

Overseas Background Director, Internal Control and Corporate Innovation

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Abstract

Based on the high-ladder team theory, this paper selects A-share listed companies from 2015 to 2019 as samples to study the relationship between directors' overseas background, internal control and enterprise innovation. The results show that directors with overseas background have significant influence on innovation input and innovation output. Internal control quality also has a significant inhibiting effect on innovation input and innovation output. Further research finds that the quality of internal control plays a mediating role in the relationship between overseas directors and firm innovation. It enriches the theoretical achievements in the field of technological innovation, expands the research field of the characteristics of executives' overseas background, and provides theoretical reference for the government to introduce high-level talents and enterprises to select high-level talents with overseas study background for evaluation.

Keywords

Director with Overseas Background; Internal Control; Enterprise Innovation.

1. Introduction

In order to meet the needs of The Times and solve development problems, the Fifth Plenary Session of the 18th CPC Central Committee put forward the five development concepts of "innovative, coordinated, green, open and shared". Among these five concepts, the first one emphasizes the importance of innovative development. Under the guidance of such high-quality development concept, Chinese enterprises have further clarified the view that "scientific and technological innovation is the source of the development of social productive forces, and is an important way for enterprises to form unique products and technologies, so as to have their own core competitiveness", and set off a wave of "mass innovation". There are many internal governance factors that affect innovation, such as employee satisfaction (Liu Jing et al., 2020), executive compensation (Xu Yue, 2018; Sun Xixian et al., 2021), equity incentive (Xu Changsheng, 2018; Li Xuejing et al., 2020), governance contract (Zhang Min et al., 2014), executive characteristics (Wang Changrong et al., 2019; He Xu et al., 2020). With the acceleration of globalization and the deepening of "the Belt and Road Initiatives" development strategy, more and more enterprises tend to recruit managers with overseas background to join the team. Overseas talents have become the backbone of Chinese enterprise management and influence the decision-making activities of enterprises with their own unique values and cognitive views. Previous studies have found that managers with overseas backgrounds play a positive role in enterprises' foreign investment, overseas mergers and acquisitions, overseas financing, technological innovation and improvement of economic performance. Few scholars have studied the role of internal control between directors' overseas background and enterprise innovation from the perspective of directors' overseas background. Therefore, it is still an empirical study to clarify the relationship between directors with overseas background, internal control and enterprise innovation. This paper manually selects A-share listed companies from 2015 to 2019 as samples, and based on the theory of high-ladder team, studies

the promotion effect of directors with overseas background on technological innovation from the perspective of individual characteristics of executives, so as to enrich the research content in the field of executives' overseas background.

The research significance of this paper is as follows: First, it clarifies the relationship between directors with overseas background and innovation input and innovation output. The higher the proportion of directors with overseas background, the greater the innovation input and output of enterprises. Second, the quality of internal control has a inhibiting effect on the innovation input and output of enterprises. Thirdly, the effectiveness of internal control plays an intermediary role between directors with overseas background and innovation input and innovation output, which provides theoretical guidance for the government and enterprises to select high-level talents with overseas background.

2. Theoretical Analysis and Research Hypothesis

Is a standing body of the company, the board of directors of the board of directors of the company's senior management team members, director of personal characteristics and ability is very important to the development of the enterprise, personal factors such as its values, cognitive view decides its preferences in the work of the enterprise strategic target, strategic planning, resource configuration choice plays an important role, and ultimately to influence the financial performance and long-term development of enterprises. If a company director has work experience and study experience abroad, these important life experience will affect the director's cognitive ability and concept, and will certainly affect the company's innovation decision. Bill Gates believes that America's ability to recruit innovative minds from around the world is its greatest advantage in the global high-tech market. In the United States, policy attracts talent, and talent creates wealth for the country. It is an inevitable choice and historical responsibility for China's large state-owned enterprises to go global by implementing the strategy of strengthening enterprises with talents and leading technology and attracting technology and talents from developed countries. Large state-owned enterprises should deeply understand the strategic decision of the central government to introduce overseas high-level talents, pay close attention to the introduction of overseas high-level talents with broader thinking and the spirit of being eager for talents, and give full play to and tap the wisdom of each overseas high-level talents through institutional innovation. Enterprises attract talents with sincerity, and talents promote enterprise progress with wisdom. Yang Lin (2018) put forward that technological innovation is complicated and uncertain, and the cooperative and mutual relationship network of returnees provides a strong social resource endowment for technological innovation, which has also become one of the important factors for the improvement of corporate innovation performance.

