

MANAGERIAL STRUCTURE OF BUSINESS GROUPS IN TAIWAN: THE INNER CIRCLE SYSTEM AND ITS SOCIAL ORGANIZATION

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This paper examined the management structure of Taiwan's business groups. The objective was to determine how independent group firms coordinate their business. Employing longitudinal data of the top 100 groups, I investigated the "inner circle" system and its evolution. I found that group leaders occupied overlapped positions at the director rather than at the manager level, which implied a separation of strategic planning and routine administration. Secondly, the dynamics of inner circle management did not hinge upon the group president as in the Korean *chaebol*, nor on the norm of corporate community as in the Japanese *keiretsu*, but on the social ties in the inner circle. Analyzing the background of the leaders indicated that family never dominated the scene even in the early years, and their significance decreased along with environmental changes. The transition in Taiwan in the late 1980s motivated business groups to introduce more "outside" talent into decision-making.

I. INTRODUCTION

BUSINESS groups represent a special type of enterprise organization that can be found in almost every market economy. Researchers have studied this organizational form in mature economies, developing countries, and newly industrialized societies.¹ Although these business groups exhibit slight differences in various contexts, they all share one organizational characteristic—group firms with distinct corporate identities and legal status do not operate as isolated units in the market but forge institutionalized relationships with each other and work coherently as an entity. This quality of "neither market nor hierarchy" raises several issues (Powell 1990). Indeed it is important to determine how independent group firms coordinate their business and also how the decision-making process of the whole group is organized and how the final agreement is reached.

Due to their centrality in business groups studies, Granovetter (1995a) classified these issues under the heading of "authority structure," one of the six key dimen-

¹ For a review, see Goto (1982), Koike (1993), Granovetter (1995a), and Shiba and Shimotani (1997).

TABLE I
ECONOMIC SIGNIFICANCE OF TOP 100 BUSINESS GROUPS IN TAIWAN, 1970–96

Data Year	Number of Business Groups	Average Number of Firms	Number of Employees (1,000)	Business Groups Employee/Total Work Force	Net Sales (NT\$100 Million)	Business Groups Net Sales/ GNP	Governmental Net Sales/ GNP
1970	100	6.25	235	4.96	547	24.16	22.88
1973	111	7.06	277	5.38	1,346	32.81	21.26
1975	106	6.40	286	5.18	1,655	28.23	24.44
1977	100	6.51	300	5.02	2,364	28.70	25.15
1979	100	6.45	313	4.87	3,819	31.93	26.88
1981	100	7.13	308	4.62	5,076	28.77	26.21
1983	96	7.76	330	4.67	6,337	30.13	23.90
1986	97	7.61	335	4.33	8,402	28.72	19.96
1988	100	8.32	375	4.63	12,193	33.76	22.98
1990	101	8.08	397	4.79	16,886	38.27	24.87
1992	101	9.09	436	5.05	18,727	34.42	24.78
1994	115	9.48	489	5.47	27,077	41.95	24.17
1996	113	10.75	577	6.36	33,771	44.79	21.54

Source: *Business Groups in Taiwan, 1998/1999* (Taipei: China Credit Information Service, 1998).

sions he proposed to study business groups.² This paper joined this endeavor by examining the data of Taiwan's 100 largest business groups (*jituan qiye*) compiled in 1973, 1986, and 1994.³ Given the significance of these large conglomerates in various sectors of Taiwan's economy (Tables I and II), the current study not only helped understand the function of business groups as a distinct organizational form and their managerial dynamics, but also Taiwan's economic development in the past thirty years.

Studying business groups in Taiwan also sheds light on the cultural perspective of business organizations (Redding 1990; Fukuyama 1995). The culturalists con-

² The other five dimensions suggested by Granovetter (1995a) are as follows: (1) source of solidarity, (2) extent of moral economy, (3) structure of ownership, (4) role of financial institutions, and (5) relation of groups to the state.

³ The criterion for the top 100 ranking is annual sales (see Appendix A for details of my data sources). As can be seen in Table I, the directory of *Business Groups in Taiwan (BGT)* (*Taiwan diqu jituan qiye yanjiu* compiled by China Credit Information Service in Taipei) did not present data on exact top 100 groups. This was due to the limitation on data collection and economic conditions in different periods. For some years such as 1983 and 1986, the selected groups refused to provide data, which resulted in a smaller sample. For other years such as 1994 and 1996, the groups prospered and many shared the same scale of sales. The directory hence included a larger sample. In spite of these difficulties and unpredictability, the directory has been able to keep the criterion consistent for more than thirty years. Since the objective of this paper was to understand the changes in the management structure of large business groups, I adopted BGT's definition and criterion in data collection and analysis.

TABLE II
TOP TEN INDUSTRIES OF GROUP ENGAGEMENT, 1973, 1986, AND 1994

Top Ten Industries in 1973		Top Ten Industries in 1986		Top Ten Industries in 1994	
Textile mill products	14	Textile mill products	14	Electrical and electronic machinery	15
Food manufacturing	13	Food manufacturing	13	Food manufacturing	12
Chemical matter manufacturing	11	Electrical and electronic machinery	8	Textile mill products	11
Electrical and electronic machinery	7	Chemical matter manufacturing	8	Building construction	6
Wood and bamboo products	6	Nonmetallic products	8	Nonmetallic products	6
Plastic products manufacturing	5	Retail trade	6	Chemical matter manufacturing	6
Basic metal industries	5	Chemical products manufacturing	5	Machinery and equipment	5
Transport equipment	5	Wearing apparel and accessories	5	Transport equipment	5
Chemical products manufacturing	4	Transport equipment	5	Chemical products manufacturing	4
Wearing apparel and accessories	4	Insurance carriers	3	Basic metal industries	4
Other fifteen industries	25	Other twelve industries	23	Other fourteen industries	24
Number of Groups	111		97		115

sider the managerial structure of Chinese business firms as a “cultural artifact” which reflects the core value of the society in which the organizations operate (Redding 1990, p. 143). They explain organizational structure and processes by shared belief and cognition systems. For a few hundreds years, Chinese people have treated family business as a part of the family assets which ought to be maintained within the family and inherited by male descendents. These cultural elements led culturalists to argue that the ownership and management of the Chinese firms were concentrated in the hands of family members (Redding 1990, pp. 143–81).

Moreover, family control persists even when environments change since family members are the only personnel that are trustworthy, and the key positions within corporations must remain in their hands from generation to generation. Fukuyama’s argument clearly reveals this deterministic view of Chinese familism.

What is striking about Chinese industrialization . . . is the very difficulty Chinese family business seem to have in making the transition from family to professional management. . . . There is a very strong inclination on the part of Chinese to trust only people related to them, and conversely to distrust people outside their family and kinship group. (Fukuyama 1995, pp. 74–75)

If the cultural explanation is valid, one would expect to observe the overall and

continuous domination of family members in the key position of Taiwanese business groups. However, as will be shown later, the institutional transformation between 1987 and 1993 triggered significant changes in the composition of the top management team within business groups.⁴ Family members were no longer the dominant group within the managerial population. These changes are difficult to explain by focusing on cultural heritage.

