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Institutional theory and isomorphism: limitations in multinational companies

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ABSTRACT

Today's popular thinking is that every organization is unique and, in their processes and organizational behavior, specific. However, we witness how organizations, particularly those operating within the same industry, are becoming similar and the same as each other. The explanation for this occurrence is the institutional theory of organization that was created primarily as a critique to contingency theory that supports idiosyncratic of organizations. Institutional theory of organization explains how organizations operating within the same industry or organizational fields tend to adapt to the same structures, behaviors and activities. In the foreground of the institutional theory of organization is the institutional isomorphism that explains the similarity of the companies in an organizational field. In this paper, the author will present the current knowledge regarding this approach in management and will emphasize the lacks of this theory when it is applied with multinational companies and its subsidiaries; the multinational companies are interesting to researchers because of the complexity of operations and the complexity of the external environment and intra-organizational environment.

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1. INSTITUTIONAL THEORY OF ORGANIZATION: ASSUMPTIONS, IDEAS AND MOST IMPORTANT CONCEPTS

The main objective of this paper is to gather some of the relevant literature and crucial concepts regarding institutional theory and institutional isomorphism. The author will use the collected knowledge for further research of institutional theory and the impact it has on multinational companies in the Republic of Croatia.

Popular thinking is that every organization is unique and, in their processes and organizational behavior, specific. However, we witness how organizations, particularly those operating within the same

same industry, are becoming similar to each other. The explanation for this occurrence is the institutional theory of organization that was created primarily as a critique to contingency theory that supports idiosyncratic of organizations. Institutional theory assumes that the organizational action is limited by the normative regulations (Donaldson, L. 1995), and the room for maneuver of individuals has been narrowed due to the presence of institutions that impose the modus operandi (Scott, W. R. 2005). As the most powerful argument of institutional theory is that the behavior and functioning of the organization in the same industry is imposed by the institution, not the market itself (Meyer, Rowan 1997). For better understanding of this approach it is necessary to define what the institution represents. Barley and Tolbert define the institution as a set of common rules and relationships that define the categories of social actors: their related activities and relationships. Institutional theory of organization is based on the fact that organizations operating within the same industry or organizational field tend to adapt the same structures, behaviors and activities (Shonk and Bravo 2010). Authors of this idea and concept are DiMaggio and Powell. In their research they focused on finding the answer to a question why similar organizations operate by nearly same principles, how organizations respond to the pressures of the environment and, finally, what impact institutions have on the development of organizational strategy and structure (DiMaggio and Powell, 1983). Organizational field (Kostova, Kendall, Roth, 2008) is defined as a socially acceptable pattern of behavior and organizational structure. DiMaggio and Powell define the organizational field as "those organizations that, in general, participate in the creation of institutional area: key suppliers, resources, consumers, regulatory agencies and other organizations that produce similar services or products." (DiMaggio and Powell, 1983).

The organization is required to prove its legitimacy in order to gain right to use and to deploy resources. Legitimacy is perceived as desirable action of one entity within the framework of social values, norms, beliefs and definitions (Scott, 2001). Since the patterns of socially acceptable behavior is defined by the environment (Tipurić 2004 from Meyer and Rowan 1977) managers make decisions that are socially acceptable (not necessarily rational) and are strongly influenced by social pressures and are actually an imitation of previous decisions, in most cases, market leaders (Robbins, Barnwell, 2006).

The process of institutionalization results in three types of institutions (Scott, 2011):

• *regulatory institutions* rely on rules that have an obligatory dimension; they consist of laws and policies that create an obligation to a certain behavior, and failure to comply with the same is being sanctioned

• *normative institutions* are based on the standards of behavior, social values and professional standards

• *cognitive institutions* define social reality through common values and concepts; most often socially acceptable behavior is "taken for granted" and as such, the only right one.

The institutions propose guidelines for an organizational behavior that is considered proper and desirable (Barley and Tolbert, 1997), and which will ultimately be legitimate: therefore, will eliminate the potentially undesirable behavior. The environment in which the power of the institution is emphasized give impetus to those organizations that operate in accordance with the set of norms and standards, and on the other hand, it is easier to sanction those who do not adapt their behavior to isomorphic. Factors such as the conditions of insecurity, lack of prestige and / or reputation condition certain organizations to identify themselves with what is considered traditional and socially acceptable (Phelps and Dickson, 2009).

Although the process of institutionalization is placed at the level of economic activity, its impact depends on the activity of organization. Logically, some activities such as the banking industry are more exposed to institutional pressures than for example in the music industry. The degree of exposure to the process of institutionalization depends on two factors (Janićijević 2014):

1. degree to which the output of organizations in the same organizational field can be measured, evaluated and standardized

2. degree to which organizations can control the flow of resources in the same organizational field

The higher degree of output standardization, the less will the organization be exposed to the pressures of institutionalization and vice versa. Consequently, the less possibility of influencing social resources and their use, will increase the exposure of institutional isomorphism and conformity with the aim of achieving legitimacy.

Institutional theory is characterized by the conditions in the environment in which organization operates and the impact of the environment on the organization itself. Limitations that are imposed affect contextual shaping of desirable behavior and it is different depending on organizational field. When composing its behavior isomorphic within organizational fields, organizations achieve legitimacy, enhance and ensure its chance of survival. Doing business in an environment characterized by uncertainty proved to be a fertile ground for isomorphism among organizations. In time when organizations are faced with a strategic decision-making supported by incomplete information regarding the changes in the environment, often look to competitors trying to find answers to their questions and closely monitor behaviors and reactions of competitors. Previously mentioned limitation of human activity can be seen just in terms of uncertainty, when the organization are set to make strategic decisions based on the decisions of competitors, but they are not always in line with the initially set targets (DiMaggio and Powell, 1983; Galaskiewicz and Wasserman, 1989). Often this behavior under uncertainty leads to a vicious circle where "the blind leads the blind" (O'Brien and Slack, 2004). When there is a gap between institutional expectations and efficiency, the company decouples formal structure from current business practices and conformity tends to have ceremonial character (Tipurić, 2014 from Meyer and Rowan, 1997).

2. INSTITUTIONAL ISOMORPHISM

The main focus of institutional organization theory is on the institutional isomorphism which explains the similarity among organizations in an organizational field (Tipurić, 2014) and how organizations become similar to their competitors (DiMaggio and Powell, 1983). Isomorphism explains the degree of conformity of organization to norms and practices that have been established in a given organizational field (Johnston, 2013). This process leads to homogeneity of organizations and it is called isomorphism. In the background of institutional isomorphism lays the fact that organizations tend to find indications in the environment for the formation of appropriate actions and practices for business. Theorists support this concept indicating that over time organization operating within the same field adopt similar organizational structures and patterns that will ultimately appear isomorphic (Deephouse and Carter, 2005; Washington and Patterson, 2001).

There can be identified 3 types of isomorphism (DiMaggio, Powell 1983):

• coercive isomorphism

• normative isomorphism

• mimetic isomorphism

Coercive isomorphism
Coercive isomorphism results in institutional pressures by the organization forcing those organizations that depend on them (DiMaggio and Powell 1983). In the background of coercive isomorphism are formal and informal pressures by the state legislatures, regulatory agencies but also the cultural expectations that society has from organizations (Tipurić, 2014). Coercive isomorphism is emphasized in situations where leading organizations affect other followers in such way that imposes desired behavior in order to achieve legitimacy and additional benefits (Edwards et al. 2009), primarily related to increasing the availability of social resources and avoiding sanctions (Johnston, 2013).

Mimetic isomorphism
Organizations tend to form their practices and policies mimicking those organizations which are considered to be successful and legitimate. This phenomenon is called mimetic isomorphism. Mimetic isomorphism is a consequence of the uncertainty in the environment and unclear organizational

objectives. Benefits of mimetic isomorphism are numerous: low cost of human capital, decisions arising from mimetic isomorphism are based on finding a viable solution with minimal cost since the problems occur in unclear and uncertain environment (DiMaggio and Powell, 1983). The uncertain environment can be seen as a force that encourages organizations to imitate each other within the same organizational field. Furthermore, mimetic isomorphism can serve as a practical solution for those organizations that are not able to solve their problems by themselves (Lee, Penings, 2002) Organizations apply almost identical structures of those successful ones, believing that will achieve the same level of success, but at the same time do not take into account the context in which these structures are applied (Janićijević, 2014). For those organizations whose core business is closely related (operating in the same organizational field) is more likely that over time will appear isomorphic (Edwards et al, 2009).

Normative isomorphism

Normative isomorphism is the result of professionalization within a specific organizational field (Tipurić, 2014; Johnston, 2013). Professionalization is defined as the collective effort of members in the same profession in order to establish rules and restrictions for governing business performance in that profession by setting the cognitive basis of their autonomy (Ashworth et al, 2007). As a consequence, individuals that are connected through the same profession will develop skills and homogeneous characteristics over time and gain legitimacy (Johnston, 2013). The normative pressures on an organization can potentially have a significant impact; experiences and beliefs of individuals within the organization can lead to a fact whether the organization will be considered legitimate or not. Qualification and individual characteristics of individuals are helping the organization to achieve conformity within the organizational field (Johnston, 2013); For example, the accounting service will not be perceived as legitimate if its employees are not qualified and certified accountants.

3. CHALLENGES AND LIMITATIONS OF INSTITUTIONAL THEORY AND INSTITUTIONAL ISOMORPHISM IN MULTINATIONAL COMPANIES

The research work of scientists in the field of institutional theory and multinational companies offers a theoretical background for a better understanding of this theory. Multinational companies are in their characteristics and practices considerably different from domestic companies mostly due to a combination of multidimensionality and heterogeneity (Doz and Prahalad, 1991).

Organizational field

Institutional theory defines the organizational field as an environment in which the organization operates. Field defines socially acceptable structures and practices. Kostova, Roth and Dacin suggest that organizational field is nonexistent in the context of multinational companies: multinational companies create their own "metaorganizational field".

Institutional isomorphism

Kostova, Roth and Dacin state how "classical" institutional isomorphism in multinational companies cannot be identified. They propose the concept of limited institutional isomorphism because it occurs within the organizational field (which in the business of these organizations is again specific) and a definition of the organizational field in this case does not exist. Furthermore, considering that multinational companies operate in a host country and are introducing something new are less likely to adopt the established domestic business practices and routines (Kostova, Roth, Dacin 2008). These organizations are seen as an unique class since they are "foreigners", therefore, taking into account this fact, local presence of isomorphism on them will be less pronounced. Furthermore, given that the boundaries of an organizational field are shifted host country faces difficulties in the systematization to which organizational field multinational company or its subsidiaries belong to. Also, the scarcity of resources in the local environment is superseded by alternative sources. In "institutional freedom" multinationals will enjoy as long as they comply to the law and legislation of host country.

Legitimacy

Achieving and maintaining the legitimacy of multinational companies is a critical factor because of the complexity of the environment in which they operate and intra-organizational processes. Kostova and others criticize the traditional thinking of achieving legitimacy especially because of the specific context in which the multinational companies operate. Customizing to the myriad of regulatory, cognitive and normative expectations deriving from conflicting sources that create pressures and complicate the process of achieving legitimacy (Kostova, Roth, Dacin, 2008). The authors propose an alternative approach; negotiating access with key groups. Legitimacy is therefore more a social construct rather than a function of isomorphism. Multinational companies often use their corporate reputation (especially if it is stable and strong) as a source of achieving legitimacy in the host country.

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The Utilization of Social Media Marketing in Destination Management Organizations

Birgit Bosio*, Stefanie Haselwanter and Michael Ceipek

ABSTRACT

The emerging use of social media fundamentally changes the communication and interaction of societies and organizations. It revolutionizes the way organizations market their products and interact with their customers. Social media acts as an agent of change within the marketing and communication of organizations. In particular, the tourism sector is affected by these disruptive changes. Social media influences and changes the interaction between touristic supply and demand sides fundamentally. These upcoming opportunities and challenges are especially relevant for destination management organizations (DMOs), which try to coordinate and market the intangible and immaterial tourism product of a destination. Social media marketing transforms the classical marketing and communication of these destination management organizations. Nevertheless, destination management organizations are still in an experimental stage of utilizing social media as a marketing tool, as they slowly start to realize the potential benefits of social media as an agent of change. This study investigates how DMOs in alpine regions implement social media marketing in their classical marketing strategies through a quantitative survey. Furthermore, the paper outlines which upcoming challenges and opportunities DMOs face by conducting qualitative interviews with social media managers in the destinations. Finally, implications and recommendations for DMOs are presented to cope with the emerging use of social media as a marketing tool.

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1. INTRODUCTION

The emerging use of social media has fundamentally altered the communication and interaction of humans (Shu-Chuan & Yoojung 2011, Ngai, Tao & Moon, 2015) and how humans disseminate information (Buhalis & Law, 2008; Xiang & Gretzel, 2010). Social media applications enable customers to present their thoughts, opinions and ideas through user-generated content in social networks and make them visible to a big crowd. Therefore, social media is more than a technological development; it is a social innovation (Ngai, Tao & Moon, 2015; Amersdorfer, Bauhuber & Öllrich,

2012) and it is claimed to be the “modus operandi of the 21st century” (Lange-Faria & Elliot, 2012, p. 193). Especially in an entrepreneurial and organizational context, the use of social media revolutionizes the way organizations market their products/services and communicate with their customers (Felix, Rauschnabel & Hinsch, 2017; Ngai, Tao & Moon, 2015). Social media therefore acts as an agent of change within the marketing and communication of organizations.