From the perspective of returnees themselves, directors with overseas experience have enhanced their frustration ability and adaptability due to their unique long-term experience of studying and working abroad alone. After returning to China, they can more quickly get familiar with the operation mode of domestic enterprises and the practice mode of enterprise innovation activities. Innovation failure rate is bigger, the risk is higher, net inflow is big, is not an overnight activity, site director to study and work overseas background is commonly in the developed countries, innovation atmosphere more thick, more profound understanding the importance of innovation to the enterprise core competitiveness, so the region technology not only stand on the international front, technology management experience is more rich. In addition, the number of high-level talents with overseas background is rare in China, and they have a certain "star effect". Compared with the locally trained executive talents, they have a stronger voice among the management, can better play the advisory and advice function of the board of directors, and improve the investment in innovation.

From the perspective of relationship network, overseas directors are easy to get in touch with cutting-edge technology, learn advanced technology and management experience abroad, and form a more accurate judgment on the market trend. Back to home after the integration of the resources of the directors will abroad, establish lasting contact with overseas institutions and overseas talent and communication, at the same time, combining with the domestic consumer demand, in the domestic to foreign advanced technology into the latest product market preferences, also conducive to the domestic products to the world, thus promote enterprise strengthen innovation.

From the perspective of government connection, many domestic scholars have demonstrated that private enterprises have a stronger desire for innovation than state-owned enterprises with endowment. That is to say, the closer the relationship between enterprises and the government, the worse the innovation efficiency of enterprises, and directors with overseas background can improve the situation that is not conducive to corporate innovation. The presence of directors with foreign backgrounds weakens the relationship between government and business. Directors with overseas background have no strong desire to study and work abroad for rent-seeking, have no strong connection with the domestic government, and have a relatively strong sense of innovation. After returning to work in China, they rationally allocate resources, increase the company's research and development efforts, improve the company's innovation level, and then improve the company's innovation performance.

Internal control is an important means of enterprise risk management, and scholars have drawn different conclusions about what impact it will have on enterprise innovation. Scholars who agree with the "internal control promotion theory" believe that internal control can provide target guidance and structural support for enterprise innovation, which is conducive to enterprises to increase innovation input (Dey, 2010). Domestic scholars measured the quality of enterprise internal control by the implementation of Basic Standards of Enterprise Internal Control, Xiamen University Index (internal control index constructed by Xiamen University Internal Control Research Group) and DIB Index respectively, and found that high quality internal control is conducive to enterprises to increase innovation input (Zhong Kai et al., 2016; Yang Daoguang et al., 2019; Zhou Xuefeng and Zuo Jing, 2019). Identity "internal control theory of inhibition of scholars argue that the internal control will worsen enterprise innovation environment to some extent (Jensen, 1994), affect the enthusiasm of management to increase investment in innovation (Engel et al., 2007), from the enterprise to carry out innovation activities of economic resources (Cohen et al., 2008), as a result, the internal control will be harmful to enterprise innovation investment. Bargeron et al. (2010) compared the data of companies in the United States, Canada and the United Kingdom before and after the promulgation of Sarbanes-Oxley Act, and found that the institutionalization of internal control was not conducive to the increase of investment in innovation. Based on the data of China's listed companies, Li et al. (2017) measured the quality of internal control by using the internal control index (DIB index) constructed by Dubault Company, and found that the higher the quality of internal control, the less the innovation input of the enterprise. This paper agrees with the view of internal control inhibition theory, and believes that the higher the quality of internal control, the weaker the innovation enthusiasm of enterprises, and the lower the innovation input and output.

