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Defensive Practice Adoption in the Face of Organizational Stigma: Impression Management and the Diffusion of Stock Option Expensing

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ABSTRACT

Although most diffusion research focuses on firms adopting new practices to maintain their legitimacy, this paper examines a setting in which firms adopted a controversial practice to defend themselves against challenges relating to corporate deviance. We argue that understanding defensive adoption requires attending to both the dynamics of organizational stigma and impression management, and test our theoretical claims by analyzing the diffusion of an accounting practice, stock option expensing (SOPEX), following the Enron scandal. We first provide evidence that the media and shareholder activists transformed the practice into a defensive device by theorizing it as a solution to problems relating to corporate fraud and corporate governance. Using event history analysis, we then show that corporations that became targets of stigma-inducing threats were more likely to adopt SOPEX and that the media were a key force channeling these threats.

KEYWORDS: diffusion, impression management, scandal, stigma

Recent research on practice diffusion has challenged the classic two-stage model, which theorizes diffusion unfolding through a process in which early adopters attempt to realize technical gains from a new practice, while late adopters attempt to gain legitimacy as a practice becomes institutionalized (Tolbert and Zucker, 1983). Kennedy and Fiss (2009), for example, have found that legitimacy concerns matter for both early and later adopters, while Lounsbury (2007) and Schneiberg and Soule (2005) have shown that organizational fields are more contested and heterogeneous than the classic two-stage model assumes. Recognizing the complexity of both organizational fields and the processes through which legitimacy develops suggests that a generalizable diffusion model is unrealistic, and should “redirect the study of institutional diffusion toward finer-grained mechanisms” (Lounsbury, 2007, p. 289). Gaining a deeper understanding of the multiple pathways of diffusion, therefore, requires identifying mechanisms that may not be applicable across all instances of diffusion, but may be generalizable within specific contexts of diffusion.

One context that has been largely ignored in the institutional literature has been the diffusion of practices that firms adopt to defend themselves against challenges emerging from perceived or actual deviance from laws, informal norms, and cultural standards. This inattention can be partly attributed to the often implicit assumption in institutional theory that potential adopters are already perceived as legitimate, and adopt new practices to maintain their alignment with normative, regulative, and cognitive elements in their environments (DiMaggio and Powell, 1983; Meyer and Rowan, 1977; Ruef and Scott, 1998). However, we contend that firms can also adopt new practices as a defensive tactic against attacks by challengers who question the appropriateness of organizational behavior and actions. Do firms engage in defensive practice adoption in the face of such pressures? If so, what types of practices do firms adopt? Which field-level factors are the most important? Do these factors change over time?

Research on how firms react to controversies has focused on verbal strategies of impression management at the firm and industry levels (Carter, 2006; Desai, 2011; Maguire and Hardy, 2009; Marcus

and Goodman, 1991), and how firms defend their behavior by referring to their legitimate practices (Elsbach, 1994; Elsbach and Sutton, 1992). However, since impression management at the firm level generally refers to “tactics designed to effect the perceptions of the image, identity, or reputation of an organization” (Elsbach, 2006, p. xvii), impression management tactics likely extend beyond the rhetorical to include defensive practice adoption. Although Suchman (1995) suggested the possibility of defensive practice adoption, there has been little empirical work on this topic.¹ Understanding defensive adoption has become especially important in contentious markets, with stakeholder groups more actively mobilized in attempts to reform corporate behavior (King and Pearce 2010) and more attuned to corporate deviance in the face of recurring corporate scandals and financial crises.

In this paper, we propose that the key to understanding diffusion in these settings lies in attending to both the processes through which organizational stigma emerges and the nature of impression management. A number of recent studies have focused on the causes and consequences of organizational stigma (Devers et al. 2009; Jonsson et al., 2009; Pozner, 2007), but have not examined how field level pressures that stigmatize multiple firms may generate common impression management tactics that drive broader institutional change. Since the media are key intermediaries shaping stigmatization processes (Desai, 2011; Jonsson and Buhr, 2011; Yu et al. 2008), they should also be key drivers of defensive adoption, helping to both define specific practices as defensive devices and to expose corporate deviance. In addition, we argue that adoption will be more potent as a defensive device for early adopters and that, therefore, the temporal characteristics of diffusion dynamics may differ from either the classic two stage model (Tolbert and Zucker, 1983) or recent extensions of it (e.g., Kennedy and Fiss, 2009).

We test our theoretical claims by analyzing the diffusion of a contentious accounting practice, stock option expensing (SOPEX), between January 2002 and July 2004. In 1995, the Financial Accounting Standards Board (FASB) implemented Financial Accounting Statement (FAS) 123, which encouraged firms to recognize an expense for employee stock options, but did not require them to do so. Although recognizing an expense directly reduced the earnings, earnings per share, and potentially the

stock prices of adopting companies, between July 2002 and July 2004, 753 companies voluntarily adopted the practice (Bear Stearns, 2004). Why did the practice diffuse at this time, especially considering a history of corporate resistance to it?

We argue that the diffusion of SOPEX was fundamentally driven by defensive reactions to stigmatization pressures. In our analysis, we first demonstrate how field-level actors identified and theorized problems relating to corporate fraud and ineffective corporate governance, and redefined SOPEX as a solution to these problems following Enron. Through qualitative evidence, we show how the media played a key role in broadcasting these debates and turning SOPEX into a defensive device as it became redefined as a symbol of resurgent norms of financial transparency and constraints on executive compensation. Second, although all companies would have been motivated to adopt SOPEX as a way to ensure stakeholders of their effective governance practices after Enron, we show that corporations that became targets of unwanted attention from different field-level actors, including the media, were more likely to adopt SOPEX.² For example, in August 2002, Citibank announced that it was voluntarily adopting SOPEX, claiming that it was at the “forefront of progressive industry change” (Moyer, 2002, p. 20). However, in May 2002, the company was named as a defendant in a class-action lawsuit filed by investors who alleged that Citibank enabled fraud at Enron (Greider, 2002). In addition, in March 2002, Citibank shareholders placed three corporate governance-related resolutions up for a shareholder vote. SOPEX adoption was, therefore, a way for Citibank to demonstrate its commitment to resurgent norms at a time when it was being scrutinized for breaching the same norms.

To develop our argument, we first examine the contested history of stock option accounting and analyze how a new theorization of SOPEX emerged after Enron. Drawing upon theories about stigma and impression management, we then develop hypotheses regarding the forces shaping defensive adoption and present our quantitative analysis.

THE REEMERGENCE OF STOCK OPTION EXPENSING

A stock option is a contract that gives an employee the right to purchase a fixed number of shares at a fixed price for a fixed period of time. An employee can exercise their options (i.e., purchase the shares) after a certain period of time but is not required to do so. The popularity of executive stock options soared during the 1990s, in part because payments made from the exercise of stock options were not included in the calculation of new limits on the tax-deductibility of executive compensation enacted in 1994 (Hall and Murphy, 2003). In addition, prior to 2004, firms did not have to recognize an accounting expense for stock options. Historically, however, the accounting treatment of stock options has been the subject of intense conflict and debate between corporate managers, the accounting profession, regulators, legislators, and shareholders. These conflicts have revolved around whether it is possible to accurately value a stock option at the time it is given to an employee. Proponents of expensing have argued that stock options have a value to both the employee (as future compensation) and to the firm (to attract and retain employees), and therefore, firms should recognize it as an expense. Opponents of expensing have countered that options are only contracts that cannot be sold and have no real value to an employee.

In 1992, FASB announced its intention to require companies to recognize stock options as an expense. This ignited a three year conflict that pitted accounting regulators against Silicon Valley and the booming high-tech sector, which relied heavily on stock options as compensation. In an attempt to prevent FASB from issuing the requirement, high-tech executives and industry associations waged an intensive public campaign against FASB (Pearlstein, 2002). Ultimately, FASB backed down from its initial proposal (Levitt, 2002) and released Financial Accounting Statement 123 (FAS 123) in 1995, which only recommended, but did not require, that firms make stock options an expense. However, FAS 123 stipulated that if a firm did not expense its options, it had to reveal in a footnote to its financial statements what the financial impact of an expense would have been. Between the release of FAS 123 and June 2002, only 13 publicly traded companies voluntarily expensed their employee stock options (Aboody et al., 2004). All other public companies complied with FAS 123 by disclosing their potential option expense in a footnote. However, between July 2002 and July 2004, 753 publicly traded companies voluntarily

decided to adopt SOPEX (Bear Stearns, 2004). Figure 1 tracks the incidence of SOPEX adoption from January 2002 to July 2004 among all public companies and the Fortune 500.

Insert Figure 1 about here

Past research suggests several reasons for this wave of voluntary adoption. Aboody et al. (2004) argue that firms made a cost-benefit calculation and adopted SOPEX because the market saw it as a signal of financial transparency, especially for larger, more visible firms. Brandes et al. (2006) argued that institutional investors and interlocking directorates encouraged SOPEX adoption. Although these studies highlight the role of institutional pressures as well as the agency problems inherent in making the potential cost of stock options more transparent, we still have an incomplete picture of the forces driving voluntary SOPEX adoption. Cost-benefit considerations alone, for example, cannot explain why firms adopt new accounting practices (Mezias, 1990). More importantly, past research has not fully explored how the scandals may have altered the meaning of the practice and how this may have influenced diffusion.

PRACTICE ADOPTION AS IMPRESSION MANAGEMENT

In this section, we first analyze how, in the aftermath of the Enron collapse, shareholder activists, business intellectuals, journalists, and some regulators theorized new connections between the problems of executive malfeasance, corporate fraud, and the accounting treatment of stock options. We focus on the role of the media in broadcasting these debates, making the practice more visible, and reframing the practice. We then turn to theorizing the specific ways in which stigmatizing pressures emerged following the Enron collapse to motivate our hypotheses regarding which firms were more likely to adopt.

Theorizing Problems and Solutions: Executive Stock Options and the Scandals

An important stage in the diffusion of any practice is its theorization as effective “in terms of standardized notions of efficiency, justice, or progress” (Strang and Meyer 1993, p. 497). New organizational practices

do not just emerge out of thin air as easy solutions to organizational problems or as ways for firms to demonstrate their legitimacy, but are discursively theorized, framed, and advocated by different field-level actors (Phillips et al., 2004). The collapse of Enron was a triggering event (Hoffman and Ocasio, 2001) that generated public debate about core market institutions of American capitalism, including corporate governance and systems of reporting, accounting, and auditing (Levitt, 2002). As these debates intensified in early 2002, SOPEX was brought back from dormancy and became redefined as a logical solution to problems relating to fraud and ineffective governance.