The tourism sector is particularly affected by these disruptive digital changes (Landvogt, 2017; Xiang & Gretzel, 2010), especially regarding the interaction between supply and demand sides (Buhalis & Law, 2008; Arsal, Backman & Baldwin, 2008; Law, Leung & Buhalis, 2009). Social media not only fundamentally influences and changes the customer journey, but also how tourism providers market and distribute their product portfolio (Buhalis & Law, 2008; Arsal et al., 2008). In the context of tourism destination marketing, social media has led to disruptive changes in the past decade (Xiang & Gretzel, 2010; Buhalis & Law, 2008). Social media marketing offers tourism destinations numerous opportunities to foster the relationship between the supply and demand sides (Tussyadiah & Zach, 2013). Nevertheless, Munar (2012) postulates that even though there is strong interest in the effects of digitization in tourism, only little empirical evidence exists regarding the strategic extent and effects of social media marketing at the destination level.

Destination management organizations (DMO) are still in an experimental stage of utilizing social media applications as a marketing tool (Usalki, Koc & Sönmez, 2017). They slowly start to realize the potential benefits of social media as an agent of change. Hays, Page & Buhalis (2013, p. 213) therefore claim “[...] a clear understanding of why and how social media function is vital to tourism destination marketing”.

“Social media is no longer a trend for marketers: It is a reality” (Chung & Austria, 2010, p. 582). The introduction of Web 2.0 alters the communication and interaction behavior of organizations (Ngai, Tao & Moon, 2015; MacKay, Barbe, Van Winkle & Halpenny, 2017). As an integral part of Web 2.0, social media can be defined as “[...] a group of internet-based applications that build on the ideological and technological foundations of Web 2.0, and allow the creation and exchange of user generated content” (Kaplan & Haenlein, 2010, p.61). Social media is more than just social networking and content sharing sites; it also includes blogs, business networking sites, collaborative sites, commerce communities, podcasts, educational material sharing, as well as open source software (Anderson, 2007). These channels influence the customer’s behavior in terms of awareness, information seeking, attitudes, decision-making, purchasing and post-purchase communication and evaluation (Mangold & Faulds, 2009). Social media supports social structures and interactions online (Hinterholzer & Joos, 2013) by posting and sharing content on social networks like Facebook, YouTube, Instagram or Twitter (Lange-Faria & Elliot, 2012; Sigala, Gretzel & Christou, 2012). Social media applications enable users to spread their own thoughts, opinions and ideas through user-generated content in social networks and make them visible to a global crowd (Hays et al., 2013). Before the emergent use of Web 2.0, organizations were able to manage and control the content available to their customers and build a certain brand to align with how they want to be perceived by their customers (MacKay et al., 2017). “With this rise in social media, it appears that corporate communication has been democratized. The power has been taken from those in marketing and public relations by the individuals and communities that create, share, and consume blogs, tweets, Facebook entries, movies, pictures, and so forth.” (Kietzmann et al., 2011, p. 242). The term user-generated content (UGC) thus refers to the way users share their ideas in the form of blogposts, videos or photos and interact with each other (Lange-Faria & Elliot, 2012) and refers to “a mixture of fact and opinion, impression and sentiment, founded and unfounded tidbits, experiences, and even rumor” (Blackshaw & Nazzaro, 2006, p. 4)., From a marketing perspective, it is helpful to take a more consumer-centered approach. Several researches propose to use the term consumer generated content (CGC) instead, as this term puts emphasis on the commercial use of social media as a marketing tool, which refers to online information created, initiated, spread and used by consumers with the intention to give recommendations and opinions on products or organizations (Lange-Faria & Elliot, 2012).

Within the 21st century, social media became an integral and indispensable part of the marketing and communication of organizations (Felix et al., 2017). Already in 2004 Holloway proclaimed that “information and communication technology, as it is now known, has come to play a key role in all elements of the marketing mix, and the new term recognizes the importance of communication in the interface between a business and its customers. Electronic, or ‘online’ communications have become affordable and practicable for even the smallest SMEs, and no sector of the travel industry is unaffected by this revolution.” (Holloway, 2004, p. 197-198). Barker et al. (2012, p. 3) define social media marketing as follows: “Social media marketing (SMM) uses social media portals to positively influence consumers toward a website, company, brand, product, service, or a person. Typically, the end goal of social media marketing is a “conversion,” such as the purchase of a product, subscription to a newsletter, registration in an online community, or some other desirable consumer action.” Social media marketing aims to support an organization to achieve their marketing goals. Through the combination with traditional marketing tools, products/services can be advertised virally on social networks to a bigger audience (Felix et al., 2017). Social media marketing enables customers to move from passive consumption of advertising messages to conjoint interaction with an organization and other customers (Zehrer & Grabmüller, 2012). Social media marketing enriches the traditional communication strategies of classical marketing (Felix et al., 2017). Social media marketing thus offers several advantages to companies and organizations as its applications emerge as an influential and low-cost marketing tool with a global reach (Usakli et al., 2017). Furthermore, through social media, the scope of marketing activities is no longer limited to the geographical location of the organization (Lange-Faria, 2012).

In the tourism industry, social media has changed the way in which potential guests disseminate and how potential tourism suppliers create information (Buhalis & Law, 2008; Xiang & Gretzel, 2010). The tourism product is an intangible and immaterial bundle of services, which is considered to be a highly information-intense purchase with high involvement (Bieger, 2004). Due to these inherent characteristics, potential customers seek reliable information about potential destinations as well as about possible activities within the destination before and during their consumption (Munar, 2012; Usakli et al., 2017). Therefore, user-generated content on social media is a relevant source of information, which influences the whole customer journey (Amaro, Duarte & Henriques, 2016).

Social media applications are thus used along the whole customer journey, which includes the pre-travel phase, the consumption phase and the post-travel phase (Minazzi, 2014). During the pre-travel phase, potential travelers use social media for inspiration. Applications such as Pinterest, Youtube and Blogs are used to generate an image of the future destination and to communicate with like-minded consumers (Xiang & Gretzel, 2010; Fotis, Buhalis & Rossides, 2012). Potential travelers use social media to get specific information about activities, restaurants and tourist attractions to plan their future journey (Amaro, Duarte & Henriques, 2016). Especially relevant within this phase are online recommendations and ratings on platforms like Tripadvisor, Facebook and HolidayCheck, generated from other consumers (Miguens, Baggio & Costa, 2008). Also during the consumption phase, travelers actively use the social media platforms mentioned for decision-making and as a source of information for activities within the destination (Gretzel, 2009; Cox, Bourgess, Sellitta & Buultjens, 2009). During the post-travel phase, social media enables virtual storytelling for the consumers and also provides a sense of belonging to virtual travel communities (Gretzel, 2009; Fesenmaier, & O'Leary, 2006; Fotis, Buhalis & Rossides, 2012). Moreover, travelers share their experiences during and after the journey in form of videos and photos on platforms like Instagram and Facebook. The diffusion of CGC on blogs, social networks and video portals provides potential and actual customers with reliable information about the destination from other customers; it enables them to share independent opinions and spread the satisfaction or dissatisfaction with their purchase (Xiang & Gretzel, 2010). Through sharing personal experiences and recommendations during and after their journey on social networks, consumers generate electronic word-of-mouth (eWOM), which is spread virally to a bigger and more global audience (Phelps et al. 2004; Thorson & Rodgers 2006; Dwyer 2007; Hung & Li 2007; Shu-Chuan & Yoojung, 2011). Social media applications therefore act as a multiplier of eWOM and as an enabler of direct interaction between customers (Hudson, Roth, Madden & Huddson, 2015; Landvogt, 2017).

Tourismus organizations need to listen, engage with customers and react to their complaints in order to prevent negative eWOM (Kietzmann et al., 2011). History has shown how CGC can harm an enterprise if not reacting properly to customer complaints. The story of Dave Carroll with United Airlines breaking his guitar is just one good example (Carroll, 2013). Many executives still do not fully understand the power of social media and ignore both, opportunities and threats, which can come from consumers (Berthon et al., 2007; Kaplan & Haenlein, 2010). Culnan, McHugh & Zubillaga (2010) point out the importance of implementing a strategy when applying social media into their marketing mix. Companies need to develop a social media strategy, which aligns with the corporate marketing strategy, and includes goal setting, defining the target audience, analyzing competitors and setting activities. Goals may vary, from brand building to an increase in customer satisfaction, driving eWOM (Armelini & Villanueva, 2011; Barker et al., 2012). Examples from big companies have proven that strategic social media marketing leads to returns by creating turnover or saving costs. However, many companies still fail to monitor the economic impact of social media marketing (Barker et al., 2012). Social media as a marketing tool in a touristic context is especially relevant for destination management organizations (DMOs) (Munar, 2012). In alpine tourism areas, DMOs act as leading institutions in coordinating the various tourism providers and managing the immaterial and intangible tourism product (Peters & Strobl, 2013). Due to the community-based nature of alpine tourism destinations, they can be described as amalgams of stakeholders with a big variety of touristic offers (Buhalis, 2000).

Alpine tourism destinations in the Tyrol differ from corporately managed destinations in Northern America, as their structures emerge from the local community and embedded stakeholders (Flagestad & Hope, 2001). Tyrolean DMOs are collectively financed and characterized by a strong municipality. Furthermore, there is strong presence of family-owned small and medium sized enterprises (Flagestad & Hope, 2001; Strobl & Peters, 2013). Until 2002, 254 small DMOs existed in the Tyrol; nearly every municipality had its own DMO. In 2002, the Tyrolean government decided to merge the DMOs to benefit from synergetic effects and a stronger marketing appearance. This merging process was carried out gradually until 2008. Since 2008, 34 DMOs on a local level manage and coordinate the touristic alpine tourism offer. The Tirol Werbung as the subordinate regional tourism organization tries to bundle the activities of the local DMOs and market the region as an alpine winter and summer destination (Lehar & Reisner, 2015). The primary functions of DMOs are 1) tourism destination planning and development, 2) coordination and improvement of the destination offer and the infrastructure, 3) network-building and representation of interests among stakeholders and 4) strategic and operative marketing of the destination, including destination branding and positioning, coordinating marketing strategies, promotion and distribution of the tourism product and providing information for customers (Munar, 2012; Bieger, 2004).

For this study, strategic and operative marketing is of high interest, as DMOs try to market and promote the intangible and immaterial bundle of products of a destination to potential and existing customers as a whole (Munar, 2012; Bieger, 2004). Their core function is the creation and promotion of a strong inimitable destination brand (Munar, 2012). For destinations, the technological and social innovation of social media is a major driver for competitive advantage (Munar, 2012) and this new form of marketing has transformed the classical marketing and communication of these destination management organizations (Aldebert, Dang & Longhi, 2011). Destination management organizations are obliged to be present on various channels and to communicate with potential and actual customers throughout the whole customer journey. However, it also enables them to interact directly and communicate in reciprocal ways with customers (Kiralova & Pavliceka, 2015). Quinton (2013, p. 913) claims that the “linear, relational, exchange-based partnerships” that organizations had with their customers are no more valid and that there has been a power shift to more reciprocal and collaborative communication between demand and supply side. As a collaborative marketing tool, organizations can give feedback, react to recommendations, interact and influence users on social networks (Hvass & Munar, 2012). Thereby, social media applications act as an agent of change by enabling co-creation of content between the supply and demand side (Usakli et al., 2017).

The viral characteristic of social media marketing has resulted in a greater need for destination management organizations to actively participate on social networks (MacKay et al., 2017). Nevertheless, previous studies indicate that DMOs are still in an embryonic stage of using social media channels as an advertising tool and generally perform on a modest level when it comes to interacting and communicating with tourists virally (Usakli et al., 2017). The majority of DMOs simply transfer their existing marketing activities to social networks, rather than exploiting the whole potential of these applications and integrating social media into their existing marketing strategies (Usakli et al., 2017). Although research on the phenomenon of social media marketing in a touristic context is an emergent area of interest among scholars, few studies identify the utilization of social media marketing in destination management organizations (Usalki et al., 2017; Munar, 2012; Lange-Faria & Elliot, 2012; Alizadeh & Mat Isa, 2014, Hays et al., 2013). Furthermore, few studies show the strategic dimensions, which come along with the utilization of social media for DMOs (Munar, 2012), as the phenomenon social media has largely been examined from a demand perspective (Aye, Au & Law, 2012; Lee, Lowry & Delconte, 2015). The majority of existing research investigates the demand side and focuses on the traveler’s social media behavior before, during and after the consumption of the tourism product (Usalki et al., 2017). “This findingindicates that there is still ample room for research about suppliers’ perspective such as in communication, management, and market research.“ (Lee, Lowry & Delconte, 2015, p. 6) Consequently, there exists little understanding of how destination management organizations are integrating social media marketing into their marketing strategies (Alizadeh & Mat, 2015; Lange-Faria & Elliot, 2012). It is assumed that social media thus generates opportunities and challenges for DMOs. There is a strong claim in tourism management literature to understand how these destination management organizations implement social media to market the destination and the fragmented tourism product and which challenges and opportunities occur regarding marketing and communication through social media (Usalki et al., 2017; Munar, 2012; Lange-Faria & Elliot, 2012; Alizadeh & Mat, 2014, Hays et al., 2013, Stankov Lazic & Dragicevic, 2010).

This study therefore focuses on the strategic scope as well as operative practices of the use of social media for DMOs in an alpine context, more specifically in the Austrian region of the Tyrol. Furthermore, this paper aims to close this existing research gap by exploring the utilization of social media marketing in destination management in the Austrian region of Tyrol with the following research questions:

1) How do destination management organizations integrate/implement social media marketing within their marketing strategies?

2) Which challenges may occur for destination marketing organizations regarding social media marketing?

3) Which potential opportunities may arise for destination marketing organizations regarding social media marketing?

