

Corporate Governance and Compliance of Integrated Reporting: Evidence from Malaysian Listed Companies

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Received Date: 27 September 2019

Accepted Date: 16 October 2019

ABSTRACT

Integrated reporting is an emerging practice progressively catching the consideration of organizations. The idea of sustainability reporting increased more significance in the companies' annual report, a pattern that is implanted likewise in integrated reporting. The governance structure all the more precisely the board of director is the main role to decide whether the company will issue an integrated report. Hence, the purpose of this paper is to examine the relationship between corporate governance (managerial ownership, family ownership, institutional ownership and government ownership) and consistence of coordinated integrated reporting elements disclosure. To achieve this objective, we analysed the way in which integrated reports of 30 companies are following the guidance provided by the International Integrated Reporting Framework (IIRF). As a result, we noticed that most annual report scored the highest compliance level and consistence with the guidance of the IIRF. In addition, the result also demonstrated institutional ownership and government ownership positively affect and significance integrated reporting elements disclosure. Our findings contribute to comprehend the practice of integrated reporting and may have suggestions for regulators in emerging countries for company sustainability reporting.

Keywords: *Integrated reporting; Sustainability reporting; Listed companies, Corporate governance*

INTRODUCTION

Emerging markets have turned into the focal point of international corporations, personal and institutional investors due to their high rates of economic growth (Millar et al., 2005). However, they suffer from low financial specialist assurance rehearses, especially expropriation of minority shareholders both by managers and by controlling investors (Gonenc & Aybar, 2006). They have higher information asymmetry among managers and investors (Gul and Leung, 2004; Chau & Gray, 2010), and have lower level of disclosure than those in developed market economies (Salter, 2002; Wang et al., 2008; & Tower et al., 2011), while high-development firms need more voluntary disclosure than low-development firms due to their need for external finance (Core, 2001). The board of directors is a significant component in the financial reporting of present day firms. Many studies focus on corporate governance and its features in different countries (Rouf & Harun, 2011; Rouf, 2011). In later, the theme of corporate governance has been thoroughly analyzed. According to Van der Walt & Ingley (2003), corporate governance refers to the variety in the ownership structure of companies. This study use four elements of corporate governance consist of managerial ownership, family ownership, institutional ownership and government ownership.

The present corporate governance literature perceives that significance, however, the impact of corporate governance on corporate voluntary disclosure practices, remains unexplored in emerging stock markets. There has been extensive number of examines on the relationship between corporate governance on the level of voluntary disclosure. However, most of these researches have been concentrated on developed countries and unfortunately, what is true for a developed country can be completely different for a developing country or the other way around. Therefore, motivation of this study is to examine the extent of voluntary disclosure in annual reports and web-sites of companies and to find out whether the variables of corporate governance has found to be significant in explaining voluntary disclosure practices in developed countries apply in a developing country such as Malaysia. Rapidly making super floats in innovation, populace and assets together with expanding vulnerability in the worldwide economy and money related markets make it key that associations reconsider their internal and external offering an explanation to guarantee they have the information to make a choice and clarify the procedures, needs, execution and prospects of their organizations. The aftereffects of analysis demonstrate that while Malaysian associations have the basics of reporting covered; their reporting is not yet incorporated (PwC, 2014). Corporate governance research has evolved into a challenging research issue in academia for the most recent decades. A large portion of this examine has initiated from the fact that there are increasing numbers of women in top management as well as on corporate boards (Singh et al., 2001). Corporate governance in term of board diversity literature emphasizes that diversity may benefit the board's decision making process as new recognitions on various issues are given and consolidated with a mutual exchange of thoughts coming from board members with dispersed backgrounds and experience (Rouf, 2012).

