Code of Corporate Governance and Firm Performance

Norazian Hussin  
Faculty of Accountancy, Universiti Teknologi MARA Sabah, Malaysia

Dr Radiah Othman (corresponding author)  
School of Accountancy, College of Business, Massey University, New Zealand  
Email: r.othman@massey.ac.nz

Abstract
This study focuses on the impact of good corporate governance mechanism and Malaysian Code of Corporate Governance (MCCG) on corporate performance in Malaysia listed companies. Data are obtained from the top 100 constituent firms which comprised the FTSE Bursa Malaysia Index as of 2009, for the years ending 2007 to 2009. This study finds a significant positive result for the association of independent Chairman with ROA and ROE. Although contradictory to the prediction of the agency theory, the results show that a higher proportion of independent non-Executive Directors are negatively associated with the firm’s performances. The result of this study indicates that an elected independent chairman is an important factor for a company's financial performance as well as an important aspect to attract social investors and consequently will increase shareholder’s wealth.

Keywords: Corporate Governance, Malaysia, Listed Firms.

Introduction
Good corporate governance is centered on the principles of accountability, transparency, fairness and responsibility in the management of the firm (Ehikioya, 2007). The emergence of high profile corporate scandals throughout the world such as Enron and WorldCom in the United States and Transmile, Megan Media and Nasioncom in Malaysia has brought the importance of good corporate governance in the limelight. Many researchers believed that the Asian financial crisis in 1997 and 1998 was due to the lack of sound and poor corporate governance (Mohammed et al., 2006; Hashim and Devi, 2008; Che Haat et al., 2008; Ponnu, 2008). Abdul Rahman and Mohamed Ali (2006) highlighted that the 1997 economic crisis in Malaysia had exposed serious weaknesses in corporate governance practices namely, weak financial structure; over-leveraging by companies; and lack of transparency, disclosure and accountability. As a result, foreign investors lose their confidence with the Malaysian capital market (Abdul Rahman and Haniffa, 2005).

The development of corporate governance in Malaysia started in the 1990s and is still evolving. The establishment of the Malaysian Code of Corporate Governance (MCCG) in the year 2000 with its principles and recommendations for best practices for corporate governance and disclosure requirements has been made the general guideline for the public listed companies on their accountabilities. Later in August 2000, the Minority Shareholder Watchdog Group (MSWG) was established to encourage companies to comply with the principles of corporate governance and to improve the awareness among the minority shareholders about their rights and methods in enforcing their rights. The MCCG was revised in 2007 and subsequently, a new ruling was announced by Bursa Malaysia to make it compulsory for all companies listed on the Main Market and Ace Market, to have an internal audit function and prohibit executive directors from being part of the audit committee to enhance the independence of the audit committee, effective from 1st February 2009. A recent proposed amendment to Bursa Malaysia’s listing requirements introduced the Corporate Disclosure (CD) Guide requiring listed companies to reveal
more details about their key developments, including changes of directors, chief executive officers (CEOs), chief financial officers (CFOs), external auditors and independent advisers (The Star, July 16, 2010). This is aimed to promote further transparency, quality and efficiency of the Malaysian capital market. Nonetheless, the issues on board of directors’ transparency relating to Sime Darby and Kenmark have put corporate governance in Malaysia in bad light. The news that both companies reported a huge loss due to unsuccessful projects has shocked all Malaysians and all blames were directed to the directors who denied of any knowledge of the projects, the risk factor and the losses. Thus, the issues of Corporate Governance and the impact of MCCG need to be examined further, which is the main aim of this paper.

Literature Review

According to James Wolfensohn, President of the World Bank: ‘The governance of companies is more important for world economic growth than the government of countries.’ Sound corporate governance system enables more useful information to be provided to reduce information asymmetry (Hsiang-tsui, 2005). While an effective system of corporate governance is necessary to restore investors’ confidence and public trust, the role of the board of directors (BOD) is also essential to maintain accountability to shareholders, authorities and other stakeholders. BOD is a collective of people who are nominated by the shareholders of a company, and responsible for making decisions on their behalf as it would be impossible for shareholders to meet frequently to make detailed decisions especially when the company has a large number of shareholders (Yung, 2009). BOD generally oversees top management, monitoring and supervising the company’s resources and operations with the primary objective of protecting the firm’s shareholders’ interests (Abdullah, 2004). Nonetheless, there are many unsettling issues in relation to BOD performance. Question such as, whether independent directors are really independent, how does BOD handles a dominant CEO or Chairman, how volatile the BOD’s members in maintaining their positions, as contrast to the fact that they are a team and are jointly and severally held accountable for whatever happens in the company, still remains subjective.

Some studies have focused on the impact of BOD composition and size, as part of corporate governance mechanism, and relate them to corporate performance or value. However, the results are mixed. For instance, a study by Brown and Caylor (2004) found a strong correlation between corporate governance and performance, valuation and dividend payout for a large sample of firms in the US. Hossain et al. (2001) documented that, in New Zealand, the firm performance is positively impacted by the proportion of outside members on the board. However, in Ireland evidence shows that: (i) board size exhibits a significant negative association with firm performance; (ii) the relationship between board size and firm performance is significantly less negative for smaller firms; and (iii) a positive and significant association between firm performance and the percentage of non-executives on the board is apparent (O’Connel and Cramer, 2010). Inconclusive results have also been reported in developing countries. A study in Ghana by Coleman & Biekpe (2006) finds inconclusive results on board size and CEO duality on firms’ performance. The empirical investigations in Nigeria show that there is significant evidence to support the fact that CEO duality adversely impacts firm performance (Ehikioya, 2007). A study in Iran revealed that board size and institutional investors is negatively associated; leadership structure has no relationship; and only board independent is positively associated with firm performance (Mashayekhi and Bazaz, 2008). Using data from the year 1999 and 2005 annual reports of 87 non-financial listed companies, Ponnu (2008) finds that there is no significant relationship between duality and board independence to company performance. In fact, none of the corporate governance variables is statistically significant in explaining corporate performance. This finding is similar to a local study by Che Haat et al. (2008)’s who also failed to provide evidence that internal governance mechanisms such as NED, duality and directorship may have contributed to a better company performance. Another study by Mokhtar et al. (2009) also find that
there was no difference in performance between companies that practiced good corporate governance and companies that did not.