Research on business groups considers not only cultural heritage but also market forces. The market-centered approach to corporate structure suggests the existence of atomized and independent corporations and focuses only on the vertical dimension within the firm.⁵ For example, the central issue of agency theories is to seek institutional arrangements that generate least costs for shareholders to effectively control managers (Fama and Jensen 1983a, 1983b; Jensen and Meckling 1976). Consistent with the atomized assumption, their answers fully rely on market equilibrium. The market for corporate takeover, the capital market and the labor market of managers are treated as major mechanisms for managerial discretion.

Business groups, an enterprise system with firms linked to each other through multiple relationships such as cross-shareholding and leadership overlaps, constitutes a theoretical domain beyond the theory of agency costs (Gerlach 1992, p. 225; Moerland 1995a, 1995b). Should the atomized approach be employed to study business groups, the focus is likely to be directed toward the vertical dimension of managerial control and the essence of horizontal coordination between member firms may be overlooked. As will be demonstrated, the inner circle management, a system built upon an interlocking structure, is crucial to understand the operation of business groups. By ignoring horizontal relationships among corporations, the agency theory lacks proper concepts and methods for this task.

The recent development of the institutional approach in explaining organizations and economic development provides an alternative. In this approach, the focus shifts from static cultural values and atomized actors in the market to the dynamic relationships between institutions and organizations. Scholars in this group have emphasized the effects of regulatory institutions on organizational structure, behavior, and performance (North 1981, 1990; Orrù, Biggart, and Hamilton 1991; Powell and DiMaggio 1991; Scott 1995). Given the "Great Transition" in the late 1980s in Taiwan (Tien 1989), the biggest wave of economic liberalization and political democratization in Taiwan's modern history, one would expect that significant changes in the inner circle management system would have taken place after 1986. As will be illustrated, more professional managers were recruited into the inner circle due to various institutional forces such as deregulation of financial markets and privatization of monopolized industries.

The cultural theories of Chinese familism have been stationary and determinis-

⁴ For a concise introduction of this institutional transformation, see Appendix B.

⁵ For a review, see Barney and Hesterly (1996).

tic, precluding the possibility of cultural change and also effects from other environmental factors such as regulatory institutions. On the other hand, the market-centered approach has been atomized and market-bound. The analytical angle of vertical managerial control overlooks the important horizontal structure and interorganizational practices, which makes it difficult to conduct research on an organizational form such as business group. The institutional approach proposed, with no prior setup of explanatory mechanisms and with emphasis placed on institutional evolution, provides a useful way to study organizational changes. As I will show later, this approach leads to fresh insights that had not been revealed before.

In the next section, I described the inner circle system of Taiwan's business groups. I analyzed the group leaders' structural positions in group management as well as the roles played by the peak office and the presidents' council. Furthermore, I provided a comparison with the managerial structure of the Korean *chaebol* and Japanese *keiretsu* to underscore the uniqueness of Taiwan's system. In Section III, I examined the social organization within the inner circle. I decomposed the inner circle into social categories and analyzed their demographic characteristics over time. The analyses provided substantial reflections on cultural theories and market-centered arguments. I moved the analysis a step further in Section IV. Instead of treating the inner circle system as a homogeneous phenomenon across business groups, I defined a typology of the inner circle system by cluster analysis (Aldenderfer and Balshfield 1984). I then offered hypotheses regarding the relationships between organizational characteristics and types of the inner circle system. Lastly, I summarized the major findings and discuss their implications in Section V, the conclusion.

II. INSTITUTIONALIZED PATRIMONIALISM, CORPORATE COMMUNITY, AND THE INNER CIRCLE

In conceptualizing the authority structure inside business groups, it is appropriate to draw on Granovetter's proposal of a continuum along the dimension of power centralization among group members (Granovetter 1995a, p. 114). At one end of this continuum is the highly hierarchical and consolidated management system, with an organizational device or an individual on top of all group constituencies. At the other end is the loosely coordinated governance body composed of more equal partners; decisions within this body are made through communication and mutual consensus.

Scholars in comparative studies of business organizations have described business groups in two neighboring countries of Taiwan, namely Korea and Japan, as ideal types in this continuum. For example, Biggart (1990) suggested that member firms of a Korean *chaebol* are under tight control of an individual, the group president, *haejang*. The control is so thorough that Biggart described the president as a

patriarch and the management system as patrimonialism. In contrast, companies in Japan's *keiretsu* participate in group-wide affairs by joining the presidents' council. Each company keeps its own privileges and interests, and although there are status differences among firms, relationships are less vertical. Biggart designated this system as "communitarianism." Subsequently, Orrù, Biggart, and Hamilton (1991) referred to the *chaebol* as examples of corporate patrimonialism and the *keiretsu* as a community of firms. Setting the Korean *chaebol* and Japanese *keiretsu* at the two ends of the centralization continuum, Hamilton and his associates (Hamilton 1997; Hamilton and Kao 1990; Orrù, Biggart, and Hamilton 1991) located the management system of Taiwan's business groups in the middle. They suggested that there is less hierarchical control in the *jituan qiye* compared to the *chaebol*, but more coordination than in the *keiretsu*. The major management mechanism inside the *jituan qiye* is not hinged upon a single person such as the group president, nor the community of a president's club, but on a group of closely related core leaders designated by Hamilton as the "inner circle" (1997, p. 265).⁶ These cliques of actors occupy duplicate commanding positions in member firms and set the course of group planning and development. Inspired by this clue, this section examined the leadership overlap among member firms of the 100 largest groups in Taiwan. The significance of this coordination system was illustrated by comparing it to that of the Korean *chaebol* and Japanese *keiretsu*.

According to the 1990 data, the top ten Korean *chaebol* had a total of 303 subsidiaries, and their total sales amounted to 51.64 per cent of GNP (or value added) (Chang 1997). It is amazing to note that the operation of these huge conglomerates is concentrated in the hands of several individuals, the group presidents. The patriarch is able to maintain his ultimate authority over the large number of giant member firms because of three organizational settings: (1) the centralized multi-level ownership structure, (2) the competent group headquarter or secretarial office, and (3) the regular president's council.

As a recent study of the ownership structure of the top forty-nine *chaebol* showed (Chang 1997), the prototypes of the cross-shareholding network inside the group are similar to those of Taiwan's *jituan qiye*. They both have a controlling center on top of the other group components. However, there are two differences: first, less reciprocal equity ties among group firms are found in the *chaebol*. According to Chang's study, only three of the forty-nine *chaebol* have mutual shareholding ties, whereas in Taiwan's case, more cross-shareholding networks have such ties (Chung

⁶ The term "inner circle" was originally coined by Michael Useem (1984) to describe the phenomenon of interlocking managerial positions held by a small group of American elite executives. While the context in Useem's book referred to an interlocking directorate among distinct, independent firms, Hamilton (1997) used the term to delineate the duplicate commanding positions within the group that are held by the founding family. The term "inner circle" hence implied collective actions and class formation of business elites in Useem's work and was more related to the family control of business groups in Hamilton's work and in the current study.

forthcoming). This mutuality dilutes the centralized nature of ownership control, and the extent of this reciprocity is even more significant in the Japanese *keiretsu*. Secondly, there are more intermediary levels in the ownership network of *chaebol*. There is a hierarchical structure even within the controlling center of group equity, and this configuration was labeled “nested hierarchy” by Chang (1997).