To conclude, the paper derives recommendations and implications for DMOs on how to successfully implement social media into their destination marketing, overcome potential challenges and benefit from upcoming opportunities.

2. MATERIALS AND METHODS

The study at hand analyses the social media utilization of destination management organizations in the Austrian province of Tyrol. As past research on social media has focused either on quantitative or qualitative methods (Lee, Lowry & Delconte, 2015), this study applies a mixed-method approach which is divided into three phases. In a first step, the presence of 34 Tyrolean DMOs on social media channels as well as available performance indicators were captured through desk research in August 2016 and May 2017. In a second step, a quantitative survey was conducted to analyze the use of social media in these 34 destination management organizations in the Tyrol. Therefore, social media managers within each DMO were invited to complete a quantitative online questionnaire regarding their strategic approach and operational management of social media within their marketing activities as well as daily challenges and opportunities for marketing their destination. This online survey was online from February 14th until March 30th, 2017. The response rate was high, with 97% (33 out of 34 DMOs) participating in this survey. Data was analyzed with SPSS.

Based on these findings, qualitative interviews with social media managers in various destinations where conducted to identify the potential opportunities and challenges of social media marketing in tourism. "Qualitative research provides complementary insights into quantitative research to gain an understanding about how DMO social media strategies are spoken of and conceived versus how they are actually executed." (Hays et al., 2013, S. 217) With this in mind, the aim of this qualitative part of the study was to identify potential opportunities and challenges of social media in tourism DMOs. 12 qualitative guided interviews were carried out in summer 2017. These were recorded, transcribed and paraphrased following the qualitative content analysis of Mayring. The authors decided to reduce the material through abstraction in order to interpret data material and thus apply the summary approach as an inductive category formation. Furthermore, the software MAXQDA was used for paraphrasing (Mayring, 2014). The analysis focuses on the central questions of integration of social media into the marketing strategy: opportunities and challenges of social media for DMOs. The 12 participating DMOs were furthermore divided into three categories according to their budget of 2015 to analyze differences within smaller and bigger entities: while 4 DMOs (DMO1, DMO2, DMO3, DMO4) have a budget of more than € 6.5 million per year, 5 are in between 3.0 to 6.5 million (DMO5, DMO6, DMO7, DMO8, DMO9) and further 3 below € 3.0 million (DMO10, DMO11, DMO12).

3. RESULTS

According to the research questions defined at the end of chapter 1, the results are divided into the general use of social media in DMOs, its integration into the marketing strategy as well as defined challenges and opportunities for the organizations.

3.1. Utilization of Social Media in Destination Management Organizations

Desk research has shown that Tyrolean DMOs are present on a total of 13 Social Media channels. While all of them are present on Facebook, 91% are on YouTube, 85% on Instagram, 82% on Google+, 73% on Twitter, 62% run their own blog and 58% use Flickr. Only 44% run a Pinterest, 32% an Issuu, 18% a Vimeo and 12% a WhatsApp account. Two destinations use Tumblr and only one destination uses Snapchat. 4 DMOs claim to be present on 4 other channels which have not been listed in the survey. The intensity however varies from just one channel up to 10 channels (3 DMOs). Further 9 DMOs are rather present on 9 and 6 DMOs on 8 channels.

Performance indicators analyzed through desk research show a high diversity of the intensity of utilization. Facebook fans vary from 1,000 to 145,000, Check-Ins from 8 to 163,000 and the number of evaluations from 9 to 6,200. Evaluations are rather positive with means reaching from 4.5 to 4.9. Only one DMO shows an evaluation of 4.1 on average. A similar picture emerges from YouTube. Views range from 28,900 to 5.7 million. Numbers highly depend on the entry date and the size of the DMO. While the first ones already started to run a YouTube channel in 2009, others only followed in 2015. The presence on Instagram shows a similar pattern. Posts vary from 6 to 1,800; followers from 60 to 21,400. Again, the performance depends on the size of the DMO, but also on posts concerning mega events within the region, such as the Hahnenkamm ski race in Kitzbühel or the Ski World Cup in Sölden. On Twitter, tweets range from 52 to 5,600 and followers from 10 to 6,900. The majority of destinations started their Twitter account in 2008 or 2009, while some others followed later in 2014 and one in 2016.

The presence on various social media channels demonstrates the high relevance of social media for marketing of tourism DMOs within the Tyrol. Likewise, the qualitative research shows the high significance of this new marketing tool for DMOs. 88% of interviewees claim that social media has a high significance within their DMO's marketing activities.

On average, social media managers evaluate their own social media presence with 1.78 (on a scale from 1 = very good to 4 = very bad). Results, however, vary depending on the channel. While the performance of blogs are considered the best (1.48), followed by Facebook (1.58), Instagram (1.71) and WhatsApp (1.75), YouTube (2.03), Twitter (2.44), Google+ (2.46), Tumblr (2.5) and Flickr (2.69) demonstrate a below average performance. Qualitative interviews provide explanations for these results. Most DMOs concentrate sparse personal and financial resources on Facebook and Instagram. Many DMOs do not have the necessary budget, know-how or equipment to make high-quality videos, which can be posted on YouTube. Google+ is a channel, which is used for SEO reasons rather than the initial network idea behind it. Accounts on the networks Tumblr and Flickr often exist without actively participating or posting on them.

3.2. Integration of Social Media into the DMO marketing strategy

As already mentioned, the first Tyrolean DMOs started to use social media and create accounts in 2008 and 2009 (DMO1, DMO2, DMO3, DMO 7, DMO9). Social media started off as an add-on activity within most DMOs, sometimes within the IT department (DMO1, DMO2), sometimes as part of public relations (DMO 5), sometimes as part of the marketing team (DMO3, DMO4, DMO7, DMO9, DMO12). Most of them started with a Facebook profile, as business sites did not exist at that time (DMO1, DMO2, DMO3, DMO7, DMO9). However, a real focus on social media was only set around 2012-2014, when social media became the focus of at least the marketing of bigger DMOs. This also involved the introduction of the first social media manager positions (DMO1, DMO2, DMO3, DMO5).

Smaller DMOs still have neither the human and financial resources nor the know-how to efficiently use social media as a marketing tool (DMO8, DMO11, DMO12).

Nowadays, most DMOs (91%) have a social media manager. In reality, these people often only focus a small amount of their work time on social media and have other tasks and online marketing duties to complete. Mostly, only 10-20% of their time is really dedicated to social media (DMO4, DMO5, DMO6, DMO7, DMO8, DMO9, DMO10, DMO11, DMO12). Only two DMOs (DMO 1, DMO2) have installed social media teams of 3-4 full time staff members and are even thinking of employing one more full time person in the near future.

As already described in the theory, most DMOs engage in social media without following a strategic approach but use a process of trial and error as well as learning by doing (DMO5, DMO6, DMO7, DMO10, DMO11, DMO12). Even though 76% of DMOs claim to have some sort of social media strategy in the quantitative survey, qualitative interviews showed that these are mostly just guidelines or directives, not an integrated social media strategy (DMO5, DMO6, DMO7, DMO10, DMO11, DMO12). Two thirds of DMOs have defined guidelines and directives for posts, response times and approvals. However, in 9% such guidelines or directives are missing. Some social media managers claim that they have a strategy in mind (DMO8, DMO10) and three are currently working on formalizing their strategy (DMO1, DMO2, DMO3, DMO9).

63% carry out all their activities on social media internally, while 30% work together with marketing agencies and 9% with freelancers (multiple answers). External agencies are accountable mainly for ad campaigns and content management. 60% have installed editorial schedules and hold regular team meetings. 76% of DMOs offer or foster further education for their employees in the field of social media. These include internal workshops as well as participating in fairs and conferences and meetings with external agencies.

3.3. Challenges for DMOs

Even though DMOs have recognized the high importance of social media for their destination marketing (88% high significance), the reality - especially in smaller organizations - presents a different picture. Social media often receives insufficient attention (DMO 8, DMO11, DMO 12) as other tasks have higher priority. The biggest challenge seems to be resources, both human and financial. As already shown, only two DMOs have a real online marekting team. In most other cases, 1 to 2 staff members are taking over social media as part of their work in online marketing, but do not have enough resources for strategic issues, for content production on various channels, monitoring or reacting to interactions in time (DMO4, DMO5, DMO6, DMO7, DMO8, DMO9, DMO10, DMO11, DMO12). Interviewees also mention financial restrains as a burden (DMO4, DMO6, DMO7, DMO8, DMO10, DMO11, DMO12).

Social media managers affirm that they are using most of their time for content management (1.81) followed by conception & strategy (2.56), customer contact (2.72), technical issues (3.72) and monitoring (3.91) (scale 1=highest time exposure, 5=lowest time exposure). Producing good content also proved to be a big challenge within qualitative interviews (DMO2, DMO5, DMO9, DMO11, DMO12). However, good content does not always mean high-quality pictures or well-investigated articles. Often, snapshots and background stories are more appreciated by users (DMO1, DMO9). Social media managers are aware that videos are the future of social media marketing, but they are lacking human as well as financial resources in order to produce good video content (DMO6, DMO9, DMO10, DMO11). DMO1 is planning to install a new position for a video social media editor in 2018. Furthermore, it is a challenge to produce good content in low season (DMO10) as well as channel-specific content (DMO9, DMO11). Some DMOs are concerned about the fact that achieving visibility and online coverage on Facebook becomes more and more difficult. They are concerned that the focus of Facebook will be more and more on paid ads in the near future (DMO7, DMO10).

Mangold & Faulds (2009, p. 358) claim that “many managers lack a full appreciation for social media’s role in the company’s promotional efforts.” This also seems to be the case in Tyrolean DMOs. 5 DMOs claim that the internal awareness for social media within the management board is missing (DMO3, DMO4, DMO6, DMO7, DMO12). Only 3 DMOs seem to have the full support from the management board. In these cases, social media is an integral part of the marketing strategy and therefore part of any marketing activity of the DMO (DMO1, DMO2, DMO9).

Another challenge arises from the cooperation with stakeholders within the destination. Only 24% of respondents from the quantitative survey claim that there is a good cooperation, further 42% affirm that there is some kind of cooperation. 30% however confirm that there is no cooperation at all. At the same time, 85% of DMOs wish to have a better cooperation with other service providers and stakeholders within as well as outside the destination. They would like to improve the stakeholder communication, develop a joint social media strategy, organize common stakeholder meetings, and help service providers to become more professional when it comes to social media.

The strongest cooperation partners within the destinations are cable-car companies (DMO1, DMO3, DMO6, DMO7, DMO9). Cooperation, at the moment, ranges from sharing posts from other service providers in the region (mainly accomodation or cable-car companies) (DMO6, DMO7, DMO9, DMO10, DMO11) to establishing a coordinated marketing strategy (DMO1, DMO2). In the latter case, DMO2 and the cable-car company share a common online presence (both website and social media channels), content production and budget, hold regular meetings and staff trainings. DMO1 even solves the problem of weekend shifts by letting cash desk staff of the cable-cars answer social media requests on weekends. DMO10 shares a common website with the cable-car company, however has separate social media accounts. DMO9 shares a common online marketing budget with the cable-car company and reconciles their social media presence with them.

Many DMOs claim that their function of representing and marketing the service providers and thus accomodation providers in the region becomes difficult when it comes to social media. As they cannot share posts from all accommodation providers for example, they have to find a balance (DMO1, DMO2, DMO3, DMO7, DMO8). However, a newly established position of a so-called host coach within Tyrolean DMOs should function as a link between the DMO and local hosts. Host coaches get a special training carried out by the host academy. This further education is coordinated by the association of Tyrolean tourism management organitzions (VTT Verband der Tiroler Tourismusverbände). One part of this training also contains online and social media marekting. Host coaches are supposed to transfer their knowledge to accommodation providers in order to push profesionalization within the tourism industry. However, this does not seem to work out so far (DMO4, DMO6, DMO8, DMO10, DMO11). Only few destinations have organized workshops for accommodation providers (DMO1, DMO3, DMO9).

In the quantitative study, only two thirds of DMOs claim to have installed some sort of marketing control systems for their social media activities, which mainly means tracking fans, followers, range or interactions through monitoring tools offered by social media channels. Only two DMOs (DMO1, DMO3) have installed a real monitoring system, including defined performance indicators and integrating results in reformulating the strategy and measures undertaken.

3.4. Opportunities for DMOs

All DMOs are present on social media and therefore have perceived it as a crucial part of today's tourism marketing. 61% of DMOs claim that they plan to boost their presence on social media in the future. DMOs consider the direct contact with guests (96%) as well as the quick communication of content (88%) as the main opportunities of social media for their marketing. Further opportunities include the fact that social media is a rather cost-effective marketing channel and offers proximity to customers (73% each). Interviewees further value the active recommendation through social media and the possibility to acquire new potential target groups (55% each). In order to increase the number of users, 94% of the DMOs interviewed try to integrate social media channels in their website, 88% run ad campaigns, 79% try to deliver creative content, 76% run sweepstakes, 70% AdWords campaigns and 42% include social media into offline communication. Further 18% also use it for surveys.

Making use of CGC for their tourism marketing has been recognized by some DMOs, but yet not at a sufficient level (DMO5, DMO7, DMO8). Two DMOs claim that they want to integrate local residents for content production as well as other third parties (DMO5, DMO11). Local residents are not just important users of the destination’s social media channels (DMO6, DMO7, DMO11, DMO12), they are sometimes actively integrated and write blog posts or provide social media managers with pictures or videos from the region (DMO4, DMO7, DMO12). DMOs have furthermore actively started to work with influencers for content production (DMO1, DMO2, DMO3, DMO4, DMO6, DMO9, DMO10).