Since the media play a critical role in exposing new practices (Strang and Soule, 1998) and publicizing contests within organizational fields (Deephouse and Heugens, 2009; Jonsson and Buhr, 2011), we analyzed media coverage of SOPEX to gain an understanding of how the practice was theorized after the Enron scandal. The media do not just broadcast the framing of other actors, however, but can function as an important field-level actor in their own right by covering the viewpoints of specific actors more intensively or by journalists advocating specific points of view. Furthermore, since the media are businesses dependent on sales and advertising revenues, they often create dramatic narratives (Rindova et al., 2006) and function as “fight promoters” (Jonsson and Buhr, 2011), increasing attention to specific issues and amplifying their importance.

Insert Figures 2 and 3 about here

Figure 2 shows annual media coverage of SOPEX from 1990 – 2004 in all media outlets and in seven of the leading business media outlets.³ For both groups of sources, we counted the total number of articles in which SOPEX was one of the main topics.⁴ Both follow a similar pattern: coverage intensified between 1993 and 1995 because of FASB’s push for SOPEX, declined between 1996 and 2000, and then increased dramatically in 2002. Figure 3 tracks monthly media coverage between 2001 and 2004. These two figures reveal that in the six years between the release of FAS 123 in 1995 and the collapse of Enron at the end of 2001, SOPEX received only occasional coverage in the mainstream business press. In fact,

the number of articles about SOPEX that appeared in these six years was approximately equal to the coverage that appeared in the six *months* between January and June 2002. We located and read 72 articles relating to SOPEX that appeared in the seven mainstream business media outlets during this six month time period, 17 of which focused exclusively on SOPEX. We conducted a close textual analysis of these 17 articles because their depth of coverage and visibility in the business press make them a logical source for understanding how the media in general framed SOPEX during the period preceding the initial wave of diffusion. These articles reveal a reinvigorated debate between proponents and opponents of SOPEX. Although there were few supporters of SOPEX in the mid-1990s, after Enron, the media highlighted a much broader range of support among shareholder activists, regulatory officials, and legislators. However, the high-tech industry, other regulators and legislators, and industry and trade associations continued to oppose SOPEX.

Shareholder activists were one of the more prominent groups in the debate. These activists included “gadfly” investors, institutional investors, social and economic justice organizations, and investor advisory firms such as the Council of Institutional Investors (CII) and Institutional Shareholder Services (ISS). Although shareholder activists initially focused attention on the widespread problem of accounting fraud, stock options quickly became a target of criticism. Activists framed stock options as one of the primary motivations for accounting fraud, arguing that their excessive use as executive compensation during the 1990s made it attractive for executives to bolster short-term earnings by manipulating financial statements. As the chief executive of ISS, explained: “I firmly believe that there is a relation between very aggressive accounting policies and efforts to drive earnings per share, to drive the stock up, so management can maximize the value of its options” (Spiro, 2002, p. 4). Shareholder activists argued that the system of accounting machinations at Enron exemplified this culture taken to its logical extreme. The executive director of the CII, for example, noted that “a company can’t be turned into a Ponzi scheme without options. The only way an executive can get a lot of money out of the company before it crashes is

with stock options. They get these megagrants, (and) they cash them in before the problems come home to roost” (Pender, 2002, p., G1).

Shareholder activists further criticized the lack of a required earnings charge for stock options as an incentive for directors to increase the size of executive stock option grants, which in turn exacerbated the incentives for executives to boost short-term stock prices and more generally stigmatized stock options as fraudulent (e.g., Pearlstein, 2002). Stock options were originally intended to help mitigate managerial self-dealing by aligning their incentives with those of shareholders (Fama, 1980; Fama and Jensen, 1983), but after Enron, shareholder activists argued that stock options posed a serious agency problem, in part because of their accounting treatment. According to this criticism, not only did the lack of an accounting charge motivate boards to grant large option packages, but it also motivated boards to grant stock options that were *not* linked to specific individual or corporate performance targets. Since options that were granted with performance conditions required an accounting charge, most firms instead granted “plain vanilla” options that had no such conditions (Bebchuk and Fried, 2004). These created incentives for executives to boost short-term stock prices without incurring any financial risk. If share prices went up, executives could realize substantial gains; if share prices fell, they could leave their options unexercised, and lose nothing.

This critique of stock options led shareholder activists to support voluntary SOPEX (Pearlstein, 2002), and this support rested primarily on the grounds that it would add transparency to financial statements and help curb some of the excesses that created the problems at Enron. SOPEX, therefore, addressed two issues at the center of the scandals, accounting fraud and executive malfeasance, and the media broadcasted these views prominently. The *New York Times*, for example, quoted Alan Greenspan, then chairman of the Federal Reserve, explaining that “one step towards better earnings quality would be forcing companies to treat the value of stock options granted to employees as an expense” (Ip, 2002, p. A3). Similarly, in a commentary in the *Wall Street Journal*, Joseph Stiglitz supported SOPEX on the grounds that it provided more accurate information and that “such information is like a public good: better

standards-more transparency-lead to better resource allocation and better functioning markets” (Stiglitz, 2002, p. A10). In addition, journalists themselves helped to reframe SOPEX, both by highlighting the views of stock option critics and by theorizing the links between the scandals and stock option accounting:

“As the excess of the 90s are laid bare, it’s becoming clear that options played a central role at numerous companies. Option grants that promised to turn caretaker corporate managers into multimillionaires in just a few years encouraged some to ignore the basics in favor of pumping up stock prices...Add to that the controversy over the way options are accounted for on corporate income statements. Under current accounting rules companies are not required to record any expense...at the same time, when employees exercise options, companies derive huge tax benefits. The combination of those benefits skews the corporate incentives towards offering up oodles of options to executives.” (Henry et al., 2002, p. 39)

There were also, however, opponents of the view of SOPEX as solution, including executives of high-tech firms, then SEC chief Harvey Pitt, the Business Roundtable, U.S. Chamber of Commerce, and the Bush Administration. Although the claims of SOPEX opponents were weakened by the Enron scandal, they were still politically organized and well-funded. FASB remained remarkably silent on the issue until October 2003, when it announced its desire to implement a new SOPEX requirement. On March 31, 2004, it opened up a 90 day comment period about SOPEX. A group of technology companies proceeded to heavily lobby Congressional leaders to derail FASB, but they were ultimately unsuccessful. On July 1, 2004, FASB announced that it was going to implement a formal SOPEX requirement. On December 16, 2004, FASB issued its final statement, which required SOPEX implementation for all publicly traded firms by the end of 2005.

Prior to this new requirement, however, SOPEX had acquired new meaning as a symbol of the new normative emphasis on accounting transparency and limits on excessive executive compensation. Voluntary SOPEX adoption showed that a firm recognized the new normative environment, was taking its demands seriously, and was taking action to conform to it, even incurring an economic cost to do so. Had FASB implemented a requirement immediately after the Enron scandal, SOPEX adoption would have demonstrated regulatory compliance and would not have carried the same weight as the voluntary recognition of this expense. Given SOPEX’s newly-theorized status, most publicly traded firms could enhance their legitimacy by adopting it. However, we argue that SOPEX adoption had particular

resonance as a mechanism of impression management for companies that became connected to the problems of fraud and ineffective governance.

Defensive Adoption in the Face of Stigmatization

Although organizations maintain their legitimacy by behaving in ways that are considered appropriate by different groups of stakeholders (DiMaggio and Powell, 1983; Meyer and Rowan, 1977), these same stakeholders can challenge the appropriateness of an organization's practices when they perceive that these are out of line with a "socially constructed set of norms, values, or definitions" (Suchman, 1995, p. 574). Past research has focused on the characteristics and consequences of different types of organizational misconduct (Janney and Gove, 2011; Marcus and Goodman, 1991; Perrow, 1999), but our understanding of how assessments of deviance emerge is less developed (Devers et al., 2009). The concept of stigma provides a fruitful way to conceptualize judgments about organizational deviance and to theorize the dynamics driving the defensive adoption of SOPEX after Enron.

According to Devers et al. (2009, p. 155) organizational stigma is "a label that evokes a collective stakeholder group-specific label that an organization possesses a fundamental, deep-seated flaw that deindividuates and discredits the organization." Similar to the positive judgments of legitimacy, status, celebrity, and reputation (Bitektine, 2011), stigma emerges through a socially constructed process (Devers et al. (2009). A stigmatization process begins with the judgment of organizational action as illegitimate by at least one stakeholder, followed by a subsequent judgment that the act is not idiosyncratic but representative of a deeper misalignment between their values and those of the organization (Devers et al., 2009). The ultimate label of stigma only emerges when a critical mass of other stakeholders accepts the judgment of value incongruence (Adut 2005; Devers et al, 2009). The initial exposure of deviance alone, therefore, will not necessarily lead to stigmatization; rather, the more public the accusations of deviance become, the greater the likelihood that multiple stakeholders will become aware of the deviance and judge an organization as fundamentally flawed. The most severe outcome is the complete loss of an

organization's legitimacy, which can lead to bankruptcy, dissolution, or criminal prosecution of executives (e.g., Enron). Although complete losses of legitimacy are rare, any pressures that can potentially lead to stigmatization can affect an organization's ability to govern and maintain healthy relationships with stakeholders.

In the wake of Enron, the most common forms of deviance that came under scrutiny were related to corporate fraud and corporate governance. The first annual report of the Corporate Fraud Task Force (CFTF), an interagency task force created by the Bush Administration in July 2002, defined corporate fraud as: "(1) the falsification of corporate financial information; (2) self-dealing by corporate insiders; or (3) obstruction of justice, perjury, or tampering or other obstructive behavior relating to either of the categories mentioned above" (CFTF, 2003, p. 2.2). Acts of fraud are not always visible to stakeholders, but the severity of fraud at Enron, Worldcom, and other companies in 2001 and 2002 focused attention on these issues. These scandals also focused attention on ineffective corporate governance, including the weakness of directors in monitoring executives, and as discussed above, the incentives for malfeasance created by stock-based compensation.

