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CORPORATE GOVERNANCE DISCLOSURE – AN INTERNATIONAL OVERVIEW OF RESEARCH TRENDS

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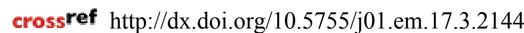 http://dx.doi.org/10.5755/j01.em.17.3.2144

Abstract

Our paper approaches "corporate governance disclosure" concept from a different perspective – the researchers one - presenting an overview image of what has already been studied, analyzing and discussing the trends of research on this topic, which is important to all researchers interested on it. The main reason of focusing our research in this area was the continuously increasing importance given to corporate governance and transparency, as a consequence of the most recently corporate failures and accounting scandals, not only among regulatory authorities and at companies' level, but in academic environment, too, where we have assisted at an increasingly interest in measuring the level of transparency by developing disclosure indices in this respect. Thus, unlike previous research studies which were focused on a specific aspect of corporate governance disclosure our paper provides a different approach, by analyzing the trend of research studies focused on disclosure indices developed for measuring the level of transparency and their possible relationship with the most important corporate governance attributes.

Keywords: corporate governance, disclosure, transparency, quantitative analysis, academic literature
JEL Classification: M10, G30

Introduction

Corporate governance disclosure had gradually become one of the most debated and challenging topic of worldwide research. Many changes that appeared in legislation, most of them due to the financial crisis that spread all over the world in the latest years, made from corporate governance an attractive and dynamic research area.

The increasingly concern of international researchers on it was our main reason of focusing our research in this area, followed by the continuously increasing importance given to corporate governance and transparency, as a consequence of the most recently corporate failures and accounting scandals, not only among regulatory authorities and at companies' level, but in academic environment, too, where we have assisted at an increasingly interest in measuring the level of transparency by developing disclosure indices in this respect.

Starting from the topicality of this concept, our paper approaches corporate governance from researchers' perspective, by reviewing the international literature that comprises a diversity of studies from conceptual and normative papers to comprehensive empirical ones.

Therefore, the objective of our paper is to provide an overview of international academic research in the area of corporate governance disclosure, by identifying its trend, pointing out the main topics of interest and research methodologies used, thus approaching this concept from a different perspective – the researchers' one.

For achieving our main goal, firstly we selected a sample of papers dealing with "corporate governance disclosure" concept, by searching through the most well-known international databases. Thus, the research methodology used is based on a literature review of a significant number of research papers published in the most well-known international journals on economic sciences field. Consequently, our study comprises a quantitative analyze which reveals the evolution of the state of research in the area of corporate governance disclosure, being aimed to find a comprehensive and justified answer at one of the most debated and controversial issue related to disclosure: *"What are the attributes of a good corporate governance system that are able to ensure the highest level of transparency?"* For achieving our goal we considered for analysis the three most important "key-players" of the corporate governance system – board of directors, ownership and audit - that were highly debated and analyzed in prior studies dealing with disclosure and transparency.

The paper proceeds as it follows. Firstly, we briefly present the theoretical background of "corporate governance disclosure". Then, we started performing our comprehensive quantitative analysis of prior academic literature, focusing on disclosure indices developed for measuring the level of transparency and the relationships tested between these indices and the most important corporate governance attributes. Finally

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our paper ends by discussing the implications of our research findings and presenting the limitations of our study.

Corporate governance disclosure – theoretical background

"Corporate governance disclosure" concept derives from the most well-known agency theory that explains the differences in behavior or decisions between the two parties - "the principal" that delegates work to "the agent"- by noting that the two parties often have different goals and, independent of their respective goals, may have different attitudes toward risk, all of these leading to the agency problem.

In order to control the agency problem and to ensure that managers act in the interests of shareholders two corporate governance tools can be used. The first one is to monitor agents' behavior in order to make sure that they are acting in the interest of shareholders, which is generally perceived as a way of reassuring investors that a company's board and management have in place appropriate strategies, structures and controls that enable them protecting from conflicts of interest and maximizing their value (Kiel and Nicholson, 2003). The other one consists of voluntary disclosure for providing the more comprehensive image of the company's overall activity, which may serve as a complement of a firms' governance mechanism (of monitoring activity) in reducing information asymmetry, especially in a countries where legal protection of investors is high, thus being more likely to be credible (Cormier, et al., 2010). It is mainly because information asymmetry might lead to "moral dilemmas" among principals due to the impossibility of accurately evaluate and determine the value of decisions taken by the agent, who is in an advantage position of direct access to the information, having thus the possibility to take decisions in his personal goals. Prior studies also stated that mandatory disclosure rules ensure equal access to basic information (Lev, 1992) and help firms to communicate with their investors, but they do not fully solve the challenges posed by information asymmetry (Healy and Palepu, 1995), thus additional voluntary disclosure being recommended.