Only few DMOs use their network and cooperate with other DMOs for either joint marketing (DMO5, DMO7) or benchmarking (DMO1, DMO2). Some informal contacts exist between social media managers as loose networks (DMO3, DMO4, DMO7, DMO8, DMO10, DMO11). Some DMOs cooperate with the Tirol Werbung as the subordinate regional tourism organization of the province. They either share content of the Tirol Werbung (DMO12) and provide them with their own content (DMO4, DMO9, DMO12) or participate in meetings or trainings (DMO1, DMO3). While some Tyrol-wide networks exist for other special topics like geo-data (DMO4, DMO5), a network for online marketing once existed, however has not been active for a while (DMO1, DMO2, DMO3, DMO9). More than 90% confirm that they would appreciate a stronger interaction and exchange with Tirol Werbung. This was also explicitly mentioned during qualitative interviews (DMO3, DMO4, DMO5, DMO9, DMO11). 88% would like to foster the cooperation between social media managers of DMOs.

Negative feedback does not seem to be a big problem on social media. Most DMOs have not experienced a firestorm on their social media channels so far (DMO2, DMO3, DMO6, DMO7, DMO9, DMO10, DMO11, DMO12). Only two DMOs report firestorms within their destination (DMO1, DMO5). Social media managers experience that guests estimate their tourism products and destination and that most comments and feedback is rather positive (DMO3, DMO9, DMO10). One social media manager experienced that negative comments get discredited by other users. Users even apologized when urging them not to use rude expressions. One Facebook fan even wanted to get to know the social media manager, once the fan was in the destination (DMO3). In order to be prepared for negative comments, one DMO has prepared a complain book including guidelines on how to handle them (DMO1). For severe cases – like natural catastrophes – DMOs also have guideline for crisis communication (DMO1, DMO2). One DMO has discussed this topic with their external agency (DMO3), but others do not seem to be prepared for a firestorm.

One DMO's social media manager sums it up by saying that social media is made for tourism destinations to spread their message, their content and brand. He considers social media as an instrument, which plays into the hands of DMOs (DMO2).

4. DISCUSSION

The current study shows the importance of social media for the destination marketing in alpine regions. DMOs have recognized the importance of social media for their marketing. However, they are facing various challenges in their daily, operational implementation of social media as an integral part of marketing. To provide DMOs with necessary knowledge, this study concludes with practical implications for social media marketing managers in DMOs.

First of all, a strategic approach is missing. Many activities follow the approach of learning by doing and gut instincts dominate the decision-making process. This can be mainly attributed to the lack of personal and financial resources for social media activities as well as the missing awareness of the management boards. DMOs should be encouraged to focus on social media marketing from a more strategic point of view. A well formulated marketing strategy, which integrates social media marketing as a crucial role, should be present in every DMO. All the internal stakeholders like cash and information desk staff, marketing managers, the management team and the boards of directors should be included in the strategy formulation process. Furthermore, idea generation and strategy formulation input of the members of all management levels may lead to a more integrative and holistic social media strategy, as operational and strategic issues are considered. As Mangold & Faulds (2009) mention, and the findings of our study prevail, there clearly is a lack of awareness in the top management team. This integrative strategy approach may also foster the internal awareness and appreciation of social media marketing within the management team and the board of directors.

However, there is strong evidence that it is important to provide DMOs with the necessary human and financial resources in order to professionalize social media marketing. This again comes along with the issue of awareness within the top management level. By regarding social media marketing not only as an operational tool for the promotion of the destination, but more as a strategic tool for market research and brand positioning, financial resources for more workforce in social media marketing could be allocated by the board of directors.

A stronger emphasis has to be put on the education and further training of social media marketing managers in DMOs. Today's world is ever-changing and disruptive, social media marketing managers should therefore be up-to-date with current issues and trends. A relevant factor is consequently the education within universities; they have to integrate online and social media marketing into their curricula to improve social media marketing knowledge and skills of the future generation of social media marketing managers. Furthermore, a new generation of digital natives - born and raised with social media applications - is taking over important functions, both within accommodations as well as in DMOS. The view of social media marketing as solely a “nice-to-have” tool for promotion might change over time.

5. CONCLUSIONS

At the moment, social media is mainly considered as a platform for providing information and interacting with customers. This means that within the customer journey, destinations use social media for the pre-service period for attracting potential guests and providing them with necessary information. In the service-period, once in the destination, guests can access information about activities within the destination, events and opening hours. However, destination in the future should put more focus on social media as a distribution channel, as there is strong evidence, that social networks like Facebook are becoming more and more a sales platform for products and services. Further focus has to be put on marketing control systems and measuring social media activities by establishing KPIs. A critical evaluation of goals reached and KPIs is necessary for a more professional approach to social media marketing in destinations. Furthermore, results from such reports have to build the basis for future strategic decisions.

In addition, DMOs should ensure high quality content with special regard to their target groups. In a first step, it is necessary to evaluate the current target groups on social media. In a second step, relevant platforms and networks should be assessed and selected carefully according to the preferences of the target group. In a third step, DMOs should actively post target- and channel-specific content in form of blogposts, videos or photos. Furthermore, it is relevant that the social media marketing activities do fit with the image of the DMO, as the use of high-professional and highly edited pictures may cause a lack of authenticity and credibility. Another content-related issue that is appreciated by customers is social media marketing activities, which tell a personal story of a destination. The DMO should engage with interesting locals, who are willing to share their particular stories about the region with a viral crowd.

Another major issue of DMOs and their social media activities is the cooperation with and among other stakeholders and tourism providers in the destination. Synergy effects are not exploited at a sufficient level so far. Cooperation within the destinations however is necessary in order to achieve more output in marketing. DMOs should take a leading role in promoting and fostering collaborative work on social networks. This can range from reposting posts and content from several tourism providers or integrating blog articles on the DMO website within the destinations to running only one joint account on one platform together. The DMO and the whole destination as such can thus profit from synergy effects and a bigger viral crowd. In addition, DMOs should act as a mediator between the tourism providers within the region and actively promote cooperative approaches in social media marketing between the different stakeholders.

Tyrolean DMOs are not only lacking cooperation within their destinations and the stakeholders, but also between social media managers from the different Tyrolean DMOs. In order to learn from each other and profit from an internal B2B social network of experts, relevant networking platforms for information exchange have to be established. This is why the tourism department at MCI Management Center Innsbruck as well as the Tirol Werbung are planning to form a network of social media managers within the Tyrol to foster knowledge and know-how exchange within destinations, build up a strong network of personal relationships and better coordinate social media activities in the Tyrol.

Even though only one Tyrolean DMO did not participate in the current study, correlation or regression analysis did not produce any significant values due to the low sample size. Therefore, the quantitative part is rather descriptive. Regarding the qualitative analysis, it lies in the nature of qualitative interviews that bias during the interviews cannot be excluded. Furthermore, qualitative research highly depends on the domain specific knowledge of the interviewee and their willingness to answer the questions (Malhotra, 2010; Lamnek, 2010).

Another possible weakness of this study lies within the generalization of the results (Lamnek, 2010). This study was conducted within the alpine region of Tyrol, the structure of DMOs in alpine region is special as it is fragmented and community-based and therefore region-specific governing and financial issues have to be considered (Falgestad & Hope, 2004). Due to these inherent characteristics of alpine DMOs, their approach to social media marketing may differ from other DMOs which are more corporate-based and privately financed. Nevertheless, relevant implications regarding content and strategy issues can be derived for the social media marketing in DMOs with a different structure. Further research should focus on other alpine DMOs outside of the Tyrol to compare results, and to show whether structural issues make a difference in social media marketing.

As social media evolves as an important part of destination marketing and DMOs become more professional over time, opportunities and challenges might change over time. Therefore, periodical studies would be interesting. DMOs also should be encouraged to turn the challenges that are created by social media into potential opportunities within social media marketing.

Special issues, such as influencer marketing as a part of destination marketing, require separate consideration. Social media marketing in cooperation with bloggers or influencers seems to be a trend for destinations. Nevertheless, there are special considerations regarding the cooperation with online key influencers, such as authenticity and credibility. Further research should focus on how cooperation with influencers can be effectively used for online and social media marketing of destinations.

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The Nomination Committee in Maltese Listed Companies[1]

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A B S T R A C T

The aim of this study is to examine the Nomination Committee (NC) in Maltese listed companies. The study achieves this by assessing the Maltese regulatory framework relating to this Committee, as well as its roles, status and effectiveness. A predominantly qualitative mixed methodology was employed to achieve these objectives. Twenty-five semi-structured interviews were held with two financial analysts, two MFSA representatives, eight audit firm representatives and 13 representatives of Maltese Listed Companies (MLCs) Research findings show that the NC is not as yet not well established among MLCs. There is a particular lack of insistence on the part of local regulatory authorities, as well as substantial resistance from listed companies, with regard to the adoption of this committee. Furthermore, most NCs in such companies are not performing all of the roles listed in their Code while the roles currently performed may need to be carried out in a more structured manner. Yet it is highly worthwhile for such companies to devote more attention to the NC, this being one of the best possible bastions of appropriate corporate governance. The change in the status of the NC from being merely recommended by the Code of Principles of Good Corporate Governance to becoming mandatory by the Listing Rules is increasingly called for. In this way, Maltese listed companies will need to embrace such a change. It is hoped that this study will contribute towards fostering more awareness about the NC and the corporate governance of Maltese listed companies.

A R T I C L E I N F O

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Board of Directors, Corporate Governance, Listed Companies, Malta, Nomination Committee

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1. INTRODUCTION

The board of directors ('Board') may delegate, totally or partially, various roles and responsibilities to its committees (Mallin, 2004). According to Kim, Nofsinger and Mohr (2010), a substantial amount of

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Board work is carried out by these committees so as to improve efficiency in view of the more specialised nature of the committees.

For the purpose of this study, the Nomination Committee ('NC') is studied in greater depth. The NC is a committee appointed by the Board to which it delegates the key responsibility of identifying candidates qualified for Board membership (Mallin, 2004). Such a committee ensures that director appointments are made on "merit rather than by patronage" (McKnight and Weir, 2009, p.143).

In Malta, the appointment of the NC is included as a provision in the Code of Principles of Good Corporate Governance 2010 ('Code'). The Code was issued by the Malta Financial Services Authority ('MFSA'), and it lists the principles and provisions relating to good corporate governance ('CG'). Along with the MFSA Listing Rules 2016, the Code recommends that Maltese listed companies ('MLCs') adopt such principles and provisions in order to contribute towards enhanced CG (MFSA, 2016).

The NC is the "bona fide working unit of the Board" (Murphy, 2008, p.147). However, despite its significance, the NC has been paid scant attention and has not been subject to ample research (Kaczmarek, Kimino and Pye, 2012; EY, 2016). This study is therefore aimed at contributing towards bridging this literature gap, by assessing the Maltese regulatory framework relating to the NC, and the NC's roles, status and effectiveness. The research is conducted in Malta, a small island state economy.
The rest of this paper is divided into five main sections. The second section provides a summary of the relevant literature on the NC, followed by the third section which discusses the methodology employed in this study. The fourth section presents the findings, while the fifth section discusses such findings. Finally, the concluding section summarises the findings and presents the limitations of the study.

2. LITERATURE REVIEW

The Maltese Regulatory Framework

The Code stipulates that the company's shareholders have the jurisdiction to appoint and elect directors (MFSA, 2010). Similarly, the Companies Act requires that company directors, other than the first directors, are elected by the shareholders at the annual general meeting (AGM), unless otherwise indicated in the company's Memorandum and Articles of Association. However, Bezzina, Baldacchino and Azzopardi (2014) found that a number of MLCs have a tendency to be dominated by an absolute controlling shareholder, who holds more than half the company's shares in the aggregate.

In such companies, the controlling shareholder has the right to directly appoint directors to the Board, and to thus control most of the Board's composition.

The Code recommends MLCs to appoint a NC to recommend director candidates to the Board (MFSA, 2010). However, the appointment of the NC is still not mandatory as at the date of this study. Nevertheless, such a committee has been made mandatory for significant credit institutions and investment companies, pursuant to the issue of the Fourth Capital Requirement Directive and Regulation in June 2013. As from January 2014, each Member State was obliged to adopt the requirements set out by this regulation and to transpose this directive into national law (European Parliament and the Council of the European Union, 2013).

The Roles of the Nomination Committee

A common misconception is that the role of the NC is simply to nominate director candidates (KPMG, 2012). However, as recommended by the Code, the roles of the NC should also include the following: determining director independence and advising the Board regarding any issues that may affect director independence (KPMG, 2012); reviewing Board composition through an assessment of the size, composition and membership of the Board (Higgs, 2003); reviewing Board performance through annual self-evaluations (KPMG, 2012); considering succession planning via an assessment of the possible gaps in the skills and expertise of the Board and senior management (EY and ICSA, 2016); and selecting competent candidates to fulfil senior management positions and recommending them to the Board and chief executive officer (EY and ICSA, 2016).

The Status of the Nomination Committee

The roles of the NC tend to be less clearly defined than those of the Audit and the Remuneration committees, even though "it is arguably the most important of the three" (EY and ICSA, 2016, p.4). It has also been noted that "in recent years the NC has been portrayed as the poor relation of the main BCs" (EY and ICSA, 2016, p.4). In fact, the appointment of the NC has been much slower in comparison with the appointment of the Audit and Remuneration Committees (McKnight and Weir, 2009). A probable cause for such a delay may be attributed to this lack of clarity regarding the roles of the NC (Kaczmarek, Kimino and Pye, 2012). In addition, the NC has not been afforded the same amount of guidance as the other BCs (EY and ICSA, 2016), and the attention provided to it "seems to have fallen off the radar" (KPMG, 2012, p.70). The CG codes of various jurisdictions particularly insist on the appointment of the Audit and Remuneration Committees, yet the NC receives much less attention. This lack of insistence may also be another cause for the delay in the appointment of the NC (Higgs, 2003; Kaczmarek, Kimino and Pye, 2012). However, Masulis (2012) argued that "forward-looking corporations that are trying to maximise shareholder wealth should be in front of regulators, and should want to make the changes first".