Without exception, Malaysian researchers have also investigated the relationship between corporate governance and firm performance. For example, Chang and Leng (2004) demonstrated that firm performance among companies in Malaysia had a negative association with board independence, duality, concentration of ownership and leverage. They, however, found that board size and institutional investors on the board had a positive impact on the firms’ performance. A study analysing the relationship of board independence and CEO duality with financial distressed status was also found to be not associated (Abdullah, 2006). Another study by Haniffa and Hudaib (2006) examine the relationship between corporate governance structure and firm performance and their results show that board size and top five substantial shareholdings have significant relationship with market and accounting performance measures. A latest study by Ramli et al. (2010) also find that independent outside directors and foreign directors have a significant positive effect on firm performance after controlling for the influence of other corporate governance variables such as firm ownership and board sizes. In general, the impact of a good governance mechanism on firm performance produced a mixed and inconclusive result all over the world. These evidences however are still not convincing in proving a connection between good corporate governance practices and firm performance (Heracleous, 2001). This can be due to many reasons. The dynamics and development of the corporate economy in developing countries are often different from those in countries with more developed economies, such as the US and the United Kingdom (UK) due to their differences in legal system, political stability, smaller market size, corporate ownership and the nature of individual financial system (Gul and Tsui, 2004) in addition to the difficulty in identifying reliable and robust measurements of corporate governance (Larcker et al., 2007).

This is a very interesting issue as more countries are now concerned in strengthening their corporate governance practices but yet the results do not seem to support the convention. The South East Asia countries and in particular, Malaysia are also experiencing such dilemma of these inconsistent results. Therefore, this study re-examines the impact of corporate governance mechanism relating to the proportion of non-executive directors on the board, independent chairman, the role of CEO duality and board size on firm performance. This study differs from that of Abdul Rahman and Mohamed Ali (2006) which studied the impact of the board, audit committee and culture characteristics to earnings management for the periods of January 2002 to December 2003 and that of Rahmat et al. (2009) which focus on the characteristics of the audit committee in financially distressed and non-distressed companies for the year 2001. The present study includes a more recent sample of companies for the years ending 2007 to 2009.

After a decade from the establishment of the MCCG in the year 2000, it is expected that the adoption of the best practices in Malaysia has improved. This study tests the impact of MCCG on corporate performance in Malaysian public listed firms for the year 2007 and 2009 which is before and after the implementation of the new rulings. It is based on the expectation that the issuance of the new rulings might increase corporate awareness on good governance. Consequently, as the ultimate objective of corporate governance is to realise long-term shareholder value, it may be expected that companies which adopt best practices in corporate governance will perform better than others.

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Hypothesis Development

Non-Executive Directors (NED) and Firm Performance

The board of directors is an important mechanism for monitoring management behaviour, resulting in better corporate accountability and disclosure. Globally NED is defined as non-executive directors, directly known as those directors who are independent however in Malaysia the definition is quite different. As defined by Bursa Malaysia, NED is a director who has no direct or indirect pecuniary interest in the company other than their directors’ emoluments and their “permitted” shareholdings in the company; those who are not employees of the company or affiliated with it in any other way and are not involved in the day-to-day running of business but may have pecuniary interest in the company, whether direct or indirect; or those who are not employees of the company but are standing as nominees for substantial shareholders.

In Bursa Malaysia Revamped Listing Requirements, the importance of having independent directors on boards are highlighted by ensuring the board of directors of the Malaysian public listed companies has a sufficient independent element to safeguard the interest of investors. NEDs are perceived to be more independent of management (Ajinkya et al., 2005) and are unlikely to collude with managers to engage in actions which compromise shareholders’ interests (Mangena and Pike, 2005). The proportion of NED on the board is seen as a key indicator of the independence of the board from the management. The proportions of the outside directors can be measured in terms of the ratio of outside directors to board size. The literature suggested that increases in the proportion of outside directors on the board should increase firm performance as they are more effective monitors of managers (Adams and Mehran, 2003). In the Corporate Governance (CG) guide 2010, it is stated that a listed company must ensure that at least two directors or one-third of its board (whichever is the higher) are independent directors.

Efficient monitoring from NED that is free from managerial influence is capable to improve the quality of financial information conveyed to the user of the financial statement (Higgs Report, 2003). A number of studies in developed countries have reported a positive role of having higher proportion of independent NED sitting on the board and reporting quality financial reporting (Peasnell et al., 2000; Klein; 2002, Davidson et al., 2005). In China, Lai and Tam (2007) conclude from their research that where independent directors are included on the board of a corporation there is a negative relationship between the change in cash flows and accruals and a resultant less-severe practice of income smoothing. Choi et al. (2007) also report that in Korea there is a positive effect on firm performance as a result of having independent directors on the company board. On the other hand, some researchers find that although the proportion of independent directors on the board is high, the level of board independence and professionalism is not necessarily good (Chen et al, 2005). Abdullah (2006) concludes, from research into financially distressed and non-distressed companies listed on the Bursa Malaysia, that board independence is not associated with a financially distressed status. Locally, a study by Jaggi et al. (2007) provide evidence of an insignificant relationship between proportions of NED and accrual quality in high family-ownership samples of Hong Kong listed companies which suggested that the monitoring effectiveness of independent directors is reduced in family controlled firms. A study by Abdullah and Mohd Nasir (2004) and Abdul Rahman and Mohamed Ali (2006) also fail to find any significant evidence between the independence of boards and earnings management in the Malaysian context.

