

# **Impact of Business Nature on Corporate Governance Report through a Degree of Independence of Board of Directors: A Case Study of Listed Companies in the Stock Exchange of Thailand**

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## **Abstract**

The objective of this research is to develop causal relationship model of the impact of business nature on corporate governance report through a degree of independence of board of directors by using a case study of listed companies in Stock Exchange of Thailand (SET). This model adopted three kinds of latent variables and utilized Form 56-1 data and notes to financial statement year 2016 of 175 listed companies in SET by using a statistical method of descriptive analysis, causal relationship model and LISREL 8.80 Student Edition Program.

The results show that the hypothetical model and the empirical model are in harmony. There is the positively direct impact of nature of business (NTB) on independence of the Board of Directors (IBD) with a statistical significance of 0.01 and a coefficient value of 1.17\*\* and there is the positively direct impact of IBD on Corporate Governance Report (CGR) with a statistical significance of 0.01 and a coefficient value of 1.01\*\*.

**Keywords:** Board of Directors, Corporate Governance, Report

## **Introduction**

The global economic crisis during 2007-2009 raised organizations' awareness of the importance of financial information disclosure and the role of an organization that monitors corporate governance as OECD (The Organization of Economic Cooperation and Development). The Financial Stability Forum has designated the principles of corporate governance as one of the 12 key standards for sound financial system to be a major basis for consideration of good corporate governance in a report on the criteria of good practice and code of conduct of countries in disclosure practices. Business information and corporate governance disclosure practice are considered very important to the growth and sustainability of a company. In addition to reduce conflict of interest and comply with applicable laws, good corporate governance can promote a company to be an attractive business alliance partner. Therefore, it helps companies to have investment opportunities for gaining more profits (Bonna, 2012). Relationship and corporate governance characteristics, relationships between groups of people involved in corporate governance system have impact on corporate governance because shareholders who are authorized to control the corporation's business affairs, no matter individual or family or business alliance or holding company or cross holding, have greatly influence on corporate behavior and practices. Corporate governance can be used as an efficient method to reduce corruption in administration and enhance company's efficiency (Elshandidy & Neri, 2015). Moreover, corporate creditors start to play a vital role in intensifying companies that makes loan from them to follow guidelines and principles of corporate governance more and more. It can be said that corporate creditors

plays their roles as external auditors (Kang et al., 2007)

However, corporate successful financial performance originates from different characteristics of corporate governance in terms of firm size, debt to equity ratio, audit committee existence, and Board independence is associated with a firm's level of disclosure practices (Xia & Beelde, 2018) and the level of disclosure practices with different characteristics of corporate governance such as firm size and financial ratio (Nerantzidis & Tsamis, 2017). Based on the mentioned above reasons, the researcher is interested in studying about impact of business nature on corporate governance report through a degree of independence of board of directors: Case study of listed companies in the Stock Exchange of Thailand.

## Research Objective

The objective of the research is to analyze causal relationship of the impact of nature of business on corporate governance report through a degree of independence of board of directors: case study of listed companies in the Stock Exchange of Thailand.

## Literature Review and Research Hypotheses

With regards to a review of literatures to analyze the impact of nature of business on corporate governance report through a degree of independence of board of directors: case study of listed companies in the Stock Exchange of Thailand, the review of related research studies can be concluded as shown in Table 1.

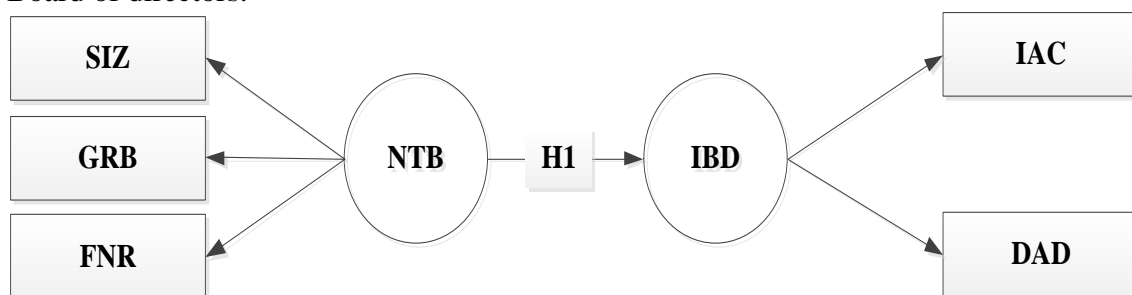
**Table 1** The summary of research studies that are related to the study