Based on the above analysis, this paper puts forward the following hypotheses:

H1: Other conditions being the same, directors with overseas background promote innovation input and output of enterprises.

H2: When other conditions remain unchanged, internal control quality inhibits enterprise innovation input and output.

H3: When other conditions remain unchanged, the quality of internal control plays an intermediary role between directors with overseas background and innovation input and output of enterprises. In other words, the higher the quality of internal control, the weaker the promoting effect of directors' overseas background on enterprise innovation, the lower the quality of internal control, and the more significant the promoting effect of directors' overseas background on enterprise innovation.

3. Research Design

3.1. Sample Selection and Data Sources

In this paper, the A-share listed companies from 2015 to 2019 were selected as samples, ST companies and samples with missing data were excluded, and 2652 data were finally obtained. Overseas background data of directors (download the annual report of each company from JCCIO, search the key word "director", and read whether the director in the annual report of each company has overseas study background, study visiting background and overseas work experience) Through manual collection of the company's annual report, the internal control quality data comes from the internal control index database of Dibo. The enterprise innovation data and financial data are from the national Tai 'an database.

3.2. Definition and Interpretation of Variables

(1) Director with overseas background. The director with overseas background refers to the director who has studied and worked in overseas regions and countries in the previous year. Overseas study refers to studying abroad as a student/studying abroad as a visiting scholar, etc. Overseas work refers to working in overseas enterprises, but does not include working experience in overseas branches of China. Overseas Overseas Background Measure the proportion of directors with overseas background selected by directors to board members.

(2) Enterprise innovation. At present, the following methods are used to measure innovation in domestic and foreign studies. From the perspective of innovation investment, there are two ways: the proportion of R&D investment in operating revenue and the proportion of R&D personnel in the total number of people. From the perspective of innovation output, there is the number of patents applied by enterprises (2015, Pan Qingquan). In order to fully measure innovation performance, this paper selects innovation input and innovation output. Innovation input is equal to the proportion of annual R&D expenditure in annual business revenue. Innovation output is equal to the annual number of patents filed by enterprises.

(3) internal control of quality. The internal control index of China's listed companies is the most comprehensive method to reflect the quality of internal control at present. The value of the index is within the range of [0,1000], which is divided by 100 during the regression to ensure the unity of units.

(4) Control variables. According to the research of existing scholars, enterprise performance, enterprise size, the separation of chairman and general manager, the shareholding ratio of top ten shareholders, asset-liability ratio and geographical location are all factors affecting enterprise innovation. These variables are selected as the control variables in this paper.

3.3. Model Design

In order to test the relationship between directors with overseas background and enterprise innovation, this paper constructs a model (1); In order to test the relationship between internal control quality and enterprise innovation, model (2) is constructed. In order to test the relationship between the quality of internal control in overseas directors and enterprise innovation, model (3) and model (4) are established on the basis of model (1).

Table 1. The names and assignments of the relevant variables

| Variable types | Symbolic | Variable name | Measurement method |
|-----------------------|----------|--|--|
| Explained variable | TI | RD | The innovation |
| | | PATENT | Number of patent applications |
| Explanatory variables | FOR | The proportion of directors with overseas background | T annual R&D investment /t annual total operating revenue |
| Intervening variable | ICINDEX | Internal control quality | Number of directors with overseas background/total number of directors in the year t |
| Control variables | ROA | Enterprise performance | Deb internal control index of China listed companies |
| | NAT | Property rights | T annual net profit /t annual total assets |
| | SIZE | The enterprise scale | Dummy variable, state-owned enterprises take 1, non-state-owned enterprises take 0 |
| | TOWP | Separate positions of chairman and general manager | Logarithm of ending total assets |
| | SHAR | The shareholding ratio of the top 10 shareholders | 1 for both positions; If you do not hold two concurrent posts, you will get 0 |
| | DEBT | Asset-liability ratio | Number of shares held by the top ten shareholders in t year/total number of shares in t year |
| | PROVINCE | The geographical location | T Annual total liabilities/total assets |
| | | | The province of the enterprise, the eastern region is 1; 2 in the central region and 3 in the western region |

