings suggest that U.S. acquirers select well-performing firms in countries with weak investor-protection; however, they do not exhibit this tendency in countries with strong investor-protection.

The coefficients on *MB*, one of firm-level control variables, also exhibit similar pattern. Firms with higher *MB* are less likely to become acquisition targets, which has been well-documented in previous studies (e.g. Palepu, 1986). However, this negative relation occurs only in the above-*IP* sample. In the below-*IP* sample, the impact of *MB* on the likelihood of being a target is significantly positive. To the extent that MB measures investors' expectation of firms' future performance, these results on *MB* imply that U.S. acquirers target well-performing firms in weak *IP* countries but poorly performing firms in strong *IP* countries. *Leverage* is significantly positively related to the likelihood of being a target in the below-*IP* sample, but not for the above-*IP* sample. This suggests foreign investors tend to select high leveraged firms in countries with weak investor-protections but not in countries with strong investor-protection. To the extent that debt has a disciplinary effect on management (e.g. Jensen, 1986), and hence highly leveraged firms are better governed, this finding is consistent with the hypothesis that U.S. acquirers tend to select well-governed firms in weak investor protection target countries, but not in strong investor-protection countries. As for liquidity, U.S. firms are attracted to more liquid firms regardless of strengthen of investor protection. One country characteristics that stands out is the regulation on restructuring. When local regulation makes restructuring more costly, U.S. firms tend to stay away from those countries, perhaps because of such regulations make it difficult to obtain operating synergies through

restructuring. Lu (2007) investigates this issue further and demonstrates the importance of restructuring regulations on cross-border M&As.

The regressions in Column (1) to (4) are estimated with clustering by countries in lieu of country fixed effects. The same regressions are estimated with country fixed effects, and in Column (5) through (8) the coefficients of *EBITDA/TA_Gr*, *SALES/TA_Gr* and *MB* are mostly unchanged in terms of both magnitude and the level of significance.

In sum, the initial regression estimates suggest that target selection decisions of U.S. acquirers depend on local investor-protection. They select well-performing in countries with weak investor-protection, but no such tendency is observed in countries with strong investor-protection.

IV. Corporate Governance Reforms and Target Selections

Although the above empirical methodology is intuitively appealing, it may not be correctly identifying the impact of investor-protection on target selections. The legal environment indices have low within country time series variation. As a result, the results above are mostly estimated with cross-country variation. As a potential remedy, I include country fixed effects to control for time-invariant unobserved country characteristics. However, it is possible to have time-varying country characteristics that affect U.S. firms target selection decisions.

Over the past decade, many countries have enacted significant corporate governance reforms (CGRs), which generate within-country variation in investor-protection. Also, when a country undertakes a CGR, its legal investor-protection may change at a faster speed than other country factors. Thus, I use CGRs to identify the impact of changes in investor-protection.

In this section, to better utilize within country investor-protection variation, I identify the most important CGR for each target country from 1990 to 2006, if the country has undertaken any CGRs during this period. I then utilize these CGRs to examine the impact of investor-protection changes on U.S. firm cross-border acquisition target selection.

A. Corporate Governance Reforms

A.1. Background

Corporate governance reforms (CGRs) are defined as deliberate interventions in a country's corporate governance traditions by the state, the local security and exchange commission, or local stock exchanges. CGRs are undertaken in the form of a *CGR code*, which is a set of codified corporate governance norms pertaining to such issues as the role and composition of the board of directors; the installment of board subcommittees (e.g., audit, compensation, and nomination committees); the appointment and rules of operation applying to external auditors; the distribution of rights and powers over professional managers, various groups of shareholders, and other stakeholders; the role of media in information dispersion; and the protection of employees who "blow the whistle" (Aguilera and Cuervo-Cazurra, 2004). Typical examples of CGRs around the world include Sarbanes Oxley Act of 2002, Higgs Review (UK, January 2003), and so on.

Recent worldwide CGRs are generated by three major impetuses, and in many countries, these three impetuses are indistinguishable. The first is international pressure for domestic institutional evolution. For example, the OECD issued its corporate governance principles (1999, 2004).[22] These principles provide specific guidance for policymakers, regulators, and market participants in improving the legal, institutional, and regulatory framework that underpins corporate governance, with a focus on publicly traded companies. They focus on the rights and equitable treatment of shareholders, the role of stakeholders, disclosure and transparency, and the responsibilities of the board. In practice, the impact of OECD Corporate Governance Principles is not restricted to OECD countries. Recently, the OECD principles have been used extensively by the World Bank as a framework for policy dialogue to promote regional CGRs and roundtables in some non-OECD countries in Asia, Latin America, and Eastern Europe. The participation of most non-OECD countries confirms the adaptability of the OECD principles as a reference in varying legal, economic, and cultural contexts.[23] Additionally, in response to the OECD principles, various regional organizations around the world have come up with their own corporate governance principles to enhance corporate governance environments in their regions. Organizations such as the Asia-Pacific Economic Cooperation (APEC), Pacific Economic Cooperation Council (PECC), Asian Development Bank (ADB), Commonwealth Association of Corporate Governances (CACG), European Commission (EC), and the UN Economic Commission for Africa (UNECA) have published their own principles.[24]

[22] OECD corporate governance principles (1999, 2004) is one of the most important and influential standards of corporate governance over the world. There are 6 broad principles: 1. Ensuring the basis for an effective corporate governance framework; 2. The rights of shareholders and key ownership functions; 3. The equitable treatment of shareholders; 4. The role of stakeholders in corporate governance; 5. Disclosure and transparency; 6. The responsibilities of the board.

[23]The roundtable dialogues have resulted in some common corporate governance issues across participating developing countries: 1. Strengthening effective legal enforcement; 2. Protecting shareholders, particularly minority owners; 3. Dealing with conflicts of interest; 4. Strengthening company oversight by boards.

[24] For instance, the APEC-PECC Guidelines are committed to a process of aligning their corporate governance practices with global best practices, consistent with the OECD principles and provide a non-binding and voluntary framework for the implementation of global best practices consistent with OECD core principles. This suggests that regulatory authorities may then issue specific regulations that facilitate and encourage – clearly setting the

The second impetus is financial crises. In some countries, corporate governance has not received much attention until financial crises took place. Weak corporate governance has been considered to be an important factor causing financial crisis. After financial crises, the most effected countries undertook CGRs to improve their corporate governance systems, and these CGRs are viewed as part of the post-crisis restructuring process. For example, after the Asian financial crisis of 1997, rapid Chaebol reform was started by the newly elected administration. Chaebol reforms were initiated to change the traditional characteristics of Chaebol, and to build an Anglo-American corporate governance system. [25] Through forcible government's Chaebol reform, accountability, transparency, and financial health in the Chaebol were drastically improved (Kim and Kim, 2008).

The third impetus is big corporate scandals. The Sarbanes Oxley Act (SOX) enacted in July 2002 is a typical CGR in response to business scandals, including major corporate failures at Enron, Vivendi, Arthur Andersen, and Marconi. SOX is one of the major government regulations passed in recent history, with the aim to enhance corporate governance of U.S. listed firms. SOX has 11 sections, which can be grouped under three headings: board-related changes; changes in disclosure and accounting rules; and audit-related changes. These rules consist of provisions from several different perspectives, and mostly focus on improving board structure, the quality of financial statements, and internal controls to strengthen anti-self-dealing restrictions. The general evidence of existing studies on the impact of SOX on U.S. corporate governance is positive.[26] Thus, I assume that U.S. corporate governance has been further improved by SOX.

These U.S. business scandals and SOX have a broad effect on corporate governance system around the world. For example, the fall of Enron also spurred corporate governance issues in the U.K. To response to the U.S. business scandals, the Higgs Report (2003) deals specially with the role and effectiveness of non-executive directors, and makes an important practical recommendation that a non-executive director assume chief responsibility as a champion of shareholder interests. The Smith Report (2003) is another response to the U.S. business scandals, and it makes recommendations on the relationship between the external auditor and the

direction towards – the OECD core principles"; "in the spirit of assisting corporate directors, committed to making their board work more effectively in line with the OECD core principles"; It is evident that the Asian corporate governance guidelines have been influenced by the OECD principles.

[25] Corporate governance systems around the world have prevailed in two major parallel forms, Anglo-American and Non-Anglo-American (European and Asian) corporate governance system, since the diverse origins of capitalism. The Anglo-American corporate governance system usually involves a dispersed ownership model characterized by strong and liquid securities markets, high disclosure standards, high market transparency, and an outsider-based system. The Non-Anglo-American corporate governance system usually involves a concentrated ownership model characterized by insider-based controlling shareholders, weak securities markets, low transparency and disclosure standards and often a central monitoring role for large banks that have a stake in the company. The Anglo-American system, therefore, is considered with more efficient security markets and stronger investor-protection.

[26] For example, Cohen et al. (2008) document a significant decline in earnings management after the passage of SOX; Gordon et al. (2006) show that SOX has impacted the voluntary disclosure of information security activities by firms; Chhaochharia and Grinstein (2008) demonstrate that SOX can enhance the efficiency of the managerial compensation system.

companies they audit, and the role and responsibilities of companies' audit committees. Also, many other countries began to update their existing corporate governance codes or quickly adopted one if they did not have one before. Big business scandals also took place in some other countries, and served warning to local governments to improve their corporate governance systems. For example, French market was rocked by several scandals in 2003, which helped to raise legislator's awareness of issues relating to corporate governance and independent auditors.

A.2. Identifying the CGRs of Each Country

To identify the major CGR of each country, I collect information by searching the website of the World Bank, European Corporate Governance Institute, and countries' stock exchanges. Many countries gradually change their corporate governance system by undertaking multiple CGRs. I take the most effective and influential CGR as the CGR of the country based on three criteria[27]: (1) The CGR is applied to all publicly listed firms; [28] (2) the CGR is mandatory rather than voluntary;[29] (3) the central intent is to improve financial transparency, provide monitoring by independent board members or audit systems, and establish effective legal systems.