The appropriate size of the NC depends on its own remit, the size of the Board, and the availability of independent NEDs on the Board (KPMG, 2012). Such a committee should ideally comprise a minimum of three members (ICSA, 2013). However, according to EY and ICSA (2016), an apparent disadvantage of having the Board members constituting the NC is the potential lack of challenge, lack of scepticism and of questioning from such members. In addition, this requirement may also lead to common committee membership, which is greatly opposed by Higgs (2003).

The Effectiveness of the Nomination Committee

In view of the delegation of the various roles of the Board to the NC, the NC effectiveness will have an impact on the Board's effectiveness (KPMG, 2012). In particular, an effective NC enhances the Board's ability to discharge its roles (Hillman and Dalziel, 2003). In fact, Vafeas (1999) found that a Board with a NC will ultimately vary in effectiveness from one that does not have such a committee. This is because having a NC will benefit from group screening of the director candidates, potentially diminishing any limitations in the director nomination and appointment processes (Vafeas, 1999; Petra, 2005; Masulis, 2012). This renders an effective NC a key component for an equally effective Board. Furthermore, as stated by Higgs (2003), the increased use of the NC plays a pivotal role in raising the standards of CG, owing to the added assurance that the most significant roles of the Board are being effectively discharged.

3. RESEARCH METHODOLOGY

A predominantly qualitative mixed methodology was implemented to achieve the objectives of this study. Data was collected through the use of 25 semi-structured interviews employing both closed-ended and open-ended questions. These interviews were carried out with two financial analysts, two MFSA representatives, eight audit firm representatives and 13 MLC representatives. Purposeful sampling was used, whereby the researcher selected those participants with the ability of contributing, through their knowledge, to the various topics of this study. The interview schedule consisted of five sections. The first four sections elicited the interviewees' views on the Maltese regulatory framework and the NC's roles, status and effectiveness. The last section inquired about certain characteristics of the interviewees.

The audio recordings of the interviews were transcribed shortly after the interviews were held, leading to the analysis and subsequent interpretation of the interviewees' responses. The quantitative data collected from Likert-type items (with responses ranging from 1=strongly disagree to 5=strongly agree scale) were analysed using IBM SPSS V22. To investigate differences in mean ranks across the Likert scales, the Friedman test was used with paired samples while the Kruskal Wallis test was used with independent samples. In the presence of a significant effect, post-hoc tests were conducted. Due to word count limitations, only statistically significant findings ($p<0.05$). are being referred to in this paper.

On the other hand, the qualitative data was analysed by summarising the transcripts, allowing key themes to be identified from each open-ended question, which rendered the process of drawing up conclusions easier.

4. RESULTS

Nomination Committee in the Interviewee Companies

Company interviewees (13/25) were asked whether or not their companies have an NC. Eight companies confirmed that they have a NC ('NC-including interviewees'), while five do not have an NC ('NC-excluding interviewees'). Most of the 13 companies interviewed (8/13) have a NC which is not standalone, having three independent NEDs and with a chairman who is also the chairman of the Board. Meetings are held at varying frequency, occurring up to once a month. All NCs have members who also hold positions in other BCs.

The Maltese Regulatory Framework

All interviewees maintained that the power to appoint and elect directors needs to remain vested solely in the shareholders. However, most of them (19/25) added that other parties, which they specified, are best to be involved in recommending such appointments. The most mentioned parties include the NC (9/25) and the MFSA (6/25). Interestingly, six interviewees argued that no other parties should be involved.

Almost all interviewees agreed (24/25) that Board members are generally biased when recommending new members to stand for election. They claimed that it is easier to recommend someone with whom one is acquainted and feels comfortable to work with, especially in a small state like Malta where people tend to know each other. Furthermore, interviewees identified the following barriers which may impair the engagement of the most suitable directors: bias of controlling shareholders towards persons of trust (7/25), shortage of competent individuals (6/25), inability of competent individuals to attract sufficient votes (5/25), inadequate remuneration (5/25), lack of interest (4/25) and insufficient time to devote to the Board (4/25).

Moreover, interviewees marginally agreed that an independent outside consultant should act as an advisor to the NC 3.60). Two agreeing interviewees (2/14) commented that the NC "has blank authority to appoint advisors, as the Board members do not know everything". Therefore, appointing outside advisors to assist the NC will render its work more effective.

Interviewees expressed neutral views as to whether the appointment of the NC should be made mandatory by law 3.36). Six of the agreeing interviewees (6/14) explained that the present 'comply or explain' Code provision is insufficient and tends to spur MLCs not to comply, but then to try to explain. On the other hand, six of the disagreeing interviewees (6/7) contended that imposition by law is not to be the way forward as each MLC has its own particular circumstances and it is best to leave it up to each company to decide whether or not to appoint an NC.

Additional comments were requested specifically in relation to how justifiable it is that the NC has become mandatory only in the case of significant credit institutions and investment companies. The interviewees who commented favourably (17/25) to this maintained that both the operations and systemic importance of these companies are of such a magnitude that such discrimination is rendered justifiable. Conversely, the interviewees whose comments were unfavourable (8/25) stated that companies should be regulated in a uniform manner irrespective of their size, industry and whether they are listed or otherwise.

Furthermore, interviewees disagreed with the statement that the recommendations of the NC are not to be circulated to the Board before being forwarded to the AGM 1.92). Furthermore, the responses to this statement (based on mean ranks) were significantly lower ($p<0.01$) from the preceding two statements. Most of the disagreeing interviewees (13/20) emphasised that the NC is a committee of the Board and thus the Board is ultimately responsible for such committee's roles.

The Roles of the Nomination Committee

Interviewees strongly agreed with the role of the NC in reviewing Board composition .
They also agreed with three other NC roles: proposing director candidates to the Board (4.40), considering issues related to succession planning (4.28) and determining director independence (4.08). However, as regards the last two roles, interviewees only marginally agreed that the NC should review the Board policy for the selection and appointment of senior management and that the NC shall evaluate the Board performance 3.60). In fact, the interviewees' responses for the latter two statements were statistically different ($p<0.01$) from those of the former four statements.

When asked to comment about the roles which are currently performed by the NC in the companies of the NC-including interviewees, barely half of them (3/8) pointed out that their NC actually performed the roles recommended to it by the Code. Moreover, when comparing the responses of the NC-including interviewees regarding their agreement to the recommended NC roles with the actual roles such a committee plays in their companies, it was found that overall, not all the recommended roles were in fact actually being taken up by the NC in many MLCs. This indicates an inconsistency between what the interviewees agreed with, and what actually happened in real life in the respective NCs.

Furthermore, in the absence of the NC, NC-excluding interviewees commented that the parties responsible for the recommended roles usually assigned to the NC are mainly the shareholders, the Board and the chief executive officer.

The Status of the Nomination Committee

Interviewees expressed neutral views with respect to the statement that only members of the NC are to be permitted to attend the meetings of such committee 3.12). Two of the agreeing interviewees (2/13) explained that the other Board members are not to attend such meetings as they might influence the decision/s taken by the NC members. Conversely, almost all disagreeing interviewees (9/12) stated that other Board members may be invited to attend for specific meetings, at the NC chairman's discretion, to observe (without having a right to vote), and thus contribute with their knowledge and experience.

Interviewees also expressed mixed views as to whether the NC may successfully be combined with another committee 3.08). Two of those who agreed (2/12) with this possibility stated that when nominating directors to the Board, remuneration needs to be taken into account, thus implying that it makes sense for the NC to be combined with the Remuneration Committee. In fact, most of the companies of the NC-including interviewees (5/8) have a combined NC-Remuneration Committee. However, three disagreeing interviewees (3/8) argued that it is best for the NC to be a separate committee because each committee has its own specific roles and focus.

Furthermore, interviewees were marginally neutral tending to disagree with the statement that the members of the NC are not to be members of other committees 2.68). Six of these interviewees (6/13) commented that common committee membership is inevitable, especially when the Board is small and the company has quite a number of committees in existence. In fact, such common membership has been seen to be the case in the MLCs of the interviewed companies.

Interviewees mostly disagreed with the statement that the NC does not deserve the same amount of attention and guidance as other committees 2.24) with ratings to this statement differing significantly between interviewees ($p=0.04$). Seven of these interviewees (7/17) emphasised that the NC plays a crucial role in proposing candidates for Board and senior management positions, which parties are responsible for the direction of the company; also that, given such importance, the NC should deserve the same amount of attention and guidance as other committees.

Furthermore, NC-including interviewees were asked whether another independent NED would be more appropriate to chair the NC than the chairman of the Board. Most of them (6/8) disagreed, adding that the chairman of the Board is more than capable of chairing the NC as well. In fact, most of the NCs in the companies of the NC-including interviewees (5/8) are chaired by the chairman of the Board. Conversely, the other interviewees (2/8) agreed, stating that if the same chairman chairs both the Board and the NC, then such chairman is more likely to unduly influence the final decision.

NC-including interviewees were also asked whether the report of the NC in the annual report provides enough assurance to the users that relevant issues are being addressed. Some (3/8) maintained that such a report is quite transparent, however others (2/8) stated that the disclosures on the work performed by the NC in the annual report are quite limited in view of the sensitivity and confidentiality of such work.

In addition, all interviewees agreed that the setting up of the NC is relatively delayed owing to various barriers. The following barriers were identified by interviewees: the appointment of the NC not yet being mandatory by law (10/25), the lack of awareness by MLCs of the use and importance of the NC (8/25), the appointment of the Audit Committee being given precedence (3/25), the fact that controlling shareholders are commonly not very willing to promote such a committee (2/25), the reluctance by the Board to delegate the responsibility of nominating directors to the NC (2/25) and the perception that such a committee might be "too much of a burden" (1/25).

The Effectiveness of the Nomination Committee

Interviewees were neutral as to whether the NC reduces the likelihood of appointing new directors based on personal connections . A few of them (4/19) remarked that the appointment of the NC made up of independent members would convey a more transparent and objective view and ensure that they are not biased for improper reasons when nominating directors to the Board.

Interviewees were also marginally neutral as to whether that the Board having the NC will ultimately differ in effectiveness from one not having such a committee. A few of them (3/19) emphasised that having a dedicated committee entrusted to actively filter and nominate the most suitable directors and to ensure that there is appropriate synergy around the table would contribute to the Board's effectiveness. Moreover, they added that a NC composed of independent NEDs would result in more objectivity, independence and less bias in the execution of its roles, thus enhancing the effectiveness of the Board.

However, interviewees expressed mixed views with respect to whether the Board can effectively perform the roles of the NC and therefore replace the NC 2.96). A few of the agreeing interviewees (4/10) commented that disagreeing with this statement would in effect be implying a lack of confidence in the Boards of most companies in Malta to perform these roles, given that in practice, such companies did not have an NC. A further four interviewees commented that since there are no legal distinctions between the duties and liabilities of executives and NEDs, and since the NC is composed of Board members, then its roles may effectively be replaced by the main Board. On the other hand, most of the disagreeing interviewees (7/10) argued that the NC is composed of independent members having the required qualities, has fewer roles than the Board, and may therefore focus more effectively on performing such roles.

Overall, it was found that a common viewpoint of the interviewees was that in order for the NC to reduce Board bias, enhance Board effectiveness and enhance CG, such a committee needs to be composed of independent outside consultants.

In addition, interviewees specified the following benefits of appointing a NC: greater scrutiny of candidates for directorship positions (10/24), a more transparent director nomination process (7/24) (since the NC is composed of independent members), more time for the NC to conduct an effective discussion (6/24), a higher probability of reaching consensus given that the NC has fewer members than the main Board (5/24), a more dedicated focus on the director nomination process (5/24), the possibility of benefitting from external independent perspectives (4/24), and the additional comfort provided to the shareholders arising from the fact that the recommendations of the Board would have been substantiated by the NC (2/24).

On the other hand, interviewees also identified the following limitations: limited scope of a NC in MLCs having controlling shareholders with the right to appoint the majority of the directors (7/20), the lack of experience of Board members with regard to the operations of the NC (6/20), the limited available pool of independent NEDs given Malta's small size (5/20) and the possibility of conflicts of interest owing to the NC members also being part of the main Board itself (5/20).

DISCUSSION

Who Needs to Be Involved in the Engagement of Directors?

In Malta, the power of appointing and electing directors is conferred on the shareholders of the company, pursuant to the Code and the Companies Act. However, as also stated by most interviewees, other parties may be involved to provide guidance to the shareholders in appointing the most suitable and competent directors. These parties mainly include the NC and the Board. The positive input that such parties can contribute arises from the fact that they hold a position that makes them most cognisant of the needs of the company. As a result of this, they are able to properly guide shareholders in appointing the most suitable directors.

In addition, independent outside consultants are also to be involved since, owing to their independence, they are in a better position to guide the shareholders in appointing the most competent directors. One suggestion that was mooted by one interviewee was to go a step further and even involve the company's creditors and employees in the appointment of directors on the basis that they too have an interest to appoint the most suitable directors to ensure the continued smooth running of the company. Nonetheless, owing to the tendency for most MLCs to be dominated by controlling shareholders (Bezzina, Baldacchino and Azzopardi, 2014), the controlling shareholders would wish to retain the power to appoint directors, and would therefore be reluctant to permit any interference from other parties in this regard. In particular, controlling shareholders are biased towards their persons of trust and might want to appoint Board directors who they are confident will ensure that the shareholders' interests are promoted and pursued. This may occur irrespective of whether or not such directors are competent enough to give a fair contribution to all the stakeholders of the company.