Voluntary disclosure refers to sharing information publicly other than what is required by laws or regulations accomplished for organizations' images, investors and accusation risk avoidance (Tian & Chen, 2009). It gives both financial and non-financial information. A high level of disclosure attracts great attention from members of the public and hence increase the investors' confidence, which explain the reasoning behind which companies are striving to achieve maximum disclosure. Besides, it is a way of minimising adverse selection and moral hazards and ultimately reduces information asymmetry (Wang, Sewon & Claiborne, 2008). Voluntary disclosure has been classified differently by past studies however this examination receives three categories as done by (Eng & Mak, 2003; Lim, Matolcsy & Chow, 2007; Zhou & Panbunyuen, 2008); strategic information, financial and non-financial information. First, strategic information focuses on the future of the company and the past, which conveys the status of the company both national and transnational. Strategic information emerges from company policy, objectives, capital expenditure and research and development expenditure budget. Second, financial information is communicated in monetary terms that can be assessed through ratio such as liquidity, profitability, gearing/leverage and investors' ratio, forecasting sales and profit and analysis of market shares. These ratios communicate much about the company financial position and as such they should be computed and summarized for a period mostly three or two years to improve comparison. In conclusion, non-financial information relates to employee and activities that support corporate social responsibility for example society, environment (reducing pollution), donations, and charity and so on. For employees' disclosure is concerned about their welfare, any staff training and again (Zhou & Panbunyuen, 2008).

Voluntary disclosure can be shown anywhere, for example annual reports, public announcement, booklets, website, road show, etc. whereas compulsory disclosure is normally shown in the annual report, interim report, and season report. Presently to sum it all, voluntary disclosure is a significant indicator of the earning quality of a company that would help investors in settling on better decisions on allocation of their capital. In recent years, the role of external reporting has developed, demonstrating the significance of non-financial information that has to be included in integrated reporting (Manes Rossi, 2018). In fact, non-financial information, together with financial information, explains the entire status of the firm, satisfying the required level of transparency and accountability for stakeholders (IIRC, 2013) and better supporting the decision-making process (Adams, 2011). The International Integrated Reporting Council (IIRC) features

that integrated reporting is “a concise communication about how an organization’s strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value over the short, medium and long-term” (IIRC, 2013) (Part 1.1). Integrated reporting discloses interactions between financial and non-financial information, with an emphasis on the company’s future worth creation story (Montecalvo et al., 2018). The objective of this study is to examine the relationship between corporate governance (managerial ownership, family ownership, institutional ownership and government ownership) and integrated reporting disclosure of Malaysian Listed Companies. Therefore, the problem discussed in this study is to examine what are the impacts of corporate governance on enhancement of the level of compliance of integrated reporting. The empirical findings presented in this study contribute to the academic literature on corporate governance and integrated reporting. The next section discusses the past research and followed by research method. Section four is the analysis and discussion, followed by the fifth section, the conclusion of the study.

RELATED WORKS

A board is commonly composed of inside and outside members. Inside members are selected from among the executive officers of a firm. They either have a place with the management group or are the family that owns the firm. Outside directors are members whose only affiliation with the firm is their directorship. Patelli, L., and A. Prencipe (2007) revealed that composition of the board is one of several factors that can mitigate agency conflicts within the firm. Rouf (2015) argument is that independent directors are required on the boards to monitor and control the activities of executive directors who may engage in opportunistic behavior and furthermore to ensure that managers are working in the best interest of the principal. Voluntary disclosure and its determinants have been distinguished as an important research area and have attracted both analytical and empirical researchers in accounting since the 1970s. In the literature, various of studies have been undertaken to examine the relationship between corporate governance mechanisms and voluntary disclosure. Cheng and Courtenay (2006) found that boards with a larger proportion of independent directors are significantly and positively associated with higher levels of voluntary disclosure in Singapore. In addition, Chen and Jaggi (2002) examined the relationship between independent directors and corporate disclosure. They found a positive relationship between a board with a higher proportion of independent directors and related financial disclosure.

In Malaysia, Ghazali and Weetman (2006) address the relationship among ownership and voluntary disclosure in the annual reports of Malaysian companies. Companies that only concentrate on the basics of financial reporting are not sufficient in this competitive and questionable market environment. This is because financial report does not include information on non-financial performance that can decide to determine a company’s long term financial background (Eccles & Saltzman, 2011; Ghani & Said, 2010). Magarey (2008) also concurred that the information provided in the conventional annual report is not relevant enough as the information does not give an all encompassing picture and understanding of a company’s business activities. Therefore, by implementing integrated reporting framework, it improves business communication and upgrades the nature of corporate information available to investors and empowering them to value a company effectively (Ernst & Young, 2012). Integrated report conceptual framework declared that all significant types of resources utilized by companies for worth creation (Cheng et al., 2014). The International Integrated Reporting Council proposed a new categorisation that distinguishes between relational capital and social capital. In spite relational capital vital job in company value creation, this theme has not been disclosed in the mandatory annual report or in other standalone report drafted voluntarily by companies. Ownership structure is, among others, an important factor that can determine corporate disclosure level. In this study, we analyse the impact of managerial, family, institution and government ownerships on integrated reporting disclosure.