When a country has multiple CGRs that are more or less equivalent, then the earliest CGR is treated as the CGR of the country. For example, Australian ASX Corporate Governance Council released the first edition of its Principles of Good Corporate Governance Practice and Best Practice Recommendations on March 2003. On 2 August 2007, the Council released the second edition of the Corporate Governance Principles and Recommendations.[30] In this case, the releasing of the first edition is identified to be the CGR of Australia. I take the first year a CGR is in effect, rather the year of announcement or of publication as the year of a CGR implementation. When CGRs do not have precise effective date, the effective year is estimated as one year after the year of announcement or publication. Appendix2 contains a brief description of history, contents, and issuing and effective years of CGRs.

Although these CGRs undertaken by different countries contain different regulations, there are commonalities across countries. The central intent of all these CGRs is to improve financial transparency, provide monitoring

[27]The identification of major CGRs is relatively subjective, and it is based on large reading of website information and articles.

[28] Some CGRs only apply to sub-group of firms instead of all public firms in the country. For example, In Finland, Handling of Corporate Governance Issues (2000) only applies to State-Owned companies and their associated companies.

[29]The corporate governance codes associated with some CGRs around the world vary considerably in terms of content and legal status and origin. Basically, they have two types, mandatory codes and voluntary compliance codes. Mandatory codes could be the codes with the "comply or explain" principles or the codes with the enforcement. Voluntary compliance codes do not have precise enforcement date and criteria. For example, Danish Shareholders' Association Guidelines (2000), Berlin Institutive Code (2000) and NAPF Corporate Governance Code (2000) in UK are all voluntary compliance. Because it is not clear how effective, voluntary compliance codes are, I do not treat them as CGRs.

[30] http://www.asx.com.au/supervision/governance/index.htm

by independent board members and/or audit systems, and establish effective legal systems. They mostly focus on the following four issues: strengthening the mechanisms of internal governance by specific requirements concerning the role and composition of the board of directors; empowering shareholders; enhancing disclosure requirements; toughen public enforcement.

These CGRs can be seen as a source of within country variation in investor-protection. Each country undertakes a CGR based on its specific economic and/or political needs at different points in time. The staggered passages of CGRs by different countries allow us to estimate the impact of CGRs on target selections with a difference-in-difference approach.

B. Empirical Methodology

A difference-in-difference (D-I-D) approach is employed to examine the effect of CGRs on target selections. I firstly consider the impact of CGRs in target countries on the types of firms being targets by comparing the pre-acquisition performance of target firms before and after a major CGR in the target country. This approach can be easily understood with an example. To estimate the effect of a CGR in India in 2004, I compare the pre-acquisition performance of target firm after 2004 with those of targets before 2004. However, other things in 2004, such as a recession, may affect the performance of these Indian firms. Having a control country that does not have CGR in the same year (e.g. China, which had a CGR in 2002), would help control for changes in economic conditions in India. I would, therefore, compare the difference in the pre-acquisition performance of Indian target firms before and after 2004 to that of Chinese target firms before and after 2004. The difference of those two differences, δ, would serve to identify the impact of the CGR undertaken in India on target selections of Indian firms by U.S. acquirers. I expect δ to be negative, namely the tendency of U.S. investors to select well-performing firm decreases after the target country undertakes a CGR. One important distinction between this example and the regression framework is that the regression accounts for the fact that there are many CGRs staggered over time. These staggered passages of CGRs implicitly treat all target firms located in countries not enacting CGRs at time t to be the control group of the target firms located in countries which undertake CGRs at time t. The countries as the control group may have undertaken or may undertake CGRs later.[31]

The sample to estimate this D-I-D model is constructed at the deal level. Since there are no multiple acquisitions of a target firm in the sample, one deal is associated with one unique target firm. The specification is as follows,

[31] This empirical strategy is similar to the method used by Bertrand and Mullainathan (2003).

$$Perform_{ijct} = \beta_{jt} + \beta_c + \gamma X_{ijct} + \delta TCGR_{ct} + e_{ijct}, \quad (9)$$

where *i* indexes deals; *j* indexes industries of target firms; *c* indexes target countries; *t* indexes time; $Perform_{ijct}$ is the dependent variable, measured as *EBITDA/TA_Gr* or *SALES/TA_Gr* in one year prior to the announcement of the acquisition bid; β_{jt} is year-varying target industry fixed effects (defined as one-digit SIC); β_c is country fixed effects, X_{ijct} is a vector of control variables; $TCGR_{ct}$ is an indicator that equals one if a major CGR[32] is undertaken by time *t* in target country *c*; e_{ict} is error terms. The full sample includes 969 acquisitions which are associated with 755 U.S. acquiring firms. To address the heteroskadasticity due to multi-acquisitions by a common acquirer, all regressions are estimated by clustering at the acquirer level.

Regression (9) can be extended by accounting for the impact of SOX, the CGR of the acquirer country, the U.S. Doing so can better control for the change in the legal environment of the acquirer country and more precisely estimate the impact of CGRs of target countries on target selections. Additionally, it allows us to test the impact of investor-protection of the acquirer country on target selection decisions. A difference-in-difference approach is also employed to examine how SOX affects the type of target firms. First, I compare the pre-acquisition performance of target firms of the acquisitions before and after SOX. This procedure cannot fully identify the impact of SOX, since the time trend cannot be controlled. Although SOX applies to all firms listed on US stock exchanges, the realized effects vary across firms. SOX basically includes the four provisions: boards should have a majority of independent directors; an independent audit committee; an independent nominating committee; an independent compensation committee. Some firms voluntarily implemented some or all of these four provisions before SOX. As a result, the firms that were less compliant with the provisions before SOX are expected to experience greater impacts of SOX (Chhaochharia and Grinstein, 2007). These varying implementations by firms provide a cross section variation in the affect of SOX on U.S. acquirers. To control for time trend (cohort) effects around the legislation of SOX, I treat the acquisitions conducted by the less SOX affected U.S. firms as the control group for the acquisitions conducted by the more SOX affected U.S. firms, and compare their cross sectional difference in targets' pre-acquisition performance. The difference of those two differences, λ, would serve to identify the impact of SOX on target selections of U.S. acquirers. I expect λ to be positive; namely suggests that SOX increases U.S. acquirers' tendency to pursue better performing firms, and this effect is greater for U.S. acquirers affected more by SOX.

[32] The year of the CGR in each target country can be found in Appendix 2.

To estimate the effect of the intensity of the effects of SOX on U.S. firms, I follow Chhaochharia and Grinstein (2007) and construct a variable, *SOXEff*, which is calculated as *(4 - BoardDep) * After2002*. *After2002* is an indicator, which is equal to one when the acquisition bid is announced after 2002, and zero otherwise. *BoardDep* takes the value of 0 to 4. Zero means that a U.S. firm is compliant with none of the four provisions, and hence the most affected by SOX, and four means a U.S. firm is compliant with all four provisions, and hence the least affected by SOX. If the acquisition bid is announced before 2003, *BoardDep* is the number of provisions in the year of the bid announcement. If the acquisition bid is announced after 2002, *BoardDep* is the number of provisions in 2002. The data on board and committee are taken from the Investor Responsibility Research Center (IRRC).[33]

After accounting for the impact of SOX, the specification becomes,

$$Perform_{ijckgt} = \beta_{jt} + \beta_c + \beta_g + \gamma X_{ijckgt} + \delta TCGR_{ct} + \lambda SOXEff_{kt} + e_{ijckgt}, \quad (10)$$

where *k* indexes acquirers. In addition, β_g is added to control for SOX shock intensity fixed effects, which group firms into five groups according to *BoardDep*. This is to control for potential endogenous issues in shock intensity; for example, there might be factors affecting both firm's selection of its board structure and acquisition targets.

C. Data

To estimate Regression (9) and (10), the sample is constructed at the deal level. Table 4 presents the country distribution of the sample. The full sample includes 969 U.S. acquisitions taken place in 40 countries announced from January 1, 1990 to December 31, 2007. The acquisition screening criteria are the same as before, but the target size is bigger because this empirical approach allows inclusion of targets which do not have matched non-target firms in WorldScope. The sample includes 705 acquisitions before the CGRs of the target countries, and 264 acquisitions after the CGRs. The sample includes 653 acquisitions taken place before the passage of SOX, and 316 acquisitions taken place after the passage of SOX.

D. Results

D.1. Impact of CGRs in Target Countries on the Types of Firms being Targeted

[33] The IRRC Directors database provides details on the structure and practices of the boards of directors of U.S. firms starting in 1996. To maximize the sample size, the data before 1996 are filled with the information in 1996.

Table 5 presents the impact of CGRs undertaken in target countries on the type of firms being targeted by U.S. acquirers. The estimated coefficient of interest is δ on the variable *TCGR*. Column (1) estimates the relation between a CGR undertaken in a target country and the mean of the pre-acquisition *EBITDA/TA_Gr* of target firms. The negative coefficient of *TCGR* suggests that mean value of pre-acquisition *EBITDA/TA_Gr* of target firms significantly decreases by 0.463 after the target country undertakes a CGR. This is consistent with the prediction that improvement in target country's investor-protection decreases U.S. acquirers' tendency to target well-performing firms.