The possibility of such resistance from the controlling shareholders renders the role of the MFSA, as the regulator, much more significant. The MFSA requires candidates to undergo a due diligence process so that it may establish whether they are 'fit and proper'. Therefore, as emphasised by an MFSA representative, "irrespective of whom the shareholders would like to appoint, if any candidate is not deemed 'fit and proper' by the regulator, then such candidate will in any case not be appointed " However, this does not mean that the Board may rely on the checks being placed by the MFSA. The responsibility of the Board should probably extend towards the appointment of the appropriate directors in the first place, if there is to be a proper first line of defence with regard to CG.

Should the Nomination Committee Be Made Mandatory?

With the NC not being mandatory, in their annual report most companies tend to neither comply nor explain sufficiently and reasonably the reasons for their non-compliance. Boards may be using different tactics – such as delaying or dominating ones – to retain their say about who will ultimately be appointed. Given such resistance, it is also not surprising that only eight of the 22 MLCs have a NC as at the date of this study. This is in line with the findings of Muscat (2012), Bezzina, Baldacchino and Azzopardi (2014), as well as Deguara (2014), all of which confirmed that the appointment of the NC was still not common practice among most MLCs as at the date of their studies. Therefore, within this context, more vigilance needs to be exercised by the regulator. On the one hand, this committee may not need to be enforced on MLCs. In line with Masulis (2012) and some of the interviewees' responses, companies should not wait on the regulators to enforce the appointment of the NC on them; instead, they should adopt a more pro-active approach and voluntarily set it up. On the other hand, if the objective is to have more companies appoint a NC over the short term, the NC is best made mandatory by law, possibly in the Listing Rules in the same manner as the Audit Committee.

To Whom Should the Nomination Committee Report?

In line with most interviewee responses and Prasad (2011), the Board should retain responsibility for and make the final decisions relating to the roles delegated to the NC. Therefore, the recommendations of the NC are to be approved by the Board before being forwarded to the AGM. Nevertheless, as the owners of the company, shareholders constitute the party that is most interested in the Board composition and any recommendations related to it. Thus, the question arises as to whether the NC should be empowered to report directly to the shareholders at the AGM. This would avoid the possibility of any NC recommendations being rejected by the Board which, on their part, shareholders could find valid. With such direct reporting, it will be up to the shareholders to decide whether or not to accept the recommendations of the NC, without any material influence on such a decision by the members of the Board. While it remains questionable whether the Board would be ready to accept that it is bypassed in such an important decision, it is probable that such an arrangement would do away with undue Board politics.

Are the Recommended Roles Sufficient?

According to the majority of the interviewees, the roles designated for the NC as required by the Code are quite sufficient, particularly for those NCs which are operating effectively. The Board need not delegate more roles to it because, as also remarked by an interviewee, "this would overburden such committee and render more difficult the fulfilment of its roles "

Do Companies Practise What They Preach?

For most of the recommended NC roles, it was difficult for the NC-including interviewees to practise what they preach within their NC. The indications are that a high level of resistance relates to the role of the NC to evaluate Board performance. Perhaps such apparent resistance to the evaluation of Board performance emanates from the idea that each of the existing Board members is to be assessed directly by the other Board members. Therefore, in line with Barlow (2016), the role of an independent outside consultant to help the NC in such evaluations might prove to be particularly important. Such outside views may help ensure that the appropriate picture is drawn of each director, irrespective of their acceptance or otherwise within the Board. Surprisingly, the NC in most MLCs rarely has a role in proposing director candidates to the Board, even though their representatives agreed to it and identified it as being "its key role". This is because, as most of the NC-including interviewees explained, most directors are directly nominated and appointed by the controlling shareholders, and that therefore the NC has a limited role in such nominations.

Moreover, with regard to the other recommended roles of the NC, particularly the review of Board composition, these may need to be carried out in a more structured manner than at present. For example, the use of a 'board skills matrix' as explained by Clune, Hermanson, Tompkins and Ye (2014), which none of the interviewees actually referred to, would probably help ensure a more thorough review than that being performed at present, which too often is performed in a very unstructured manner.

Furthermore, as stated in the findings, in the absence of a NC, the parties responsible for such roles are the Board, the chief executive officer and the shareholders. However, all parties would probably be unable to supplant the NC roles successfully in view of insufficient focus and lack of specialisation. A properly structured NC with skilled NEDs should go a long way to fulfil such roles.

What About Combining the Nomination Committee?

From the findings of this study, it emerged that most NCs in Malta are combined with the Remuneration Committee. As indicated by Higgs (2003) and some interviewees' responses, in order to be in a position to propose director candidates to the Board, the NC requires feedback from the Remuneration Committee to enlighten it about the remuneration of such candidates once these have been appointed to the Board. This is because the NC needs to be assured that the minimum level of director remuneration is sufficient to be attractive to the right calibre of candidates with the appropriate qualifications and experience. Nevertheless, as also indicated by the interviewees and Higgs (2003), such a link does not mean that the NC has to be combined with the Remuneration Committee. Both committees have separate and distinct roles to fulfil, and combining them would probably give rise to the disadvantage of overburdening those directors involved in these committees.

How Wise is Common Committee Membership?

One problem of BCs is perceived to lie in the fact that most Boards appoint the same directors on such committees (KPMG, 2012). This is in line with most of the interviewees' responses, who claimed that common committee membership is inevitable owing to the size of the Board and the numerous BCs. In fact, it was found that common committee membership is the case for the Boards of all MLCs included in this study. Directors who are highly involved in such committees may be overloaded, leading to a lack of balance in Board deliberations. Therefore, while for the sake of cooperation and continuity, links may need to be maintained, on the other hand, indulging in too many committees would probably turn out to be detrimental to the CG of the company.

Is the Board Chairman to Chair the Nomination Committee?

As stated by most of the NC-including interviewees, the chairman of the Board may be sufficiently competent to also chair the NC. In fact, it was found to be common practice for most NCs in MLCs to be chaired by the Board chairman. However, normally it is considered best practice for both positions to be segregated. This would ensure that the Board chairman, who is also typically the most powerful Board member, does not treat Board and NC matters as one and the same. Additionally, it ensures that the NC is composed of members who are most detached from the Board.

What Constitutes the Nomination Committee Report?

In line with EY and ICSA (2016) and interviewees' responses, it may be the case that the report of the NC contained in the company's annual report is not adequately transparent, owing to the sensitivity of the matters discussed by such committee and the general lack of regulation relating to it. While it may be clear that in view of such sensitivity involved, transparency at shareholder level is not always attainable, the NC may attempt to compensate for this by lodging regular reports – including the more confidential matters – to the Board. These may be further supported by the written viewpoints of independent outside advisors.

What Barriers Hinder the Nomination Committee Appointment?

McKnight and Weir (2009), as well as Kaczmarek, Kimino and Pye (2012), maintained that the lack of awareness on the scope and benefits of the NC has resulted in the slower rate of the setting up of the NC. This has also been found to be the case in Malta. Furthermore, as also pointed out by the interviewees, the Audit Committee is given much more importance than the NC, even though as argued by EY and ICSA (2016), the NC is considered more important than the Audit and the Remuneration committees in view of the roles assigned to it. This is indicative, therefore, of the need to make the NC mandatory. Interviewees also pointed out that a small Board commonly bars the appointment of the NC. However, all these 'barriers' could merely be betraying a hidden resistance to the appointment of the NC. Moreover, such reasons are hard to justify given the public interest nature of the listed companies involved.

Should More Attention Be Given to the Nomination Committee?

The NC does not receive the attention and guidance it requires for its effective functioning (KPMG, 2012; EY and ICSA, 2016). In particular, there is a general lack of insistence on its appointment (Higgs, 2003; Kaczmarek, Kimino and Pye, 2012). As indicated by the interviewees' responses, the NC deserves the same amount of attention and guidance. This is because, as explained by such interviewees and in accordance with EY and ICSA (2016), the roles of the NC are crucial ones and therefore the NC requires more guidance, especially from the regulator. In this context, the need for such a committee to be made mandatory is heavily implied.

Does the Nomination Committee Reduce Board Bias?

One may agree with most interviewees who claimed that Board members seem generally biased when recommending new members, because they would rather recommend someone they are familiar with and trust rather than someone they barely know. However, being composed of independent NEDs, the NC helps reduce bias by ensuring that the Board nominees are not recommended for illicit reasons. This is in line with the findings of Vafeas (1999), Petra (2005) and Masulis (2012), which indicate that having a NC will benefit from better screening of the director candidates, potentially diminishing the bias in director appointments and working towards the effective functioning of the Board.

Can the Board Replace the Nomination Committee?

A further controversy lies in whether the Board can replace the NC. It is true that the Board can in theory perform all roles delegated to the NC, as well as those assigned to any other BC. However, in practice, the question arises as to whether the Board is in a position to carry out such roles effectively. In line with Dalton, Daily, Ellstrand and Johnson (1998), most of the key decisions are primarily derived from BCs. As pointed out by some interviewees, without such committees, there would definitely be less room for proper discussions and examinations, as well as possibly the need to hold numerous meetings. This was confirmed by Hillman and Dalziel (2003), who claimed that an effective NC enhances the Board's ability to discharge its roles more effectively.

Does the Nomination Committee Enhance Corporate Governance?

The NC plays a crucial role in ensuring that the most suitable directors are appointed. As stated by Higgs (2003), Murphy (2008) and KPMG (2012), this has a significant impact on the quality of CG in the company. Furthermore, results clearly indicated that interviewees with a NC in place disagreed significantly more ($p<0.01$) than those without such a NC with the claim that, in practice, the increased use of the NC would hardly raise the standards of CG. This indicates that the practical experience of having a NC is one of positive enhancement and of changing preconceptions.

How Can the Nomination Committee Be Effective in Malta?

In accordance with Petra (2005) and Masulis (2012), as well as with the NC-including interviewees' responses, having an NC leads to the nomination of the most suitable and independent candidates. This is because key matters will have already been discussed primarily at a committee level, in this manner deploying more focus and time for effective discussion, and resulting in a more formal and transparent nomination process. This indicates that the company interviewees with hands-on experience within the NC perceived the appointment of such a committee to be good CG practice. This also indicates that the perception of NC-excluding interviewees who commented that the NC is not effective in Malta stems from their lack of experience on such a committee.

Overall, most interviewees repeatedly maintained that in order for the NC to be effective in a small state like Malta, it would need to be composed of outside consultants rather than Board members. Indeed, as a tiny island Malta has "close interweaving personal relationships" (Magri and

Baldacchino, 2004, p.956). As a result, the pool of independent NEDs is limited and, being composed of Board members, the NC may lead to potential conflicts of interest, as was also indicated by a number of interviewees. This also aligns with the findings of KPMG (2012), EY and ICSA (2016), which also suggest that having the NC composed of Board members may result in a lack of scepticism and objectivity on the part of its members. Within this context, while, as has already been referred to, there is a need for such a role for outside consultants, a NC composed of NEDs but supported by such outside consultants would probably be a more balanced solution.

6. CONCLUSION

This study revealed that at present, the NC is not well established within MLCs yet, both in terms of the regulatory framework and also in terms of the NC's roles, status and effectiveness.

With regard to the Maltese regulatory framework, it is somewhat lacking, particularly in view of the 'comply or explain' provision of the Code. In addition to rendering such Code mandatory in the Listing Rules, the need arises for the regulator to issue more specific guidance to not only ensure that the NC is appointed in all listed companies, but that more significance is attached to it by those companies which already have a NC. Furthermore, better regulatory provisions relating to the engagement of new directors are called for, particularly to compensate for the potential or actual biased influence of existing Board members.

As regards the roles of the NC as already listed in the Code, they are in themselves sufficient. However, most NCs are not performing all of these roles. In particular, there seems to be a persistently strong resistance against the NC's role of evaluating Board performance. In addition, even those roles currently performed by the committee may need to be carried out in a more structured manner if they are to be improved.

The status of the NC within MLCs needs further clarification. Examples of this relate to whether the said committee should stand alone or be combined; whether there should be common membership between committees; whether it is recommendable for the chairman of the Board to be the NC chairman; what qualities, such as experience and qualifications, NC members are to be expected to have; and what constitutes an appropriate NC report. Such clarifications should go a long way to ensure that the NC receives the status it properly deserves.

Finally, our findings show that, with regard to the effectiveness of the NC in the CG of MLCs, companies that have such a committee find it somewhat effective. Nonetheless, the NC reduces Board bias and enhances CG if it is composed of external consultants. Therefore,in order for the NC to be effective in Malta, it needs to be supported by independent outside consultants.

The results of this study are subject to the following limitations. In spite of the efforts exerted to render the interview questions as clear as possible, the possibility of interviewee misunderstandings could not be fully eliminated. Furthermore, at times where comments on individual MLCs were requested, company interviewees refrained from giving specific information. This might have prevented the researchers from arriving at a complete picture of the overall situation of the NC in MLCs. Finally, although efforts were also made by the researchers to avoid bias and impartiality, the possibility of the presence of such factors cannot be discounted, particularly in view of the probing questions that needed to be placed in the open-ended sections of the interview schedule.