The mixed results could be reflective of a corporate culture wherein corporate boards are controlled by the management and the presence of independent NED has no discernable impact on management
decisions (Petra, 2005). Despite this conflicting result, the Malaysian evidence is re-tested and it is hypothesises that:

\[ H_1. \text{ Proportion of NED to board size has a positive significant relationship to firms' performance} \]

**Leadership Structure: Independent Chairman, CEO Duality and Firm Performance**

CEO duality refers to the same person being the CEO and the chairman of the board. Efficiency in monitoring management could be enhanced through CEO-Chairman duality, where a single person assumes the position of Chairman and CEO simultaneously because less contracting is needed and information asymmetry is reduced (Haniffa and Cooke, 2000). However, the agency theory argues that, if the chairman and the CEO are handling the same position, it is likely to create misuse of power and the resources, since this individual will be very influential without successful checks and balances. Abdul Rahman and Haniffa (2005) show that Malaysian companies with role duality seemed not to perform as well as their counterparts with separate board leadership (based on the accounting performance measurement). Similarly, Haniffa and Hudaib (2006) reported CEO duality have no significant relationship with performance. Higgs report (2003) views a chairman who is independent of immediate executive concerns is more likely to provide an objective opinion on proposals, be more effective in monitoring decisions and be more likely to promote shareholder interests.

It is a common practice in the UK and Australia for the role of the chairman to be separated from that of the CEO. The UK’s Code of Best Practice, initially formulated through Cadbury (1992), recommends that the functions of CEO and chairman of the board should be split, with the chairman responsible for the leadership of the board and acting as the external face of the company, particularly in relation to investors. Through such division of responsibilities, no one individual emerges with unfettered power over the firm’s strategic and operational decisions (Cadbury report, 1992; Higgs report, 2003). According to Mailin (2007), the roles of CEO and chairman should be separated and carried out by a different person. In the latest CG Guide 2010 it is stated that ‘there should be a clearly accepted division of responsibilities at the head of the company which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision’. In Malaysia, the MCCG recommends that the role of CEO and Chairman should be distinct and separated to ensure the balance of power of the two designations as well as to avoid conflict of interest. It is also to avoid a single person in the board to dominate the others in decision making process so as to promote fair judgment and reasonable concern. If there is a duality, the MCCG recommends that strong independent elements should be included and such information are disclosed to the public for transparency purposes. In the event the roles are combined, the CG Code recommends that ‘there should be a strong independent element on the board’ to strive for independent decision-making. A decision to combine the roles of chairman and CEO should be publicly explained in the annual report.

The impact of chairman independency on firm’s performance and value has been examined. For instance, Bhagat and Black (2002), Sanda et al, (2003) and Ogbechie et al. (2009) all argued that firms are more valuable when the CEO and board chair positions are separate. By having role separation, the boards are given a structural basis for acting independently and for nurturing an environment which will allow the chairman and other board members to challenge the CEO without the fear of giving (or attracting) offence (Coombes and Wong, 2004). On the contrary, the relationship between CEO duality and firm performance was considered to be not significant in a different study done using the Malaysian public
listed companies as sample in 2004 by Chang and Leng. Similar to a study conducted by Ponnu (2008), it was found that there is no significant relationship between duality and board independence to company performance. Although the literature is not unanimous in its conclusions, the weight of opinion is that there is a significant relationship between CEO duality towards firm performance. Thus, this study hypothesises that:

\[ H_2 \quad \text{Independent chairman has a significant positive relationship to firms' performance, and} \]
\[ H_3 \quad \text{CEO duality has a significant negative relationship to firms' performance} \]

**Board Size and Firm Performance**

Previous studies have proven that the size of the board has a material impact on the quality of corporate governance. For example, Fuerst and Kang (2000) demonstrate that board size is negatively related to firm value as a smaller board may be less encumbered with routine problems and may provide better firm performance. Several studies supported the idea that large boards could be dysfunctional. Hermalin and Weisbach (2003) believe that board size proxies for the board’s activity may be plagued with free rider and monitoring problems. Yawson (2006) and Pye (2000) argue that larger boards suffered from higher agency problems because it was difficult to coordinate and make value maximising strategic decisions. In contrast, larger boards tend to provide an increased pool of expertise, greater management oversight, and access to wider range of contracts and resources (Goostein et al., 1994; Psaros, 2009; Williams et al., 2005) and are more effective in preventing corporate failure (Dallas, 2001).

Rose (2005) uses a sample of Danish listed firms and the results shows that board size, proportion of insiders, and positions held by board members have insignificant influence on firm performance. Basu et al. (2007) analyze 174 large Japanese corporations and find a negative relationship between board size and subsequent accounting performance. Contrary to the literature above, there has been a positive relationship between board size and Tobin’s Q (Adams and Mehran 2002). Haniffa and Hudaib (2006) found that board size and top five substantial shareholdings have significant relationship with market and accounting performance measures.

The results of the effect of board size on corporate performance are mixed; however, it could be argued that this effect is generally negative. The hypothesis to be tested is as follows:

\[ H_4 \quad \text{Board size has a negative significant relationship to firms' performance} \]

**Audit Committee Effectiveness and Firm Performance**

The audit committee plays an important role in overseeing and monitoring the financial reporting process, internal controls and the external audit. From an agency perspective, an effective audit committee fulfils its oversight role when it is independent of management, has a level of financial and industrial experience to carry out its duties, and actively monitors internal controls and financial reporting (Carcello, Hollingsworth, Klein and Neal, 2006). Prior researches that focused on the consequences of audit committee meetings had clearly demonstrated that greater meeting frequency is associated with a reduced incidence of financial reporting problems and greater external audit quality (De Zoort et al, 2002). Regulators believe that more frequent audit committee meetings indicate the audit committee’s diligence in effectively discharging its responsibilities so that agency problems are minimised (Raghunandan and Rama, 2007). Based on these prior researches, an effective committee is assumed to be the one that meets frequently and is comprised of independent and appropriately experienced directors (DeZoort et al., 2002). The following hypotheses are therefore tested:
H3. Audit committee independence has a significant relationship with firms’ performance
H6. Audit committee expertise has a significant relationship with firms’ performance
H7. Audit committee meetings has a significant relationship with firms’ performance

Research Design

Sampling
The samples included in this study comprise of the 100 companies in the Financial Times Stock Exchange (FTSE) Bursa Malaysia index. Companies included in the FTSE Bursa Malaysia index are generally actively traded and large in size. Given their high volume of trade, it is thus appropriate to assume that these are the companies that more readily attract the interests of investors. Consequently, it may be expected that these companies would apply good corporate governance practices.