The robustness results of the effect of *TCGR* are presented in the rest of the table. Column (2) shows that the negative effect of *TCGR* is robust to the inclusion of deal-, target firm-, and target country-specific controls. *Num of Deals* is the number of deals taken place in each target country during each year, which is be used to control for the impact of merger waves in a particular country during a particular period. CGRs may also affect the number of acquisitions by improving domestic firms' corporate governance. With a greater number of acquisitions, there will be greater variation in the pre-acquisition quality of target firms. *Horizontal* is an indicator, which equals one, when the acquirer and target are sharing the same first two-digit SIC code, and zero otherwise. Target selections in horizontal acquisitions may differ from those of vertical ones. *Cross List* is an indicator for cross-listing of the target shares in a foreign stock exchange at the time of acquisition announcement. Cross listed firms are affected by the corporate governance regulations of both countries.[34] *Crisis2* is an indicator for the acquisition bid announced in the following country-year combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-199. *GDPPA* is GDP per capita of the target country one year prior to the acquisition announcement year. Over the past two decades, some large developing countries, such as China, experienced significant economic growth. The change in pre-acquisition performance of targets could be driven by local economic growth. Of the five control variables, *Cross List* and *GDPPA* show significantly negative coefficients. The coefficient of *Cross List* shows a weaker tendency to select well-performing firms if the target firms are cross-listed firms. This seems to reflect the fact that cross-listed firms tend to be subject to stronger invetor protection regulations than non-cross listed domestic firms. The negative coefficient of *GDPPA* suggests that U.S. acquirers target well-performing firms in poor countries but under-performing target firms in rich countries.

Column (3) presents the robustness check of the impact of *TCGR* by accounting for the possible non-randomness of CGRs in target countries. As mentioned earlier, CGRs might be followed by financial crises or

[34] For a robustness check, I control for an *ADR* dummy, instead of this *Cross List* dummy, and the results are unchanged.

major business scandals. These reasons would make CGRs less exogenous. One possible way to deal with this issue is an inclusion of additional variables to control for these potential factors. Following the method in Duflo (2001), two variables are included in the regression to deal with this issue. The first is the product of *TCGR* and *Have_Crisis*. *Have_Crisis* is an indicator, which equals one if a financial crisis took place before the year of issuing the CGR in a target country. The second is the product of *TCGR* and *Have_Scandal*. *Have_Scandal* is an indicator, which equals one if some big business scandals happened before the year of issuing a CGR in a target country. Again, the estimated coefficient on *TCGR* is largely uneffected in terms of both the level of significance and magnitude.

The change in target's pre-acquisition performance may simply reflect changes in the performance of all firms in the same country, industry and year. To address this concern, Column (4) conducts a robustness check by accounting for the change in the location of target firms in the distribution of all firms' performance in the same country, year and industry (defined as the first two digit-SIC code). I employ the numerical cumulative density functions (CDFs) of target firm's *EBITDA/TA_Gr* as the dependent variable, which is calculated based on all observations with the same country, year and industry. CDF represents the relative performance position of a target firm in its matched country-, year- and industry sample. Additionally, it also reduces the importance of extreme outliers by normalizing the variable into a unit interval. One weakness of the CDF approach is that it depends on the number of observations in each country-, year- and industry-specific sub-sample. When the number of observations is small, which is typically the case for emerging countries, CDF is a quite noisy measure of relative performance. Since the negative effect is predicted for weak investor protection countries, which are predominantly emerging economies, this CDF approach biases against finding a significant negative effects. With this build-in bias, the coefficient of *TCGR* is -0.1 and significant at the 10% level. This implies that after a target country improves its corporate governance by undertaking a CGR, the performance of target firms is 10 percentile lower within the same country-, year- and industry-specific sample.

In Column (5) to (8), I repeat the same exercises with *SALE/TA_Gr* as the measure of firm performance. The results are basically unchanged.

D.2. Impacts of both CGRs in Target Countries and SOX on the Types of Firms being Targeted

The results above focus solely on CGRs of target countries. The gap in investor-protection between the acquirer and target country is determined by the regulations of both countries. This gap will be changed, when regulations in either country are changed. I estimate the model (10) to test the impact of the CGRs of both

acquirer and target countries and report the results in Table 6. The impact of the CGR of the target country is estimated by the coefficient of *TCGR*, and that of the acquirer country is estimated as *SOXEff*.

Column (1) displays the basic results of the impact of *TCGR* and *SOXEff* on the mean of pre-acquisition *EBITDA/TA_Gr* of targets. The coefficient of *TCGR* is still negative and significant. The estimated coefficient on *SOXEff* is positive, but insignificant.

However, in Column (2), when I control for deal, firm and country characteristics, and the change in the legal environment of the target country, the estimated coefficients of both *TCGR* and *SOXEff* become significant at the 5% level. Thus, I conclude that when the acquirer country strengthens its investor-protection regulations, the tendency to select well-performing firms becomes stronger because the acquirer's valuation of control premiums becomes lower.

Column (3) displays whether the results are driven by an endogenous treatment of SOX. I consider the following possibility. Suppose that there are acquirer-specific factors that affect SOX treatment intensities by affecting U.S. acquirer's self-selection of board structures before SOX and that are also related to this U.S acquirer's target selection decisions. Then, the estimated coefficient of *SOXEff* would be biased due to endogeneity. The ideal method to address this issue is controlling for acquirer fixed effects, which requires multi-acquisitions by an acquirer both before and after SOX. However, there are not enough such observations in the sample. Instead, I include several acquirer-specific variables: *Acquirer Tobin's Q*, *Acquirer Firm Size*, and *Acquirer Eindex*. *Acquirer Tobin's Q* is measured as a ratio. The numerator is the book value of total assets of the acquirer (Compustat: data6) subtracting the book value of equity (Compustat: data60), plus the market value of equity (Compustat: data24*data25). The denominator is the book value of total assets (Compustat: data6). *Acquirer Size* is the log of the book value of total assets (Compustat: data6). *Acquirer Eindex* is the entrenchment index of acquirers provided by Bebchuk et al. (2004).[35] For deals which are announced before 2003, the values of these acquirer-specific variables are taken in the year of the announcement. For deals which are announced after 2002, the values of these variables are taken in year of 2002. The estimated coefficients on the *TCGR* and *SOXEff* are essentially the same.

[35] This entrenchment index is taken from IRRC database, which include eight year publications: 1990, 1993, 1995, 1998, 2000, 2002, 2004, and 2006. Following Bebchuk et al. (2004) and Masulis, Wang, and Xie (2007), I fill the missing years with the entrenchment provision data for the most immediate preceding years with IRRC publication data (e.g., data for 1994 are filled with 1993's data).

Column (4) presents the robustness check of the impact of *TCGR* and *SOXEff* on types of firms being targets by using the CDF of *EBITDA/TA_Gr* as the dependent variable. The results are robust. The coefficient of *TCGR* is still significantly negative. The positive coefficient of *SOXEff* suggests that U.S. acquirers exhibit more willingness to target well-performing firms if they are more affected by SOX. Column (5) to (8) repeat the same set of exercises with *SALE/TA_Gr* as the measure of firm performance. The results are robust.

In sum, all the findings indicate that the tendency of U.S. investors to select well-performing targets is related to the gap in investor-protection between the acquirer and target countries. When investor-protection in the target country is strengthened, the tendency for the U.S acquirer to select well-performing firm decreases; in contrast, this tendency becomes stronger, when acquirers are subject to stronger investor-protection.

E. Other Robustness Checks

I conduct the following robustness checks on the results reported in Table 5 and 6. The availability of the data varies across target countries. Larger countries have better coverage (e.g., the U.K. or Canada) than small countries (e.g., Czech Republic). The estimation of well-covered countries is more precise than that of poorly-covered countries due to the greater variance of estimators. To address this concern, I repeat all regressions with sampling weights of each target country. Sampling weights denote the inverse of the probability that the observation is included due to the sampling design.[36] The results are unchanged.

Additionally, I try several different specifications with other control variables. Foreign acquisitions of state owned enterprises (SOEs) tend to be related to privatizations and may have special attributes of performance. In the sample, there are 23 acquisitions of SOEs. Controlling for a *SOE* indicator does not change results, and the coefficient of *SOE* is insignificant different from zero. I also control for the annual growth rate of *GDPPA*, and the results are unchanged. The results are also robust to controlling for *Restructure_Reg* index.

Finally, the results are estimated with the full sample, which includes both complete and incomplete acquisitions. I repeat all analyses with the sample only including complete acquisitions; the results yield a similar pattern but are weaker in terms of significance. This is probably due to smaller sample size. I also exclude the acquisitions of firms in financial services (SIC codes: 6000-6999) and utility (SIC codes: 4911-4931) and repeat the above analyses. The results are robust for this sub-sample. Furthermore, I restrict the

[36] Previous studies deal with the problem of unbalanced samples across countries by removing the observations in the countries which do not have more than a certain number of observations. I do not adopt this method for the following reasons: First, in general the sample size for each test is small, and removing any observations could lead to a big loss for the regression analysis. Second, the criterion (i.e., the number of observations in each country) seems to be arbitrary, so to avoid this, I employ sampling weights, instead of removing observations.

sample to acquisitions of at least 10% or 20% of outstanding shares transfers. Although the sample size is dramatically reduced, the results qualitative remain unchanged.

VIII. Summary

This paper explains how the gap in investor-protection between the acquirer and target countries affects cross-border target selection. An acquirer from a strong investor-protection country values control premiums less than does an incumbent controlling shareholder in a weak investor-protection country. To pay lower control premiums, the acquirer will select well-performing firms, because well-performing firms self-select better governance and require lower control premiums. Thus, an acquirer from a country with stronger investor-protection than the target country tends to target well-performing firms, and this tendency becomes stronger as the acquirer country's investor-protection strengthens or the target country's investor-protection weakens.

These predictions are tested with data on U.S. cross-border acquisitions in 40 developed and developing countries. U.S. firms tend to acquire well-performing firms in countries with weak investor-protection, but do not in countries with strong investor-protection. Using a difference-in-difference approach based on variation in investor-protection generated by staggered passages of CGRs in target countries, I find that U.S. acquirers exhibit more willingness to target underperforming firms after the target country undertakes a CGR. Sarbanes-Oxley Act (SOX) had the opposite effect of increasing U.S. acquirers' tendency to pursue better performing firms, and this effect is greater for U.S. acquirers affected more by SOX.