$$TI = \alpha_0 + \alpha_1 * FOR + \alpha_2 * Control + \epsilon \tag{1}$$

$$TI = \alpha_0 + \alpha_1 * ICINDEX + \alpha_2 * Control + \epsilon \tag{2}$$

$$ICINDEX = \alpha_0 + \alpha_1 * FOR + \alpha_2 * Control + \epsilon \tag{3}$$

$$TI = \alpha_0 + \alpha_1 ** FOR + \alpha_2 * ICINDEX + \alpha_3 ** Control + \epsilon \tag{4}$$

Where, TI represents innovation, including innovation input and innovation output, represented by RD and PATENT respectively. FOR represents the proportion of directors with overseas background, and ICINDEX represents the effectiveness of internal control. Control is the Control variable, which mainly includes company performance (ROA), property right (NAT), company size (SIZE), separation of chairman and general manager (TOWP), shareholding ratio of top ten shareholders, asset-liability ratio (SHAR), and geographical location (PROVINCE).

4. Empirical Analysis

4.1. Descriptive Statistical Analysis

Table 2 is the descriptive statistical results of the variables. As can be seen from the descriptive statistical results of variables in Table 2, most of the sample enterprises are from the eastern region, and some are from the central and western regions. The average ROA of the sample enterprises is 4%, the average asset-liability ratio DEBT is 46%, and the average shareholding ratio of the top ten shareholders is 59.19%. There is a huge difference between the maximum and minimum values, so it is necessary to do the tail reduction treatment of 0.01 when doing

the regression analysis. In the sample enterprises, the average annual government patent application is 8.98, and the average proportion of R&D investment in sales revenue is 3%. Since there is a huge gap between the maximum and minimum number of PATENT applications, they are standardized in the actual regression, and the original value is divided by 100 as the value of the PATENT variable for regression analysis.

Table 2. Descriptive statistics of variables

| Variable | Obs | Mean | Std. Dev. | Min | Max |
|----------|-------|-------|-----------|-------|-------|
| FOR | 2,652 | 0.18 | 0.21 | 0 | 1 |
| PATENT | 2,652 | 8.98 | 37.61 | 0 | 287 |
| RD | 2,652 | 0.03 | 0.04 | 0 | 0.23 |
| ICINDEX | 2,652 | 6.15 | 1.77 | 0 | 8.09 |
| TOWP | 2,652 | 0.31 | 0.46 | 0 | 1 |
| PROVINCE | 2,652 | 1.48 | 0.77 | 1 | 3 |
| NAT | 2,652 | 0 | 0.03 | 0 | 1 |
| SIZE | 2,652 | 22.67 | 1.54 | 19.74 | 28.86 |
| ROA | 2,652 | 0.04 | 0.06 | -0.26 | 0.22 |
| SHAR | 2,652 | 59.19 | 16.7 | 19.94 | 93.52 |
| DEBT | 2,652 | 0.46 | 0.21 | 0.06 | 0.93 |

4.2. Regression Results and Analysis

4.2.1. Regression Analysis of the Relationship between Directors with Overseas Background and Enterprise Innovation

In order to investigate the relationship between the overseas background of directors and enterprise innovation, this paper makes a regression score for Model (1)

Analysis. In the analysis, 1% of the continuous financial variables were reduced, and the specific results are shown in Table 3. The regression results show that directors with overseas background are positively correlated with the innovation input and innovation output of the firm, that is, the higher the proportion of directors with overseas background, the higher the innovation input and innovation output of the firm, which verifies Hypothesis 1. In addition, the dual position of chairman and general manager, geographical location, firm size, shareholding ratio of top ten shareholders, asset-liability ratio and innovation input have significant effects, and firm size, firm performance and innovation output have significant effects.