Considering the severity of the potential negative outcomes of stigmatization, organizational leaders will attempt to defend the organization against emerging stigmatization threats (Ashforth and Gibbs, 1990; Suchman, 1995), i.e., to demonstrate to constituents that challenges are off-base, or that the behaviors under scrutiny are anomalies or are being fixed. By defending itself against stigmatizing pressures, a firm attempts to mitigate damage to its reputation and derail momentum towards more severe consequences. Existing work on defensive actions has focused primarily on how firms use verbal accounts to manage stakeholder impressions (e.g., Marcus and Goodman, 1991; Elsbach and Sutton, 1992; Elsbach, 1994; Carter, 2006). However, impression management relating to organizational legitimacy "extends well beyond traditional discourse to include a wide range of meaning-laden actions and nonverbal displays" (Suchman, 1995, p. 586). The adoption of a new practice, therefore, is a concrete way for an organization to show its intent to abide by field-level norms and help a firm achieve the primary objective

of impression management: influencing the perceptions that different audiences have of an organization (Elsbach, 2006).

For defensive adoption to influence these perceptions, however, the new practice should be meaningfully connected to the perceived deviance. As we demonstrated in our qualitative analysis, since SOPEX became symbolic of resurgent norms of transparency and constraints on executive malfeasance, it was well-connected to the issues of corporate fraud and corporate governance. SOPEX adoption, therefore, represented a form of strategic restructuring that Suchman (1995, p. 298) has described as “disassociation,” in which a firm attempts to “symbolically distance [itself] from the bad influences.”

While disassociation often consists of changes to existing practices, we propose that disassociation can also entail the adoption of new practices that are closely related, in meaning or substance, to the behaviors and actions at the core of stigmatization challenges. The adoption of such practices demonstrates that the firm is behaving legitimately within this particular area of organizational activity without necessarily drawing attention to the specific practices under scrutiny or acknowledging any related stakeholder judgments. After Enron, SOPEX adoption disassociated firms from claims of corporate fraud and ineffective corporate governance inasmuch as SOPEX signified a firm’s commitment to normative standards of proper accounting and governance. Furthermore, voluntary SOPEX was also an effective way for firms to deal with the negative side-effects of explicit impression management. Since defensive actions may lead to increased scrutiny by stakeholders and can be perceived as ingenuine, “implicit forms of communication (organizational rituals and folklore) tend to be more credible than explicit forms (press releases, policy statements, annual reports)” (Ashforth and Gibbs, 1990, p. 178). Following the Enron scandal, SOPEX adoption became just such an implicit form of communication, allowing firms facing negative scrutiny to demonstrate their commitment to the new normative environment without admitting wrongdoing. Finally, since SOPEX adoption reduced corporate earnings, it potentially held more credibility with stakeholders than less costly acts of verbal defenses. Adopters indicated that they were

willing to take a financial hit to demonstrate their legitimacy, and executives showed they were willing to potentially sacrifice the value of their equity-based compensation.

SOPEX adoption, therefore, was a unique defensive action that firms could take to buffer themselves from stigma following Enron's collapse. Although very few firms became labeled as fundamentally flawed by a critical mass of shareholders (e.g., Enron and Worldcom), we argue that firms would have reacted defensively to any pressures that could have potentially led to such stigmatization, with the likelihood of adoption increasing with the strength of stigmatization pressures. To identify firms that would have been attracted to defensive SOPEX adoption, we now assess the primary channels through which stigmatizing pressures relating to fraud and corporate governance emerged.

The State and Investigations

Since the state plays a powerful role in conferring legitimacy and forcing organizational compliance with myriad laws and regulations (Scott, 2008), it can also question specific actions as illegal and expose corporate deviance. For example, in their studies of verbal impression management, Elsbach (1994) and Marcus and Goodman (1991) found that regulatory and enforcement agencies played a key role in identifying deviant behavior and setting in motion stigmatization. A number of federal agencies can take action against organizations suspected of fraud, including the SEC and Department of Justice. Such investigations can lead to criminal charges against executives, restatement of earnings, or the disgorgement of illegally acquired profits. Even if such investigations do not result in punitive outcomes, an investigation itself can set the stage for stigmatization. Firms facing these investigations, therefore, will try to defend themselves and derail the threat. Hence:

Hypothesis 1: Organizations that were the targets of federal investigations for corporate fraud were more likely to adopt SOPEX than organizations that were not targets.

Shareholder Activism

Shareholders, and in particular institutional investors, were active in exposing and criticizing deviant corporate governance practices after Enron. Shareholder activism has traditionally been used to pressure firms to implement practices that allow for more effective monitoring of management and to provide more transparent information to the market (Davis and Thompson, 1994; Useem, 1996). Social movement scholars have argued that shareholder activism can be a powerful form of collective action that shapes the corporate agenda (King and Pearce, 2010; Proffitt and Spicer, 2006; Vasi and King, forthcoming). Such activism usually takes the form of informal negotiation with boards or the submission of proxy resolutions as a tactic to pressure companies to change their policies (Rehbein et al., 2004).

Although earlier literature in finance found that shareholder activism led to small (but significant) changes in corporate governance (Bizjak and Marquette, 1998; Del Guercio and Hawkins, 1999; Karpoff, 2001; Smith, 1996), more recent work has suggested that shareholder activism can lead to more substantial changes in governance (Del Guercio et al, 2008; Eritimur et al., 2010; Thomas and Cotter, 2007). In addition, organizational theorists have demonstrated that shareholder resolutions can influence the implementation of new governance practices (Rao and Sivakumar, 1999) and shape variation in verbal impression management tactics (Porac et al., 1999; Wade et al., 1997). Corporations are not legally required to implement changes called for by resolutions; however, since all resolutions are presented in a public forum, they provide an opportunity for activists to broadcast their claims and grievances widely, and set the stage for the development of stigma. While a majority of shareholder proposals have historically called for changes in specific corporate governance practices (Gillan and Starks, 2007), such as the structure of the board, board decision-making processes, and anti-takeover defenses, the Enron scandal provoked an increase in the number of these types of proposals, particularly those relating to executive compensation (Georgeson Shareholder 2002, 2003, 2004). In their proposals, many shareholder activists theorized links between corporate governance practices, the scandals, and other social problems. Voluntarily adopting SOPEX was, therefore, a way for firms to demonstrate to shareholder activists their

intent to address corporate governance problems and potentially temper the stigmatizing threat posed by shareholder resolutions. Hence:

Hypothesis 2: Organizations that were the targets of shareholder proposals regarding corporate governance practices were more likely to adopt SOPEX than organizations that were not targets.

The Media

Although a number of recent studies have demonstrated how the media directly influence social processes relating to organizational legitimacy, (e.g., Deephouse, 2000; Kennedy, 2008; Kjaergaard et al., 2011; Rindova et al., 2006), our understanding of how media-induced perceptions shape the diffusion of new practices remains underdeveloped. Since stigma is fundamentally about the flow of perceptions of deviance and illegitimacy (Devers et al., 2009), the media play a key role as intermediaries in shaping stigmatization processes (Deephouse and Heugens, 2009; Desai, 2011; Jonsson and Buhr, 2011; Yu et al. 2008). It is likely that the media's influence can be important at each stage of the stigmatization process. The first stage entails the exposure of deviant behavior (Devers et al., 2009), and the media can be the first channel through which stakeholders are made aware of such behavior. In the next stage, this initial exposure gives way to a more general judgment of deviance as "not just some idiosyncratic event, but indicative of some stable, underlying features ... suggesting that the organization's values are globally and completely incongruent with their own" (Devers et al, 2009, p. 160). The media can promote such a judgment through repeated exposure and framing (Pollock and Rindova, 2003). In the final stage of stigmatization, stakeholders develop more generalized judgments from these media accounts (Devers et al, 2009). By disseminating information about stakeholders' and third-parties' negative assessments of the firm's actions, media accounts publicly shame the deviant company and can create long-lasting negative perceptions. As the media focus more attention on deviant behavior, the threat of stigmatization becomes stronger, and an organization will be more likely to take steps to mitigate the threat. Following the Enron scandal, the media focused significant attention on various forms of corporate fraud. Therefore:

Hypothesis 3: Organizations that received higher levels of media exposure relating to corporate fraud were more likely to adopt SOPEX than organizations that did not receive such scrutiny.

In addition to exposing deviant corporate behaviors directly, the media can accelerate the process of stigmatization when coverage occurs in conjunction with other pressures. For example, the media covered the Enron scandal extensively, making the alleged illegal actions of Enron employees front page news across the world. Moreover, since the ultimate manifestation of stigma is related to the negative assessments of multiple stakeholders, it is likely that firms facing formal investigations will feel a more acute need to take action in the additional presence of media exposure about corporate fraud. Therefore, we predict that:

Hypothesis 4a: Organizations that were the targets of federal investigations for corporate fraud were more likely to adopt SOPEX if they were also the targets of higher levels of media exposure relating to corporate fraud.

The media can also exacerbate challenges by shareholder activists. Such activism is akin to social movements that do not have access to the formal decision-making channels of management and the board, and who often rely on the media to amplify image threats made by activists against corporations (King, 2008; King and Soule, 2007). The effects of movements and the media are therefore complementary in shaping public perceptions of a company and stigmatization pressures. Media exposure of deviant behavior likely becomes more salient if there is also observable discontent among a firm's shareholders. Similarly, as media exposure of deviance intensifies, shareholder proposals calling for governance reform gain credibility. Therefore:

Hypothesis 4b: Organizations facing shareholder activism were more likely to adopt SOPEX if they were also the target of higher levels of media exposure relating to corporate fraud.

Temporal Dynamics of Stigma and Defensive Adoption

Diffusion research has recently challenged the classic two stage model in which early adopters attempt to realize technical or economic gains from a new practice, while later adopters attempt to gain legitimacy as a practice become institutionalized. Kennedy and Fiss (2009), for example, found that legitimacy concerns can also matter for early adopters. They also propose that early adopters are more concerned with

achieving gains (either technical or social) and later adopters are more concerned with avoiding losses (either technical or social). How might the temporal dynamics of diffusion have played out in the case of defensive adoption in reaction to stigmatization?