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Appendix 1: Variable Descriptions	
Panel A: Legal Variables *(Note: A higher score indicates stronger investor-protection)*	
Anti-self-dealing	It measures the amount of disclosure before and after the transaction has occurred, the need for approval by disinterested shareholders and litigation governing a specific self-dealing transaction. It is time invariant and at the country level. (Source: Djankov, et al. (2008))
Law-and-Order	It measures the strength and impartiality of the legal system and of the popular observance of the law. It is annual frequency and at the country level. (Source: International Country Risk Guide)
IP	It is measured as (*0.5*Anti-self-dealing + 0.5*Law-and-Order*).
Panel B: Corporate Governance Reform Variables	
TCGR	It is an indicator, which is equal to one if a major corporate governance reform (see in Appendix 2) is undertaken in the target country, when the acquisition bid is announced.
After2002	It is an indicator, which is equal to one if the acquisition bid is announced after 2002.
DepBoard	When the acquisition bid is announced before 2003, it measures how many of the following four provisions with which the U.S. acquirer has been compliant in the announcement year. When the acquisition bid is announced after 2002, it measures how many of the following four provisions that the U.S. acquirer has been compliant in 2002. It takes the value of 0 to 4. Zero means that the U.S. acquirer is compliant for none of these four provisions, and four means the U.S. acquirer is compliant for all four provisions. The four provisions: a majority of independent directors; an independent audit committee; an independent nominating committee; an independent compensation committee. (Source: the Investor Responsibility Research Center (IRRC)). [Note: The data taken from IRRC are available only after 1996. The data before 1996 are filled with the information in 1996.]
SOXEff	It measures SOX shock intensity on U.S. acquirers. It is constructed as: *(4- DepBoard) * After2002*. It takes the value of 0 to 4, and a higher value indicates stronger impacts of SOX on a U.S. acquirer.
Have Crisis	It is an indicator, which is equal to one if a financial crisis took place before the corporate governance reform defined in Appendix 2 in the target country. Countries which have had crises include Thailand, South Korea, Indonesia, Argentina, Brazil, and Mexico.
Have Scandal	It is an indicator, which is equal to one if any big business scandals took place before the corporate governance reforms defined in Appendix 2 in the target country. Countries which have had scandals are identified as China, France, Ireland-Rep, Japan, and Philippines.
Panel C: Firm and Deal Variables	
EBITDA/TA_Gr	It is the growth rate of earnings before interest expense, income taxes, depreciation and amortization *(EBITDA)* divided by the book value of total assets. It is winsorized at the 1 and 99 percentile respectively. (Source: SDC, Bloomberg and WorldScope)
SALES/TA_Gr	It is the growth rate of sales divided by book value of total assets. It is winsorized at the 1 and 99 percentile. (Source: SDC, Bloomberg and WorldScope)
Firm Size	It is measured as the natural logarithm value of the book value of total assets. The book value of total assets is denominated in 2000 $US. (Source: SDC, Bloomberg and WorldScope)
Leverage	It is measured as the total debt (long term + short term debt) divided by the book value of total assets. (Source: SDC, Bloomberg and WorldScope)
MB	It is measured as the ratio of the market value of the common equity to the book value of equity. The observations with negative *MBs* are replaced by zero. (Source: SDC, Bloomberg and WorldScope)
Liquidity	It is measured as current assets divided by current liabilities. (Source: SDC, Bloomberg and WorldScope)
Cross List	It is an indicator, which is equal to one, if the target firm's listing location is different from its nationality, when the acquisition bid is announced. (Source: SDC)
HHI	It is the Herfindahl-Hirschman Index of a country-year specific industry. Industries are defined as the first two-digits of the SIC code. It is calculated as the sum of the squares of the market shares of top four firms in each country-year specific group. (Source: WorldScope)
PPE/TA	It is the gross value of property, plant and equipment divided by total assets of a target firm in one year prior to the announcement of the acquisition bid. (Source: SDC, Bloomberg and WorldScope)
OWN	It is measured by the ratio of close-held shares to the number of total equity shares of a target firm one year prior to the announcement of the acquisition bid. (Source: WorldScope)
Acquirer Tobin's Q	It is measured as a ratio. The numerator is the book value of total assets subtracting the book value of equity, and then adding the market value of equity. The denominator is the book value of total assets. All variables are measured in one year before the announcement of the acquisition. (Source: SDC and Compustat)

Acquirer Firm Size	It is measured as the natural logarithm value of the book value of total assets of U.S. acquirers one year before the announcement of the acquisition bid. The book value of assets is denominated in 2000 $US. (Source: SDC and Compustat)
Acquirer EIndex	It is the entrenchment index of U.S. acquirers, and takes the value of 0 to 6. A higher value indicates greater entrenchment. (Source: IRRC database) [Note: There have been eight publications; 1990, 1993, 1995, 1998, 2000, 2002, 2004, and 2006. The data of missing years are filled with the data for the most immediate preceding years with IRRC publication data.]
Horizontal	It is an indicator, which is equal to one if the first two-digits of SIC codes for the acquirer and target are the same. (Source: SDC)
Panel D: Other Country-level Variables	
GDPPA	It is GDP per capita, and denominated in 2000 $US. (Source: except Taiwan, the data are taken from the World Development Indicators; for Taiwan, the data are taken from Global Insights)
InwordFDI/GDP	It is net inflows of foreign direct investments as the percent of GDP
Restructure Reg	It is an index measuring the regulation barriers of restructuring. It has three components: labor laws taken from Botero et al. (2004); regulations of closing a business taken from the World Bank Doing Business Indicator; the enforceability of contracts taken from Djankov et al. (2003). These three regulation indexes are normalized into the range from zero to one. Stronger enforceability of contracts (*Enforce Reg*) is associated with lower restructuring costs, so to be consistent with the other two indexes enforceability of contract index is reversed as *Rev Enforce Reg = 1- Enforce Reg*. *Restructure Reg* is constructed based on the parameters of principal component analysis. *Restructure Reg = 0.12 * labor Reg + 0.71 * Closbus Reg + 0.70 * Rev Enforce Reg*. Higher *Restructure Reg* indicates heavier regulations on restructuring.
Anti Trust Reg	It is a score of antitrust laws as it pertains to mergers for 2004. It attempts to measure the size of the competition laws net applied to mergers. Higher value indicates stronger regulations. (Source: Hylton and Deng (2007))
Num of Deals	It is the number of deals taken place in each country during each year in the sample.
Crisis1	It is an indicator, which is equal to one if the firm-year observation has any of the following country-year specific combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995.
Crisis2	It is an indicator, which is equal to one if the acquisition bid is announced in the following country-year specific combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995.

Appendix 2: Major Corporate Governance Reforms of Target Countries					
Target Country	**Corporate Governance Reforms**	**IssY**	**EffY**	**Est**	**Sources**
Argentina	The Argentine regulatory framework adapted good governance principles to the local market. Decree No. 677/01 (published at the Official Gazzette on May 28, 2001, and becoming effective on 1 June 2001) established a new Public Offering Transparency Regime.	2001	2001	N	The new corporate governance rules in Argentina, American Bar Association Section of International Law and Practice
Australia	In March 2003 the ASX Corporate Governance Council (Council) released its 10 "Principles of Good Corporate Governance" (Principles) and 28 "Best Practice Recommendations" (Recommendations) that support the Principles. Reporting (and the mandatory audit committee requirement) commences for financial years beginning after 1 January 2003 (i.e. if the entity's financial year ends on 30 June, the reporting requirements will have to be met in relation to the period 1 July 2003 to 30 June 2004, for the 2004 annual report typically sent out in September or October, and the audit committee will have to be in place during the period 1 July 2003 to 30 June 2004). But entities are encouraged to opt in earlier.	2003	2003	N	http://www.asx.com.au/supervision/governance/index.htm
Austria	The Austrian Code of Corporate Governance presented to the public on 1 October 2002 by Austrian Working Group for Corporate Governance has become an indispensable part of the Austrian corporate governance system and is viewed by investors as well as by issuers as a milestone in the drive to develop and invigorate the domestic capital market. The code is designed to increase the degree of transparency for all stakeholders, and primarily applies to Austrian stock listed companies. It is based on the provisions of Austrian corporation law, securities law and capital market law as well as on the principles set out in the OECD Principles of Corporate Governance.	2002	2003	Y	http://www.corporate-governance.at/
Belgium	The first draft of Belgian Corporate Governance Code was published by Corporate Governance Committee for consultation on the Committee's website on 18 June 2004. The comments received, together with recent EU Commission initiatives, helped the Committee to finalize the Code. On 9 December 2004, the Code was published to provide Corporate Governance Guidelines for all listed companies in Belgium, becoming applicable 1 January 2005. The code's main aim is to support long-term creation, to enhance transparency and accountability to enable firms to access external funding at a lower cost, and to bring macro-economic advantages (e.g. improving economic efficiency and growth, and protecting private investments).	2004	2005	N	http://www.corporategovernancecommittee.be/en/committee/guidelines/default.aspx
Brazil	The first edition of the Code of the Best Practice of Corporate Governance, released in 1999 by Brazilian Institute of Corporate Goverance (IBGC), focused mainly on the Board of Directors, its workings, composition, and attributions. The second edition was published in April 2001, and was a consolidation of technical arguments on the equity principle among different shareholders. Its scope was extended to all corporate governance agents: the Board of directors, Fiscal Council, Managers, and Independent Auditors, in addition to the accountability principle and discussions about conflicts of interest and ethics. In its third edition, of March 2004, the highlight was the inclusion of the corporate responsibility principle. The edition of 2001 is treaded as the CGR, since the first one does not focus mainly on improving corporate governance.	2001	2002	N	http://www.ibgc.org.br/Home.aspx
Chile	In an attempt to revive a flagging market, some vices in corporate practices have been corrected (partially) by the enacting of the so-called "Ley de OPA" (PTO law) and Corporate Governance Law ("Law 19,705") in December 2000. This law is aimed at protecting of minority shareholders' rights. Subsequently to the enactment of Law 19,705, several complementary regulations have been issued by the Superintendence of Securities and Insurance ("SVS"), stating precisely how the new legislation should be understood and how it shall be encouraged, controlled and enforced by the SVS itself. This year 2001 will see the first effects of the new rules introduced by Law 19,075. In any case the year 2001 marks a new mile stone in the road of corporate governance and development of the securities market in Chile.	2000	2001	N	http://www.oecd.org/dataoecd/3/49/1823372.pdf
China	On January 7, 2002 the China Securities Regulatory Commission and the State Economic and Trade Commission in Beijing issued a "Code of Corporate Governance for Listed Companies in China (i.e. Zhenjianfa No.1. of 2002). This code shall come into effect on the date of issuance.	2002	2002	N	http://www.csrc.gov.cn/en/homepage/
Czech Republic	In 2001, the Czech Commercial Code was revised to address some issues related to self-dealing by Czech Securities Commission. Revised corporate governance code based on the OECD principles was public in February 2001. The code has been designed to set out the best practice for companies in the Czech Republic. This amendment would likely enter into force in December 2001	2001	2001	N	http://www.sec.cz/
Finland	HEX Plc, the Central Chamber of Commerce of Finland and the Confederation of Finnish Industry and Employers appointed a working group on 17 February 2003 to clarify the need of reviewing the corporate governance recommendation for listed companies issued by the Central Chamber of Commerce of Finland and the Confederation of Finnish Industry and Employers in 1997. This Recommendation enters into force on 1 July 2004.	2003	2004	N	http://www2.kaupakamari.fi/keskuskauppakamari/index.cfm?language=English
France	Principles of 2003 for corporate governance of listed corporations based on consolidation of the Basedon the Viénot Reports of July 1995 and July 1999 and on the Bouton Report of September	2003	2004	Y	http://www.ecgi.org/codes/documents/cg_oct03_en.pdf