Authors	Variables	Results
Madhani & Pankaj (2018)	- Firm size - Corporate governance - Disclosure practices.	Firm size had an impact on corporate governance and disclosure practices.
Toru & Helen (2017)	- Organizational citizenship behavior. - Board capital. - Informal board hierarchy order.	Board capital, informal board hierarchy order had an impact on organizational citizenship behavior.
Gaizka (2017)	- Role of stakeholders. - Corporate governance.	Role of stakeholders had an impact on corporate governance and disclosure.
Mariateresa & Andrea (2016)	- Independent directors' ratio, board size, CEO-duality. - Financial transparency and disclosure.	Independent directors and board size had an impact on financial transparency and disclosure.
Rasmussen, Lasegard, & Korhonen-Sande (2014)	- Board composition. - Corporate governance. - High-growth firms.	Board composition and high-growth firms had an impact on corporate governance.
Obigbemi, Iyoha, & Ojeka (2015)	- Firm size - Corporate governance - Financial Performance	Firm size and financial performance had an impact on corporate governance and disclosure practices.
Yasser, Entebang, & Mansor (2015)	- Corporate governance. - Firm performance.	Good corporate governance had an impact on firm performance.
Reegan & Iam (2014)	- Responsibilities of Board of directors.	Responsibilities of Board of directors were important to

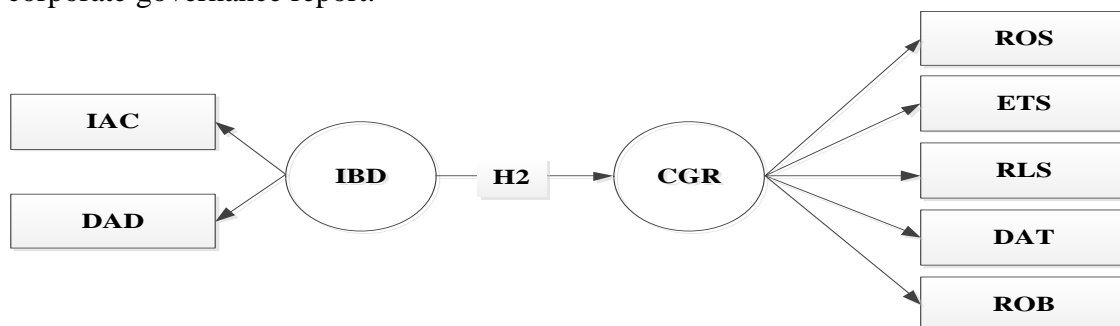
	- Corporate governance.	corporate governance system.
<b>Table 1</b> The summary of research studies that are related to the study		
<b>Authors</b>	<b>Variables</b>	<b>Results</b>
Dwi, Tyasing, & Malangkuçewara (2013)	- Corporate governance - Firm size - Earning Management	Corporate governance in terms of firm size, board of directors, and audit quality had an impact on earning management.
Souhir & Khamoussi (2013)	- Corporate governance disclosure. - Disclosure and Transparency.	Disclosure and transparency had an impact on corporate governance.
Wei & Asokan (2009)	- Corporate governance. - Shareholder rights. - Earnings quality.	Corporate governance in terms of shareholder rights had an impact on earnings quality.
Helen (2003)	- Operation of Independent Directors. - Independence. - Remuneration. - Qualification. - Assurance and autonomy	Independence, remuneration, qualification, and assurance and autonomy had an impact on operation of independent directors.
Jesover (2001)	- Shareholder rights - Equitable treatment. - Corporate governance.	Rights of Shareholders Equitable treatment of shareholders affect the supervision and disclosure of information of the business.

Based on the literature review as mentioned above, the researcher determined the research hypotheses as follow:

**The research hypothesis 1:** Business nature had a direct positive impact on independence of Board of directors.



**Research hypothesis 2:** Independence of Board of directors had a direct positive impact on corporate governance report.



## Methodology

### Population

The population in this research study was the listed companies in the Stock Exchange of Thailand which was the annual information for the year 2016. There were totally 310 companies (data dated on 1 January 2017). The population did not include companies in the MAI and financial groups and other companies that their data were not in line with this research study as these companies could not identify clearly the objective of fundraising that might affect good corporate governance report and would have impact on data analysis accordingly (Booth et al., 2000; Sukcharoensin, 2003)

### Sample

The researcher used probability sampling method to determine the sample size when finite population; a total of 310 companies, was given. The sample size of this research was calculated by using Taro Yamane Yamane (1973)

$$\text{Formula} \quad n = \frac{N}{1 + Ne^2}$$

where

n	=	sample size
N	=	population size
e	=	margin of error for sampling

$$\text{Then the sample size was} \quad n = \frac{310}{1 + 310(0.01^2)}$$

When the calculation was complete, the researcher found that there were 175 companies being appropriate sample group. Then data were collected from the sample group accordingly.