We have argued that part of the reason why SOPEX adoption was a useful way for firms to defend against stigmatizing pressures was because the practice was substantively connected to two of the core problems at the heart of the Enron scandal: accounting fraud and executive malfeasance. It is likely, however, that SOPEX adoption was most useful as a defensive tactic for initial adopters. Once a larger group of firms adopted or other field-level forces altered motivations for adoption, the power of adoption as a unique defensive device likely became diluted. In fact, a key field-level shift occurred at the end of 2002 relating to the technical rules of voluntary SOPEX adoption. More specifically, according to the original 1995 guidelines of SFAS 123, if a company voluntarily adopted SOPEX, it would have recognized only the value of new stock option grants after the adoption date and not for prior grants (the “prospective” method). In December 2002, however, FASB released Statement 148, which called for the elimination of the prospective method at the end of 2003 (PriceWaterhouseCoopers, 2003). Voluntary adopters would then have had two choices for recognizing the expense. The first, the “modified prospective” method, required that firms recognize an expense for all future grants as well as option held by employees from past grants. The second method, “retroactive restatement,” allowed firms to expense past options by restating their earnings from pre-SOPEX adoption years. Of the three methods, the soon-to-be-obsolete prospective method was the least cumbersome and most cost effective way to implement FAS 123. Hence, there were advantages for companies to voluntarily adopt SOPEX starting in January 2003, especially if a SOPEX requirement seemed imminent.

Although FASB did not announce its intent to make SOPEX mandatory until July 2004, a widespread perception that such a requirement was imminent seemed to emerge earlier. On October 9, 2002, Robert Herz, then chairman of FASB, told a group of investor relations professionals that “political winds have changed to the point where there is now support for mandatory expensing of stock-based

compensation” (Stempel, 2002, p. 3). Furthermore, on November 8, 2002, the International Accounting Standards Board (IASB) issued a draft proposal to make stock option expensing mandatory for non-US companies. Although the IASB’s standards do not apply to U.S. companies, the proposal was widely perceived as something that would exert significant pressure on FASB to adopt similar standards (Schwanhausser, 2002). The elimination of the prospective accounting method after 2003, combined with the evidence that a SOPEX requirement was imminent, likely increased the attraction of voluntary SOPEX adoption beginning in January 2003 for motivations other than defense. Hence, we believe that firms would have been more likely to adopt SOPEX in reaction to stigmatization pressures before January 2003. Therefore:

Hypothesis 5: The effects of investigations, shareholder activism, and media exposure were stronger during the early period of SOPEX adoption.

METHODS AND DATA

We used event history analysis to model the effects of stigmatization pressures on the hazard rate of SOPEX adoption. In line with a number of existing analyses of the diffusion of corporate governance practices (e.g., Rao and Sivakumar, 1999; Wade et al., 1997; Westphal and Zajac, 1994), we used the Fortune 500 as our sample, as published by Fortune magazine in April 2002. We dropped 32 organizations from the original Fortune 500 sample for a variety of reasons: fifteen firms were privately held and did not file audited financial statements with the SEC, four firms did not grant stock options, four firms had stock option plans that were designed in ways that made SOPEX adoption irrelevant, two organizations were noncorporate, two firms had adopted SOPEX prior to the beginning of the observation period, two firms had gone bankrupt just prior to or at the very beginning of the observation period, and three firms were missing substantial amounts of data. The final sample included 468 companies, of which eight became right-censored at various points during the observation period because of bankruptcy, merger, or acquisition.

We measured the time of SOPEX adoption on a monthly basis, with the observation period beginning in January 2002 (the approximate time of the exposure of widespread fraud at Enron) and ending in July 2004 (the date when FASB released its first definitive statement that it was going to require SOPEX). To incorporate the effects of the time-varying covariates into the models, we employed the method of episode splitting (Blossfeld and Rohwer, 2002). Relevant changes in specific covariates were measured either monthly or annually depending on data availability. After all splits were complete, the final dataset consisted of 12,432 total spells, with 123 events (i.e., voluntary SOPEX adoption) occurring during the observation period. This research design improves upon earlier cross-sectional studies of SOPEX adoption, which only analyzed the first wave of adopters in 2002 (Aboody et al. 2004; Brandes et al., 2006).

We modeled our dependent variable as the instantaneous hazard, $h(t)$, of SOPEX adoption between time t and time $t + \Delta t$, given that a firm had not adopted at t . We used the piecewise exponential model commonly employed in organizational research (e.g., Ingram and Lifschitz, 2006; Stuart, Hoang, and Hybels, 1999). This specification allows the observation period to be divided into different time periods, assumes a constant baseline hazard rate during each time period, and allows the effects of the independent variables to vary between time periods (Blossfeld and Rohwer, 2002). We have strong substantive reasons to believe that the effects of stigmatization pressures varied over time, as expressed formally in Hypothesis 5. In settings where such effects are expected to be change over time, the piecewise exponential model provides a flexible way to model the effects of the independent variables without committing to the more stringent assumptions of parametric specifications (Bijwaard, 2009; Blossfeld and Rowher, 2002).⁵ We split the observation period at January 2003 because of the shifting position of FASB on SOPEX and the technical advantage of adopting SOPEX after December 2002. Both of these factors likely diluted the power of SOPEX adoption as a defensive device. Our observation period therefore consisted of two subperiods: one from January 2002 to December 2002 and the second from January 2003 to July 2004. The piecewise model takes the form:

$$\log h_{jkp} = x(t) \beta_{jkp}$$

where h is the transition rate from state j (nonadoption) to state k (adoption) during time period p , $x(t)$ is a vector of covariates, and β is a vector of coefficients associated with the covariates during time period p .⁶

Dependent Variable

Data on SOPEX adoptions were collected from a publicly available list compiled by the former investment banking firm Bear Stearns, which dated adoption by examining corporate press releases, media reports, and SEC filings (Bear Stearns, 2004). We manually cross-checked SEC filings of all Fortune 500 firms on the Bear Stearns list to confirm whether each firm actually adopted. Since our primary claim is that the motivation for initial SOPEX adoption was related to impression management concerns, we measured adoption as the first date that the firm announced its intention to adopt, either in the media or in SEC filings.

Independent Variables

The data for our three primary independent variables of interest were collected from a variety of archival sources and lagged by one month. We measured investigations using annual reports released by the Corporate Fraud Task Force (CFTF), which listed “significant cases” under investigation by the SEC, the Department of Justice, and other federal agencies. We supplemented these cases with the list of all enforcement actions listed by the SEC in its “Selected Accounting and Enforcement Releases” (Beasley, 1996; Bonner et al., 1998) on its website. We created a dichotomous variable coded as 1 if an organization was listed in connection with a significant case in either of the two annual reports released by the CFTF (CFTF, 2003, 2004) or appeared on the SEC lists. This variable was measured as a time-varying covariate that changed from 0 to 1 for the months after a firm first came under investigation.

We measured shareholder proposals relating to corporate governance as a time-varying covariate by counting all shareholder proposals relating to corporate governance submitted to each company

between 2001 and 2004. We updated the number of resolutions the company received during each annual proxy season. Data were collected from reports issued by Georgeson Shareholder, a shareholder consulting firm that collects data and reports on governance proposals, the most common of which relate to board structures, executive compensation, voting procedures, and proxy procedures (Georgeson Shareholder 2001, 2002, 2003, 2004).

Similar to Staw and Epstein (2000), who used media exposure to measure the perceived connections between firms and a specific management practice, we use media exposure to capture perceived connections between firms and corporate fraud. Using the Factiva database, we first counted the number of articles that contained the company name and any of the following words in the same paragraph: “scandal,” “fraud,” “investigation,” “litigation,” “corruption,” “insider trading,” or “white collar crime.” We developed this list by inductively coding 100 articles about corporate fraud in a random subsample of ten companies, and selecting the terms that were the most exhaustive and nonredundant.

Hence, rather than code the articles by affective content (e.g., Pfarrer et al., 2010), which would be more appropriate if we were trying to capture a firm’s overall reputation (Deephhouse, 2000), we instead assumed that any association in the media with one of these negative issues risked stigmatizing a firm.

Although automated content analysis of this type may exhibit some measurement error (e.g., identifying false positives), error is less likely to be systematic because the method is not subject to inter-coder reliability issues and because the volume of articles coded is much greater than can be done by hand coding. This operationalization of media coverage is similar to the strategy used by King (2008) and King and Soule (2007) when assessing how protests or boycotts influence firms, and to the technique developed by Vergne (2011) for measuring negative assessments of firms.⁷ To capture ongoing media exposure, we used a cumulative count of articles that we updated monthly. In addition, we transformed each month’s count into its logarithm to control for outliers and because we believe that the effect of media coverage increased in an exponential fashion. Finally, to control for the overall growth in the Factiva database, we employed a strategy used by Abrahamson and Fairchild (1999) in which we multiplied the count of

negative articles in each month by the ratio of the number of total articles in the database as of the first month of our observation period to the total number of articles in the database during each specific month.

We did not restrict our search to specific media sources because negative coverage emerging from many different sources, from mainstream media outlets to specialty trade journals to the alternative press, could form the basis for potential stigmatization.

Control Variables

We also collected data on a number of control variables. We first measured contagion effects related to mimetic isomorphism. In an earlier study of voluntary SOPEX adoption, Brandes et al. (2006) found that structural equivalence with previous adopters (Galaskiewicz and Burt, 1991) was significantly related to adoption. We measured this equivalence at the industry level by measuring the percentage of firms in a company's primary industry (4 digit SIC code) that had previously adopted SOPEX. We updated this variable monthly and used a cumulative count. We also measured board interlocks to previous adopters (Davis and Greve, 1997) on a monthly basis, which increased cumulatively when a company to which a firm was linked to through an interlock adopted SOPEX (using both Fortune and non-Fortune 500 adopters). Data on board interlocks was provided by authors of a previous study (Davis et al., 2003). We lagged both measures by one month.