	2002. All three reports represented initiatives of the business community itself, which attached importance to defining certain principles of good operation and transparency intended to improve management practices and to reinforce the confidence of investors and the public. This collection of recommendations has been developed by working parties composed of Chairmen of French listed corporations, at the request of the Association Française des Entreprises Privées (AFEP) and the Mouvement des Entreprises de France (MEDEF).				
Germany	In Germany, attempts have been made through the German Corporate Governance Code of February 26, 2002 to provide a regulatory framework for this concept, apart from its already existing embodiment in the Stock Corporation Act ("Aktiengesetz"), and the code of Commercial Law ("Handelsgesetz"). The code has a legal basis, and entered into force on July 26, 2002.	2002	2002	N	http://www.corporate-governance-code.de/index-e.html
Hong Kong	On 30 January 2004, Hong Kong Exchanges and Clearing Limited ("the Exchange") published an Exposure of Draft Code on Corporate Governance Practices and Corporate Governance Report (the "Exposure Paper"). The Code would become effective for accounting periods commencing on or after 1 January 2005.	2004	2005	N	http://www.hkex.com.hk/index_c.htm
India	In 2000, Clause 49 (of the stock exchange listing agreement for publicly traded corporations) was introduced in India, mandating greater board independence, enhancing disclosure requirements, and increasing the power of audit committees for affected firms. Importantly, however, not all Indian corporations were subject to Clause 49. Even among affected firms, not all were immediately subject to the new provisions. A small number of very big firms were expected to comply by 2001, a larger number of medium sized firms were expected to comply by 2002, and the remainder of the affected firms (which were mostly quite small in size) was expected to comply by 2003. In addition, firms that listed for the first time in 2000 (or later) were expected to comply from the time of listing.	2000	2003	N	http://www.sebi.gov.in/
Indonesia	In May 2000, the National Committee on Corporate Governance (NCCG), a high-level advisory group appointed by the Indonesian government, produced a draft of Indonesia's first code on corporate governance. The content closely followed global standards and the 1999 OECD Principles on corporate governance. In March 2001, NCCG published the final version of the Code. This is a model code deliberately designed as a "guide to excellence in corporate governance" for Indonesian companies. It is intended to apply eventually to all companies, but in the initial stage only to public companies, state-owned enterprises and companies "utilizing" or "managing" public funds.	2001	2001	N	http://www.governance-indonesia.or.id/main.htm
Ireland-Rep	The Companies (Auditing and Accounting) Act, 2003 is considered to be one of the most significant Irish company law initiatives of the past ten years. The key element of the 2003 Act are: Directors Compliance Statement and Annual Compliance Statement: The directors of public limited companies and private companies of a certain size must prepare annually two statements: the directors' compliance statement and the annual compliance statement. The ICEX Rules came into force on 1 January 2005 and the Companies' Act is considered to be fairly recent.	2003	2005	N	http://www.iaim.ie
Israel	The Israeli Companies Law of 1999 (hereinafter 'the new law') came into effect on February 1, 2000, and replaced most parts of former Companies Ordinance, which was originally enacted in 1929, and has been amended many times (hereinafter 'the old law'). The new law has brought into effect a new conception of corporate governance. This new conception is based on a clear separation of powers and better-defined checks and balances.	1999	2000	N	http://www.jewishvirtuallibrary.org
Italy	Reform of Italian Corporate and Securities Laws: The Investor Protection Act - January 12, 2006 - Prompted by a wave of financial scandals and inspired by legislation recently enacted in other countries under similar circumstances, the Italian Parliament has adopted the "Investor Protection Act," a set of rules designed, among other things, to enhance the rights of minority investors, the accountability of corporate directors and officers and the reliability of financial information of Italian listed companies1 (the "Act"). The Act amends and supplements various provisions of Italian securities and corporate laws relating to matters such as (i) the appointment of directors and statutory auditors, (ii) the responsibility for preparing financial information, (iii) the appointment and dismissal of outside auditors, the scope of their audit, and the range of non-audit services they can provide, (iv) disclosure relating to affiliates located in certain blacklisted jurisdictions, and (v) the criminal penalties that attach to the violation of these laws. The Act generally took effect on January 12, 2006, except for certain provisions, including those that require amendments to a company's organizational documents (which will have to be amended by January 12, 2007) or further rule-making by CONSOB, the Italian securities regulator, or other administrative bodies.	2006	2006	N	http://www.jura.uni-duesseldorf.de/dozenten/noack/Texte/Sonstige/Investor%20Protection%20Act%202006.pdf
Japan	By the early 2000s, financial reporting standards for listed firms had converged with international accounting standards. Beginning in 2000, firms were required to report their cross-shareholdings and shares for investment at market levels. Corporate Code reform in 2002 made corporate firms to choose between two options for board structure: the American-type system with independent subcommittees (on auditing, managerial compensation and nomination) or a modified traditional system with a semi-independent statutory auditor's board.	2002	2002	N	http://www.law.usyd.edu.au/anjel/documents/ZJapanR/ZJapanR19_07_Takahashi_Sh.pdf
Malaysia	The Malaysian Code on Corporate Governance (Code), first issued in March 2000, by Securities Commission Malaysia, marked a significant milestone in corporate governance reform in Malaysia. It codified the principles and best practices of good governance and described optimal corporate governance structures and internal processes.	2000	2001	N	http://www.sc.com.my/
Netherlands	The Code was issued by the Tabaksblat Corporate Governance Committee on 9 December 2003. It applies on and after financial years beginning 1 January 2004.The Code has five sections: I. Compliance with and enforcement of the Code, II. The Management Board, III. The Supervisory	2003	2004	N	http://www.mazars.com/news/corporate_governance_nl.php