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Corporate Governance and Ownership Structure

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ABSTRACT

The highly concentrated ownership in the Bosnia and Herzegovina market provides a rich environment to explore corporate governance practices. The paper will assess effects that ownership structure of companies has on the level of implementation of corporate governance in companies listed on the Official market of the Banja Luka Stock Exchange. Results of implementation of the corporate governance in companies will be presented using Scorecard analysis for evaluation of the implementation of practices and principles of corporate governance for companies which are listed on the Official market of the Banja Luka Stock Exchange. Ownership structure will be presented in three groups of owners determined by controlling owner: government, domestic and foreign owners. Paper will show correlation and effect which different owners of companies have on the level of implementation of corporate governance in these companies.

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1. INTRODUCTION (Style: Times New Roman, 12 pt, Bold, CAPITALISED)

Corporate governance is a key element for improvement of investors' confidence, increase of competitiveness and improvement of economic growth. Corporate governance is on the top of agenda for international development as stated by James Wolfensohn (1998) that "the governance of the corporation is now as important in the world economy as the government of countries".

Good corporate governance is not possible without appropriate legal framework and quality rules, regulations and standards. Without these assumptions it is not possible to create business environment in which shareholders, especially minority shareholders, will be able to successfully and equally fulfil their rights and interests in companies in which they invested their capital.

Research problem of this paper is determining effects that ownership structure of companies has on the level of implementation of corporate governance in companies listed on the Official market of the Banja Luka Stock Exchange. For investors one of the most important aspects when making an investment decision is a level of implementation of corporate governance principles.

2. THEORETICAL BACKGROUND AND RESEARCH HYPOTHESIS

In the last few years corporate governance has become subject of the large interest in theory, as well as in practice. Parker stated that "corporate governance has commanded the highest levels of attention and debate among legislators, regulators, professions, business bodies, media and in the general community" (Parker, 2007:1). Despite existence of many different approaches and definition of corporate governance, it can be broadly defined as "basically the system by which companies are directed and controlled" (Cadbury, 1992).

Most basic and widely used definition of corporate governance is given by Sir Cadbury by whom "corporate governance is the system by which companies are directed and controlled" (Cadbury, 1992). More accurately, it is the framework by which interest of various stakeholders are balanced, or as stated by the International Financial Organization (IFC) it „concerns the relationships among the management, Board of Directors, controlling shareholders, minority shareholders and other stakeholders"(IFC, 2005). The Organisation for Economic Co-operation and Development (OECD) also defines corporate governance in its Principles of corporate governance „corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined "(OECD, 2004). There is evidence from many researches that good corporate governance system produces direct economic benefit to the company, making it more profitable and competitive. Lipman (2006) states that good corporate governance helps to prevent corporate scandals, fraud, and potential civil and criminal liability of the organization. Good corporate governance enhances image and reputation of a company and makes it more attractive to investors, suppliers, customers and other stakeholders of the company.
Recent research in this field shows that investors have a tendency to invest more in companies which have better governance systems. Bushee, Carter and Gerakos (2007), as well as Leuz, Lins and Warnock (2007) support this claim that investors exhibit preference for well-governed firms.

Merton (1987) argues that investors are more likely to invest in those companies that they know about. Results of studies of Brennan and Cao, (1997); Kang and Stulz, (1997); Covrig, Lau and Ng, (2006); and Choe, Kho and Stulz, (2005) indicate that foreign investors tend to invest primarily in those companies associated with less information asymmetry.

According to McKinsey Global Investor Opinion Survey on Corporate Governance (2002) 73% of investors say that corporate governance is equally or more important relative to financial issues (e.g., profit performance and growth potential) in evaluating which companies they will invest in. Also this Survey indicates that corporate governance does matter to investors, and that 76% of investors said that they are willing to pay a premium for a well-governed company. This indicates that investors, especially in crisis, value more companies which are well governed.

One of the central points of the corporate governance literature is the role of the ownership structure as a governance mechanism. Most of the literature deals with the relation between ownership structure and firm performance. Ownership structure is mostly viewed through ownership concentration. The debate on ownership structure and firm performance was firstly started by Berle and Means (1932). Relationship between the ownership structure and firm performance was tested by Jensen and Meckling (1976), Shleifer and Vishny (1986), Morck, Shleifer and Vishny (1988), McConnell and Servaes (1990), La Porta R, Lopez-de-Silanes F, Shleifer A, Vishny R. (1999), Thomsen and Pedersen (2000), Gedajlovic and Shapiro (1998, 2002), Demsetz and Lehn (1985), Himmelber, Hubbard, and Palia (1999), Demsetz and Villalonga (2001) as well as by many other researchers.

This paper focuses on different aspect of ownership structure dividing it into three groups of owners determined by controlling owner: government (state), domestic and foreign owners. Paper focuses on determining correlation and effect which different owners of companies have on the level of implementation of corporate governance in these companies.

To offer useful answers to the research problem and realize the study objectives, the following hypotheses were tested.
H1: There is a correlation between level of implementation of corporate governance and ownership structure.
H2: Foreign owned companies have higher level of implementation of corporate governance standards in each of seven areas of Scorecard analysis than companies which are domestic and state owned.
H3: State owned companies have lowest level of corporate governance and do not comply with best practices and principles of corporate governance.

3. RESULTS AND METHODOLOGY

3.1 Methodology

The highly concentrated ownership in the Bosnia and Herzegovina market provides a rich environment to explore corporate governance practices. The paper will assess effects that ownership structure of companies has on the level of implementation of corporate governance in companies which are listed on the Official market of the Banja Luka Stock Exchange. Results of implementation of the corporate governance in companies will be presented using Scorecard analysis for evaluation of the implementation of practices and principles of corporate governance for companies which are listed on the Official market of the Banja Luka Stock Exchange. The research for the Scorecard analysis was

done for a period of 3 years (2010, 2011 and 2012). Ownership structure will be presented in three groups of owners determined by controlling owner: government (state), domestic and foreign owners.
The research data was gathered from the database of the Banja Luka Stock Exchange, the National Assembly of the Republic of Srpska, Securities Commission, companies' annual reports and WebPages. Scorecard analysis for corporate governance.

The Scorecard for the Standards of governance of Joint Stock Companies (The Banja Luka Stock Exchange 2009) was developed by the Banja Luka Stock Exchange with the assistance of the International Finance Corporation (IFC) based on the model of the Scorecard for German corporate governance (DVFA Corporate Governance Working Group 2002).

The purpose of the development of the scorecard is to facilitate the work of analysts and investors by providing a systematic and simple overview of all relevant issues with regard to good corporate governance, enable companies to easily determine the scope and quality of own corporate governance and enable comparison with other companies, industries and countries.

The structure of the Scorecard analysis contains the main criteria which are included in the standards and recommendation of best practice of corporate governance, with the relevant set of questions for each area.

The structure of the Scorecard analysis consists of seven areas:

1. Commitment to corporate governance principles;
2. Rights of shareholders;
3. Equal treatment of shareholders;
4. Role of stakeholders in governance of joint stock companies;
5. Publishing and transparency of information;
6. Role and responsibility of the boards; and
7. Audit and internal control system.

These seven areas of the Scorecard analysis are comprised of 42 questions on which every tested company should give an answer (yes, partially or no).

Conceptually, the evaluation of the implementation of the principles of corporate governance should have the score between 65% - 75%, which is possible by the implementation of mandatory principles of corporate governance defined in the Standards of Governance of Joint Stock Companies, i.e. in the legal framework of the capital market of the Bosnia and Herzegovina. Achieving the total score of 100% should be an incentive for companies to implement higher principles of corporate governance (Strenger 2002).

3.2 Results

The research for the Scorecard analysis was done for a period of 3 years (2010, 2011 and 2012) in companies which are listed on the Official market of the Banja Luka Stock Exchange. Research results are derived from more than 2.000 survey answers. Moreover, results are presented by each area of Scorecard analysis for corporate governance.

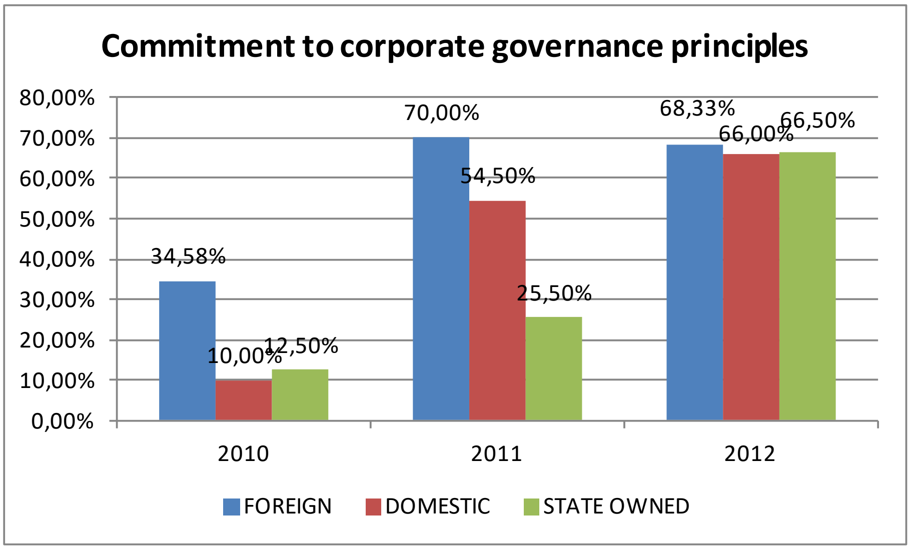

Chart 1: *Commitment to corporate governance principles*

On the Chart 1 it has been shown that foreign owned companies have been more committed to corporate governance principles and have been engaged in implementation of corporate governance systems than domestic and state owned companies. Results also indicate that domestic and state owned companies have improved its commitment to corporate governance principles over the period of three years. This is mainly due to obligation which has been put on them by new Company Law. Through further analysis it has been determined that 50% of foreign owned companies have adopted its own corporate governance codes, which are based on company specific situation, industry and market. While none of the domestic owned and state owned companies have adopted its own company specific corporate governance codes.

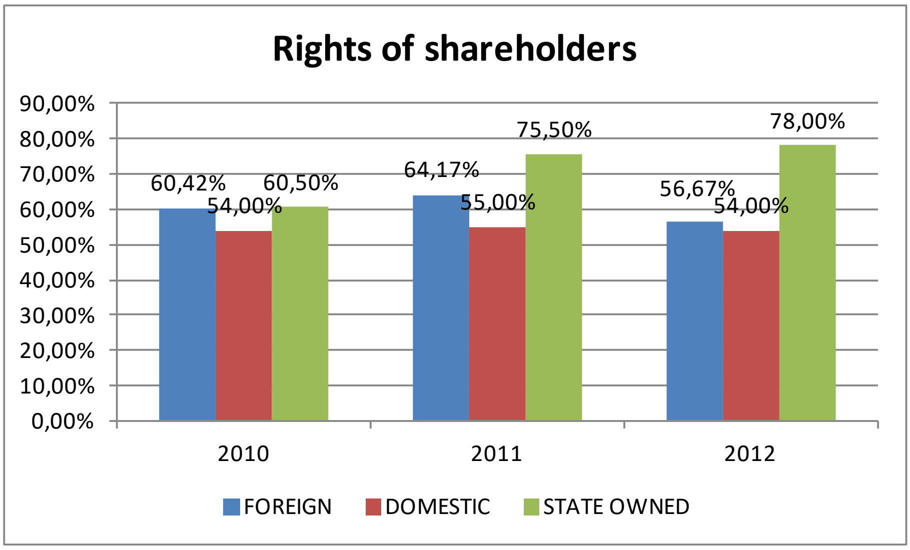

Chart 2: Rights of shareholders

On the Chart 2 it has been shown that state owned companies protect rights of shareholders more than foreign and domestic companies. Further analysis has shown that state owned companies, which have a highest score in protection of shareholders rights, have adopted documents regarding the rights of shareholders as they are required by law, but they do not comply with these rights. Furthermore, appointments of members to the Boards are not publicly announced or are publicly announced but person who would be elected is earlier known.

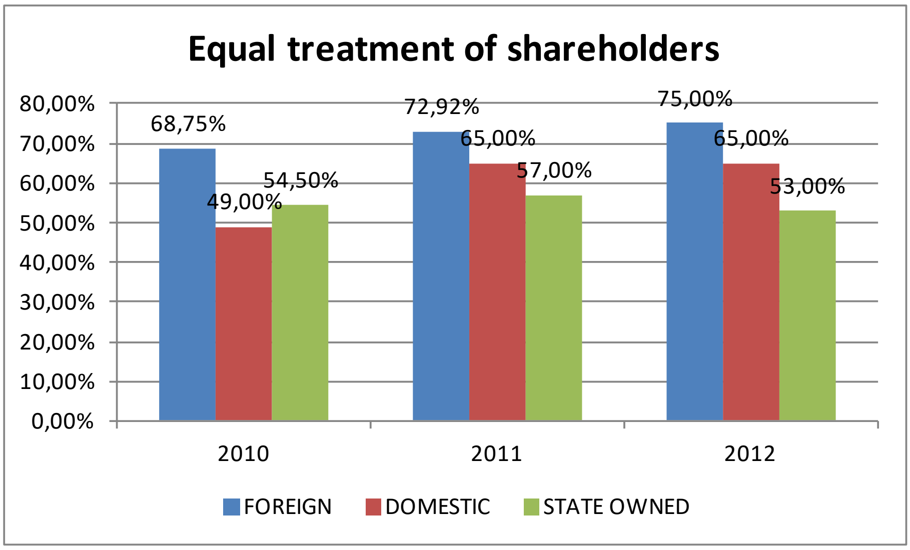

Chart 3: Equal treatment of shareholders

Results from Chart 3 have shown that foreign owned companies have highest score in equal treatment of shareholders, while state owned companies have lowest score. Furthermore, foreign owned companies have adopted procedure for protection and equal treatment of shareholders. While, domestic and state owned companies usually do not have additional internal acts and procedures which protects minority shareholders. Also, most of tested companies have not adopted internal regulations and procedures for the prevention of share trade based on insider information.