Under the Bursa Malaysia Listing Requirements, all companies listed on the Main Market and ACE Market were required to comply with the requirements on the revised composition of the audit committee by January 31, 2009. Thus, the study examines the 100 constituent firms which comprised the FTSE Bursa Malaysia Index as of 2009, for the years ending 2007 to 2009. The final sample comprises of 77 companies after excluding 13 companies in the finance sector which are regulated separately under the Banking and Financial Institutions Act of 1989. 10 Companies are also excluded due to unavailability of their annual reports.

Data collection
The main source of the data relating to the board of directors and the audit committee attributes such as board size (BSize), non-executive directors (NED), Independent Chairman (IndepChair), Chief Executive Officer is Chairman of Board of Directors (CEO Duality), Audit Committee Independence (ACindep), Audit Committee Expertise (ACexpert) and Audit Committee Meeting (ACmeeting) are gathered from the Companies’ Annual Reports as disclosed on the Bursa Malaysia web site. This information is obtained manually by calculating the number of directors and the number of NED on the board, and determining the duality role of the CEO and chairman of the company as well as the information on audit committee for the years 2007 to 2009. Financial data are obtained from the Datastream.

Period of study
The period of study between the years ending 2007 and 2009 are chosen for the purpose of analysing the pre- and post-effect due to the new rulings. The year ending 2007 is included prior to the announcement made on the new listing requirement by Bursa Malaysia. The year ending 2009 is chosen to investigate any effect of the mandatory requirements to the firm performance.

Measurement of Variables

Dependent Variable.
This study follows Ponnu (2008) and Chu (2009), using profitability as the dependent variable in examining the effect of an effective governance on firm performance. Profitability is measured by the accounting measure Return on Assets (ROA) and Return on Equity (ROE). ROA measures the ability of the assets of the company to generate profits and is considered a key factor when taking into account the future firm investments. While the ROE is the amount of net income returned as a percentage of shareholders’ equity. ROE measures a corporation’s profitability by revealing how much profit a company generates with the money the shareholders have invested. While market based measures tend to be more objective than accounting based measures, they are also affected by many uncontrollable factors.
(Gani and Jermias, 2006). Hutchinson and Gul (2004) argue that accounting based performance measures reflect the results of management actions and were therefore preferable to market based measures when investigating the relationship between corporate governance and firm performance.

As suggested by Ponnu (2008), ROA and ROE are derived from Earnings before Interest and Taxes (EBIT) scaled by the book value of total assets and total equity, leaving aside the financial performance of the firm. EBIT is a traditional method of measurement that does not include capital costs and, instead, includes only the operating margin and operating profit. Like any accounting metric, ROA is essentially a historic measure which is independently audited.

**Independent Variables**

NED is the percentage of non-executive directors on the board. In analysing the impact of the MCCG after a decade of its implementation and to provide a more comprehensive analysis, the variable on proportions of NED is further segregated into NED 33 and NED 50. NED 33 is measured as a dummy variable of one if the independent directors represent at least one third of the board. A dummy variable of zero is used when the independent directors make up less than one third. Firms which have more than one third of the board member are expected to perform better. NED 50 will be measured as a dummy variable of one if the independent directors represent 50 percent of the board. A dummy variable of zero represents that the independent directors are less than 50 percent. Firms which have more than 50 percent of independent directors are expected to perform better than firms which do not.

Independent chairman (IndepChair) is measured as a dummy variable given the value of 1 when the board chair is independent and 0 when he or she is not independent. CEO duality is measured as a dummy variable which is assigned 1 if the CEO (or managing director) additionally occupies the position of the chairman of the board, or 0 if otherwise. Board size (Bsize) is the number of directors on the board, similar to that employed by Abdul Rahman and Mohamed Ali (2006) and Peasnell et al. (2001).

The effectiveness of the audit committee is measured using three independent variables. They are: (i) Audit Committee Independence (ACindep), (ii) Audit Committee Expertise (ACexpert) and (iii) Audit Committee meetings (ACmeetings). ACindep is the percentage of NED with no related party transactions on the audit committee. ACexpert is the percentage of NED with financial and/or auditing expertise. ACmeetings is the number of audit committee meetings during the year.

**Control Variables.**

Companies are more likely to have an effective function of internal audit when agency costs are high. Therefore, there are a number of control variables which have been shown to affect agency costs and have not been addressed in hypotheses. The firm size (Size) variable can also influence the relationship between ownership and firm performance (Barontini and Caprio, 2005; Carter, Simkins, and Simpson, 2003; Chu, 2009; Santalo’ and Diestre, 2006). In order to avoid problems with extreme values, it is constructed using the natural logarithm of total assets. The percentage of total directors’ share ownership (Dirownership) is included as a control variable. Consistent with Che Haat et al. (2008), leverage is computed as long term debt divided by total assets. The measure of shareholder concentration is the proportion of shares held by the top 20 shareholders (Top20ownership). Big Four auditor is a dummy variable coded 1 when the company’s auditor is a Big Four auditor and 0 when it is a smaller audit firm.
Research Model
The model tested is as follows:

\[ FP = \beta_0 + \beta_1 NED + \beta_2 \text{IndepChair} + \beta_3 \text{CEODuality} + \beta_4 \text{BSIZE} + \beta_5 \text{ACindep} + \beta_6 \text{ACexpert} + \beta_7 \text{ACmeetings} + \beta_8 \text{Size} + \beta_9 \text{Dirownership} + \beta_{10} \text{Top20ownership} + \beta_{11} \text{Big5} + \beta_{12} \text{Debt} + e \]