	Board, IV. The shareholders and general meeting of shareholders, V. The audit of the financial reporting and the position of the internal auditor function and of the external auditor.				
Norway	The Norwegian Code of Practice for Corporate Governance is based on the provisional national code of practice for corporate governance published in December 2003. Its English version of the original document "Norsk anbefaling – Eierstyring og selskapsledelse (Corporate Governance)" is prepared in Norwegian and dated 7 December 2004 by Norwegian Shareholders Association Norwegian Institute of Public Accountants. The Code of Practice is intended to strengthen confidence in companies, and help to ensure the greatest possible value creation over time in the best interests of shareholders, employees and other stakeholders. Companies should apply this Code of Practice with effect from the 2005 financial year.	2003	2005	N	http://www.aksjonaerforeningen.no/
Peru	In 2002, a committee under the leadership of National Supervisory Commission of Companies and Securities (Comisión Nacional Supervisora de Empresas y Valores - CONASEV) issued a voluntary Code of Good Corporate Governance. It includes general recommendations on board organization and functions, as well as the protection of minority rights. 2005 will be the first year when listed companies are required to "comply or explain" their adherence to the Code in the annual report.	2002	2005	N	http://www.conasev.gob.pe/
Philippines	The Philippine Securities and Exchange Commission (SEC), a principal player in matters of corporate governance, issued Memorandum Circular 2, Series of 2002, otherwise known as the Code of Corporate Governance, under resolution no. 135 dated April 4, 2002. The Code aims to promote corporate governance reforms that will raise investor confidence, develop the capital market and help achieve high sustained growth for the corporate sector and the economy. All corporations affected by this Code shall submit their manual by July 1, 2002 to be effective January 1, 2003.	2002	2003	N	http://www.sec.gov.ph/
Poland	Best Practice Committee is founded in May 2001 for the preparation of corporate governance principles. The Codes of Best practices in Public Companies were implemented into Warsaw Stock Exchange Rules in 2002.	2001	2002	N	http://www.pfcg.org.pl/pfcg/index_eng.htm
Singapore	The Code of Corporate Governance (the "Code") was first promulgated by the Corporate Governance Committee on 21 March 2001. The Government announced its acceptance of the Code on 4 April 2001. The Code came into effect in 2003. For annual general meetings held from 1 January 2003 onwards, listed companies are required under the Listing Rules of the Singapore Exchange to describe in their annual reports their corporate governance practices with specific reference to the principles of the Code, as well as disclose and explain any deviation from any Guidance Notes of the Code.	2001	2003	N	http://www.ccdg.gov.sg/
South Korea	In early 1998, President Kim Dae-Jung met the chairmen of the five largest chaebols and agreed on the five principles: 1) Enhance transparency of the management through accounting reforms, independent directors, and minority shareholders rights; 2) Clarify debt guarantees among chaebol affiliates, ban new ones and require existing ones to be cleared by March 2000; 3) Improve financial structure by lowering debt-to-equity ratios, and divesting unprofitable, non-core businesses; 4) Focus on core competencies; 5) Increase accountability of the shareholder with the *de facto* controlling stake. The Committee on Corporate Governance was founded as a non-government body in March 1999 to develop a code of best practices, a source to guide preparations in establishing proper corporate governance structure. It is the high expectation of the Committee that this Code guide corporations toward improved governance structure and serve as a model of proper corporate governance structure.	1999	1999	N	http://eng.krx.co.kr/abk/abk_d_024.jsp
Spain	First edition of the Code of Good Practice for Boards and Directors was published in June 2004. the Spanish Transparency Act (Ley de Transparencia), Order ECO/3722/2003, as well as the Spanish Securities and Exchange Commission (CNMV) Circular 1/2004 issued in March 2004 on the Annual Corporate Governance Report, as the most relevant milestones to date.	2004	2004	Y	http://www.iconsejeros.com/
Sweden	In January 2003, the Swedish Academy of Directors (StyrelseAkademien) published its Guidelines for Good Board Practice, the first comprehensive code of practice for boards of directors of Swedish companies. In autumn 2004 these comments and proposals will be reviewed and will compose the basis of the code's final form Swedish Code of Corporate Governance, A Proposal by the Code Group. After the proposal had been circulated for comment, the final version of the Code was presented on 16 December 2004. The aim is that the code can then be put into practice beginning in 2005.	2004	2005	N	http://www.bolagsstyrningskollegiet.se/en/0000004.asp
Switzerland	The Swiss Code of Best Practice for Corporate Governance was unanimously approved on 25th March 2002 by the Board of Directors of economies cuisse on the unanimous recommendation of the Panel of Experts. It applies to all annual reports for financial years beginning on 1 January 2002 or later.	2002	2002	N	http://www.economiesuisse.ch/d/webexplorer.cfm?id=351&tlid=1
Taiwan	Taiwan Corporate Governance Best-Practice Principles was issued in 2002 by Taiwan Stock Exchange and GreTai Securities Market. To provide the legal basis for protecting investors, SFC has enacted the "Securities Investors and Futures Traders Protection Law". The Law was passed by the parliament in July 2002 and enacted on January 1, 2003. The TSE and GTSM have amended their listing rules that require all companies seeking IPO after 2002 to have at least two independent directors and one independent supervisor. In addition, the SFC had mandated the definition of qualification of independent directors and independent supervisors on April 4, 2003.	2002	2003	Y	http://www.twse.com.tw/en/

Thailand	The Principles of Good Corporate Governance, published in 2006, is an updated version of the 15 principles announced in March 2002. Before 2006, the Code of Best Practice for Directors of Listed Companies is published by the Exchange of Thailand's (SET) is not a legal requirement but used as guidelines for all board members concerning their behavior while holding such appointments. The new code takes a "comply or explain" approach to corporate governance. Companies are required to disclose the extent of their compliance with the code's principles in their 2007 annual statements (Form 56-1) and annual reports. In practical terms, this means that the first reports will not be seen until March and April 2008.	2006	2008	N	http://www.set.or.th/en/index.html
Turkey	In 2003, the Turkish Capital Market Board introduced a set of Corporate Governance Principles that apply on a comply-or-explain basis. The Principles are based on the concepts of equality, transparency, accountability and responsibility. Each listed company is required to issue a report disclosing the extent to which it complies with these principles and its reasons for non-compliance. CMB Principles are compatible with the OECD Principles on Corporate Governance. They also take into consideration specific problems of Turkish corporate law and practice. In the filed of corporate governance, the CMB issued its corporate governance principles for the first time in July 2003 and updated them in February 2005 in order to reflect the changes made to be OECD Principles in November 2004 (Decision No. 4/100 of the CMB of 7 February 2005).	2003	2004	Y	http://www.cmb.gov.tr/
United Kingdom	UK Combined Code on Corporate Governance issued in July, 2003, and was put into effect November 1st 2003. This Code supersedes and replaces the Combined Code issued by the Hampel Committee on Corporate Governance in June 1998. Higgs Review was published in January, 2003.	2003	2003	N	http://www.frc.org.uk/

Table 1: Country distribution of the sample for testing international target selections of U.S. firms

This table reports the distribution of the sample for testing the international target selections of U.S. acquisitions by target countries. The data are mainly taken from the WorldScope and SDC. Column (1) and (2) present the investor protection index (IP) defined in Appendix 1 and average GDP per capita (GDPPA) from 1989 to 2005 for each target country, respectively. Column (3), (5) and (7) present the number of firm-year observations of the full, target, and non-target sample for each target countries respectively. Column (4), (6) and (8) present the percentage of firm-year observations of the full, target, and non-target sample for each target country respectively. Target sample includes only the firms which receive acquisition bids from U.S. acquirers in year t+1. Each firm in the target sample has at least more than one industry- (defined as two-digits SIC code), year- and country-matched observations in the non-target sample.

Target Country			**Full sample**		**Target sample**		**Non-target sample**	
	IP	**GDPPA**	**N**	**%**	**N**	**%**	**N**	**%**
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**
Argentina	0.43	7184.11	6	0.07	1	0.21	5	0.06
Australia	0.88	21017.71	744	8.83	34	7.07	710	8.94
Austria	0.61	23267.98	10	0.12	3	0.62	7	0.09
Belgium	0.74	21422.09	7	0.08	3	0.62	4	0.05
Brazil	0.39	3606.13	35	0.42	1	0.21	34	0.43
Canada	0.82	22333.20	1280	15.19	77	16.01	1203	15.15
Chile	0.70	4611.67	18	0.21	5	1.04	13	0.16
China	0.76	1363.07	145	1.72	4	0.83	141	1.78
Czech Republic	0.58	5321.85	2	0.02	1	0.21	1	0.01
Denmark	0.73	28270.04	20	0.24	3	0.62	17	0.21
France	0.63	21655.73	428	5.08	33	6.86	395	4.97
Germany	0.63	22497.47	419	4.97	28	5.82	391	4.92
Hong Kong	0.90	24231.16	74	0.88	5	1.04	69	0.87
India	0.62	520.86	173	2.05	14	2.91	159	2.00
Indonesia	0.66	852.32	10	0.12	2	0.42	8	0.10
Ireland-Rep	0.81	14342.66	4	0.05	1	0.21	3	0.04
Israel	0.78	17726.10	51	0.61	15	3.12	36	0.45
Italy	0.64	17622.20	39	0.46	8	1.66	31	0.39
Japan	0.73	36232.54	1101	13.07	22	4.57	1079	13.58
Malaysia	0.89	3624.76	19	0.23	2	0.42	17	0.21
Mexico	0.31	5496.97	20	0.24	7	1.46	13	0.16
Netherlands	0.60	23880.29	49	0.58	7	1.46	42	0.53
New Zealand	0.98	13694.43	7	0.08	2	0.42	5	0.06
Norway	0.71	36266.44	69	0.82	13	2.70	56	0.71
Peru	0.48	2084.99	15	0.18	3	0.62	12	0.15
Philippines	0.44	972.57	18	0.21	3	0.62	15	0.19
Poland	0.48	4253.35	3	0.04	1	0.21	2	0.03
Singapore	0.98	22181.27	89	1.06	11	2.29	78	0.98
South Africa	0.61	3019.97	5	0.06	1	0.21	4	0.05
South Korea	0.65	10600.02	255	3.03	18	3.74	237	2.98
Spain	0.62	12170.24	19	0.23	5	1.04	14	0.18
Sweden	0.67	26537.90	143	1.70	17	3.53	126	1.59
Switzerland	0.63	33219.49	44	0.52	5	1.04	39	0.49
Taiwan	0.63	14174.10	355	4.21	7	1.46	348	4.38
Thailand	0.82	1962.95	27	0.32	3	0.62	24	0.30
United Kingdom	0.96	23311.31	2721	32.30	116	24.12	2605	32.80
Full Sample			**8424**		**481**	**5.7% of full sample**	**7943**	**94.3% of full sample**
Median	**0.65**	**14174.10**						
Std. Dev.	**0.16**	**10917.98**						

Table 2: Statistics of variables in target selection regressions

This table reports the statistics of the variables used in target selection regressions. *EBITDA/TA_Gr* is the growth rate of EBITDA divided by the book value of total assets. *SALES/TA_Gr* is the growth rate of sales divided by the book value of total assets. *Firm size* is measured as the log value of total assets. *Leverage* is measured as the total debt (long term + short term debt) divided by the book value of total assets. *MB* is market to book value, measured as the ratio of the market value of the common equity of the firm to its book value of equity. The observations with negative *MB* are replaced by zero. *Liquidity* is the ratio of the current assets to current liabilities. *Crisis1* is an indicator, which is equal to one if the firm-year observation has any of the following country-year combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995. Panel A, B and C report the statistics of the full, target and non-target firm sample respectively.