4.2.2. Regression Analysis of the Relationship between Internal Control Quality and Enterprise Innovation

In order to investigate the relationship between the quality of internal control and enterprise innovation, this paper conducts a regression score for Model (2)

Analysis. In the analysis, 1% of the continuous financial variables were reduced, and the specific results are shown in Table 4. The regression results show that the quality of internal control significantly restrains the innovation input and innovation output of the firm, that is, the higher the quality of internal control, the lower the innovation input and the less the innovation output of the firm, which verifies Hypothesis 2. The dual position of chairman and general manager, geographical location, enterprise size, shareholding ratio of top ten shareholders, asset-liability ratio and innovation input have significant effects, and enterprise size, enterprise performance and innovation output have significant effects.

Table 3. Regression of the relationship between directors with overseas background and enterprise innovation

| Variable | RD | PATENT |
|----------------|-----------|-----------|
| FOR | 0.017*** | 0.091** |
| | (4.700) | (2.510) |
| TOWP | 0.009*** | 0.017 |
| | (5.630) | (1.070) |
| PROVINCE | -0.007*** | -0.006 |
| | (-7.01) | (-0.610) |
| NAT | 0 | -0.181 |
| | (-0.020) | (-0.680) |
| SIZE | -0.002*** | 0.018*** |
| | (-4.000) | (2.970) |
| ROA | 0.007 | 0.560*** |
| | (0.590) | (4.190) |
| SHAR | 0.000*** | 0.000 |
| | (-3.100) | (0.390) |
| DEBT | -0.042*** | -0.027 |
| | (-9.020) | (-0.580) |
| Control | 0.119*** | -0.360*** |
| | (9.470) | (-2.84) |
| R ² | 0.126 | 0.019 |
| Obs | 2652 | 2652 |

Table 4. Regression of the relationship between internal control quality and enterprise innovation

| Variable | RD | PATENT |
|----------------|-----------|-----------|
| ICINDEX | -0.001*** | -0.014*** |
| | (-3.500) | (-3.340) |
| TOWP | 0.009*** | 0.017 |
| | (5.550) | (1.040) |
| PROVINCE | -0.007*** | -0.008 |
| | (-7.300) | (-0.880) |
| NAT | 0 | -0.175 |
| | (-0.010) | (-0.660) |
| SIZE | -0.002** | 0.025*** |
| | (-2.480) | (4.060) |
| ROA | 0.017 | 0.656*** |
| | (0.221) | (4.790) |
| SHAR | 0.000*** | 0.000 |
| | (-2.860) | (0.470) |
| DEBT | -0.044*** | -0.039 |
| | (-9.320) | (-0.820) |
| Control | 0.110*** | -0.401*** |
| | (8.880) | (-3.210) |
| R ² | 0.123 | 0.020 |
| Obs | 2652 | 2652 |

4.2.3. Regression Analysis of the Relationship between Directors with Overseas Background, Quality of Internal Control and Enterprise Innovation

In order to investigate the relationship between the quality of internal control of directors with overseas background and enterprise innovation, this paper conducts a regression analysis on models (3) and (4) based on model (1). In the analysis, the continuous financial variables were reduced by 1%, and the specific results are shown in Table 5. Regression results show that the overseas background board quality is significantly negative correlation with internal control, internal control quality in overseas background played an intermediary role between directors and enterprise innovation, namely the higher the quality of internal control, director of the overseas background on enterprise innovation promoting effect is weak, the lower the quality of internal control, director of the overseas background to the enterprise innovation to promote the more significant role. Hypothesis 3 is true.