Basing on this background, "corporate governance disclosure" and especially "voluntary disclosure" stood as a topic of interest in various studies. Thus, very often debated was the relationship between monitoring and disclosure, two different opinions being identified in this respect, stating that there might be either a complementary relationship (Leftwich et al. 1981; Welker, 1995) or a substitutive one (Rediker and Seth, 1995; Cheng and Courtenay, 2006). In case of a complementary relationship, enhancing monitoring in order to reduce opportunistic behavior and information asymmetry is expected to lead to a greater extent of disclosures, because in an intensive-monitoring environment managers have no interest to withhold information for their own benefits. Opposite are the expectations of an intensive-monitoring environment in case of the substitutive relationship, where it is appreciated that an additional governance device, such as disclosure, is useless if information asymmetry could be reduced through internal monitoring.

Another topic of interest that was widely encountered in academic research refers to the two categories of agency costs related to the control mechanism of reducing agency conflicts adopted, namely: the costs related to monitoring activity - monitoring costs, bonding costs and residual loss (Jensen and Meckling, 1976) and the costs related to voluntary disclosure - proprietary costs (Verrecchia, 1983; Wagenhofer, 1990; Darrough and Stoughton, 1990) and litigation costs (Skinner, 1994; Miller and Piotroski, 2000). Considering all these agency costs, the decision to disclose additional information is typically modeled in terms of a cost–benefit framework. Consequently, firms will voluntarily disclose information when the benefits of disclosure outweigh the associated costs (Verrecchia, 1983).

According to prior studies, not only agency costs are affecting managers' decisions to voluntarily disclose information, a very comprehensive review of other factors debated along time being provided by Healy and Palepu (2001), who actually emphasizes the main forces that give rise to demand for voluntary disclosure in a modern capital-market economy and the institutions that increase the credibility of disclosures. Thus, there have been formulated various hypothesis testing various factors affecting managers' decisions to voluntarily disclose information for capital market reasons, namely: the capital market transactions, the corporate control contest, the stock compensation, the management talent signaling and, the litigation and proprietary cost hypotheses.

Besides the above mentioned factors tested for identifying possible influences over voluntary disclosure decisions, their major economic consequences, namely embodied in capital market effects have been often discussed along time, thus being another important topic of research on corporate governance disclosure literature. Thus, prior studies argument for voluntary disclosure's effects on improving stock liquidity, reducing the cost of capital and increasing information intermediation, a good-structured synthesis of this being presented in a review of the empirical disclosure literature (Healy and Palepu, 2001).

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In conclusion, voluntary disclosure decision proved to be a highly sensitive one, which should weight carefully the benefits it could bring compared with the drawbacks of being less transparent. This balancing of advantages and disadvantages of voluntary disclosure lead to a researchers' increasingly interest in appreciating how more or less transparent a company is. Even if measuring disclosure level of corporate governance often raised difficulties among researchers, a wide range of prior studies have been conducted aiming to measure corporate governance disclosure, being focused either on disclosure quality or, more often on disclosure quantity, thus developing an index in this respect.

"How evolve corporate governance disclosure literature in the latest decades and "What relationships between these and the most important corporate governance attributes have been tested?" are our main research question that we are trying to answer in the most comprehensive manner through a complex quantitative analysis of prior academic literature on corporate governance disclosure.

Corporate governance disclosure – trends of research in academic literature

Our paper is aimed to find a comprehensive and justified answer, based on prior empirical findings, at one of the most debated and controversial issue related to disclosure: *"What are the attributes of a good corporate governance system that are able to ensure the highest level of transparency?"*.

The assumptions made in prior literature regarding possible associations between corporate governance and the level of information disclosed were mainly based on the *agency theory*, which is stating that due to separation between "property" and "control", as well as to the different goals, attitudes toward risk and behaviors, there are arising many conflicts of interests between the two parties – owner (principal) and manager (agent), that might be kept under control by either by a *proper monitoring* or by a *comprehensive disclosure* of the company's overall activity.

By performing a quantitative analysis of the prior research related to "corporate governance disclosure", we are approaching this concept from a different perspective – the researchers' one, thus pointing out besides the main topics of interest, its trend and the research methodologies used, adding value to international literature, too.