Managerial Ownership

Managerial ownership is the percentage of shares owned by the management (Eng & Mak, 2003). This practice could decrease agency problem because managerial share ownerships could align the enthusiasm of the managers with the owners. Therefore, reliable with Jensen and Meckling (1976), companies owned by the management may provide more disclosure than different firms to expand the liquidity of the company. However, significantly high ownership by managers may reduce the need to give voluntary disclosure resulting in lower level of disclosure (Eng & Mak, 2003; Mohd Ghazali, 2007; Chau & Gray 2010). The findings show that the owners may not have adequate motivation to signal information to outsiders as their share ownership increases. As such, it can be expected that as managerial ownership increases, integrated reporting disclosure decreases.

H₁: There is a negative relationship between managerial ownership and relational capital disclosure.

Family Ownership

The presence of family ownership and relatives on the board of directors are customary attributes of businesses in Malaysia (Claessens et al., 2000; Mohd Ghazali & Weetman, 2006), as well as in other Asian nations (Ho & Wong, 2011). A majority of prior literature such as Haniffa and Cooke (2002), Mohd Ghazali and Weetman (2006), Al-Akra and Hutchinsons (2013) discovered evidence that family impact in companies could influence voluntary disclosure practices downwards. This practice is reliable with two effects i.e. alignment effect versus entrenchment effect. Alignment effect of family ownership with the majority of other shareholders may make the intention to signal information is reduced. The demand for disclosure is decreased since a significant portion of the shareholding is held by families. Thus, the motivation to disclose information in order to show signs of improvement of external financing contracts may be reduced. The trust and familiness culture among family members may also become a factor for reduced signalling motivation. However, as indicated by entrenchment impact, families on board and the management team may lead to improper governance practices, which could results in expropriation activities. Accordingly, suggesting from Fan and Wong (2002) and Francis, Schipper and Vincent (2005) that such activity may cause the owners to limit information flows to outside parties, in order to conceal their activities from known by the outsiders. The family may obstruct their relational information more than others because these relationships or connections may reveal their expropriation activities such as through tunnelling activities. This argument implies that family owners may square or decrease signals about relationships or connections to outside parties. Thus, both arguments suggest that an increase in the family ownership would bring about lower disclosure of integrated reporting information.

H₂: There is a negative relationship between family ownership and integrated reporting disclosure

Institutional Ownership

Ten largest companies in Malaysia are possessed by institutional investors (Saleh et.al, 2010). In fact, institutional investors play crucial role in developing the economy. Therefore, institutional investors assume a significant role in the design of governance in the investee companies. Part of the governance process to monitor the progress and performance of investee companies is the corporate straightforwardness and disclosure (David & Kochhar, 1996; Saleh et. al, 2010). Kim and Nofsinger (2004) recommend that

voluntary disclosure is utilized as a mechanism used by institutional investors to monitor companies. In addition, institutional investors really contribute on behalf of retail investors. Therefore, the institutional investors are more aware of the demand for information from the retail investors. As such, prior studies found a positive relationship between voluntary disclosure and institutional investors (Barako et al. 2006; Magena & Pike, 2005). Consistent with this finding, Iatridis (2013) discovered quality disclosure is associated with institutional ownerships. Generally, it tends to be reasoned that the demand of information to monitor companies by institutional investors could become a motivation for companies to signal their private information in the form of voluntary disclosure. In addition, progressively voluntary disclosure could also attract more investments from institutional investors as company reputation increases. The reputation of companies can increase if they could demonstrate by disclosure of information that the business is well accepted by their reputable business partners. Therefore, we expect an increase in institutional ownership should results in an increase in integrated reporting disclosure.

H₃: There is a positive relationship between institutional ownership and integrated reporting disclosure.