Where

- \( FP \) = Firm Performance (measured by ROA and ROE)
- \( ROA \) = EBIT over total asset
- \( ROE \) = EBIT over total equity
- \( NED \) = the percentage of non-executive directors on the Board
- \( \text{IndepChair} \) = a dummy variable given the value 1 when the board chair is independent and 0 when he/she is not independent
- \( \text{CEO Duality} \) = a dummy variable, assigned 1 if the chief executive officer (or managing director) additionally occupies the position of the chairman of the board, or 0 if otherwise.
- \( \text{BSIZE} \) = total number of directors on the board
- \( \text{ACindep} \) = the percentage of non-executive directors with no related party transactions on the audit committee
- \( \text{ACexpert} \) = the percentage of non-executive directors with financial and/or auditing expertise
- \( \text{ACmeetings} \) = the no. of audit committee meetings during the year
- \( \text{Size} \) = natural log of total assets
- \( \text{Dirownership} \) = the percentage of total directors’ shares in the company
- \( \text{Top20ownership} \) = concentration of top 20 shareholders
- \( \text{Big5} \) = a dummy variable given the value 1 when a Big Five auditor is used and 0 when a smaller audit firm is used
- \( \text{Debt} \) = Long-term debt over total assets

Results and Data Analysis
Table 1 reports the descriptive statistics for the variables in the model. The mean of ROA and ROE is 12 percent and 26 percent respectively. The NED percentage variable revealed that the mean percentage of the NED on the board between the years 2007 to 2009 was 68.65 percent, which was more than the 27.37 percent reported by Ramli et. al (2010) for Malaysian listed companies between the years 2002 to 2007. The result indicated the high level of awareness on the importance of outside directors presence to ensure positive firms’ overall performance.
Table 1: Descriptive Statistics

For variable Indepchair, 37 percent of the chairmen were independent. Companies with CEO Duality were only 10 percent or 8 companies out of the total sample. This is similar to that of Ponnu’s (2008) who finds only 8.6 percent or 7 companies out of the total 81 companies surveyed in 2005.

Table 1 reveals that the mean board size was 8.87 or on average of 9 directors for each board size in the firm that originally, consisted of 5 to 15 board members. This was also consistent with Abdul Rahman and Mohamed Ali (2006) for the top 100 companies in 2003. On average, more than half or 58.02 percent of the audit committee members were non-executives who were unrelated to the firm. Meanwhile the percentage of audit committee with an accounting or auditing expertise was at 34.63 percent indicating that most of the companies listed in the Main Market were only complying with the minimum of only one member of who should be a member of an accounting association or body. Audit committees held an average of five meetings annually, which was more than the recommended threshold of three audit committee meetings each year.

Control Variables
The firm size in the sample was determined as the natural logarithm of the total assets and has a mean of 6.56. The mean percentage of shares owned by the total directors was 5.23 percent. While the mean
percentage of shares held by the top twenty shareholders was 76.58 percent. As compared with prior research done by Abdullah and Mohd Nasir (2004) showed that the average shareholding by the top twenty shareholders is found to be at 73 percent. In Malaysia, the distinctive feature of the companies is the tightly held shares where shares are held either by states, families or individuals. In total, 95 percentages of the firms use a Big Four audit firm.

As for long-term liabilities and the proportion of the total assets, it ranged from 0 to 2.61. Increased only by a small fraction compared to result by Ramli et al, (2010), which range is between 0 to 2.23. According to Che Haat et al.(2006), the external audits serve as an important governance mechanism for creditors, particularly to ensure that firms with high level of debt practise good debt management to improve their financial condition.

**Pearson Correlation**

Pearson’s correlation has been conducted for all variables used in this study. IndepChair was positively and significantly correlated with ROA and ROE at the 1 percent significant level as compared to CEO Duality. The result was consistent with the Agency theory on the issue of the separation of powers between the chairman and the CEO. Thus, it is crucial to separate between the two roles for the monitoring of the effectiveness of the board over management, by providing cross-checking evidence against the possibility of over-ambitious plans by the CEO (Abdul Rahman and Haniffa, 2005) which might not maximise the shareholders’ wealth. According to Ponnu (2008), duality is often cited as a primary cause for the decline of major US corporations such as Westinghouse, Sears, General Motors (GM) and IBM.

However, audit committee independent was negatively and significantly correlated with both ROA and ROE at 1 percent and 5 percent significance levels respectively. This meant that the members (shareholders) who had interest in the company would lead to a better firm performance. As the members were also owners of the company they would ensure that the decision made would maximise the shareholders’ wealth and thus subsequently increase firms’ performance. ACexpert was positively and significantly correlated with ACmeeting indicating that an audit committee with more financial or auditing expertise in the company tended to have higher frequency of meetings held annually.

Board size had negative and significant correlations with both the dependent variables, indicating that larger board size generally reflected weaker controls and, therefore, weaker performance. There was evidence that larger boards were less efficient because the directors were less cohesive and participative and it would also more difficult to reach consensus in a larger board. The results indicated that firms with smaller board size had higher firm value and this is consistent with Haniffa and Hudaib (2006), Singh and Davidson III (2003) and Sanda et al. (2003). In theory, as the number of director increases, a board’s capacities for monitoring increase. Agrawal and Knoeber (1996) point out that boards expanded for political expediency often result in too many outsiders on the board, making it large and this does not help the performance.

NED had positive and significant correlations at 1 percent significance level with firm size. This indicated that larger companies tend to appoint more NED to monitor the company. Due to the diversified segment of large companies, the need to have an outsider or independent director was crucial in promoting transparency and managing business risk. The more independent the board committee and the board chair the lesser the directors share ownership in the company.
The highest positive and significant correlation was between NED and top twenty concentrations. Concentrated shareholdings by institutional provided an incentive for diligent monitoring as they had the resources, expertise and stronger incentives to actively monitor the actions of management and prevent managers’ opportunistic behaviour (Wan Hussin and Ibrahim, 2003). The more concentrated the shareholders, the more NEDs are appointed to oversee the performance of a company. In contrast, the results of this study showed that when the managerial ownership is lower, the demand for NED to be included in the board of directors tend to be higher.