To this end, firstly we select a sample of papers by searching in the most well-known international databases (including Business Source Complete, Cambridge Journals Online, Osco Host EJS, Emerald, Informaworld, IngentaConnect, ISI Web of Knowledge, ISI Web of Science, Jstor, Proquest, ScienceDirect, Springer, Wiley Online Library) for papers that report findings on measuring corporate governance disclosure by developing an index in this respect. Our search was based on different combinations of the words "disclosure", "corporate governance" and "transparency" on papers' title, abstract and keywords. The searches yielded a total of 148 papers focused on corporate governance disclosure and transparency. From the total number of papers identified, we retained for our quantitative analysis just 55 papers, which developed a disclosure index and analyzed it closely related to corporate governance determinants and organizations' characteristics.

For achieving our main goal, we divided our analysis into three parts, according to the three most important "key-players" of the corporate governance system considered (board of directors, ownership and audit), which made the specific objectives (SO) of our study:

SO1 - The analysis of academic literature from board of directors features perspective
SO2 - The analysis of academic literature from ownership features perspective
SO3 - The analysis of academic literature from audit features perspective

After selecting the sample of journals and variables needed, we can start performing our quantitative analysis of the prior research related to "corporate governance disclosure", by trying to achieve one after another all the specific objectives proposed:

a) SO1 - The analysis of academic literature from board of directors features perspective

Board of directors has always played an important role in the corporate governance structure, mainly due to its major responsibility of enhancing the overall value of a company while serving the needs of all stakeholders. Protecting stakeholders' interests that might be endangered sometimes due to the separation between ownership and control of a company needs the adoption by the board of a proper monitoring and control system. In order to fulfill its responsibilities of being legally bound to represent the interests of the stockholders, to effectively control and allocate the firm's resources and to guarantee that the relevant interests of the stockholders are protected, board of directors must have certain *features* specific for a *good*

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corporate governance structure, such as *independence, autonomy, capability, control power, dominance or incentive*.

Prior literature focused on corporate governance disclosure aimed to identify possible associations between various features of the board and the level of transparency ensured by companies through their annual reports. Our study provides an overall image of the correlations identified by such research studies.

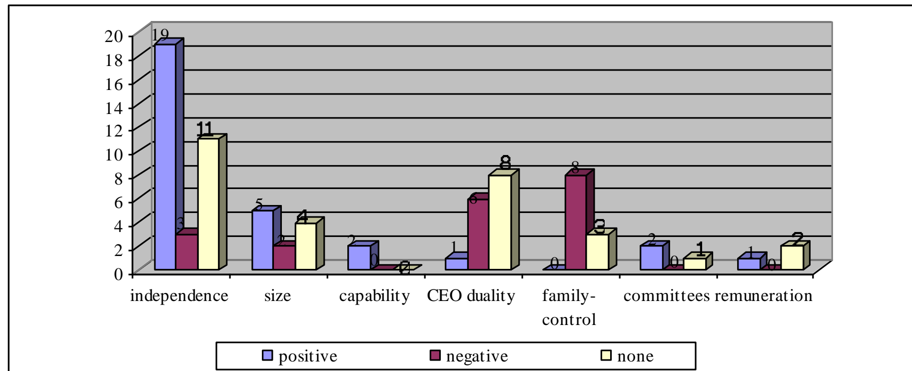

Figure 1. Literature analysis considering board of directors' features

The most analyzed feature of the board used for explaining the level of disclosure was its *independence*, assessed through the proportion of outside (non-executive) directors on the board. Our quantitative analysis reveals that most empirical researches found a *positive* association between board independence and the level of disclosure. These results are consistent with the agency theory premise, a large number of non-executive directors on the board leading to fulfill better their role in monitoring and controlling the actions of the executive directors, as well as providing a window to the outside world.

Another feature of the board that, generally, proved to be *positively* correlated with disclosure is its *size*, thus five studies reaching to significant results in this respect, while three studies proved otherwise and four papers did not find any association. We appreciate our findings not so eloquent because of the differences in measuring this variable, as long as there is not stated a certain number by any corporate governance code. Hence, there are only recommendations in this respect and various opinions, such as a small board made of seven or eight members that can help improve performance (Jensen, 1993; Lipton and Lorsch, 1992), companies having therefore the possibility to decide on their own upon it.

Even though it has rarely been considered for analysis, board's *capability,* assessed through the professional expertise of its members, had a clear *positive* influence over disclosure, too. The same impact can be observed when analyzing board's *committee* - nomination and remuneration committee – both of them contributing to a sound governance through their beneficial role in ensuring board effectiveness as a monitoring device by nominating the most suitable candidates in this respect, and motivating them to act so that all interest in company to get aligned.