Second, in addition to these common diffusion mechanisms, agency theory (Jensen and Meckling, 1978) argues that corporate executives favor compensation arrangements that maximize their wealth and reduce their risk. Executive compensation, however, can also be used to mitigate agency problems, and shareholders originally supported stock options to align the interests of executives and shareholders. Executives initially resisted stock options, but embraced them as the stock market began its dramatic increase in the 1990s (Englander and Kaufman, 2004). Bebchuk and Fried (2004) have argued that stock options are actually a manifestation of the agency problem because these plans have often been designed according to terms that are very favorable to executives. In terms of SOPEX, neither shareholders nor

executives actively favored it through the 1990s, but shareholders became more supportive after Enron. From the perspective of agency theory, executives would have opposed SOPEX because it would have exposed the real cost and value of this lucrative component of their compensation to shareholders, and given shareholders more information and potential power to alter the structure of stock option awards. Although we test the direct effect of shareholder resolutions, we also expect firms in which shareholders had more power over management were more likely to adopt. We control for this by including two conventional measures of shareholder power: the percentage of shares held by institutional investors and whether outsiders have a majority on the board. We measured the latter using a dichotomous measure that equaled 1 if outsiders members had a majority on the board of directors (Porac et al., 1999, Westphal and Zajac, 1994). We measured both of these variables as constants for 2001 using the Corporate Library's *Board Analyst* database.

Third, Aboody et al. (2004) found that firms with more information asymmetry, as measured by the percentage of institutional holdings, would be more likely to adopt SOPEX. We already controlled for this as a measure of shareholder power. Aboody et al. (2004) also found that firms that were more active in capital markets, as proxied by a firm's debt-to-equity ratio were more likely to adopt because it signaled strong future earnings. We measured this ratio using 2001 data from Computstat. In addition, since both Aboody et al. (2004) and Brandes et al. (2006) found that larger firms were more likely to voluntarily adopt SOPEX, we controlled for revenues and net income, using data from SEC filings in 2001. We also controlled for CEO stock ownership, which Aboody et al. (2004) found to be positively associated with SOPEX adoption. We measured this as the percentage of all shares outstanding owned by the CEO in 2001. Data for CEO ownership were collected from the Corporate Library's *Board Analyst* database.

Fourth, a straightforward economic argument would predict that companies with a higher potential stock option expense would be less likely to adopt SOPEX because they would incur a greater economic loss if they adopted. We therefore controlled for the magnitude of potential stock option expense. Aboody et al. (2004) measured potential option expense by calculating the difference between

reported net income and what net income would have been had options been expensed. We constructed a similar measure, but standardized it by calculating the change in the potential option expense disclosed in the footnote to a company's financial statement as a percentage of net income. Data were collected from SEC filings and measured as a constant for 2001.

In addition, to insure that media exposure of fraud was not simply capturing the effect of media coverage generally, we included a measure of nonfraud media coverage, which we measured by subtracting the number of articles relating to fraud from the total number of articles for each firm. Like our fraud media measure, we multiplied each monthly count by the ratio of the number of total articles in the database as of the first month of our observation period to the total number of articles in the database during each specific month. Finally, we controlled for reputation (firm's score on the 2001 *Fortune's Most Admired* list), firm age, percentage of foreign sales, and nine broad industry groups: mining, construction, manufacturing, transportation, wholesale trade, retail trade, financial/insurance/real estate, service, and miscellaneous.

RESULTS

Tables I and II present descriptive statistics and the correlation matrix, respectively, and Table III presents the results from six piecewise exponential models for the two time periods. Model 1 is the baseline model with only the control variables, while models 2 - 4 include the variables predicting the effect of the different stigmatizing pressures separately, and, in Model 5, together. Model 6 adds the two interaction terms.⁸

Insert Tables I, II, and III about here

With respect to the controls, the results show that firms with board interlocks to previous SOPEX adopters were more likely to adopt SOPEX in the second period. This finding is consistent with the role these interlocks have played in the diffusion of other corporate governance practices (Davis, 1991; Davis

and Greve, 1997; Rao and Sivakumar, 1999). In contrast to Brandes et al. (2006), however, we found that as the percentage of a firm's peers that adopted increased, firms were less likely to adopt in the second period. These two variables, which test standard diffusion arguments regarding contagion effects, were not significant in the first period and were the only effects that were significant in the second period. In addition, we find little support for standard agency theory predictions in either period. Firms in which shareholders had more power, as measured through outsiders having a majority on the board and the percentage of shares held by institutional investors, were not more likely to adopt. Looking at other controls, the results indicate that the magnitude of the potential stock option expense had a significant effect on SOPEX adoption in the first period, but the findings are the opposite of what a straightforward economic argument would predict. The results for all models show that companies that had a higher potential option expense were actually more, not less, likely to adopt SOPEX in the first period. Finally, larger firms in terms of revenues were more likely to adopt in the first period.

Turning to our hypotheses, the findings provide overall support for our core claim that firms adopted SOPEX primarily as a way to defend against stigmatization pressures. However, the findings present a more complex picture than one in which all stigmatization pressures influence adoption. The fully specified Model 6 allows us to assess the full range of media effects in conjunction with other pressures. For the period from January to December 2002, we find support for Hypothesis 1 that investigations increased the likelihood of SOPEX adoption. To transform these coefficients into hazard ratios, we simply exponentiate them, which reveals that firms under investigation were about 4.6 times more likely to adopt SOPEX than firms not under investigation. We do not find support for Hypothesis 2, however, which predicted that shareholder resolutions relating to corporate governance would be positively associated with SOPEX adoption. We did find that media exposure relating to corporate fraud increased the likelihood that firms adopted SOPEX, thus supporting Hypothesis 3. For each unit increase in the log of the number of articles, a firm was about 29% more likely to adopt SOPEX. Looking at the interaction between media exposure and investigations (Hypothesis 4a), the effect was statistically

significant but in the opposite direction of what was predicted. Firms facing investigations and high levels of media exposure about corporate fraud were actually less likely to adopt SOPEX in the year following the collapse of Enron. We find support, however, for Hypothesis 4b that firms facing shareholder pressures would be more likely to adopt when accompanied by media exposure relating to fraud. In fact, it appears that the effect of shareholder pressure on SOPEX adoption was conditional on media exposure. Finally, the results from the piecewise models reveal that none of these pressures were statistically significant after January 2003, and therefore offer support for Hypothesis 5 that SOPEX adoption was more likely to be used as a form of defensive adoption in the early stage of the practice's diffusion.

DISCUSSION

Our analysis reveals that firms facing stigmatization pressures relating to corporate fraud and ineffective corporate governance were more likely to adopt SOPEX after Enron's collapse, but that not all pressures had the same influence on adoption. Since investigations are a strong indicator that a firm may be behaving in ways that are illegitimate (if not illegal), it is not surprising that investigations were positively associated with adoption. Somewhat surprisingly, however, our results show that firms facing both an investigation and high levels of media exposure about fraud were *less* likely to adopt SOPEX. Although this is the opposite of our prediction, it makes sense if we consider the contradictory character of impression management. Ashforth and Gibbs (1990) have argued that although organizations under attack perceive the need to defend themselves, they also face more intensive scrutiny from audiences. Stakeholders may view any impression management actions, therefore, as empty gestures, rendering such actions ineffective mechanisms of defense that may actually accelerate stigmatization (Ashforth and Gibbs, 1990; Suchman, 1995). Taken together, an investigation and high levels of media exposure about fraud represented a strong stigmatization threat, and these firms were likely under the heaviest scrutiny and the most limited in what they could do in terms of impression management. Organizations facing weaker threats (e.g., investigations with no media coverage) may, therefore, have more flexibility in

taking defensive actions. Therefore, due to what Ashforth and Gibbs (1990) have called the “double-edge of organizational legitimation,” defensive practice adoption may be more feasible as a way for organizations to buffer themselves against emerging stigma rather than to remove a stigma label that stakeholders have already accepted. For example, if Enron had voluntarily adopted SOPEX after January 2002, this would have likely done little to help mitigate its stigmatization. Hence, in settings of defensive adoption, the strength of field-level pressures will matter, but contrary to what we might expect from standard accounts of diffusion (Strang and Soule 1998), the strongest threats may actually make firms less likely to adopt defensively. Future diffusion research should, therefore, pay careful attention to the relative strength of different threats in the specific diffusion contexts under examination.

Our findings also reveal that the media played a key role in shaping defensive adoption: on their own, by influencing the effect of investigations, and by being a necessary condition for shareholder resolutions to have an effect. Since stigmatization is fundamentally a process of social construction, it is logical that the media drive defensive diffusion in powerful ways. Recent work on organizational stigma has demonstrated the role of the media in exposing deviant behavior and creating spillover effects for similar organizations (Jonsson et al, 2009; Jonsson and Buhr, 2011), but has not examined how the media promote the diffusion of new practices in settings where many firms face stigmatization. Our study also contributes to an emergent stream of work demonstrating how the media and other external constituents, such as stock analysts (Nicolai et al., 2010; Rao, Greve, and Davis, 2001; Westphal and Graebner, 2010), influence the adoption of corporate practices. Furthermore, by illuminating one way in which the media shape the adoption of new practices, we add to a growing body of research that has revealed new mechanisms through which the media influence how new firms and sectors gain legitimacy (Kennedy, 2006; Pollock et al., 2008; Pollock and Rindova, 2003), how existing firms garner celebrity (Kjaergaard et al., 2011; Rindova et al., 2006), how social issues become salient for adoption by firms (Deephhouse and Heugens, 2008), and how boards react to corporate misconduct (Wiersema and Zhang, forthcoming). An important implication is that diffusion research generally should attend more carefully to the role of the

media in both directly theorizing the meaning of specific practices and in functioning as a field-level pressure similar to the state, shareholder activists, and others that are commonly at the center of diffusion research. In addition, in line with research showing that the media activates social movement influence (King, 2008), we find that shareholder activism only influences defensive adoption when the media has sufficiently stigmatized a firm by publicly associating it with fraud. We extend this work by examining a corporate response that differs from the capitulation to movement demands examined by King (2008).