The results of the audit committee effectiveness showed that ACexpert and AC meeting were positively and significantly correlated at 1 percent significance level with firm size. This showed that the larger the firm size the more effective was its audit committee function. Due to the complexity and greater dispersion of stockholding in larger firms, more extensive monitoring of the financial reporting process was required which can be achieved through greater internal monitoring (Raghunandan and Rama, 2007). An effective internal monitoring can be achieved through the appointment of financial expert members and more frequent meetings. These results were consistent with Mendez and Garcia (2007) and Raghunandan and Rama (2007).

For the results of the control variables, debt had a significant influence over firm performance which is ROA at 1 percent significance level. This is similar to the findings made by Mohammed et al. (2006) and Che Haat et al. (2008). The significant positive correlation of debt to firm performance agrees with the theory that debt is an important mechanism for solving agency problems in corporations characterised by the separation of ownership and control in Malaysia (Jensen and Meckling, 1976; Jensen, 1986; Hart and Moore, 1995).

Regression Results
Table 2 provides linear regression results. The independent variables explained about 24 and 12 percent of the cross-sectional variation in ROA and ROE respectively. The percentage of NED on the board had a negative 10 percent level of significance with ROA and ROE. These results suggested that the agency theory’s theoretical predictions of a positive relationship between outside (independent) directors and firm performance might not be applicable in the sample of companies under review. The results indicated that an apparently strong monitoring structure did not necessarily produce better performance.

This finding was consistent with that of prior study in Malaysia by Che Ahmad et al. (2003), Abdullah (2004), Abdul Rahman and Mohamed Ali (2006) and Vethanayagam et al. (2006). Based on the diversification strategy suggested by Che Ahmad et al. (2003), the presence of the independent directors does not seem to influence the decision process because they do not have contact with the daily operation of the firm or they have limited qualifications and are merely appointed based on the relationship with the CEO of the firm. Abdullah (2004) also argued that, due to the dominant role played by CEOs in the director selection process, the outside directors may be incapable in providing independent judgments which raised concerns about the quality of the independent directors. Therefore, Hypothesis 1 was not supported.

Results for H2 on IndepChair were supported with positive 5 percent and 10 percent levels of significance for ROA and ROE respectively. However, results for H3 on CEO Duality were mixed and not supported.
This was consistent with previous studies in Malaysia; the independent leadership companies showed a better performance in terms of the proportion of return on asset to leverage (ROE) and profit after tax and interest to sales (profit margin) as compared to the CEO duality companies. In relation to similar results on CEO Duality, the roles of CEO duality in determining the firm’s financial distress are mixed (Abdullah, 2004; Abdullah and Mohd Nasir, 2004). Ponnu (2008) also finds no significant relationship between CEO duality and board independence to company performance. This study’s results suggested that having an independent chairman would lead to better performance and would be beneficial to the shareholders, while having a duality role of CEO in the company might lead to poor corporate governance and deteriorate firm performance. These were consistent as in the findings of McKnight and Mira (2003) and Haniffa and Hudaib (2006).

The result for H4 on BSIZE was negative correlation with ROA and ROE at 5 percent level of significance. This indicated that small boards are associated with higher firm performance, possibly through closely monitored management. This was consistent with those of Haniffa and Hudaib (2006), Singh and Davidson III (2003), Mishra et al. (2001). Also, larger boards experience greater productivity losses such as greater coordination problems, slower decision making, and more director free riding, and are more risk averse. Hence, in line with international research in the field (for instance, de Andres et al., 2005) the current study offered some support for the notion that a negative relation between firm performance and board size was also apparent in the Malaysian setting. Results for the effective audit committee were mixed and did not support H5, H6 and H7. The more independent the members of the audit committee and the higher number of meetings had no impact on firm performance. This was consistent with that of Abdul Rahman and Mohamed Ali (2006), who find no significant relationship between audit committee independence and earnings management in Malaysian firms.

For the agency cost control variables, higher concentrations of large shareholders tend to have a positive and significant effect on ROA and ROE. Thus, this was similar to that of a study by Abdullah (2006) who finds that the effect of management ownership on financial distressed status is curvilinear and negatively associated with financial distress. The presence of a majority shareholder in the board can result in agency problems between the controlling and minority shareholders (Rachagan et al., 2009). Following this argument, the result was consistent with those of other researchers who found a nonlinear relationship between ownership concentration and profitability such as Miguel, Pindado, and de la Torre, (2004). Consistent with Che Haat et al. (2005), the positive and significant relation of debt-to-asset to performance supported the theory that debt was an important mechanism for solving agency problems in corporations characterised by the separation of ownership and control in Malaysia (Jensen and Meckling, 1976; Jensen, 1986; Hart and Moore, 1995). In contrast, the size of a firm and directors’ ownership resulted in a negative and significant relationship with firm performance. There was no association between firms engaging a big four audit firm with performance.
Table 2: Regression Test of Firm Performance (ROA and ROE) on Corporate Governance Mechanism and Control Variables