### Research Format

The researcher studied related conceptual framework, theories, and research studies to defy operational definition and structure of variables to be studied according to the conceptual framework in the research. Papers were used to collect data about impact of business nature on corporate governance report so as to measure statistics of corporate governance reporting from annual report (Form 56-1), financial statement, and footnotes to financial statement for the 2016 accounting period.

### Data Collection

The researcher used paper to record information from the studied companies about business nature and independence of Board of Directors that had impact on corporate governance report according to guidelines for reporting on corporate governance of the Stock Exchange of Thailand (The Office of the Securities and Exchange Commission, 2017).

## Results

### Confirmatory Factor Analysis

The confirmatory factor analysis established according to the hypotheses for confirmatory factor analysis in structural equation modeling analysis can be described as follow:

**Table 4** Confirmatory factor analysis of variables in company characteristics

Variables	Factor			R <sup>2</sup>
	b	SE	t	
ROS	0.44	-	-	0.91
ETS	0.47	4.34	2.63	0.22
RLS	0.55	2.70	2.09	0.30
DAT	0.41	1.50	2.63	0.17
ROB	0.49	1.62	3.87	0.24

$\chi^2 = 0.00$ , df = 10, p-value = 1.00, RMSEA = 0.00

Note |t| > 1.96 means p < .05; |t| > 2.58 means p < .01

The results for the measurement model by performing confirmatory factor analysis of variables in corporate governance report (CGR) revealed that the model was consistent with the empirical data after model modification without cutting off any indicators. The Chi-square statistical test result was 0.00, statistical probability (p) was 1.00, degree of freedom (df) was 10, RMSEA was 0.00, SRMR was 0.00, GFI was 1.00, CFI was 1.00, and AGFI was 1.00. In other words, corporate governance report (CGR) was comprised of 5 factors, namely rights of shareholders (ROS), equitable treatment of shareholders (ETS), role of stakeholders (RLS), disclosure and transparency (DAT), and responsibilities of the Board (ROB). The role of stakeholders was the most important, followed by responsibilities of the Board, equitable treatment of shareholders, rights of shareholders, and disclosure and transparency respectively.

**Table 5** Confirmatory factor analysis of variables in independence of Board of Directors

Variables	Factor			R <sup>2</sup>
	b	SE	t	
DAD	1.00	-	-	1.00
IAC	0.20	1.28	4.09	0.04

$\chi^2 = 0.00$ , df = 0, p-value = 1.00, RMSEA = 0.00

Note |t| > 1.96 means p < .05; |t| > 2.58 means p < .01

The results for the measurement model analysis by performing confirmatory factor analysis of variables in independence of Board of Directors (IBD) revealed that the model was consistent with the empirical data after model modification without cutting off any indicators. The Chi-square test result was 0.00, statistical probability (p) was 1.00, degree of freedom (df) was 0, RMSEA was 0.00, SRMR was 0.00, GFI was 1.00, CFI was 1.00, and AGFI was 1.00. In other words, independence of Board of directors (IBD) was comprised of 2 factors, namely degree of independence of Board of Directors (DAD) and independence of Audit Committee (IAC). The degree of independence of Board of Directors was the most important, followed by the independence of Audit Committee.

**Table 6** Confirmatory factor analysis of variables in nature of business

Variables	Factor			R <sup>2</sup>
	b	SE	t	
SIZ	0.35	-	-	0.12
CRB	0.40	4.67	4.39	0.16
FNR	0.77	0.29	2.86	0.60

$\chi^2 = 0.00$ , df = 0, p-value = 1.00, RMSEA = 0.00

**Note** |t| > 1.96 means  $p < .05$ ; |t| > 2.58 means  $p < .01$

The results for the measurement model analysis by performing confirmatory factor analysis of variables in nature of business (NTB) revealed that the model was consistent with the empirical data after model modification without cutting off any indicators. The Chi-square statistical test result was 0.00, statistical probability (p) was 1.00, degree of freedom (df) was 0, RMSEA was 0.00, SRMR was 0.00, GFI was 1.00, CFI was 1.00, and AGFI was 1.00. In other words, nature of business (NTB) was comprised of 3 factors, namely firm size (SIZ), growth of business (GRB), and financial report (FNR). The financial report was the most important, followed by growth of business and firm size respectively.

**Table 7** Path analysis results

Dependent Variable Independent Variable	IBD			CGR		
	TE	DE	IE	TE	DE	IE
NTB	1.17** (0.27)	1.17** (0.27)	-	-	-	-
IBD	-	-		1.01** (0.26)	1.01** (0.26)	-

$\chi^2 = 37.23$ ,  $df = 27$ ,  $\chi^2/2 = 1.38$ ,  $p\text{-value} = 0.091$ ,  $RMSEA = 0.039$

**Note:**  $p^* < .05$ ;  $p^{**} < .01$

Total Effect (TE), Direct Effect (DE), Indirect Effect (IE)

The test results of the congruence of the causal relationship model of nature of business (NTB) indicated that the model according to the hypotheses was consistent with the empirical data. The Chi-square statistical test result was 37.23, statistical probability (P) was 0.091, degree of freedom (df) was 27,  $\chi^2/2$  was 1.38, RMSEA was 0.039, SRMR was 0.04, GFI was 0.97, CFI was 0.97, and AGFI was 0.94.