In addition to the ownership arrangements, the overall authority of the patriarch is supported by an organizational device, the central (or secretarial) office of the group. The staff in this office performs extensive functions in research, strategic planning, recruitment and training, and financial auditing and appraisal of subsidiaries (Kang 1997; Steers, Shin, and Ungson 1989). While each member firm still has an operational autonomy, the supervision is comprehensive. Biggart (1990, p. 129) mentioned that a rigorous annual review of executives of member firms is conducted by the central office. The CEO could be discharged if the profit goal is not reached.

The third institutional mechanism for the group administration in the *chaebol* is the presidents’ council. Unlike its counterpart in the Japanese *keiretsu*, the setting of the periodical meeting is authoritarian. It not only provides an occasion for business coordination but also for the group president to confront firm executives face-to-face. Steers, Shin, and Ungson (1989, p. 39) offer a vivid description:

“The meeting of group presidents often serves to impress on the presidents that the distance between them and the group chairman is as great as the distance between them and the new recruits. . . . And they all, even those who are formerly ranking government officials or comrades of the founding group chairman, must stand at attention when the group chairman enters the meeting room, even though he may be only in his thirties.” . . . The chairman calls on each president by name, asks a series of questions concerning corporate activities, and settles pressing issues on the spot.

At the other end of the centralization continuum is the Japanese *keiretsu*. As pointed out earlier, the basis for the system of corporate community is extensive mutual shareholding. This reciprocal ownership structure not only links the fate of different group firms together but also gives them more equal standing in terms of group decisions. Futatsugi (1986, pp. 28–29) studied the internal equity structure of the six largest *keiretsu* in Japan and revealed the existence of significant reciprocal shareholding. In the example of Sumitomo, its fourteen members create ninety-one possibilities of reciprocity in ownership $[(14 \times 13) / 2 = 91]$, and Futatsugi located seventy-three of them, in other words, 80.2 per cent. This percentage is also significant in other business groups, such as 46.3 per cent in Mitsui and 57.4 per cent in Mitsubishi. These numbers indicate the existence of much denser reciprocal shareholding in the Japanese *keiretsu* than in the Korean *chaebol*, which constitutes the basis for a more communitarian system of group coordination.

In terms of commanding authority, member firms in the *keiretsu* not only are

legally independent but also managerially autonomous. There is no formal authority relationship among member firms, not to mention a position such as the group president. There is neither a central office supervising business strategies nor monitoring firm performance. The coordination of group members largely relies on interlocking directorates and the president's council (Gerlach 1992, pp. 103–59). Nevertheless, the format of the president's meeting is essentially different from that of *chaebol's*. First, the meeting is not chaired by the same person each time but on a rotation basis. Secondly, the atmosphere is more one of "camaraderie" than authoritarian compared to the meeting in a *chaebol* (Gerlach 1992, p. 107).

The uniqueness of the so-called inner circle system in Taiwan's *jituan qiye* is clearly revealed by comparing it to the patrimonialism in the Korean *chaebol* and the corporate community in the Japanese *keiretsu*. The collective coordination of Taiwan's business groups lies not in the patriarchal supremacy nor the community consensus, but in a set of core leaders who occupy duplicate leadership positions in various group firms. The following analysis provides evidence by first, locating the administrative level at which the overlap occurs and then by analyzing the details of the leadership duplication. For the first purpose, a concentration ratio was constructed to capture the degree of position overlap. The ratio was calculated as $1 - [(\text{number of persons})/(\text{number of positions})]$. The ratio hence ranged between 0 and 1, and the higher the ratio, the more position duplicates. I examined two levels of leadership, the chairman of the board of directors (Tung Shih Chang) and the chief executive (Tsung Ching Li), the two most important positions in company management. The former is the legally designated governance body and the only legal representative of the corporation, according to Company Law of Taiwan (Ke 1995, pp. 167–70). The chairman has the privilege to oversee the business administration of the whole corporation and sign contracts with external parties. This chairman also incurs legal liability for his behavior on behalf of his company. The general manager (Tsung Ching Li), only one level lower than the chairman in company charts, executes and administers plans and decisions from the chairman and supervises all the divisions and personnel of the company.

Table III shows the descriptive statistics of 323 group-years, which comprises 2,560 individual-years of presiding director and 2,242 individual-years of chief manager. My first observation was that for all three periods, the overlap at the director level was more than twice frequent than that at the manager level. Secondly, the variation among the top 100 business groups also remained constant over time at both levels. These facts suggest that the overlap, hence the group coordination, is centered around the duplication of presiding directors more than around that of general managers. This implies a separation of strategic planning and general administration in Taiwan's business groups, and the former is where the group coordination is located. Chairing the board of several member firms not only enables the group leaders to have access to the information about various member firms but

TABLE III
CONCENTRATION RATIOS OF BUSINESS GROUP LEADERSHIP IN 1973, 1986, AND 1994

	Year	Number of Groups	Mean	Std. Dev.	Min.	Max.
Presiding director (Tung Shih Chang)	1973	111	0.46	0.21	0	0.86
	1986	97	0.48	0.23	0	0.89
	1994	115	0.45	0.22	0	0.91
Chief executive (Tung Ching Li)	1973	111	0.21	0.21	0	0.83
	1986	97	0.24	0.24	0	0.86
	1994	115	0.17	0.20	0	0.80

also to influence company decisions from the viewpoint of the whole group. Moreover, this pattern did not change significantly when the scale of business groups, hence the complexities of group coordination, increased in later years (see Table I).

The statistics in Table III demonstrate the condition of leadership overlap from a global perspective. In other words, there is no distinction between the individual background of the directors and the managers who occupy duplicating positions. To further examine the overlap formed by the so-called inner circle, I analyzed the data from the viewpoint of individuals. The central issue was to identify how influential the inner circle is. The directory of *Business Groups in Taiwan (Taiwan diqu jituan qiye yanjiu)* provides a list of "core leaders" for each business group that the group firms themselves identified. For 323 group-years in 1973, 1986, and 1994, a total of 1,010 individual-years of core leaders were listed (323 key persons plus 687 other core leaders, see Appendix A for details). This list is considered to include the members of the inner circle in this study and is cross-checked with the names of chairing directors and general managers of each member firm. Table IV summarizes the analysis.