Government Ownership

Traditionally, it is normal that there is negative effect of government ownership on corporate performance (Qi et al. 2000; Wei et al. 2005; Lin & Zhang, 2009). This impact could be due to companies need to allocate funds for politicians (Sapienza, 2004) and more political interventions in government owned companies (Gul, 2006; Johnson dan Mitton, 2003). In Malaysia, Government Linked Companies (GLC) are controlled directly by the government through equity ownership by its investment arm, Khazanah Nasional Berhad. These companies involved in a scope of sectors i.e. financial, communication and media, utility, information technology and transportation. We expect the relationship between government ownership and integrated reporting disclosure is positive for various of reasons. First, consistent with the government's aspirations to develop a knowledge based economy, the implementation of such policy is expected to be occurred in GLCs. As part of knowledge, voluntary disclosure is important in a knowledge based economy. Therefore, a high government ownership should bring in high disclosure of integrated reporting. Second, government influenced companies may make more relationships or connections (including political connections) than other companies. Managers believe these connections as value maximising activity that can assure long term sustainability of the company, thus having the incentives to disclose the information. A study by Chen et al. (2013) suggest that there is higher value of politically connected companies compared to non-politically connected companies due to the expected value of preferential treatments, inclination in task choices and access to state benefits. Third, government may also act on behalf of the public at large. Due to the pressure to present good investments made in the parliament, government owner may demand investee companies to provide comprehensive reporting of the strength of the companies by voluntarily disclosing integrated reporting. Thus, it can be expected.

H₄: There is a positive relationship between government ownership and integrated reporting disclosure

RESEARCH METHOD

Samples are involved of companies listed on the Bursa Malaysia. However, this research selects companies based on a benchmark study on 30 companies that have been providing integrated annual reports as outlined

by International Integrated Reporting Framework (PwC, 2014). We choose top 30 companies listed on the Bursa Malaysia in term of the companies comprising the top 30 which is analysing data was performed 110 detailed assessment question were based on the content elements for an integrated reporting. This benchmarking study is aimed to see how far the company has adapted and prepared annual reports according to the integrated report framework. Therefore, for the purposes of collecting data for this study then the list of the same company was selected as a sample of this study. Following prior research (such as, Guthrie & Petty 2000; Brennan 2001; Bozzolan et al. 2003; Abeysekara & Guthrie 2004), the data was gathered from published annual reports in year 2015 to 2017. Annual reports are company documents issued to the public, physically (Campbell 2000), or electronically (Kamarulbaraini & Khairul 2005; Iqbal 2005), that has a impacts on the capital markets and public perception about the company (Anderson & Epstein 1997). Content analysis is also an appropriate method for performing quantitative studies. Year 2017 was the latest annual reports available at the time this study was conducted. All annual reports are acquired from the Bursa Malaysia website. There were total 90 samples observations. The number of companies selected for this study is as follows:

Table 1: Sample

Year	2015	2016	2017
Main Market	30	30	30

The dependent variable is the integrated reporting disclosure (IRD). There are four (4) independent variables tested in this study i.e., managerial ownership (MGROWN), family ownership (FAMOWN), institutional ownership (INSTOWN) and government ownership (GOVOWN). Control variables are firm size (FMSIZE), leverage (LEV), firm age (FMAGE).

$$IRD_{it} = \alpha + aMGROWN_{it-1} + bFAMOWN_{it-1} + cINSTOWN_{it-1} + dGOVOWN_{it-1} + eFMSIZE_{it-1} + fLEV_{it-1} + gFMAGE_{it-1} + \varepsilon_{it} \dots (1)$$

Integrated reporting disclosure (IRD) is measured based on total score of relational capital index. Data on the index was collected manually based on disclosure made in company annual reports. we divide the total disclosure score observed for each company (OD) by the maximum disclosure score a company could get (TD) to represent the level of integrated reporting disclosure (IRD).

$$IRD = \frac{\sum OD}{\sum TD} \dots \dots \dots (2)$$

The definition of independent variables and control variables are as follows:-

Table 2: Definition of independent variables / control variables

Independent variable / Control Variable	Expected relationship with dependent variable	Measurement (all measurement items are obtainable from annual reports)
<i>MGROWN</i>	- H ₁	Percentage of share ownership by executive directors (Mohd-Saleh et al., 2005)
<i>FAMOWN</i>	- H ₂	Percentage of share ownership of more than 1% by families of the members of the board (Munir et al., 2013; Mohd-Saleh et al. 2014)
<i>INSTOWN</i>	+ H ₃	Percentage of share ownership of more than 5% by institutional investors (e.g. Employees Provident Fund,