Panel A: Full Sample					
Variable	Mean	Median	Std. Dev.	Min	Max
EBITDA/TA_Gr	-0.104	-0.063	1.588	-11.408	12.617
SALES/TA_Gr	0.075	0.007	0.467	-0.851	5.858
log (Totasset)	11.610	11.738	2.414	-0.145	17.983
Leverge	0.225	0.198	0.185	0.000	3.507
MB	1.890	0.934	6.401	0.000	571.301
Liquidity	1.983	1.470	2.016	0.156	61.769
Crisis1	0.018	0	0.134	0	1
Panel B: Target Sample					
Variable	Mean	Median	Std. Dev.	Min	Max
EBITDA/TA_Gr	-0.061	-0.047	1.157	-7.291	5.834
SALES/TA_Gr	0.087	0.004	0.486	-0.851	3.816
log (Totasset)	5.457	5.271	1.932	-0.145	11.502
Leverge	0.244	0.171	0.302	0.000	3.507
MB	4.261	1.720	25.136	0.000	571.301
Liquidity	2.428	1.493	3.863	0.156	61.769
Crisis1	0.034	0	0.182	0	1
Panel C: Non-target Sample					
Variable	Mean	Median	Std. Dev.	Min	Max
EBITDA/TA_Gr	-0.108	-0.065	1.620	-11.408	12.617
SALES/TA_Gr	0.074	0.007	0.465	-0.849	5.858
log (Totasset)	11.971	11.883	1.897	7.182	17.983
Leverge	0.224	0.199	0.175	0.000	0.983
MB	1.751	0.878	2.461	0.000	14.310
Liquidity	1.957	1.470	1.848	0.170	20.410
Crisis1	0.017	0	0.131	0	1

Table 3: Target selections of U.S. acquisitions in different legal environments

This table reports the results of the Probit regressions modeling the likelihood of being a target of a U.S. acquirer. The dependent variable is a binary variable indicating that the firm becomes a target in year t+1; zero otherwise. *EBITDA/TA_Gr* is the growth rate of EBITDA divided by the book value of total assets. *SALES/TA_Gr* is the growth rate of sales divided by the book value of total assets. *Firm size* is measured as the log value of total assets. *Leverage* is measured as the total debt (long term + short term debt) divided by the book value of total assets. *MB* is market to book value, measured as the ratio of the market value of the common equity of the firm to its book value of equity. The observations with negative *MB* are replaced by zero. *Liquidity* is the ratio of the current assets to current liabilities. *Crisis1* is an indicator, which is equal to one if the firm-year observation has any of the following country-year combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995. *GDPPA* is GDP per capita, and denominated in 2000 USD. *Inword FDI/GDP* is net inflows of foreign direct investments as the percent of GDP. *Restructure Reg* is an index measuring the regulatory barriers of restructuring, and it includes three components: labor market regulations, regulations of closing a business, and enforceability of contracts. The details of constructing *Restructure Reg* can be found in Appendix 1. *Anti Trust Reg* is a merger related anti-trust index, which is time invariant, and taken from Hylton and Deng (2007). All regressions are estimated with year-varying industry (defined as one-digit SIC) fixed effects. Regressions in Column (1) to (4) are estimated by clustering at the country level. Regressions in Column (5) to (8) are estimated with country fixed effects. Robust standard errors are reported in parentheses. *, ** and *** indicates significant at 10%, 5% and 1% respectively.

	Dependent Variable: Target=1							
	IP<Med	**IP≥Med**	**IP<Med**	**IP≥Med**	**IP<Med**	**IP≥Med**	**IP<Med**	**IP≥Med**
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**
EBITDA/TA_Gr	0.059**	-0.001			0.060**	-0.000		
	(0.030)	(0.019)			(0.025)	(0.012)		
SALES/TA_Gr			0.275*	-0.042			0.272**	-0.023
			(0.149)	(0.077)			(0.107)	(0.049)
Firm Size	-0.018	-0.002	-0.011	-0.011	-0.027	0.005	-0.016	-0.003
	(0.028)	(0.027)	(0.034)	(0.030)	(0.024)	(0.014)	(0.024)	(0.014)
Leverage	0.574***	-0.123	0.678***	-0.080	0.575*	-0.182	0.685**	-0.132
	(0.129)	(0.159)	(0.143)	(0.157)	(0.315)	(0.170)	(0.305)	(0.172)
MB	0.009***	-0.002***	0.007***	-0.002***	0.010***	-0.002	0.008**	-0.002**
	(0.002)	(0.000)	(0.002)	(0.000)	(0.003)	(0.001)	(0.003)	(0.001)
Liquidity	0.051***	0.013**	0.047***	0.027***	0.052**	0.012***	0.049**	0.022***
	(0.012)	(0.005)	(0.012)	(0.007)	(0.026)	(0.005)	(0.024)	(0.008)
Crisis1	0.296	-0.047	0.253	-0.382	0.381	0.595	0.343	2.207
	(0.243)	(0.396)	(0.242)	(0.375)	(0.344)	(0.680)	(0.339)	(2.689)
GDPPA	0.018	-0.004	0.022	-0.015	-0.355**	0.070	-0.340**	0.074
	(0.015)	(0.017)	(0.015)	(0.019)	(0.168)	(0.073)	(0.170)	(0.077)
Inword FDI/GDP	0.026	0.030**	0.026	0.033**	-0.053	-0.005	-0.044	-0.007
	(0.025)	(0.012)	(0.028)	(0.015)	(0.051)	(0.015)	(0.048)	(0.016)
Restructure Reg	-0.909	-1.331**	-0.936*	-1.007*				
	(0.590)	(0.586)	(0.558)	(0.610)				
Anti Trust Reg	-0.013	0.079	-0.014	0.085				
	(0.049)	(0.063)	(0.046)	(0.068)				
Constant	0.853	1.315**	0.787	0.923	11.219**	-0.467	0.926	-2.232
	(0.576)	(0.658)	(0.556)	(0.640)	(5.710)	(1.104)	(1.019)	(2.987)
*Year*Industry FE*	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	N	N	N	N	Y	Y	Y	Y
Cluster by countries	Y	Y	Y	Y	N	N	N	N
Observations	1531	5817	1610	5669	1529	5976	1608	5831
Pseudo R-squared	0.10	0.08	0.13	0.09	0.15	0.10	0.17	0.11

Table 4: Country distribution of the sample for testing the impact of corporate governance reforms on the types of firms being targeted

This table reports the country distribution of the sample for testing the impact of corporate governance reforms on the types of firms being targets. Column (1) & (2) present the sample distribution of the full sample by target countries. Column (3) & (4) and (5) & (6) present the sample distribution before and after the corporate governance reform for each target country respectively. Column (7) & (8) and (9) & (10) present the sample distribution by target countries before and after the passage of the SOX (year 2003) respectively.

Target Country	**Full**		**Pre-TCGR**		**Post-TCGR**		**Pre-SOX**		**Post-SOX**	
	N	**%**	**N**	**%**	**N**	**%**	**N**	**%**	**N**	**%**
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**	**(9)**	**(10)**
Argentina	5	0.52	5	0.71	0	0.00	5	0.77	0	0.00
Australia	62	6.4	36	5.11	26	0.10	36	5.51	26	8.23
Austria	5	0.52	3	0.43	2	0.01	3	0.46	2	0.63
Belgium	7	0.72	5	0.71	2	0.01	5	0.77	2	0.63
Brazil	8	0.83	6	0.85	2	0.01	6	0.92	2	0.63
Canada	234	24.15	234	33.19	0	0.00	167	25.57	67	21.2
Chile	7	0.72	6	0.85	1	0.00	7	1.07	0	0.00
China	14	1.44	1	0.14	13	0.05	1	0.15	13	4.11
Czech Republic	1	0.1	1	0.14	0	0.00	1	0.15	0	0.00
Denmark	5	0.52	5	0.71	0	0.00	5	0.77	0	0.00
Finland	3	0.31	2	0.28	1	0.00	2	0.31	1	0.32
France	44	4.54	25	3.55	19	0.07	25	3.83	19	6.01
Germany	36	3.72	18	2.55	18	0.07	22	3.37	14	4.43
Greece	4	0.41	4	0.57	0	0.00	1	0.15	3	0.95
Hong Kong	16	1.65	10	1.42	6	0.02	9	1.38	7	2.22
Hungary	1	0.1	1	0.14	0	0.00		0	1	0.32
India	31	3.2	11	1.56	20	0.08	11	1.68	20	6.33
Indonesia	4	0.41	4	0.57	0	0.00	4	0.61	0	0.00
Ireland-Rep	8	0.83	7	0.99	1	0.00	6	0.92	2	0.63
Israel	34	3.51	12	1.7	22	0.08	21	3.22	13	4.11
Italy	12	1.24	10	1.42	2	0.01	10	1.53	2	0.63
Japan	34	3.51	25	3.55	9	0.03	30	4.59	4	1.27
Malaysia	7	0.72	3	0.43	4	0.02	4	0.61	3	0.95
Mexico	14	1.44	14	1.99	0	0.00	13	1.99	1	0.32
Netherlands	13	1.34	7	0.99	6	0.02	5	0.77	8	2.53
New Zealand	3	0.31	3	0.43	0	0.00	1	0.15	2	0.63
Norway	23	2.37	20	2.84	3	0.01	19	2.91	4	1.27
Peru	4	0.41	4	0.57	0	0.00	3	0.46	1	0.32
Philippines	4	0.41	4	0.57	0	0.00	4	0.61	0	0.00
Poland	4	0.41	3	0.43	1	0.00	3	0.46	1	0.32
Singapore	14	1.44	10	1.42	4	0.02	10	1.53	4	1.27
South Africa	2	0.21	2	0.28	0	0.00	2	0.31	0	0.00
South Korea	31	3.2	10	1.42	21	0.08	21	3.22	10	3.16
Spain	7	0.72	6	0.85	1	0.00	6	0.92	1	0.32
Sweden	31	3.2	27	3.83	4	0.02	23	3.52	8	2.53
Switzerland	11	1.14	2	0.28	9	0.03	3	0.46	8	2.53
Taiwan	20	2.06	6	0.85	14	0.05	6	0.92	14	4.43
Thailand	4	0.41	4	0.57	0	0.00	4	0.61	0	0.00
Turkey	2	0.21	1	0.14	1	0.00	1	0.15	1	0.32
United Kingdom	200	20.64	148	20.99	52	0.20	148	22.66	52	16.46
Total Sample	969		705		264		653		316	