<table>
<thead>
<tr>
<th>Variable</th>
<th>β</th>
<th>t</th>
<th>β</th>
<th>t</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>0.619</td>
<td>5.096 ***</td>
<td>1.033</td>
<td>2.983 ***</td>
</tr>
<tr>
<td>NED</td>
<td>-0.151</td>
<td>-1.901 *</td>
<td>-0.168</td>
<td>-1.963 *</td>
</tr>
<tr>
<td>IndepChair</td>
<td>0.164</td>
<td>2.506 **</td>
<td>0.206</td>
<td>2.916 ***</td>
</tr>
<tr>
<td>Duality</td>
<td>0.067</td>
<td>1.007</td>
<td>-0.075</td>
<td>-1.052</td>
</tr>
<tr>
<td>BSize</td>
<td>-0.135</td>
<td>-2.074 **</td>
<td>-0.185</td>
<td>-2.637 **</td>
</tr>
<tr>
<td>Acindep</td>
<td>-0.121</td>
<td>-1.871</td>
<td>-0.130</td>
<td>-1.872</td>
</tr>
<tr>
<td>ACexpert</td>
<td>0.065</td>
<td>1.043</td>
<td>-0.006</td>
<td>-0.089</td>
</tr>
<tr>
<td>Acmeetings</td>
<td>-0.053</td>
<td>-0.809</td>
<td>-0.005</td>
<td>-0.065</td>
</tr>
<tr>
<td>Size</td>
<td>-0.284</td>
<td>-4.054 ***</td>
<td>-0.139</td>
<td>-1.830 *</td>
</tr>
<tr>
<td>TopTwenty</td>
<td>0.143</td>
<td>2.097 **</td>
<td>0.177</td>
<td>2.406 **</td>
</tr>
<tr>
<td>Big5</td>
<td>-0.031</td>
<td>-0.470</td>
<td>-0.051</td>
<td>-0.720</td>
</tr>
<tr>
<td>Diownership</td>
<td>-0.136</td>
<td>-1.840 *</td>
<td>-0.038</td>
<td>-0.469</td>
</tr>
<tr>
<td>Debt</td>
<td>0.395</td>
<td>6.131 ***</td>
<td>0.202</td>
<td>2.903 ***</td>
</tr>
<tr>
<td>Adjusted R²</td>
<td>0.244</td>
<td>7.185 ***</td>
<td>0.119</td>
<td>3.596 ***</td>
</tr>
</tbody>
</table>

***, ** and * indicate the percentage of significance at 1 percent, 5 percent and 10 percent, respectively, based on two-tailed tests.

T- Test

Tables 3 and 4 compare the result of the performance of companies with independent chairman, CEO duality and board independence with those without independent chairman, CEO duality and board independence. This test is also conducted to investigate the impact of MCCG after a decade of its establishment on firm performance.

<table>
<thead>
<tr>
<th>2007</th>
<th>Mean ROA</th>
<th>Mean ROE</th>
<th>Mean Difference</th>
<th>df</th>
<th>Sig (2-tailed)</th>
<th>Mean Difference</th>
<th>df</th>
<th>Sig (2-tailed)</th>
</tr>
</thead>
<tbody>
<tr>
<td>IndepChair N=2</td>
<td>15.50</td>
<td>38.55</td>
<td>27.75</td>
<td>0.032**</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-IndepChair N=50</td>
<td>11.69</td>
<td>19.34</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO Duality N=8</td>
<td>19.99</td>
<td>14.51</td>
<td>33.67</td>
<td>0.362</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-CEO Duality N=6</td>
<td>12.22</td>
<td>27.42</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>NED 33</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>NED &gt;= 33% N=7</td>
<td>13.42</td>
<td>26.27</td>
<td>8.48</td>
<td>0.725</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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Table 3: Performance of Companies With and Without Independent Chairman, CEO Duality and Board Independence, 2007

Table 3 shows that in 2007, only 27 companies had an independent chairman whereas 50 companies otherwise. Consistent with the results of using regression analysis, companies with an independent chairman seemed to perform better with higher ROA (16%) and ROE (39%) significantly at 5 percent level compared to those with a non-independent chairman. For CEO duality, only 8 companies were having chairman assumed duality position as compared to the other 69 companies. Companies with duality resulted in a higher ROA (20%) but a lower ROE (15%) than those without duality. The result showed that the separation of CEO and Chairman did not contribute to improved performance in terms of ROE. In terms of NED results, companies that were having more than 33 percent and 50 percent independent directors on the board, performed higher ROA both at 13 percent and significant at 10 percent level for NED higher than 33 percent than companies that had fewer independent directors (<33% and < 50%). This result was consistent with that of Ponnu (2008) and Ramli et al., (2010). However for ROE, those with NED higher than 33 percent performed better with 26 percent, in contrast NED with lower than 50 percent seemed to perform better at 31 percent. The results on ROA supported the MCCG recommendation that required companies to have at least one third independent members on the board.

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Mean Difference</td>
<td>Df</td>
<td>Sig (2-tailed)</td>
<td>Mean Difference</td>
<td>df</td>
<td>Sig (2-tailed)</td>
</tr>
<tr>
<td>IndepChair</td>
<td>N=2 9</td>
<td>15.24</td>
<td>40.77</td>
<td>0.080*</td>
<td>35.27</td>
<td>33.31</td>
</tr>
<tr>
<td>Non-IndepChair</td>
<td>N=4 8</td>
<td>10.17</td>
<td></td>
<td></td>
<td>21.10</td>
<td></td>
</tr>
<tr>
<td>CEO Duality</td>
<td>N=8</td>
<td>17.21</td>
<td>7.68</td>
<td>0.216</td>
<td>21.51</td>
<td>17.44</td>
</tr>
<tr>
<td>Non-CEO Duality</td>
<td>N=6 9</td>
<td>11.49</td>
<td></td>
<td></td>
<td>27.01</td>
<td></td>
</tr>
<tr>
<td>NED 33</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>NED &gt;= 33%</td>
<td>N=7 4</td>
<td>12.15</td>
<td>2.45</td>
<td>0.748</td>
<td>26.14</td>
<td>26.66</td>
</tr>
<tr>
<td>NED &lt;</td>
<td>N=3</td>
<td>10.47</td>
<td></td>
<td></td>
<td>33.71</td>
<td></td>
</tr>
</tbody>
</table>

** and * indicate the percentage of significance at 5 percent and 10 percent, respectively, based on two-tailed tests.

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Table 4 shows the comparison among the variables and ROA and ROE. In 2009, as in 2007, the companies with an independent chairman had a better ROA (15%) and ROE (35%), both significant at 10 percent level each. The number of companies adopting a separate position of chairman had increased to 29 companies. It showed that more companies were aware of the importance in having an independent chairman to monitor the company’s performance. However, this was in contrast to the results in 2007 but consistent with that of Ponnu (2008) in which companies with duality in 2009 had a higher ROA (17%) than those without duality (11%). However, in terms of ROE, the results for those companies without duality performed better. Most of the companies that had duality role were family owned. Researchers suggest that the presence of a higher proportion of family members on the corporate board was more likely enhancing the earnings quality reported by the firms.