Table 5. Regression of the relationship between directors with overseas background, quality of internal control and enterprise innovation

| Variable | ICINDEX | RD | PATENT |
|----------------|-----------|-----------|-----------|
| FOR | -0.330** | 0.016*** | 0.086** |
| | (-2.02) | (4.580) | (2.390) |
| ICINDEX | | -0.001*** | -0.014*** |
| | | (-3.330) | (-3.25) |
| TOWP | 0.022 | 0.009*** | 0.017 |
| | (0.300) | (5.660) | (1.090) |
| PROVINCE | -0.156*** | -0.007*** | -0.008 |
| | (-3.62) | (-7.24) | (-0.84) |
| NAT | 0.851 | 0.001 | -0.169 |
| | (0.710) | (0.030) | (-0.64) |
| SIZE | 0.251*** | -0.002*** | 0.022*** |
| | (9.06) | (-3.37) | (3.490) |
| ROA | 6.967*** | 0.017 | 0.658*** |
| | (11.560) | (1.260) | (4.810) |
| SHAR | -0.003 | -0.000*** | 0.000 |
| | (-1.23) | (-3.19) | (0.310) |
| DEBT | -0.541** | -0.043*** | -0.035 |
| | (-2.55) | (-9.19) | (-0.74) |
| Controls | 0.823 | 0.120*** | 0.348*** |
| | (1.440) | (9.580) | (2.750) |
| R ² | 0.099 | 0.129 | 0.022 |
| Obs | 2652 | 2652 | 2652 |

5. Robustness Test

In order to test the reliability of the above conclusions, this paper first excluded the overseas backgrounds of executives with only Hong Kong, Macao and Taiwan backgrounds (the key variable in this study). Consider Hong Kong, Macao and Taiwan area and mainland China are very similar in the regional and cultural, and political and economic contact is very close, in order to ensure that executives overseas background information the authenticity and validity of this study ruled out only a working and studying experience of executives in the above areas, only to countries or regions outside China have defined as working and studying experience of director with overseas background. Then, the standardized robustness test of the value of the variable and the one-year difference between the independent variable and the dependent

variable were carried out, and the regression was continued after changing the values of the above related variables according to the regression method mentioned above. The previous research conclusions were still valid, indicating that the research conclusions of this paper had certain reliability.

6. Research Conclusions and Implications

Based on the high-ladder team theory, this paper takes A-share manufacturing listed companies from 2015 to 2019 as samples and studies the promoting effect of directors with overseas backgrounds on technological innovation from the perspective of individual characteristics of executives. The empirical results show that directors with overseas background are positively correlated with firm innovation; Internal control quality is negatively correlated with enterprise innovation; Directors with overseas background are negatively correlated with the quality of internal control; The quality of internal control plays an intermediary role between the overseas background of directors and the innovation performance of firms. In other words, the higher the quality of internal control, the weaker the promoting effect of the overseas background of directors on the innovation performance of firms.

According to the research conclusions of this paper, the enlightenment is as follows: (1) Actively introduce overseas talents. In the situation of high-quality economic development, the introduction of overseas high-level talents plays a positive role in promoting the renewal of corporate executives' internal ideas and the formation of innovative culture, which is conducive to arousal of the creative consciousness of the whole talent team and providing the level of innovation of the enterprise. (2) flexibly use the internal control system. Innovation activities are characterized by high uncertainty, high risk and large amount of capital investment. Therefore, it is not an activity that can be accomplished overnight. Therefore, enterprises need to strengthen risk management and control R&D risks within a controllable range. However, enterprises should not give up eating for fear of choking, and it is not advisable to abandon the research and development activities with good benefits and high risks. Only by flexibly using the internal control system can the innovation potential of enterprises be stimulated to a greater extent.

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