Since all but three firms in our sample actually implemented SOPEX, our findings also highlight the possibility that impression management may not be strictly symbolic (Zajac and Westphal, 1994, 2001). The lack of decoupling and the negative impact of SOPEX adoption on corporate earnings suggest that impression management may not always involve empty gestures. Obviously, the positive effect we found for potential stock option expense merits further study. More importantly, however, a fruitful avenue for future research lies in untangling the difference between substance and symbolism in the context of defensive adoption. In addition, our findings raise new questions about the applicability of the recent expansion of the classic diffusion model by Kennedy and Fiss (2009). We have shown that, contrary to their model, concerns about social losses can drive initial diffusion. Our findings also suggest that practices may only be useful as defensive devices over a relatively short period of time. As more firms, particularly industry peers, adopted SOPEX, its attractiveness as a mechanism of defense appeared to decline, and later adopters were not driven by the motivation of avoiding the social losses associated with stigmatization (Kennedy and Fiss, 2009). Hence, while recent diffusion research has usefully illuminated new patterns of temporal variation in adoption motivations, our study suggests that these patterns may be specific to more narrowly conceived diffusion contexts, and researchers should remain cautious in applying generalizable diffusion models across all settings.

Finally, although research on institutionalization processes frequently pay attention “to linkage models, to the complexities of context and time, and to the effects of institutionally driven adoption on organizational survival” (Schneiberg and Clemens, 2006, p. 201), it has focused less on how controversial

practices such as SOPEX become seen as acceptable and fit for adoption among a broader set of organizations. Moreover, work on the adoption of contentious practices has tended to focus on the dynamics leading to widespread adoption and institutionalization (Briscoe and Safford, 2008; Fiss and Zajac, 2004), paying less attention to the earlier, pre-institutionalization stage during which a contested practice is made viable for early adopters. Our analysis takes seriously the idea that before practices become institutionalized, they must be theorized as appropriate solutions to recognized organizational problems. Following Soule's (2004) suggestion, we have attempted to identify links between theorizing and practice adoption.

It is important, however, to highlight some limitations of our analysis. First, the sample excluded a number of non-Fortune 500 organizations that adopted SOPEX and a number of industries in which SOPEX adoption was prevalent, such as real estate investment trusts. SOPEX adoption may have been importantly shaped by other factors that our sample obscures. Second, although work on verbal responses to scandals has assessed the effectiveness of such tactics (e.g., Elsbach, 1994; Janney and Gove, 2011), we did not examine the effectiveness of SOPEX adoption in mitigating organizational stigma nor how SOPEX adoption was received by the media, shareholder activists, or regulatory bodies. Moreover, SOPEX was not a costless act, and our findings suggest that firms that faced the lowest cost of adoption were not the most likely adopters. In order to accurately assess the effects of defensive adoption, future research needs to carefully weigh the social benefits of defensive adoption with its financial costs, as well as examine the connections between tactics of verbal impression management, defensive practice adoption, and the framing of defensive adoption (Fiss and Zajac, 2006).

In addition to advancing our knowledge of diffusion within a novel setting, our findings have practical implications for managers regarding the threat of stigmatization and the possible ways of defending against these challenges. In examining the public debates about corporate fraud and corporate governance that emerged after Enron, we find that the media and shareholder activists can quickly redefine the meaning of a practice as legitimate. We have also highlighted the key role that investigations,

shareholder activism, and the media can play in stigmatizing firms. Our findings suggest that managers can benefit from paying close attention to the complexity of how stigmatization processes unfold. Our results also suggest that managers have a broader range of defensive tactics at their disposal beyond rhetorical strategies and highlight the conditions under which managers find the adoption of defensive practices to be the most critical. In addition, managers might benefit from proactively engaging with the media and shareholder activists before their firms become implicitly associated with stigmatizing events or practices. Finally, since our findings suggest that normative pressures emanating from the media and shareholder activists may have increased pressure on regulators and created the conditions for FASB to successfully implement SOPEX at the end of 2004, managers should monitor not only external pressures on themselves, but also how these pressures may influence regulatory bodies and the broader institutional environment.

CONCLUSION

As the widely accepted two stage model of diffusion within homogenous organizational fields (Tolbert and Zucker, 1983) has given way to more complex approaches that take seriously potential variation in the temporal dynamics of diffusion (Ansari et al., 2010; Kennedy and Fiss, 2009) and the heterogeneity of organizational fields (Lee, 2009; Lounsbury, 2007; Schneiberg and Soule, 2005), it has become necessary to develop more middle-range approaches to understand how diffusion unfolds in specific contexts. Past diffusion research has focused primarily on settings in which nondeviant firms adopt new practices in order to maintain their legitimacy (e.g., Arthur, 2003; Kang and Yanadori, 2011). In this paper, we examined the dynamics of diffusion in the understudied setting of defensive adoption and found strong evidence that firms use practice adoption as a form of impression management in reaction to stigma.

Although we know generally that disruptive field-level conditions can make managers more sensitive to stakeholder influence (e.g., Jackall, 1988), our understanding of how firms respond when such disruptions occur around stigmatization has been mostly limited to strategies of verbal impression management (e.g.,

Desai, 2011; Elsbach, 1994). We have shown that defensive practice adoption is another strategy that firms employ to manage stakeholder perceptions relating to corporate identity, reputation, and legitimacy.

Taking a broader view, this paper also contributes to work on both the contested nature of markets (King and Pearce, 2010) and institutional change by expanding our understanding of the dynamics and consequences of corporate deviance and market crises (e.g., Jonnson et al., 2009; Kang and Yanadori, 2011; Weisenfeld et al., 2008). The scandals at Enron and other companies that emerged in 2002 generated challenges to the legitimacy of core market institutions embodied in the shareholder conception of control (Fligstein, 2001). This institutional destabilization opened up broad debate, albeit for a short period, about how corporations are regulated and governed. Considering the limited reach (Cunningham, 2003) of the one significant piece of legislation passed, the Sarbanes-Oxley Act, corporate managers and their advisors who were the targets of the investigations, public scrutiny, and political pressures after Enron effectively defended the legitimacy of these core market institutions. The success with which the largest corporations in the U.S. were able to constrain the work of various institutional entrepreneurs who challenged these interests (Levy and Scully, 2007) and achieve an institutional settlement (Fligstein and McAdam, 2011) that kept core market institutions mostly in tact was in part a function of these firms defending their own legitimacy as more or less virtuous actors. In line with Jonnson et al. (2009) and Maguire and Hardy (2009), our analysis has shown that contests over the legitimacy of corporate actors and market institutions are publicly fought in important ways through discourse and in the media. The financial crisis that began in 2008 pitted a similar set of incumbents and challengers in conflict over the legitimacy of some of the same institutions that govern contemporary capitalism. This paper has not only illuminated the multiple contexts in which these contests can be fought, but the relevance of institutional organizational theory for understanding their outcomes.

NOTES

¹ Defensive adoption as an impression management tactic differs from symbolic adoption, a phenomenon that has been well-studied by institutional scholars (e.g., Westphal and Zajac, 1994, 2001). The major difference is that defensive adoption may actually lead to the implementation of a new policy or practice, whereas in symbolic adoption firms announce the adoption of a new practice but never implement it.

² We make no assumptions about the ultimate effectiveness of defensive adoption as an impression management tactic, but only assume that organizational leaders perceive adoption as potentially effective.

³ These seven publications include the *Wall Street Journal*, *New York Times*, *Business Week*, *Fortune*, *Forbes*, *Washington Post*, and *San Francisco Chronicle*.

⁴ Using the Proquest/ABI Inform database, we identified articles in which stock option expensing was the main topic by searching for those that ABI Inform indexed under the following subject terms: "stock option" AND (accounting OR disclosure OR reporting).

⁵ We also considered using a Cox specification, but a visual inspection of the relative hazard functions for different magnitudes of many of the covariates provided strong evidence that our data violated the proportional hazards assumption that is key to the Cox model (Royston and Lambert, 2011).

⁶ To control for unobserved heterogeneity and correlated errors that may arise with multiple observations for each company, we ran shared frailty models (Cleves et al., 2010). The results from the chi-square tests revealed that these results were not significantly different from those reported here for all models.

⁷ Similar to Vergne (2011), we did not use the Janis-Fader coefficient of imbalance (Deephouse 1996) because we assume that any media exposure relating to fraud can potentially stigmatize a firm, regardless of how much neutral and positive coverage a firm may also receive.

⁸ We ran additional models on a subsample of 362 firms that included controls for recent declines in reputation and sales, which King (2008) found to make firms more likely to be targets of shareholder boycotts. The results reported here were nearly identical in terms of the direction, statistical significance, and magnitude of the coefficients reported here.

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FIGURE 1: Voluntary SOPEX Adopters, January 2002 – July 2004