The first row of Table IV indicates the growth of the average number of group members from 7 to 9.6 from 1973 to 1994, associated with the corresponding increase of variation within the top 100 groups. With this trend of enterprise expansion and diversification, we observed more core leaders that business groups themselves reported. These inner circles, in aggregate, occupied substantial chairman positions. On the average of the whole 100 groups, the core leaders presided over 65 to 75 per cent of all the member firms; each of them served as chairman of the board for more than two firms. For extreme cases, core leaders presided over as many as sixteen firms in 1973 and thirteen firms in 1994. The same ratio was consistently lower for all three years in terms of overlap at the general manager level. On the average, core leaders only administered 27 to 35 per cent of the group firms. For 1994, some of the core leaders did not even serve in one firm as general manager, and this led to a value of 0.77 for the average managerial positions occupied

TABLE IV
THE INNER CIRCLE IN THE LEADERSHIP OF TAIWAN'S BUSINESS GROUPS, 1973, 1986, AND 1994

Variable	Year	No. of Groups	Mean	Std. Dev.	Min.	Max.
Number of group firms	1973	111	7.04	4.38	3	27
	1986	97	7.70	5.85	3	38
	1994	115	9.57	6.35	3	34
Number of core leaders	1973	111	2.50	1.14	1	6
	1986	97	3.19	1.96	1	11
	1994	115	3.67	2.00	1	9
Total chairs by core leaders	1973	111	5.00	2.77	2	16
	1986	97	5.77	4.16	1	30
	1994	115	6.19	4.29	1	23
Average chairs per core leader	1973	111	2.37	1.91	0.5	16
	1986	97	2.34	1.80	0.5	9
	1994	115	2.16	1.91	0.2	13
Total managers by core leaders	1973	111	2.43	1.71	0	9
	1986	97	2.66	2.22	0	12
	1994	115	2.63	2.17	0	10
Average managers per core leader	1973	111	1.06	0.86	0	5
	1986	97	1.01	0.95	0	5
	1994	115	0.77	0.63	0	3
No. of firms' core leaders as shareholders	1973	111	5.75	3.17	1	18
	1986	97	4.36	2.76	0	17
	1994	115	3.90	2.82	0	13
Average shareholderships per core leader	1973	111	4.16	1.89	1	11
	1986	97	3.20	1.78	0	8
	1994	115	2.28	1.85	0	9
Proportion of group employees controlled by core leaders	1973	102	0.87	0.19	0.02	1
	1986	97	0.90	0.15	0.22	1
	1994	114	0.83	0.23	0.02	1
Proportion of group total assets controlled by core leaders	1973	111	0.87	0.17	0.37	1
	1986	95	0.91	0.12	0.38	1
	1994	115	0.84	0.23	0.03	1

by one core leader. It is clear that the members of the inner circle in Taiwan's business groups coordinate group business by assuming duplicate chairman positions in various group firms. Such a model of supervision is made possible by their lower participation in the routine management of daily affairs.

The following rows of Table IV point out the extensive shareholdership that core leaders occupy among group firms. For 1973, members of the inner circle as a whole, on the average, owned equity in 80 per cent of the subsidiaries, and each of them held shares of 4.2 group constituents. The trend seems to have become less significant in 1994 when only 41 per cent of the group members had at least one core leader listed as major shareholder. This number, however, is misleading due to the fact that institutional shareholders were to play a major role in group ownership in later years. In my companion study (Chung forthcoming), I examined the ownership networks of eighty-three groups in 1994 and identified 131 companies as control centers in the ownership structure. By surveying the background of individual shareholders of these 131 companies, I found that in 73 per cent of them, at least one core leader was listed as major shareholder.⁷ It is therefore reasonable to argue that the overlap of core leaders in the presiding director position is upheld by their duplicate shareholding of the group firms. This gives a picture of an owner-director system in the management of Taiwan's business groups. In the last part of Table IV, the aggregate number of employees and amount of total assets of the firms that are chaired by the core leaders are listed. Although these core leaders presided over 65 to 75 per cent of the group firms, the group resources under their control reached 84 to 91 per cent, which indicates that most of the central units, the most important flagships within a group, were controlled by the inner circle.

The inner circle management system described above is essentially different from that in the Korean *chaebol* and Japanese *keiretsu*. First of all, the official position of the group president, *haejang* is far less institutionalized in Taiwan's *jituan qiye*. Except for a few cases, there is no such title attached to any of the core leaders (*Business Groups in Taiwan*, 1974, 1988/89, and 1996/97 editions), which implies a less formal and hierarchical relationship among *jituan qiye*'s members. Although this condition is closer to the Japanese *keiretsu*, the chairman overlap creates more coordination among member firms of the *jituan qiye*. Secondly, in contrast to the omnipotent headquarters of the Korean *chaebol*, the group office in Taiwan's business groups acts more like a staff whose major function is to collect and disseminate relevant information and provide services such as personnel training, financial consulting, and law and public-relations management to group members. According to a survey of thirty-two group headquarters in 1990 (Chen 1991), the central office participates in member firm's personnel affairs through the creation of a com-

⁷ The directory of *Business Groups in Taiwan (BGT)* reports a list of major shareholders in each member firm. While *BGT* did not record the percentage of shareholding until 1990, the data of the 1,100 group firms and their 5,577 shareholders reported in the 1994 version showed that on the average, the directory listed 5.07 shareholders for each firm (with a minimum of 1 and maximum of 24) and that these shareholders owned 75 per cent of the firm stock (around 15 per cent for each shareholder). These numbers confirmed that the major shareholders reported in the directory owned a dominant part of the stock.

mon personnel code and by offering basic training, but not input for recruiting or releasing specific individuals. For company finance, group offices usually conduct financial analyses and auditing for group members and they also handle fund transfers inside the group. However, each constituent keeps its independent accounting system without interference from the office (Hamilton and Kao 1990, p. 147). Group staff is also active in mediating the relationships between the group and the general public. Legal consultation and image promotion of member firms are usually taken care of by the central office. In summary, the peak offices in Taiwan's business groups are never as authoritarian and supervisory as their counterparts in the Korean *chaebol*, but their existence provides more linkages among group members than those in the Japanese *keiretsu*.

For some *jituan qiye*, there is also a similar organizational device to the president's council in the *chaebol* and *keiretsu*. However, the major difference lies in the participants and agendas of this regular meeting. The membership is more comprehensive, including not only the presidents but also the managers and other high-ranking officers of member firms (*Business Groups in Taiwan*, 1996/97 edition). However, the issues discussed are more administrative than strategic. As pointed out by Chen's survey, these meetings are forums for general routines of common concern among group members, while group-level policies and tactical planning are still concentrated within a few core leaders (Chen 1991, p. 57). Provided that member firms have substantial autonomy in production and marketing from their headquarters, and the president's council is de facto the "administrator's council," the ultimate decisions in the *jituan qiye* largely depend on the members of the inner circle who occupy duplicate chairman positions within the group.

So far, I have delineated the essential configuration of the inner circle system. Based upon these findings, the decision dynamics within the Taiwan's business groups is not hinged upon the psychological characteristics of *haejang*, as in the case of the pyramid of the Korean *chaebol*, nor on the norm or corporate culture in the firm community of the Japanese *keiretsu*, but on the social relationships among the members in the inner circle. The composition of the core leaders and the way they are related to each other are essential to understand the management practices within Taiwan's business groups. The next section provides a further analysis of these issues.