This letter aspect is one of the most controversial, which is why our analysis is not able to provide meaningful results. Thus, *incentives* of board members are appreciated in the light of the agency theory as a good way of increasing their efforts and devotion in supervising the company, but at the same time they also might be a reason for conspiracy with company management for their own benefits. These opposite opinions justify the *lack of* a clear *association* between remuneration and disclosure level.

Another controversial feature of the board is *the dominant leader*, also found in literature as "role duality" or "dominant personality", which actually refers to the situation when the same person serves as both chairman of the board and chief executive officer. According to our analysis of prior literature, this feature was often considered for testing the association with the level of information disclosed by companies, but unfortunately their results have not been able to lead to a unique sense of influence. Thus, even if the number of papers that succeeded to prove a negative relationship between CEO duality and disclosure is almost equal to the one of those studies that could not establish any link.

Our results are consistent with the arguments provided by corporate governance theories in avoiding / accepting the role duality on the board. While in the light of the agency theory the separation of duties is perceived as beneficial at least because it ensures independence between the board of directors and corporate management, avoids the entrenchment of the CEO, increases the board monitoring effectiveness and the

chairman's power to advise the CEO, the stewardship theory considers that role duality basically enhances the effectiveness of boards.

A *negative* association was often found between board's *control power* and the level of transparency. Analyzed in prior literature as "family control boards", this feature is usually characteristic to "closely held" or "owner-managed" companies, which proved to be less interested in disclosing information, due to a lower degree of conflict of interests and the direct access to the company's financial and non-financial information.

b) SO2 - The analysis of academic literature from ownership features perspective

Ownership is another important key-player of a good corporate governance system, whose features might influence the level of transparency, too. Its importance derives as well form the agency theory, because shareholders' interests may be protected differently depending on ownership structure and its ability to influence the management.

Prior literature often analyzed its *structure, concentration and composition*, assessed by means of foreign nature, trying to identify possible associations between these features and the level of information disclosed by companies through their annual reports. Our study provides an overall image of the correlations identified by such research studies.

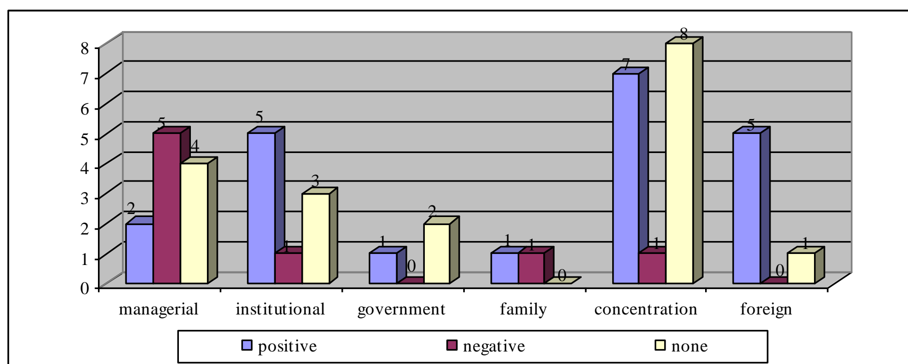

Figure 2. Literature analysis considering ownership's features

The highest debated topic of research was the relationship between *ownership concentration or dispersion* and the level of disclosure, but unfortunately empirical findings have not been able to explain a significant correlation. Thus, while half of studies reached to the conclusion that ownership dispersion is positively associated with disclosure the other half of the studies did not find any association. It can be explained by the fact that disclosure actually has the same importance in both cases – concentration or dispersion – but at different levels. Thus, while disclosure acts in case of a dispersed ownership as a measure of protecting shareholders by ensuring that managers are acting in their best interests, in case of a concentrated ownership its role is changing, thus becoming an "annihilator" of the conflict of interests aroused between insiders (controlling shareholders and managers) and outsiders (minority shareholders and other investors).

The *foreign nature* of the ownership proved to have a definitely *positive* influence over the level of disclosure, as almost all research studies considered in our analysis reveal. It can be explained, by the information asymmetry, based on the fact that foreign shareholders are usually in a disadvantage position compared to domestic ones as regards information, mainly because of distance and language barriers, which leads to an increasing need of disclosure for reducing the agency conflicts aroused between foreign and domestic investors.