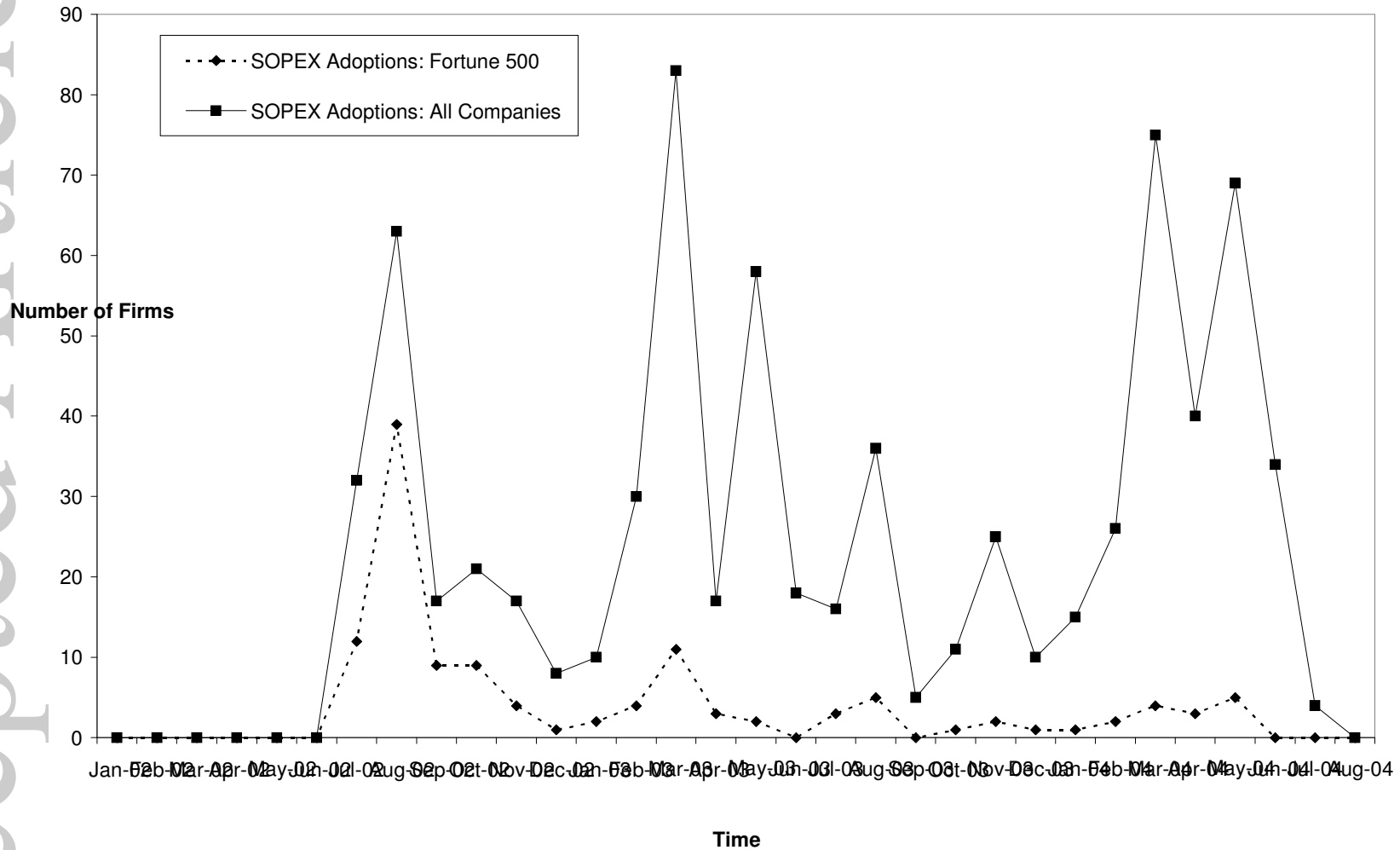


FIGURE 2: Media Coverage of SOPEX, 1990 - 2004

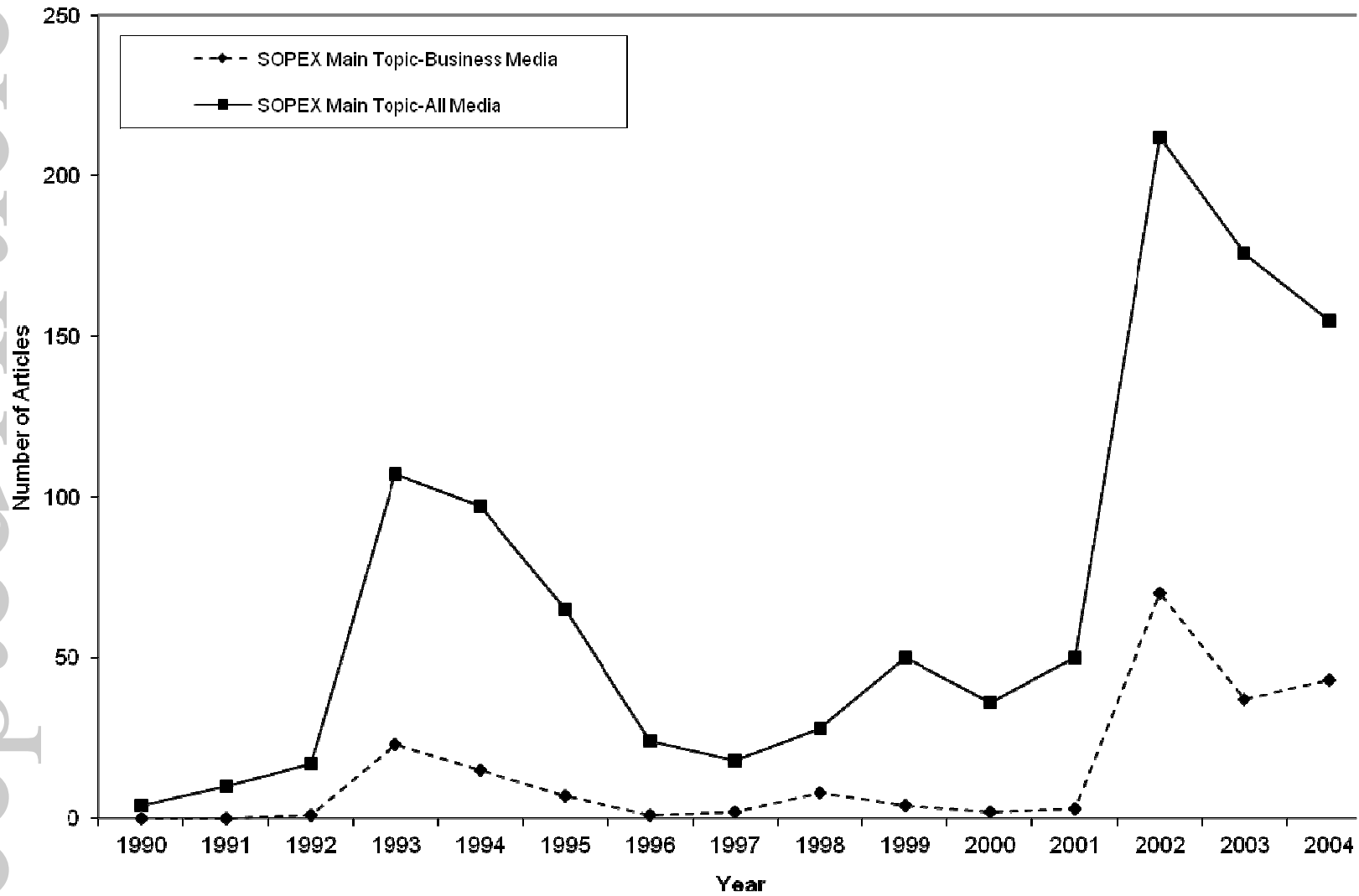


FIGURE 3: Media Coverage of SOPEX, January 2001 – July 2004

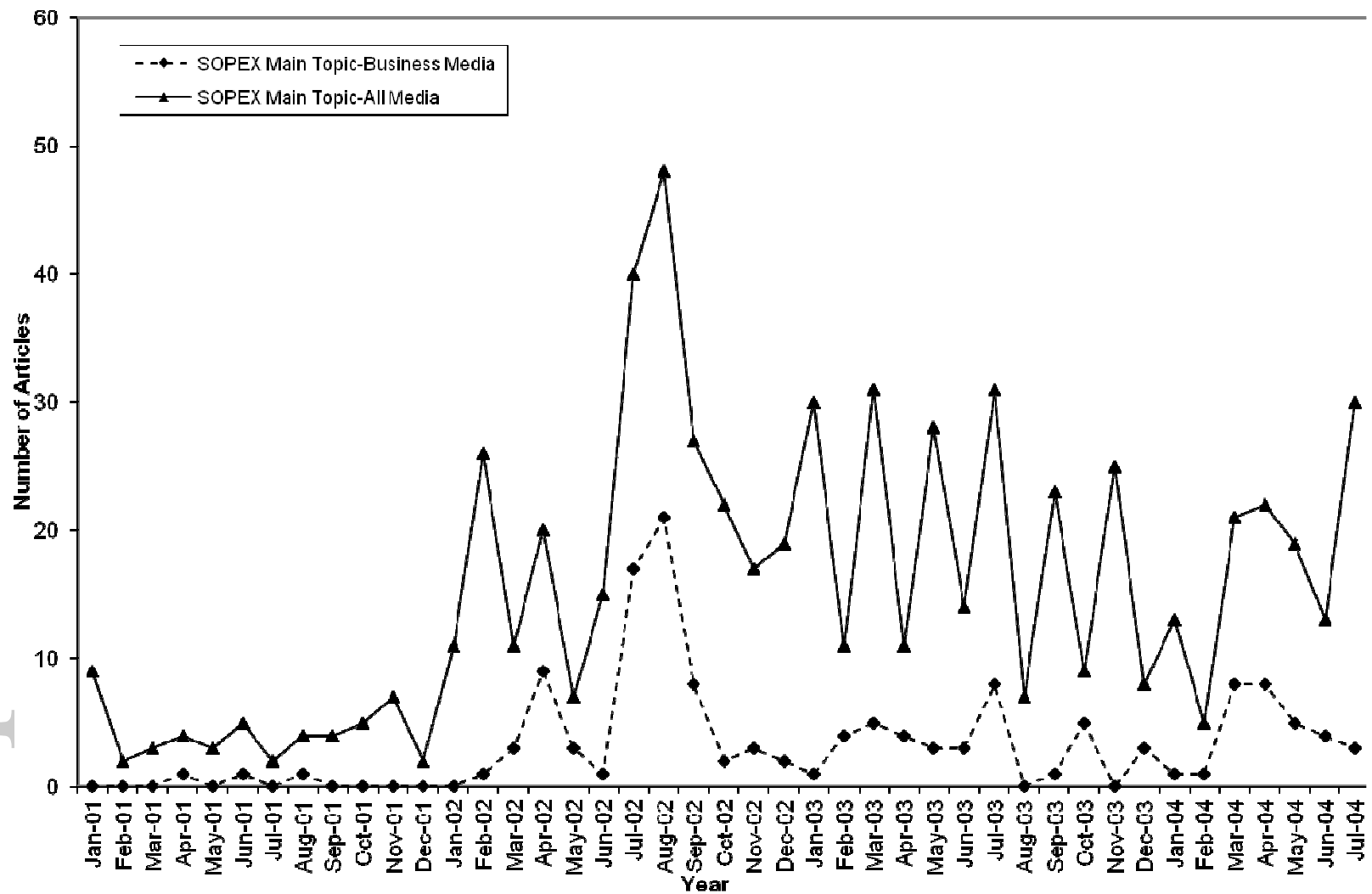


TABLE I: DESCRIPTIVE STATISTICS

	Mean	SD	Min	Max
SOE Adoption	0.26	0.44	0	1
Investigations	0.09	0.28	0.00	1.00
Shareholder Resolutions	0.55	1.04	0.00	8.00
Negative Media Coverage (ln)	2.98	1.61	0.00	9.91
Media*Investigations	0.40	1.40	0.00	9.91
Media*Resolutions	2.02	4.30	0.00	37.38
Prior Adopters-Industry	0.04	0.10	0.00	1.00
Prior Adopters-Interlocks	0.93	1.72	0.00	17.00
Outsider Majority on Board	0.94	0.24	0.00	1.00
Institutional Holdings	0.62	0.19	0.00	0.99
Debt/Equity	0.72	1.59	0.00	16.43
Revenues (ln)	9.06	0.82	8.02	12.30
CEO Stock Ownership	0.02	0.07	0.00	0.71
Stock Option Expense	0.30	2.27	0.00	84.46
Nonfraud Media Coverage	851.08	3123.28	0.00	43656.66
Most Admired	1.16	1.14	0.00	3.00
Firm Age	3.78	1.12	0.00	5.38
Foreign Sales	0.21	0.20	0.00	1.00
Construction	0.02	0.15	0.00	1.00
Manufacturing	0.40	0.49	0.00	1.00
Transportation	0.19	0.39	0.00	1.00
Wholesale	0.06	0.24	0.00	1.00
Retail	0.11	0.31	0.00	1.00
Finance, Insurance, Real Estate	0.12	0.32	0.00	1.00
Service	0.08	0.27	0.00	1.00
Miscellaneous Industry	0.00	0.05	0.00	1.00