III. THE SOCIAL ORGANIZATION OF THE INNER CIRCLE

In addition to the social structure of the inner circle, scholars have pointed out that the demographic characteristics of high-echelon management teams exert significant effects on corporate strategies, structure, and performance (Hambrick and Mason 1984; Pfeffer 1983; Smith et al. 1994). Studying the social composition and demographic attributes of the inner circle not only enables to understand the authority

structure of Taiwan's business groups but also other types of organizational behavior and outcomes. This section analyzes the inner circle of Taiwan's top 100 business groups including 1,010 individual-years of core leaders. I first categorized these core leaders into several social groups and then investigated their demographic characteristics such as age, gender, and education. I then determined how the non-family core leaders were associated with the groups. These analyses clarified the cultural argument and showed the significant effects of institutional transformation.

The data presented here are mainly coded from the directory of *Business Groups in Taiwan*. I, however, supplemented these data from various biographical sources (see Appendix A for details). Based upon this extensive survey, I identified four categories of core leaders that compose the inner circle as follows. (1) The key person, who plays the pivotal role in the management of the whole group. Most of these individuals are founding entrepreneurs. A few are core family members such as sons, and this is most likely when the founders are old or have already passed away. I coded other categories of core leaders according to their relationships to the key person. (2) Family members, in the 1974 and 1988 editions of *Business Groups in Taiwan*, core leaders who are family members, both core and extended family, of the key person were described in the text. In the 1996 version, a more complete family tree was provided. In total, I identified fourteen types of family relationships such as parents, parents' brothers or sisters, spouses, brothers, sisters, brothers-in-law, sisters-in-law, brothers' sons, sons, daughters, sons-in-law, daughters-in-law, cousins, and so on. (3) Business partners, who are co-investors, entrepreneurial partners, and business associates of the key person. These core leaders are not related to the key person in terms of blood or marriage, and have been working with the key person since the early stage of the group development. (4) Long-term employees, who are neither family members nor business partners of the key person, but are recruited from external labor markets after the groups were established. However, in order to be considered as a member of the inner circle, these employees usually have served in the business groups for a long time. These career paths are usually indicated in the data sources (see Appendix A).

Table V lists the proportion of family members, business partners, and long-term employees in the inner circle of the 323 group-years. My first observation is that family members did not dominate Taiwan's business groups as comprehensively as the culturalists stated. They accounted for around 60 per cent of the inner circle in 1973 and 1986, and this percentage decreased to 53 in 1994. The numbers challenge the orthodox argument of Chinese familism. Family members never controlled the whole decision-making process of business groups from the early years, and their significance decreased after 1986. Secondly, we can see the decreasing trend of business partners and a significant increase in the number of long-term employees in later years, especially in 1994. These statistics reveal the effects of

TABLE V
THREE COMPONENTS OF THE INNER CIRCLE IN 1973, 1986, AND 1994

	Family Members (%)	Business Partners (%)	Long-Term Employees (%)	Total
1973	62	29	9	166
1986	63	19	18	212
1994	53	13	37	309

Note: N = 687.

the institutional environment on organizations. The political democratization and economic privatization initiated in 1987 triggered dramatic changes in the contexts in which business groups were embedded (see Appendix B for details).

First, the deregulation of financial industries and the opening-up of capital markets intensified the need for international standards of corporate governance (Useem 1998). Professional managers, rather than family members and business associates, became the leading indicators appealing to foreign investors. Next, new tax incentives brought in more foreign investment and multinational companies which increased the level of international competition and accelerated the trend for professional managers. Thirdly, liberalization of monopolized industries and privatization of state-owned enterprises created unprecedented opportunities for business groups to step into lucrative industries such as banking and telecommunication. Participation in these industries, however, required managerial talents with different types of training, perspectives, and mindsets. Furthermore, due to the ambiguity and uncertainties induced by democratization and other institutional changes, decision-making became more complicated than before.

The previous authority structure dominated by family members and entrepreneurial partners might not have been able to cope with the new environmental trends, managerial complexity, and fast-changing contexts since they tended to share similar psychological makeup and personality traits by living or working together since the beginning. New executive talent became necessary for groups to continue prospering. A reasonable organizational response was to enlarge the pool from where the core leaders were recruited. As a result, the number of family members and business partners decreased and more professional managers were introduced into the inner circle.

I next examined the demographic characteristics of the core leaders. In terms of age, I found that for all three years, the average age of the key persons was almost identical with that of the business partners. This implies that the same-year cohort was an important structural constraint for entrepreneurship and business cooperation in all three periods. I also noticed that family members were the youngest among the four categories. On the average, they were eleven to thirteen years younger

TABLE VI
EDUCATIONAL BACKGROUND OF THE INNER CIRCLE IN 1973, 1986, AND 1994

(%)

Year	Education Level	Key Persons	Family Members	Business Partners	Long-Term Employees
1973	Junior high	26	22	25	—
	Senior high and professional	45	39	52	33
	College	29	39	23	53
	Graduate school	—	—	—	13
	Total number	109	101	48	15
1986	Junior high	22	6	21	—
	Senior high and professional	32	24	58	27
	College	46	51	21	63
	Graduate school	—	19	—	10
	Total number	96	132	38	40
1994	Junior high	14	8	3	—
	Senior high and professional	19	18	38	7
	College	49	46	58	63
	Graduate school	18	29	3	30
	Total number	113	160	40	104

Note: N = 1,010.

than the key persons and business associates. Entrepreneurs tended to recruit younger family members such as younger brothers, sons, and nephews rather than the older generations into their enterprises. Fathers (or fathers' brothers) seldom worked as partners or subordinates in their sons' corporations. There was an intentional alignment of authority in the workplace with that inside of the Chinese family. Another closely related characteristic was gender division. As expected, only about 3 per cent of the inner circle were females among the 1,010 cases. Most of them were either spouse or daughter of the key person. It is clear that the role of females in Taiwan's business world depended upon their husbands or fathers. Very few of them worked independently as the key person, business associate, or long-term employee in business conglomerates.

The third characteristic I examined was core leaders' educational background. I coded the data into four educational levels and presented the results in Table VI.

My first finding was that the educational credentials of the family members and long-term employees were higher than those of the key persons and business associates, presumably due to the effect of age cohort. These two categories of leaders were born later when the modern education system in Taiwan became more developed than during the period when key persons and business associates were born. It may be also due to the process of "professionalization" of family members in Taiwan's business families. Founding entrepreneurs are inclined to prepare their

TABLE VII
SOCIAL TIES OF NON-FAMILY LEADERS TO GROUP FOUNDERS IN 1973, 1986, AND 1994

	Locality Ties (%)	School Ties (%)	Either (%)	Total
A. Business partners				
1973	65	8	67	48
1986	70	8	73	39
1994	43	23	62	40
B. Long-term employees				
1973	60	13	60	15
1986	35	20	53	40
1994	20	10	27	104

Note: N = 286.

younger generation by higher education. Even as early as 1973, we found that almost 40 per cent of the family members had a college degree. This trend has continued to later years, and in 1994, about 30 per cent of the family members had a graduate degree. A substantial number of them earned MBA degrees in Japan and in the United States. Lastly, long-term employees were always the best educated among the four components. In 1973, when none of the other categories owned a graduate degree, 13 per cent of the employees had graduate-level training. In 1994, 93 per cent of them had college or graduate degrees, compared to 75 per cent of family members. Educational credentials became a necessary condition for an “external” employee to be considered as an insider in Taiwan’s business groups.