The latent variables; nature of business (NTB) had a direct positive impact on independence of Board of Directors (IBD) with a statistical significance level of .01 and coefficient of influence of 1.17. The latent variables; independence of Board of Directors (IBD) had a direct positive impact on corporate governance report (CGR) with a statistical significance level of .01 and coefficient of influence was 1.01.

**Table 8** Results of Hypothetical Testing

Research Hypothesis	Results of Hypothetical Testing	Direction/Effect
H1: Business nature had a direct positive impact on independence of Board of directors.	Accepted	+
H2: Independence of Board of directors had a direct positive impact on corporate governance report	Accepted	+

## Research Discussion and Conclusions

With reference to the study results of the causal relationship model of nature of business that had impact on corporate governance report through a degree of independence of board of directors: case study of listed companies in the Stock Exchange of Thailand, the nature of business that the researcher used in the study was financial report, growth of business, and firm size. Based on the review of previous literatures, it was found that the nature of business had an impact on corporate governance report (Dwi et al., 2013; Obigbemi et al., 2015;

Madhani & Pankaj, 2018) and measuring the mechanism of corporate government report in the study was responsibilities of the Board which consistent with a study by Reegan Grayson-Morison, Iam Ramgay (2014), who found that board of directors who had responsible for their operation to companies and shareholders were an essential part of corporate governance system. Regarding equitable treatment of shareholders, it was also consistent with a study by Jesover (2001), who found that corporate governance supported companies to treat all shareholders equitably. In relation to rights of shareholders, it was consistent with a study by Wei Jiang & Asokan Anandarajan (2009), who found that rights of shareholders had an impact on firm performance in terms of profitability and corporate governance. With reference to roles of stakeholders, it was consistent with a study by Ormazabal (2017), who found that companies should realize that stakeholders' participation was an important factor to build company to have competitive advantage and profitability. Regarding disclosure and transparency, it was consistent with a study by Souhir Neifar & Khamoussi Halioui (2013) who found that significant information about companies would be disclosed correctly and completely in a timely manner. The significant information included financial status, firm performance, ownership, and process of corporate governance. The measuring for the mechanism of independent board of directors that the researcher used in this study was a degree of independence of board of directors which consistent with a study by Helen Wei Hu (2003) who found that independence, remuneration, qualification, assurance and autonomy had an impact on operation of independent directors and independence of audit committee which also consistent with a study by Toru Yoshikawa & Helen Wei Hu (2017), who found that board capital, informal board hierarchy order had an impact on organizational citizenship behavior.

This research study indicated that nature of business had an impact on independence of board of directors with as statistical significance which consistent with a study by Dwi et al. (2013), Obigbemi et al (2015), Madhani & Pankaj (2018), Rasmussen et al. (2014) who found that for high-growth firms, independent directors' ratio, board size, and CEO-duality would facilitate an increase of higher growth in small firms.

The study also found that independent directors had an impact on transparency and disclosure of financial reporting. Corporate governance reporting from a study by Mariateresa & Andrea (2016), Yasser et al. (2015) revealed that companies with independent directors would have a greater proportion of transparency and could disclose information correctly and completely that affect a better direction of corporate governance.

## **Research Recommendation**

Restriction found in this research study was that corporate governance reporting was a study in accordance with guidelines for reporting on corporate governance of the Office of the Securities and Exchange Commission and the Stock Exchange of Thailand (The Stock Exchange of Thailand, 2016). It was only guidelines not a rule or regulations. The report on some factors was not clarified. Overall it was found that a report that had a negative impact on business would not be disclosed such as penalty, the value of fine, and quantities of hazardous materials, just to name a few. Therefore, those who would like to apply the research results to serve other benefits should make a consideration on the mentioned restriction.

This study was conducted about reporting corporate social responsibility and corporate governance from guidelines for reporting on corporate governance for 2016 of the Stock Exchange of Thailand. It was determined from integration of a conceptual framework and related research papers with a review of previous literatures. The research results indicated that the nature of business had an impact on corporate governance report through a degree of independence of board of directors according to the expected hypotheses. Such of those

guidelines have not met an international standard. The researcher then would like to suggest that a further study should be conducted by expanding a frame of reporting corporate governance to guidelines for reporting appropriate internal auditing and risk management to expand the scope of research studies.

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