Ownership *structure* was assessed in prior studies by considering various types of shareholders, such as other institutions, the government or the manager itself and the research findings were different for each type of structure considered. Thus, managerial ownership - shareholders being in managerial executive positions, proved to be negatively correlated with disclosure, due to an increased need for monitoring, while institutional ownership might have a positive influence on it, due to their highly effective role on monitoring.

c) SO3 - The analysis of academic literature from audit features perspective

Audit is considered as an important "link" in corporate governance mechanism, due to their power of detecting management "wrongdoings" and reporting inappropriate behavior to internal and external business

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stakeholders. Irrespective of owners, directors and executives, which must prove they uphold the company's mission and values in their actions, thereby rewarding shareholders with financial returns, audit often focus on transparency and accountability of a company, thus having a high impact on the level of disclosure, too.

Consequently, many prior research papers have analyzed possible associations between audit and the level of disclosure provided by companies through their annual reports, mainly focusing on two issues: *audit committee* and *external auditor.*

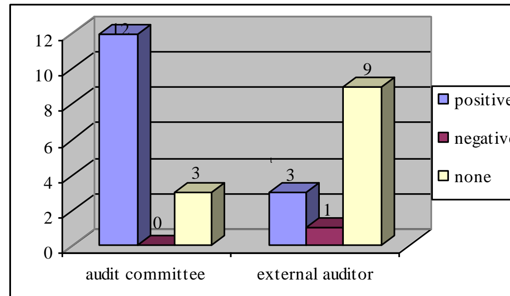

Figure 3. Literature analysis considering audit's features

The audit committee plays a primary role in the corporate governance mechanism being charged to assist the board on its oversight responsibilities in the areas of external and internal auditing, as well as in risk management and internal control. Due to its supervisory role, its presence in the corporate governance structure of a company is appreciated as beneficial for reducing information asymmetry and managerial opportunism, and consequently for improving disclosure quality. These expectations have been confirmed by empirical findings in most papers that have analyzed the correlations between the audit committee and the level of information disclosed by companies. Thus, a *positive* association has often been found, as the results of our analysis reveal, among the factors considered for assessing the audit committee the most often used being the size of the committee and the frequency of its meetings, but also various features of its members, like their independence or their expertise.

External auditor is the other issue from the audit area that was often considered for explaining the level of information disclosed. Usually it has been assessed through its size, the "Big Four" group of auditors being recognized as providing high quality services. The main reason why researchers used this issue in relation with transparency is based on the external auditors' role in the corporate governance system of enhancing the credibility of financial information through transparent financial reporting. Even if it was expected for a "Big Four" external auditor to have positive influence on corporate governance disclosure, prior research findings reached to a surprisingly different conclusion, most studies have not identified any association.

Conclusions and limitations

Even if we do not talk about "corporate governance disclosure" concept for a very long time, interests of various stakeholders of a company existed all the time. The cooperation of these interests had been gradually leading to the concept of corporate governance, which has always been a subject of controversy. Considering the aspects presented above, "corporate governance disclosure" has always been an important research area, too. The increasingly concern of international researchers on it is our main reason of developing an analysis aimed to provide an image of academic literature's interest on this concept and its evolution on time. Moreover, the purpose of our paper, as well as the criteria used in the analyzing methodology give originality to the research done, offering by thus new opportunities for future research.

Unlike previous research studies which were focused on a specific aspect of corporate governance disclosure such as analyzing the relationship between monitoring and disclosure and their related costs, the main factors affecting managers' decisions to voluntarily disclose information and its major consequences, our paper provides a different approach, by analyzing the trend of academic research.

The results of our study reveal a significant "enrichment" of corporate governance disclosure related literature, due to a continuously increasing interest on this topic mainly because of the latest financial scandals that led to the collapse of many international recognized companies, corporate governance failures being often considered as their major cause. From the research methodology perspective, the majority of

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paper succeeded to prove the existence of a significant correlation between the level of information disclosed and corporate governance system's features by using regression analysis. As regards the attributes of a good corporate governance system tested, the results of our analysis reveal either a positive or a negative impact on the level of transparency, but there were also cases where it could not be established any influence at all.

Like any other research, we are aware of the limitations of our study that come from the sample's dimension, just the most representative international databases being consulted when searching for papers dealing with our topic of interest. But, these limitations offer us outlooks for future research, by extending the sample of journals and papers included in analysis, even by considering more specific criteria for selection. Also, the research methodology might be improved by using comprehensive statistical methods for testing the relationship between the established variables, which gives us outlooks for future research.

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