Lastly, I investigated how non-family core leaders were socially related to the key person and presented the outcome in Table VII.

At least until 1986, 50 to 60 per cent of the long-term employees came either from the same locality of or were schoolmates of the entrepreneurs, and then the percentage decreased to 27 in 1994. This trend clearly showed the influence of institutional forces. The percentage of professional managers without preexisting social ties increased abruptly from 1986 to 1994, at the time when a major transformation in Taiwan’s social institutions took place. However, the new institutional environment did not completely remove the strength of social connections. I found that the social ties were still important at the business associate level. More than 60 per cent of the partners had preexisting ties to the entrepreneurs even after the transition. In other words, in terms of organizational management, changing institutional and market conditions led to the need for professional executives, but in terms of co-investment and entrepreneurship, trust and social embeddedness remained crucial in an uncertain environment (Granovetter 1995b).

IV. TYPOLOGY OF THE INNER CIRCLE

I have analyzed the 1,010 individual-years of core leaders as a whole. I identified major social categories within the inner circle and examined the evolution of their demographic characteristics. I also outlined how non-family core leaders were related to founding entrepreneurs. I moved a step further in this section. Instead of treating all the core leaders as a homogeneous class, I analyzed the inner circle in terms of individual groups. I first identified types of the inner circle system for business groups. The criterion adopted was the proportion of different social categories of core leader in the group. I secondly linked these management types to other group characteristics such as number of employees, total assets, group age, and industrial participation. I also cross-checked with individual characteristics, for example, the founders' age, education, and ethnic background. While a multinomial logit regression is likely to be unstable due to the limited number of cases in certain types, cluster analysis generates testable hypotheses for the relationships between the social composition of the inner circle and the structure of the group.

I calculated the proportion of the following five categories of core leaders in each group: family member, business partner with social ties, business partner without social ties, long-term employee with social ties, and long-term employee without social ties. For this, groups that only reported one core leader (usually the group founder) in the inner circle or contained missing data were excluded, leaving a sample size of 234 group-years. For each of these 234 cases, I computed the proportion of the core leaders (except for the founder) along the five social dimensions. I hence obtained a matrix with 234 rows and 5 columns. A cell value in the matrix represents the proportion of a specific type of core leader in the corresponding group. In order to identify the type of inner circle by its social composition, this matrix was subjected to a hierarchical clustering procedure, to assemble business groups with a similar proportion in all the five social categories. I used a dissimilarity (distance) measure to determine the degree of closeness between each pair of groups. Euclidean distance was adopted as the unit of measurement, and the average linkage algorithm was used as the clustering method (Johnson and Wichern 1998, pp. 726–99). The results are presented in Table VIII.

What we first noticed was that the “family-dominant” inner circle system, in which 96 per cent or more of the constituents were family members, never completely prevailed in the Taiwanese business world. Even as early as 1973, only 67 per cent of our sample belonged to this type; and in 1994, this percentage decreased to 55 per cent. There are other types of inner circle systems such as those dominated by business partners, those dominated by employees, and those by a mixture of family members and partners or employees. The results of this clustering corroborated those presented in Table V and contradicted the prediction of dogmatic

TABLE VIII
 TYPOLOGY OF THE INNER CIRCLE, 1973, 1986, AND 1994

Major Types Identified	Average Proportion of Five Social Categories in the Inner Circle					Number and Percent- age
	Family Member	Partner with Ties	Partner without Ties	Employee with Ties	Employee without Ties	
1973						
Family-dominant	0.96	0.04	0	0	0	56 (67)
Tied partner-dominant	0.02	0.90	0.06	0	0.02	14 (17)
Mixed	0.49	0	0.23	0.25	0.03	8 (10)
Partner-dominant	0	0	1.00	0	0	6 (7)
Total						84 (100)
1986						
Family-dominant	0.98	0.01	0.01	0	0	37 (55)
Tied partner-dominant	0.18	0.79	0	0.02	0.01	12 (18)
Tied employee and family	0.42	0.03	0.04	0.50	0.01	9 (13)
Family and employee	0.55	0	0	0.03	0.42	9 (13)
Total						67 (100)
1994						
Family-dominant	0.98	0	0	0	0.02	47 (55)
Employee-dominant	0.09	0.02	0.05	0.02	0.82	17 (22)
Tied employee and family	0.36	0.15	0	0.43	0.06	12 (14)
Family and employee	0.48	0	0.12	0	0.40	7 (8)
Total						83 (100)

Note: N = 234.

culturalists. One interesting observation regarding industrial characteristics was that this “family-dominant” type seemed to be more prevalent in domestic-oriented industries (Table IX). One may hypothesize that groups operating in export sectors are more likely to recruit managerial talent outside the family boundaries due to international competition.

The second largest type in 1973 was that dominated by business associates with social ties. On the average, 90 per cent of the core leaders in this type were partners of the founders and were socially associated. As shown in Table IX, an interesting group characteristic for this inner circle type was the low percentage of Taiwanese entrepreneurs. In 1973, the population ratio of Taiwanese to Mainlanders was 80 : 20 but for entrepreneurs in this type, it was only 57 : 43. In other words, the mainlander entrepreneurs, compared to their Taiwanese counterparts, were more likely to include tied partners into the inner circle. A plausible hypothesis is that for these immigrant entrepreneurs, extended family members were limited compared to those of their Taiwanese counterparts, and business associates were the trust-worthiest candidates.

In the 1973 sample, there was also a “mixed” type of inner circle system which comprised family members, business associates without ties, and socially connected

TABLE IX
 TYPOLOGY OF INNER CIRCLE AND AVERAGE GROUP CHARACTERISTICS

Major Types Identified	Key Person Characteristics			Group Characteristics			Characteristics of Industrial Participation					
	Age	Univer- sity	Taiwan- ese	Employ- ee	Assets	Group Age	Construc- tion/ Real Estate	Manufac- turing Domestic- Oriented	Manufac- turing Export- Oriented	Retail/ Whole- sale	Services	Total
1973												
Family-dominant	56.8	0.18	0.90	2,477	1,256	17	1	42 (71)	10 (59)	2	1	56 (67)
Tied partner-dominant	57.9	0.35	0.57	1,899	1,101	18	0	8 (14)	4 (24)	1	1	14 (17)
Mixed	58.1	0.43	0.63	6,341	5,408	16	0	5 (8)	2 (12)	0	1	8 (10)
Partner-dominant	51.8	0.17	0.50	1,604	824	15	0	4 (7)	1 (5)	0	1	6 (7)
Total							1	59 (100)	17 (100)	3	4	84 (100)
1986												
Family-dominant	63	0.43	0.89	4,365	11,622	28	0	27 (56)	4 (44)	4	2	37 (55)
Tied partner-dominant	61	0.25	0.83	1,068	3,526	25	0	8 (17)	3 (33)	1	0	12 (18)
Tied employee and family	66	0.44	0.77	5,689	9,476	33	0	7 (15)	1 (11)	1	0	9 (13)
Family and employee	54	0.44	0.88	3,003	13,205	24	0	6 (12)	1 (11)	1	1	9 (13)
Total							0	48 (100)	9 (100)	7	3	67 (100)
1994												
Family-dominant	63	0.60	0.85	5,515	57,710	34	1	29 (69)	10 (42)	1	6	47 (55)
Employee-dominant	54	0.88	0.71	2,389	24,723	27	5	3 (7)	7 (29)	1	1	17 (22)
Tied employee and family	61	0.72	0.83	4,402	59,107	31	0	7 (17)	4 (17)	0	1	12 (14)
Family and employee	59	0.43	0.71	3,027	60,503	32	0	3 (7)	3 (12)	0	1	7 (8)
Total							6	42 (100)	24 (100)	2	9	83 (100)