Table 5: Impact of CGRs in Target Countries on the Types of Firms being Targeted

This table reports the results of the impact of the corporate governance reforms of target countries on target selections of U.S. acquirers. The dependent variable is *EBITDA/TA_Gr* in Column (1) to (3), the numerical cumulative density functions (CDFs) of *EBITDA/TA_Gr* in Column (4), *SALES/TA_Gr* in Column (5) to (7), and the CDF of *SALES/TA_Gr*. *EBITDA/TA_Gr* and *SALES/TA_Gr* are the growth rate of *EBITDA/TA* and sales divided by total assets of target firms at the end of the fiscal year proceeding to the acquisition announcement years respectively. *TCGR* is an indicator that equals one if a major corporate governance reform is undertaken in the target country when the acquisition bid is announced. *Num of Deals* is the number of deals taken place in each country during each year in the sample. *Horizontal* is an indicator, which is equal to one if the acquiring and target firm are sharing the same first two-digits of SIC codes. *Cross List* is an indicator, which equals one, when the target firm is cross-listed in other country's stock exchange. *Crisis2* is an indicator, which is equal to one if the acquisition bid is announced in the following country-year specific combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995. *GDPPA* is GDP per Capita of target countries. *Have_Crisis* is an indicator, which is equal to one if a financial crisis took place before the corporate governance reform (see in Appendix 2) in the target country. Countries having crises are identified as Thailand, South Korea, Indonesia, Argentina, Brazil, and Mexico. *Have_Scandal* is an indicator, which is equal to one if a big business scandal took place before the corporate governance reforms (see in Appendix 2) in the target country. Countries having scandals are identified as China, France, Ireland-Rep, Japan, and Philippines. All regressions are estimated with year-varying industry (defined as one-digit SIC) and country fixed effects. All regressions are estimated by clustering at the acquirer level. Robust standard errors are reported in parentheses. *, **, and *** indicate significant at 10%, 5% and 1% respectively.

Dependent Variable	**EBITDA/TA_Gr**			**CDF(EBITDA/TA_Gr)**	**SALES/TA_Gr**			**CDF(SALES/TA_Gr)**
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**
TCGR	-0.463*	-0.534**	-0.428**	-0.100*	-0.334*	-0.363*	-0.390**	-0.113*
	(0.245)	(0.244)	(0.214)	(0.058)	(0.194)	(0.190)	(0.193)	(0.060)
Num of Deals		0.005	0.008	0.001		0.002	0.002	-0.006*
		(0.013)	(0.013)	(0.003)		(0.007)	(0.007)	(0.003)
Horizontal		-0.030	-0.047	0.017		0.040	0.039	0.039
		(0.090)	(0.088)	(0.025)		(0.060)	(0.059)	(0.024)
Cross List		-0.397**	-0.394**	-0.120***		-0.188**	-0.193**	-0.081*
		(0.157)	(0.157)	(0.039)		(0.095)	(0.095)	(0.045)
GDPPA		-0.000**	-0.000**	-0.000		-0.000*	-0.000*	-0.000**
		(0.000)	(0.000)	(0.000)		(0.000)	(0.000)	(0.000)
Crisis2		0.245	0.373	-0.008		0.119	0.220	0.046
		(0.478)	(0.517)	(0.116)		(0.138)	(0.152)	(0.118)
*Have_Crisis*TCGR*			0.148	-0.005			0.308*	0.037
			(0.412)	(0.124)			(0.177)	(0.126)
*Have_Scandal*TCGR*			-1.278**	0.074			-0.056	0.126
			(0.531)	(0.121)			(0.253)	(0.085)
Constant	-0.491	5.373**	5.455**	1.892***	-0.051	0.581	0.659*	1.439***
	(0.302)	(2.498)	(2.135)	(0.613)	(0.098)	(0.358)	(0.352)	(0.360)
*Year*Industry FE*	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y	Y	Y
Clustered by acquirers	Y	Y	Y	Y	Y	Y	Y	Y
Observations	841	838	838	727	903	900	900	764
R-squared	0.23	0.25	0.26	0.28	0.15	0.16	0.16	0.29

Table 6: Impacts of both CGRs in Target Countries and SOX on the Types of Firms being Targeted

This table reports the results of the impact of the corporate governance reforms of target countries on target selections of U.S. acquirers. The dependent variable is *EBITDA/TA_Gr* in Column (1) to (3), the numerical cumulative density functions (CDFs) of *EBITDA/TA_Gr* in Column (4), *SALES/TA_Gr* in Column (5) to (7), and the CDF of *SALES/TA_Gr*. *EBITDA/TA_Gr* and *SALES/TA_Gr* are the growth rate of *EBITDA/TA* and sales divided by total assets of target firms at the end of the fiscal year proceeding to the acquisition announcement years respectively. *TCGR* is an indicator that equals one if a major corporate governance reform is undertaken in the target country when the acquisition bid is announced. *SOXEff* is constructed as: *(4-BoardDep) * After2002*. It takes the value of 0 to 4, and higher value indicates stronger effects of SOX on the U.S. acquiring firm. *After2002* is an indicator, which is equal to one if the acquisition bid is announced after 2002. *BoardDep* measures the level of board dependence of U.S. firms. It takes the value of 0 to 4, and the details on this variable can be found in Appendix 1. *Num of Deals* is the number of deals taken place in each country during each year in the sample. *Horizontal* is an indicator, which is equal to one if the acquiring and target firm are sharing the same first two-digits of SIC codes. *Cross List* is an indicator, which equals one, when the target firm is cross-listed in other country's stock exchange. *Crisis2* is an indicator, which is equal to one if the acquisition bid is announced in the following country-year specific combinations: Thailand, 1997-99; South Korea, 1997-99; Indonesia, 1997-99; Argentina, 2001-02; Brazil, 1999; Mexico, 1994-1995. *GDPPA* is GDP per Capita of target countries. *Have_Crisis* is an indicator, which is equal to one if a financial crisis took place before the corporate governance reform (see in Appendix 2) in the target country. Countries having crises are identified as Thailand, South Korea, Indonesia, Argentina, Brazil, and Mexico. *Have_Scandal* is an indicator, which is equal to one if a big business scandal took place before the corporate governance reforms (see in Appendix 2) in the target country. Countries having scandals are identified as China, France, Ireland-Rep, Japan, and Philippines. *Acquirer Tobin's Q* is measured as a ratio. The numerator is the book value of total assets (Compustat #6) subtracting the book value of equity (Compustat #60), and then adding the market value of equity (Compustat #24*#25). The denominator is the book value of total assets (Compustat #6). It is measured as the natural logarithm value of the book value of assets of the U.S. acquiring firm in one year before the announcement of the acquisition bid. *Acquirer Firm Size* is measured as the book value of assets is denominated in 2000 USD (Compustat #6). *Acquirer EIndex* is measured as entrenchment index in Bebchuk et al. (2004), and takes the value of 0 to 6. All variables are measured in one year before the announcement of the acquisition bid. All regressions are estimated with year-varying industry (defined as one-digit SIC) and country fixed effects. All regressions are estimated by clustering at the acquirer level. Robust standard errors are reported in parentheses. *, **, and *** indicate significant at 10%, 5% and 1% respectively.

Dependent Variable	**EBITDA/TA_Gr**			**CDF(EBITDA/TA_Gr)**	**SALES/TA_Gr**			**CDF(SALES/TA_Gr)**
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**
TCGR	-0.642**	-0.470**	-0.564**	-0.146*	-0.204*	-0.235**	-0.306**	-0.155**
	(0.282)	(0.227)	(0.270)	(0.077)	(0.112)	(0.113)	(0.135)	(0.076)
SOXEff	0.219	0.394**	0.424**	0.111**	0.200**	0.211**	0.234**	0.130**
	(0.194)	(0.198)	(0.209)	(0.055)	(0.095)	(0.103)	(0.109)	(0.065)
Num of Deals		0.011	0.006	-0.005		-0.000	-0.020	-0.001
		(0.013)	(0.016)	(0.005)		(0.007)	(0.015)	(0.005)
Horizontal		-0.039	-0.027	0.007		0.051	0.138	0.045
		(0.092)	(0.113)	(0.042)		(0.060)	(0.093)	(0.035)
Cross List		-0.495***	-0.620***	-0.141***		-0.235*	-0.266**	-0.099*
		(0.171)	(0.197)	(0.052)		(0.132)	(0.130)	(0.056)
GDPPA		-0.000***	-0.000**	-0.000**		-0.000*	0.000	-0.000
		(0.000)	(0.000)	(0.000)		(0.000)	(0.000)	(0.000)
Crisis2		0.156	0.147	0.165		0.300	0.195	0.116
		(0.435)	(0.699)	(0.287)		(0.188)	(0.261)	(0.135)
*Have_Crisis*TCGR*		0.860*	1.019	0.236		0.269	0.194	0.029
		(0.451)	(0.749)	(0.303)		(0.247)	(0.250)	(0.179)
*Have_Scandal*TCGR*		-1.798***	-3.124***	-0.030		0.209	0.317	-0.032
		(0.640)	(1.174)	(0.182)		(0.130)	(0.243)	(0.202)
Acquirer Tobin's Q			-0.019	-0.019**			-0.021	-0.018**
			(0.027)	(0.008)			(0.020)	(0.008)
Acquirer Firm Size			0.033	0.015			0.025	-0.005
			(0.036)	(0.011)			(0.031)	(0.011)
Acquirer EIndex			0.030	-0.001			0.053	0.008
			(0.050)	(0.016)			(0.041)	(0.013)
Constant	-5.719***	-5.549***	-6.257***	2.929***	-0.248	-0.232	0.178	0.654**
	(0.217)	(0.528)	(0.844)	(0.845)	(0.605)	(0.650)	(0.744)	(0.316)
*Year*Industry FE*	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y	Y	Y
Cluster by acquirers	Y	Y	Y	Y	Y	Y	Y	Y
Observations	515	515	407	377	544	544	417	388
R-squared	0.36	0.43	0.46	0.41	0.20	0.22	0.33	0.45