These results confirm previous point that state owned companies do not comply with their acts and do not protect rights of shareholders.

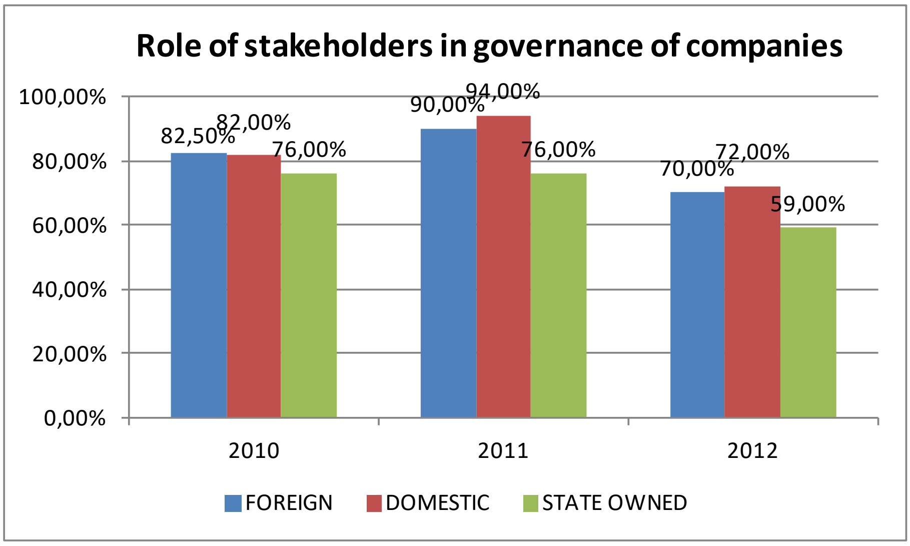

Chart 4: Role of stakeholders in governance of companies

Results from Chart 4 have shown that domestic and foreign owned companies have highest score in area of role of stakeholders in governance of companies, which indicates that they actively cooperate with stakeholders and do take into account interests of the stakeholders. State owned companies rarely cooperate with stakeholders and take into account their interests. Also, in state owned companies there are no clear procedures for disclosure of information to all stakeholders of company. Moreover, tested companies rarely have a person responsible for contact with stakeholders, or this person is not disclosed on companies' web page or annual report.

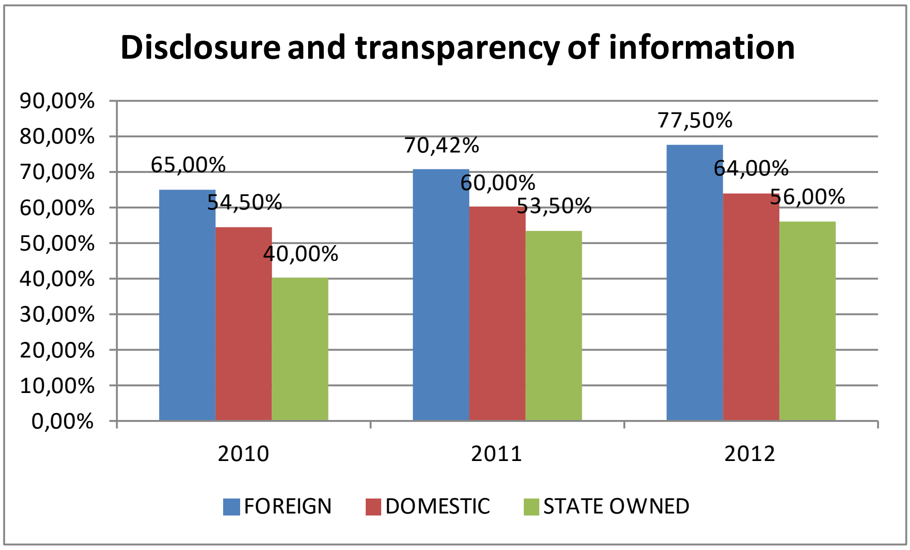

Chart 5: Disclosure and transparency of information

On the Chart 5 it has been shown that foreign owned companies have much better practice of disclosure and transparency of information than domestic and state owned companies. Majority of domestic and state owned companies do not have web-site with up to date information or information available in English. Main issue which has been detected through analysis is that companies only disclose obligatory information which are required by law and do not go further and company with best practices and requirement of OECD principles of corporate governance. Further analysis of results has snow that worst situation is with disclosure of reason why they do not comply with the Standards of Corporate Governance as this is required by these Standards if company do not comply with any standard („COMPLY OR EXPLAIN" principle). Moreover, management board of companies rarely discusses company's compliance with the Standards of Corporate Governance.

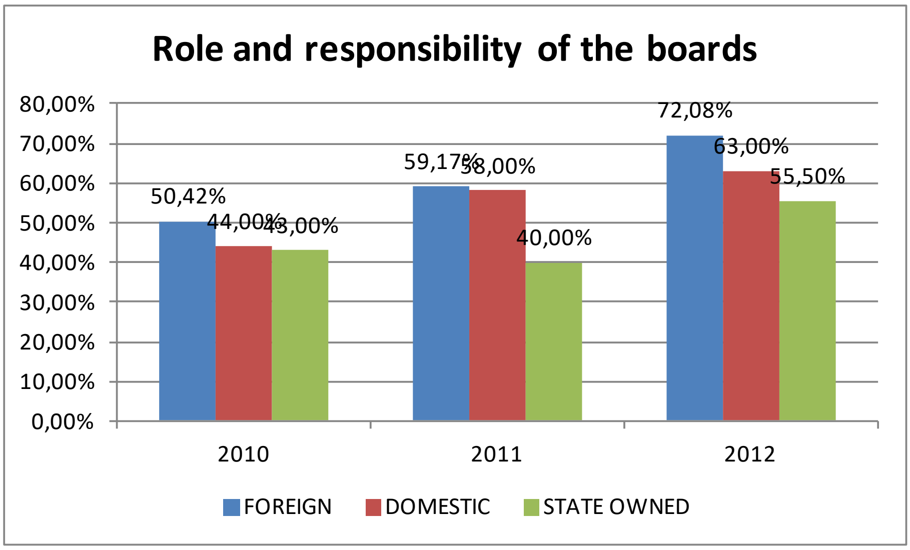

Chart 6: Role and responsibility of the boards

Chart 6 shows that foreign owned companies have highest score in role and responsibility of its boards, while state owned companies have lowest score. These results indicate that foreign owned companies' boards are more responsible in decision making and running a company. Analysis has shown that domestic owned, but mainly state owned companies do not have sufficient number of independent members. Also most of domestic and state owned companies do not have procedure dealing with conflict of interest. Most important issue in this area of analysis is that in most of tested companies board members compensation is fixed and it's not related to company's performance.

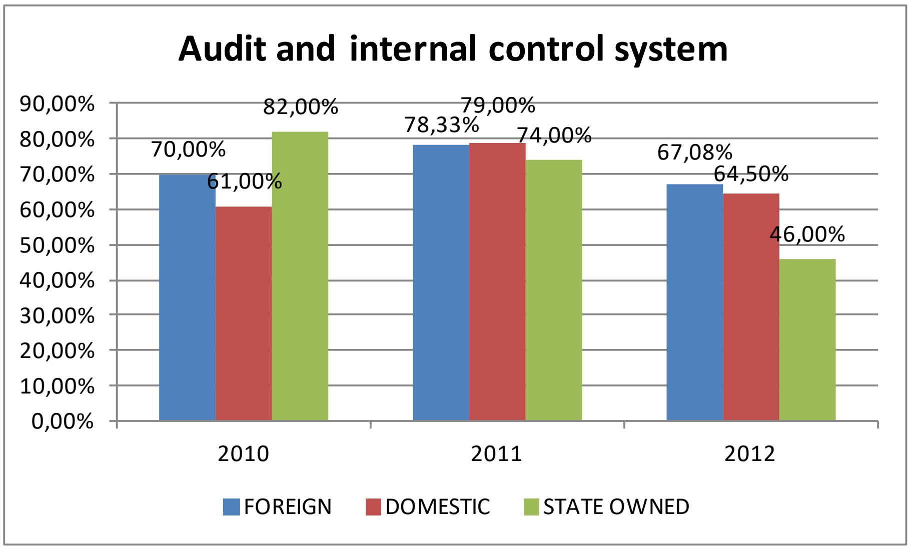

Chart 7: Audit and internal control system

Results from Chart 7 have shown that state owned companies in 2010 have highest score as they were obliged to implement audit and internal control systems. Analysis for 2011 and 2012 have shown that audit and internal control systems was not functioning in state owned companies, while foreign and domestic owned companies have kept its score at almost the same level. Main problem for all tested companies was independence of persons responsible for the internal audit and control. Furthermore, most of tested companies do not have established Risk Management. There is a place for improvement of audit and internal control systems in all three groups of companies.
paper. They should be ranked from general to specific terms.

4. DISCUSSION

Results from Chart 8 and Table 1 have shown that foreign owned companies have highest total score in Scorecard analysis and have best practice of corporate governance. This is due to origin of owners of these companies. Majority of these owners come from developed countries with good system and practices of corporate governance. Therefore, they have incorporated these practices into companies they own in the Bosnia and Herzegovina.

Most of domestic owned companies still do not have a satisfactory level of corporate governance and did not implement system of corporate governance but they do comply, to some extent, with standards and principles of corporate governance.

The worst results have state owned companies which do not have implemented system of corporate governance and do not comply with standards and principles of corporate governance. Results have shown that state owned companies only comply with minimum obligation required by law and do not go further and complay with best practices and requirement of OECD principles of corporate governance.

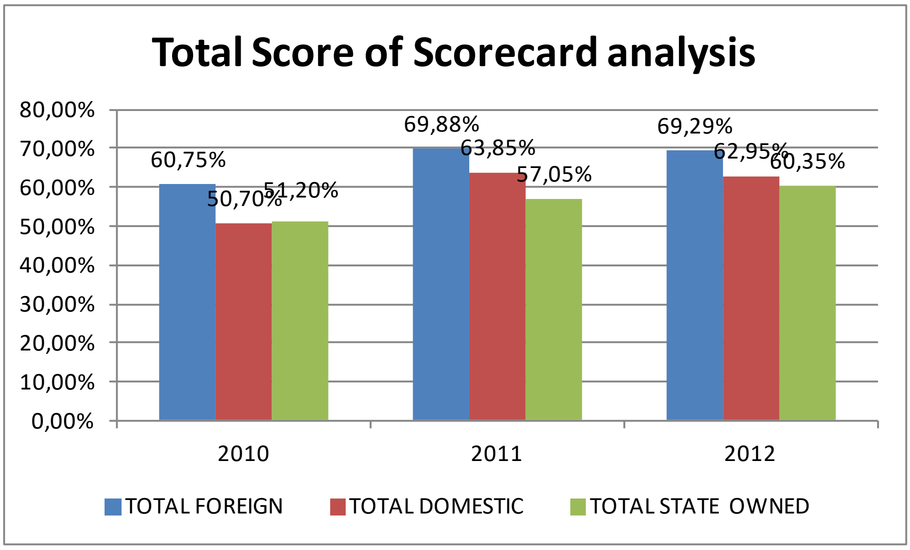

Chart 8: Total score of Scorecard analysis

	Foreign Owned	Domestic Owned	State Owned
Commitment to corporate governance principles	57,64%	43,50%	34,83%
Rights of shareholders	60,42%	54,33%	71,33%
Equal treatment of shareholders	72,22%	59,67%	54,83%
Role of stakeholders in governance of joint stock companies	80,83%	82,67%	70,33%
Disclosure and transparency of information	70,97%	59,50%	49,83%
Role and responsibility of the boards	60,56%	55,00%	46,17%
Audit and internal control system	71,81%	68,17%	67,33%
TOTAL	**66,64%**	**59,17%**	**56,20%**

Table 1: Average corporate governance score for 2010, 2011 and 2013

On average domestic owned companies have total score of 59,17%, while state owned companies have total score of 56,20% which is not on satisfactory level taking into account that companies that apply basic principles of corporate governance should have the score between 65% - 75%.

A low level of implementation and compliance with principles of corporate governance increases business risks, lowers completeness of company and increases investment risks for potential investors.

Legal and Corporate governance framework of the Bosnia and Herzegovina do not encourage companies to do more and therefore companies comply with minimum standards required by the law. Furthermore, companies see these legislations and standards only as an obligation they have to comply with because it's the law but not as way to differentiate themselves from other companies, to build company image and reputation, build investors trusts, attract new investors and raise capital at lower price.

Authors should discuss the results and how they can be interpreted in perspective of previous studies and of the working hypotheses. The findings and their implications should be discussed in the broadest context possible. Future research directions may also be highlighted.

5. CONCLUSION

Results of the Scorecard analysis of implementation of corporate governance practices and principles indicate that there is an obvious correlation and effects that ownership structure of companies has on the level of implementation of corporate governance.
Moreover, results indicate that level of voluntary governance compliance has a connection with firm ownership structure.

A low level of implementation and compliance with principles of corporate governance, in domestic but specially in state owned companies, increases business risks, lowers completeness of company and increases investment risks for potential investors.

There are many segments which should be improved in order to reach satisfactory level of corporate governance, lower business risks, attract new investors and raise capital at lower price. Most important are commitment to the corporate governance standards, rights and equal treatment of shareholders and disclosure and transparency of information.
Improvement in legal framework and companies compliance is obvious strategy which will lead to better corporate governance system, increase in investors trust and decrease in agency problem between controlling and minority shareholders as well as shareholders and managers.

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