Note: Figures in parentheses are percentages.

employees. One distinct organizational characteristic associated with this system was its large size in terms of number of employees and total assets. One possible explanation would be that the extra need of financial sources forced the entrepreneur to recruit partners outside his immediate social circle. The last system in 1973, "partner-dominant," consisted of business partners at a rate of 100 per cent. Again, one sees relatively fewer Taiwanese founders in this category, and they were also younger than those in other system types. One might postulate that there was a cohort effect in terms of business cooperation: younger generations could work more easily with partners without ascribed social affinity.

In 1986, "family-dominant" and "tied partner-dominant" were still the two largest types of the inner circle system. However, employees, with or without social ties, started participating with family members in group decisions. As shown in Table IX, an outstanding characteristic of the "family and employee" type was that the entrepreneurs were younger. It seems that younger entrepreneurs were more likely to trust "outside" long-term employees, and this was less due to the educational differences of the age cohorts.

In the 1994 sample, the most noticeable change was that employees had replaced business associates to become the second most important players in the inner circle. Consistent with my institutional argument, the significance of business associates in the inner circle has decreased in recent years. Compared to 1986, three of the four 1994 types were the same, as was the ranking order. The only difference was that the "employee-dominant" type took over the position of the "tied partner-dominant" type. The outcome was that no major type in 1994 contained a substantial proportion of business partners. For the groups in the "employee-dominant" type of 1994, family members comprised only 9 per cent of the core leaders, and employees without social ties comprised 82 per cent. Entrepreneurs in these groups were generally younger and better educated than those in the other types. The average group age was twenty-seven, the youngest among the four types. Groups in this type were also disproportionately concentrated in the export-oriented industries.⁸ While in all three years the groups in the exporting sectors tended to include a lower percentage in the family-dominant type and higher percentage in other types, in 1994 we observed the largest difference (69 per cent vs. 42 per cent and 7 per cent vs. 29 per cent). A reasonable hypothesis is that younger entrepreneurs with a higher education level who started their business later in export-oriented industries were more likely to establish non-family-dominant business groups, especially after 1986. They were inclined to promote core leaders from the internal labor market of the group, and in this internal market, ascribed social attributes were less important. This implied that the institutional deregulation between 1987 and 1993 had triggered a higher level of international competition which motivated the busi-

⁸ See Appendix A for how I determined whether an industry was export-oriented.

ness groups to include more “professional managers” into the decision-making process.

V. DISCUSSION AND CONCLUSION

In the first part of this paper, I defined the inner circle system of Taiwan’s *jituan qiye* by a comparison with the management configuration in the Korean chaebol and Japanese *keiretsu*. The comparative analysis revealed that the ways the members of the inner circle were related to each other were essential to understand the managerial dynamics within the group. I secondly analyzed the composition and attributes of the inner circle and their changes in 1973, 1986, and 1994. Furthermore, I developed a typology of the inner circle and proposed a hypothetical association between the types identified and other group characteristics. These analyses challenged the deterministic cultural argument and the market-centered approach, and demonstrated the usually understated institutional influences in organizational changes.

The cultural argument in the current studies of East Asian enterprises has been oversimplified and static. For Taiwanese business groups, Fukuyama (1995) argued that family members, most likely the entrepreneurs and core family, did not trust outsiders and thus dominated most of the decisive positions of the groups. However, the evidence provided failed to distinguish family members and non-family members, such as business associates and long-term employees, in the inner circle (Fukuyama 1995, pp. 69–82). In other words, the oversimplified judgment miscalculated the composition of the inner circle, and the force of family domination might not be as complete as expected. Secondly, only static evidence was offered and the over-time trends were ignored. By a more detailed and longitudinal analysis, this paper showed that family members have never fully occupied the inner circle since early times and their weightage in the inner circle varied in different years, depending on institutional contexts. These results imply that the concept of Chinese familism is too narrow and that it would be more sensible to incorporate the possibility of cultural permutation and the role of other institutional forces (Whyte 1996).

The inner circle system depicted in this paper also challenged the market-centered approach of corporate structure. The cross-shareholding and interlocking directorate embedded in the inner circle system clearly showed that an atomized model of corporation which ignored horizontal relationships between firms was unsuitable for understanding an organizational form such as business group. Due to the pervasiveness of business groups and other inter-organizational forms (Powell 1990; Podolny and Page 1998), scholars even suggested that “The nexus of contracts approach seemed increasingly like a theory of US corporate governance in the 1980s rather than a general theory of the firm” (Davis and Useem 2002, p. 233). My

analysis of the authority structure in Taiwan's business groups should pave the way for further research on a new approach to corporate structure.

Both the market-centered theories and the cultural determinism overlooked institutional environments that contributed to the formation and evolution of the inner circle system. For the inception of the inner circle structure, the most important clue can be found in Article 209 of Company Law of Taiwan (promulgated in 1966), which did not restrict interlocking directorates even if the companies involved belonged to the same industry.⁹ This clause is significant when compared to the Clayton Act of 1914 in the United States which restricted interlocking directorates when linked companies were in the same line of business. Based on this concept, the regulation of business firms in Taiwan provided an essential institutional infrastructure to the inner circle system of group management.

The institutional effects also appeared clearly in the evolution of the inner circle system. As the data show, the composition of the inner circle shifted significantly after 1986 when the biggest wave of economic liberalization and political democratization in Taiwan's modern history occurred. However, one may argue that Taiwan's case is unique due to its specific political conditions, and the institutional conclusion derived cannot be applied to other contexts. It is true that Taiwan has its particular history. However, the similar institutional transformation I described also appeared in other developing economies and newly industrialized countries. For example, Sachs and Warner (1995) provided a comprehensive survey on a world scale on this subject. Moreover, a special issue of *The Developing Economies* (Vol. 31, No. 4, 1993) explored how economic privatization affected the ownership and management structure of business groups in other East Asian countries such as Indonesia, Malaysia, and Thailand. In addition, management scholars studying business groups in India and Chile labeled the same phenomenon "policy shock" and statistically showed how these changes influenced the organizational structure and performance of business groups (Khanna and Palepu 1997, 1999a, 1999b). It is clear that institutional forces are an indispensable variable in explaining organizational forms and changes, and this paper provided more evidence for this argument.

⁹ The only condition for interlocking directors is for them to report to the shareholders and gain shareholders' acquiescence on their business behavior (Ke 1995, p. 147).