However, in terms of NED, the impact of the percentage of “NED higher than 33 percent in the board” to ROA performed slightly better with 12%. In terms of ROE, the performance was lower with 26%. As regards to “NED higher than 50 percent”, both ROA and ROE showed that companies adopting this practice were not performing better than those having lower than “50 percent NED”. This suggested that having independent members in the board might not necessarily improve shareholders’ wealth. As argued by Abdul Rahman and Mohamed Ali (2006) and Vethanayagam et al. (2006) the Malaysian independent directors lack expertise, skills and knowledge to understand financial reporting details which explained by their insignificant findings on the relationship between board independence and accounting issues examined. In addition, Vethanayagam et al. (2006) also argue that the domination of inside directors on the board in Malaysia highlights the issue of quality and accountability of independent directors when some independent directors are not truly independent of management.

Discussion and Conclusion
The objective of this study was to examine the relationship between firms’ performance and corporate governance characteristics, mainly of the board of directors and audit committee attributes. The results showed weak evidence to indicate that companies which adopted good corporate governance practices performed better than others. However, companies with an independent chairman had a significant relationship with firm performance compared to CEO Duality. This showed that having an outsider to monitor the overall performance was crucial to increase shareholders’ wealth. The effective monitoring role by an independent chairman would lead to a better performance. The result of the proportion of NED
in the board was negatively correlated with corporate performance and was consistent with that of other previous studies (Abdul Rahman and Mohamed Ali, 2006; Abdullah, 2006; Ponnu, 2008; Che Haat et al., 2005; Mokhtar et al. 2009). Board size had a negative significant relationship with firms’ performance, which indicated that larger board size might not have led to an effective monitoring process of management activity due to the potential conflicts of interest among the directors. However, a smaller board size was more focused in solving problems and issues that might have arisen through closed-monitored management. In contrast, CEO duality and audit committee effectiveness both have no significant influence in the firm performance. The explanation behind these may probably due to the effect of adopting a CEO duality approach and audit committee was not detected due to its long-term influence.

The results for the entire hypothesis concerning audit committee effectiveness were not significant. The findings were similar to those of Abdul Rahman and Mohamed Ali (2006), Kim and Yoon (2007), and Rahmat et al. (2009) that the audit committees had an insignificant role in preventing the incidence of earnings management indicated that the establishment of an audit committee in listed companies in Malaysia had yet to achieve success in its monitoring role. Irrespective of the mixed results in this study, the importance of strong governances is still crucial as a monitoring mechanism which may enhance transparency of the Malaysian listed companies. The contribution of this study is that it provided evidence that an independent board chair is an effective internal monitoring mechanism to promote better performance. Public listed companies that hire an independent chairman are assumed to be more properly managed and offer sound investment opportunities, which attracts the confidence of investors. Consequently, it will lead to better firm performance and maximise shareholders’ wealth.

The results of this study supports the notion that even after a decade since the establishment of MCCG, the research on the adoption of good corporate governance mechanism researches seemed to be inconclusive. It seemed that most of the good governance mechanism still seemed to be insignificant in relation to firm performance, in this case measured by ROA and ROE. According to Gul and Tsui, (2004), this could probably due to the dynamics and development of the corporate economy in developing countries are often different from those in countries with more developed economies, such as the US and the UK. Examples of the different context of institutional arrangements between developed and developing countries includes the basic legal system, political stability, smaller market size, corporate ownership and the nature of individual financial system. The result produce in this study provided more evidence on the relationship between good governance mechanism and firm performance. The overall mixed results are still consistent with those studies done previously even after a decade of the emergence issue on importance of corporate governance through the establishment of MCCG.

Limitations and Future Research
The results obtained in this study may not be generalised as to the overall context of Malaysia due to some limitations. First, the present study only focused on the use of ROA and ROE as proxies for financial performance. Prior researches (Abdul Rahman and Mohamed Ali, 2006; Ponnu, 2008; Che Haat et al, 2005; Mashyekhi and Bazaz, 2008) had linked corporate governance to firm performance using some proxies for firm valuation, such as Tobin’s Q, ROE, ROA, EPS and net profit margin. A more robust indicator would include more than two proxies for financial performance.

Secondly, the present study did not take into account the external factors that may have had a significant impact on company performance. For example, inflation, foreign exchange, macro economy, and interest
rate policy may have had a more significant impact on the company’s performance than on how a company was regulated internally (Ponnu, 2008). The study could also be augmented with a study of the qualitative aspects of the board that contributed to firm performance, such as the board decision-making process.

Finally, the third limitation of the study was that the variables such AC independence, AC expertise and AC meeting in regression models may not have been good proxies for the effectiveness factors of the audit committee that were measured in this study. Since it is important that the members of the audit committee acquire a level of accounting, financial and industrial competence that supports the monitoring role of the board, the number of AC directors with big four experience and with industrial experience may be a good measurement for AC expertise for future research.

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Authors

Norazian Hussin is a lecturer with the Faculty of Accountancy, Universiti Teknologi Mara Malaysia.

Dr Radiah Othman is a Senior Lecturer with the School of Accountancy, College of Business, Massey University, New Zealand. She has published in journals such as Corporate Governance: The International Journal of Business in Society, International Journal of Disclosure and Governance, Corporate Social Responsibility and Environmental Management and Journal of Business Ethics. She has also written in professional journals such as Accountants Today and Smart Investors Malaysia.