TABLE II: CORRELATION MATRIX

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1 Investigations	1.00																
2 Shareholder Resolutions	0.21*	1.00															
3 Negative Media Coverage	0.32*	0.23*	1.00														
4 Media*Investigations	0.93*	0.19*	0.41*	1.00													
5 Media*Resolutions	0.26*	0.93*	0.35*	0.27*	1.00												
6 Prior Adopters-Industry	0.00	0.04*	0.09*	0.00	0.04*	1.00											
7 Prior Adopters-Interlocks	0.12*	0.27*	0.27*	0.12*	0.30*	0.10*	1.00										
8 Outsider Majority on Board	0.02*	0.04*	0.01	0.02*	0.03*	-0.05*	0.17*	1.00									
9 Institutional Holdings	-0.06*	0.00	-0.04*	-0.07*	-0.01	-0.02*	0.03*	0.11*	1.00								
10 Debt/Equity	0.00	0.08*	-0.06*	0.00	0.08*	0.12*	-0.05*	-0.07*	-0.03*	1.00							
11 Revenues (log)	0.33*	0.36*	0.44*	0.34*	0.39*	0.03*	0.26*	0.02*	-0.02*	-0.03*	1.00						
12 CEO Stock Ownership	-0.02*	-0.05*	-0.05*	-0.02*	-0.04*	0.01	-0.04*	-0.20*	-0.05*	0.06*	-0.07*	1.00					
13 Stock Option Expense	0.00	0.03*	0.02*	0.00	0.02*	-0.03*	-0.02*	0.00	-0.03*	-0.02	0.02*	-0.01	1.00				
14 Nonfraud Media Coverage	0.09*	0.02*	0.42*	0.14*	0.07*	-0.03*	0.06*	0.02*	-0.06*	-0.05*	0.19*	0.01	0.04*	1.00			
15 Most Admired	0.14*	0.21*	0.34*	0.16*	0.23*	-0.06*	0.19*	0.05*	0.13*	-0.14*	0.42*	0.04*	0.01*	0.22*	1.00		
16 Firm Age	0.06*	0.11*	0.08*	0.04*	0.10*	0.02	0.10*	0.10*	0.02*	0.00	0.12*	-0.11*	0.01	0.05*	0.18*	1.00	
17 Foreign Sales	0.00	0.05*	0.14*	0.01	0.08*	-0.11*	0.11*	0.07*	0.11*	-0.02*	0.09*	-0.04*	0.00	0.00	0.20*	0.09*	1

*p<.05

**TABLE III: RESULTS FROM PIECEWISE EXPONENTIAL MODELS,
ADOPTION OF SOE: JANUARY - DECEMBER 2002**

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Investigations		0.292 (0.370)			0.158 (0.366)	1.686** (0.755)
Shareholder Resolutions			0.111 (0.103)		0.120 (0.104)	-0.499 (0.342)
Negative Media Coverage				0.306*** (0.0951)	0.303*** (0.0962)	0.315*** (0.107)
Media*Investigations						-0.394** (0.190)
Media*Resolutions						0.163** (0.0835)
Prior Adopters-Industry	-4.540 (5.544)	-4.314 (5.559)	-4.443 (5.641)	-4.726 (5.707)	-4.644 (5.823)	-4.303 (5.894)
Prior Adopters-Interlocks	0.0419 (0.130)	0.0347 (0.131)	0.0356 (0.130)	-0.0507 (0.139)	-0.0583 (0.139)	-0.0730 (0.140)
Outsider Majority on Board	-0.0736 (0.487)	-0.105 (0.488)	-0.0856 (0.487)	-0.0305 (0.494)	-0.0616 (0.496)	-0.111 (0.495)
Institutional Holdings	-0.163 (0.665)	-0.177 (0.666)	-0.165 (0.667)	-0.133 (0.662)	-0.150 (0.664)	-0.128 (0.668)
Debt/Equity	-0.0303 (0.0786)	-0.0335 (0.0799)	-0.0429 (0.0795)	-0.0499 (0.0777)	-0.0646 (0.0787)	-0.0850 (0.0801)
Revenues (log)	0.671*** (0.155)	0.639*** (0.161)	0.608*** (0.166)	0.586*** (0.167)	0.509*** (0.179)	0.442** (0.181)
CEO Stock Ownership	0.859 (1.686)	0.849 (1.688)	0.817 (1.682)	1.011 (1.782)	0.975 (1.775)	0.979 (1.763)
Stock Option Expense	0.0330** (0.0135)	0.0330** (0.0135)	0.0310** (0.0136)	0.0346** (0.0135)	0.0323** (0.0136)	0.0378*** (0.0139)
Nonfraud Media Coverage	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
Most Admired	-0.138 (0.128)	-0.137 (0.128)	-0.137 (0.128)	-0.187 (0.130)	-0.188 (0.131)	-0.156 (0.131)
Firm Age	0.0163 (0.110)	0.00962 (0.110)	0.0129 (0.110)	0.0310 (0.111)	0.0272 (0.111)	0.00178 (0.112)
Foreign Sales	-0.141 (0.901)	-0.132 (0.901)	-0.103 (0.898)	-0.272 (0.896)	-0.221 (0.894)	-0.122 (0.900)
Industry Controls	YES	YES	YES	YES	YES	YES
Constant	-9.574*** (1.714)	-9.196*** (1.785)	-8.980*** (1.796)	-9.636*** (1.792)	-8.882*** (1.910)	-8.161*** (1.922)
Log-likelihood	-335.22	-334.84	-333.71	-329.28	-327.54	-323.95
Observations	12,432	12,432	12,432	12,432	12,432	12,432
Number of groups	468	468	468	468	468	468
Standard errors in parentheses; *** p<0.01, ** p<0.05, * p<0.1						

**TABLE III (cont): RESULTS FROM PIECEWISE EXPONENTIAL MODELS,
ADOPTION OF SOE: JANUARY 2003 - JULY 2004**

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Investigations		0.186			0.119	0.530
		(0.448)			(0.469)	(1.354)
Shareholder Resolutions			-0.196		-0.202	-0.0452
			(0.151)		(0.151)	(0.602)
Negative Media Coverage				0.132	0.133	0.166
				(0.143)	(0.143)	(0.163)
Media*Investigations						-0.0852
						(0.279)
Media*Resolutions						-0.0383
						(0.140)
Prior Adopters-Industry	-4.496**	-4.426**	-4.222**	-4.737**	-4.425**	-4.465**
	(2.087)	(2.088)	(2.064)	(2.108)	(2.091)	(2.101)
Prior Adopters-Interlocks	0.169***	0.171***	0.175***	0.172***	0.181***	0.178***
	(0.0641)	(0.0647)	(0.0635)	(0.0637)	(0.0635)	(0.0645)
Outsider Majority on Board	-0.466	-0.458	-0.421	-0.428	-0.376	-0.360
	(0.659)	(0.660)	(0.661)	(0.665)	(0.668)	(0.672)
Institutional Holdings	-0.0515	-0.0145	-0.0851	-0.124	-0.134	-0.149
	(0.831)	(0.838)	(0.830)	(0.834)	(0.842)	(0.843)
Debt/Equity	0.0696	0.0720	0.0886	0.0696	0.0924	0.0953
	(0.0711)	(0.0711)	(0.0706)	(0.0710)	(0.0708)	(0.0713)
Revenues (log)	0.277	0.236	0.331	0.172	0.196	0.188
	(0.222)	(0.243)	(0.225)	(0.250)	(0.265)	(0.266)
CEO Stock Ownership	0.575	0.565	0.445	0.733	0.586	0.624
	(2.060)	(2.064)	(2.085)	(2.077)	(2.106)	(2.122)
Stock Option Expense	-1.199	-1.223	-1.247	-1.224	-1.300	-1.292
	(0.772)	(0.781)	(0.804)	(0.766)	(0.808)	(0.814)
Nonfraud Media Coverage	0.000	0.000	0.000	0.000	0.000	0.000
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Most Admired	-0.0946	-0.0958	-0.0743	-0.121	-0.101	-0.0987
	(0.156)	(0.156)	(0.157)	(0.158)	(0.158)	(0.159)
Firm Age	-0.0388	-0.0457	-0.0258	-0.0348	-0.0264	-0.0302
	(0.133)	(0.134)	(0.133)	(0.134)	(0.135)	(0.135)
Foreign Sales	0.758	0.731	0.828	0.665	0.716	0.746
	(1.116)	(1.120)	(1.121)	(1.111)	(1.117)	(1.112)
Industry Controls	YES	YES	YES	YES	YES	YES
Constant	-6.623***	-6.251**	-7.153***	-6.097**	-6.361**	-6.401**
	(2.429)	(2.589)	(2.456)	(2.492)	(2.650)	(2.654)
Log-likelihood	-335.22	-334.84	-333.71	-329.28	-327.54	-323.95
Observations	12,432	12,432	12,432	12,432	12,432	12,432
Number of groups	468	468	468	468	468	468
Standard errors in parentheses; *** p<0.01, ** p<0.05, * p<0.1						