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APPENDIX A

DATA SOURCES AND CODING

The major data source for this study was the directory of *Business Groups in Taiwan* (*Taiwan diqu jituan qiye yanjiu*) (*BGT* hereafter), which is compiled by China Credit Information Service (CCIS) in Taipei, the oldest and most prestigious credit-checking agency in Taiwan and an affiliate of Standard & Poor of the United States. This directory has been publishing information on the one hundred largest Taiwanese business groups (in terms of sales) since 1974. The definition of business group adopted by *BGT* is as follows: "a coherent business organization including several independent enterprises." For the 1974 version of *BGT*, groups were chosen under the following conditions: if more than 51 per cent of ownership consisted of native capital; if three or more independent firms identified themselves as group constituents, if the group total sales exceeded 100 million, and if the core firm was registered in Taiwan. This definition was maintained through the later versions, and a set

of more specific conditions for group membership was developed in the 1988/89 and 1996/97 versions.

For each business group, the directory recorded the history and financial information such as total assets, net sales, and return on assets. It also reported basic information about each member firm such as the name of the chairman of the board and manager. More importantly, it surveyed member firms, asked them to identify the most important decision-makers within the group, and generated a list of core leaders. It then provided a biographical description of the core leaders. This list is considered to include the members of the inner circle in this study. While the biographical description often reveals the relationship between each core leader and the group founder, it is not complete. I supplemented the directory with available biographical information in *Who is Who in Taiwan*, *Who is Who in Taiwan's Business*, *Directory of Managers of Taiwan's Enterprises*, business magazines and newspapers with regular coverage on business groups, and various autobiographies by group founders. These various data sources also allowed me to describe the career path of the core leaders.

A core leader was classified as "long-term employee" when the following descriptions appeared in the career history: "a professional manager who joined the group in 19XX," "an employee who has been working in the group for a long time and has served as general manager in XX company and deputy manager in YY company," or "a confidant of the family who joined the group in early days and had occupied various important positions within the group." A core leader was considered to have locality ties with the founder if both were from the same county or city: for example, Kaohsiung county in Taiwan or Qingdao city in Shandong province.

Since the main research issue was how institutional changes affected the management structure of a business group, I compiled data from three editions of *BGT*, 1974, 1988/89, and 1996/97, comprising data of 1973, 1986, and 1994. Appendix Table I summarizes the statistics.

APPENDIX TABLE I
BASIC INFORMATION ABOUT THE DATABASE FOR GROUP MANAGEMENT

	1973	1986	1994	Total
Groups	111	97	115	323
Member firms	783	746	1,100	2,629
Key persons	111	97	115	323
Other core leaders	166	212	309	687
Shareholders	4,291	3,758	5,577	13,626
Chairmen of the board	756	727	1,077	2,560
Chief managers	705	614	923	2,242

The 1974 edition of *BGT* is the earliest version available and the 1988/89 *BGT* recorded the situation immediately before the institutional transformation described in Appendix B. The changes between 1973 and 1986 hence were used as a pretest (or control group) to analyze the institutional effects between 1987 and 1993, when political democratization and economic liberalization were initiated. The 1994 data (presented in 1996/97 *BGT*) functioned as a posttest which enabled us to observe the immediate effects of institutional transition. I did not use later versions of *BGT* in order to avoid complicating effects such as the Asian financial crisis.

I coded the industry participation of a business group based on product information about each member firm. I assigned a two-digit industry code to each group member according to the Standard Industrial Classification (SIC) of the Republic of China amended in December 1996 (Directorate General of Budget, Accounting and Statistics, Executive Yuan). In total, seventy industries were assigned to 2,629 group firms. I then aggregated firm sales according to the two-digit code. The industry that accounted for the largest proportion of group sales was treated as the major industry of the group. On the average, the major business line accounted for 55–65 per cent of group sales in 1973, 1986, and 1994. The distribution of the major industries among the top 100 groups is presented in Table II.

To determine which of these major business areas were export-oriented, I referred to the *Input-Output Table* published by the Directorate General of Budget, Accounting and Statistics, Executive Yuan in various years. The domestic vs. export-focused orientation of an industry is clearly revealed in the amount of its export value in the transaction table. I used 50% as the cut-off point: industries in which 50% or more of their total production value was exported were treated as export-focused. For example, in 1973, electronics, garment, plastic, and wood were coded as export-oriented. The percentages of their exported production value were 70%, 67%, 51%, and 50%. The other industries such as textile, food, and chemical matters were coded as domestic-oriented due to their low percentages in export value (30%, 16%, and 6%).

APPENDIX B

INSTITUTIONAL TRANSITION BEFORE AND AFTER THE MID-1980s

There is a consensus among scholars that the government of the Nationalist Party (Kuomintang, KMT) has dominated Taiwan's economy and society since its retreat from Mainland China in 1949 (Amsden 1985; Gold 1985; Wade 1990). It had a relatively high autonomy from the economic sector and hence played a leading role in Taiwan's development in the past fifty years (Evans 1995). One important reason is that KMT inherited all the industrial and business firms from the Japanese colo-

nial administration which formed a large public sector controlling critical resources for production.^a To keep its predominance, KMT restricted new establishments in most industries starting from the early 1950s, citing the small domestic market.

Until the mid-1980s, most of the key manufacturing sectors as well as financial industries, public utilities, and transportation were still highly regulated and hence were monopolized by public enterprises. These highly profitable and capital-intensive businesses started opening to the private sector in the mid-1980s. This constituted the largest economic liberalization in Taiwan's modern history and the process was accompanied and accelerated by the political democratization which started in 1987.^b Scholars offer different explanations for this "Great Transition" (Tien 1989). Some emphasize external forces such as the pressure from the United States for fair trade practices and appreciation of Taiwan's currency (Chu 1994), while others focus on internal factors such as political opposition, social movements, and dissatisfied capitalists (Wang 1993, pp. 139–48).

While it is difficult to reach a conclusion from the evidence presented, the outcome of this institutional transition is obvious. Not only were more lenient administrative policies initiated, but new additions and amendments to the legal framework, such as the Banking Law Amendments (1989), Securities and Exchange Law Amendments (1988), the Statute for Upgrading Industries (1990), and the Statute for the Transfer of Public-Opened Enterprises to Private Operation (1991), were also implemented (Cornell 1993; Pistor and Wellons 1998). These changes in institutional regulations have exerted substantial impacts on the environment in which the Taiwanese business groups operate.

The first two law amendments induced the deregulation of financial industries and the opening-up of capital markets in Taiwan (Semkow 1994); the third statute brought in more multinational companies by providing strong tax incentives and the last policy opened up lucrative industries such as banking and telecommunication to the private sector. All these changes have exerted a significant impact on the managerial structure of the Taiwanese business groups, which is described in detail in the text.

^a According to Liu (1992, pp. 24–28), there were about 860 units in finance, utilities, transportation, and various manufacturing sectors that were combined and transformed into government-owned enterprises.

^b The process was hastened by the death of President Chiang Ching-kuo, son of Chiang Kai-shek, in January 1988.