Independent variable / Control Variable	Expected relationship with dependent variable	Measurement (all measurement items are obtainable from annual reports)
		insurance, Permodalan Nasional Berhad, commercial and investment banks) (Ahmad et al., 2012)
GOVOWN	+ H ₄	Percentage of share ownership of more than 5% by the Government Linked Companies
FMSIZE	+ (Guthrie et al. 2006)	Log of total assets (Guthrie et al. 2006)
LEV	+ (Gerpott et al. 2008; Hossain et al.1995)	The ratio of total liability to total assets (Mohd-Saleh et al. 2008)
FMAGE	+ Majumdar, 1997; Dogan, 2013; Halil & Hasan, 2012.	Natural logarithm of age of the firm from date of incorporation (Majumdar, 1997)

FINDINGS AND DISCUSSION

Table 3 shows the total integrated reporting disclosure of the companies by years. Overall, there were 64.66% of integrated reporting disclosure provided by firms in 2015, 70.26% as compared to 2016 and 70.69% in 2017. There was a sharp increase in the integrated reporting disclosure in 2016. The increase in the disclosure level signifies the importance of integrated reporting in value creation process among the preparers.

Table 3: Integrated Reporting Disclosure

ITEM	2015	%	2016	%	2017	%
Mission and vision	24	82.76	26	89.66	28	96.55
Principle activities	22	75.86	26	89.66	24	82.76
Competitive landscape	12	41.38	14	48.28	24	82.76
Macro environment	4	13.79	10	34.49	12	41.38
Board structure	28	96.55	28	96.55	28	96.55
Compliance of CG Code	20	68.97	24	82.76	24	82.76
Board and executive compensation	16	55.17	20	68.97	18	62.06
Shareholders	26	89.66	26	89.66	26	89.66
Related party transactions	14	48.28	14	48.28	14	48.28
Key inputs and outputs	12	41.38	12	41.38	14	48.28
Business Activities	22	75.86	24	82.76	24	82.76
Outcomes	8	27.59	10	34.49	10	34.49
Risk management philosophy	28	96.55	28	96.55	28	96.55
Risk and opportunity identification	24	82.76	24	82.76	24	82.76
Risk and opportunity assessment	20	68.97	20	68.97	20	68.97
Risk mitigation	20	68.97	20	68.97	20	68.97

Descriptive statistics and correlation analysis of the data are provided in Table 4 below. The mean of integrated reporting disclosure is 78.5% across the three-year period. Managerial ownership appears on average 51.2%, family ownership 65.3%, institutional ownership 62.8% and about 65.2% of the shares are owned by the government. Consistent with our prediction, there is a positive correlation between integrated reporting disclosures with institutional ownership indicating that pressure from sophisticated investment companies (the institutional investors) may be effective to demand for important integrated reporting information to be disclosed. Overall the correlation analysis also reveals that the highest correlation is only

57.4%., which is way below the threshold, raising a concern regarding multicollinearity issue. However, we also test the existence of multicollinearity problem using VIF (variance inflation factor). We scan each variable for outliers.

Table 4: Descriptive Statistics & Correlation Analysis

	mean	sd	1	2	3	4	5	6	7	8
1. SKOR	0.785	0.281	1							
2. MGROWN	0.512	0.890	0.045	1						
3. FAMOWN	0.653	0.271	0.278	0.035	1					
4. INSTOWN	0.628	0.847	0.125*	0.174	0.254	1				
5. GOVOWN	0.652	0.745	0.352	0.078	0.141	0.365	1			
6. FMSIZE	0.347	0.579	0.335*	-0.311	0.574	0.148**	0.047	1		
7. LEV	0.297	0.156	0.078	0.087	0.082	-0.089	0.053	0.091	1	
8. FMAGE	1.073	3.547	0.125	-0.014	0.069	0.217	0.084	0.047	0.014	1

Note: Figures above (under) diagonal represents Spearman (Pearson) correlation coefficients. **, * denotes significant at 1% and 5% levels (2-tailed) respectively.

The multivariate regression results are presented in Table 5. The result shows the coefficients is significant and 77.5% variance in integrated reporting disclosure can be explained by independent variables. The low level of VIF suggests that multicollinearity is not a major concern. Both results are consistent. As predicted, institutional ownership and government ownership are significantly related to integrated reporting disclosure. Consistent with prior literature, information are disseminated due to demand of information from institutional owners (D'Souza, Ramesh and Min Shen, 2010; Iatridis, 2013). This result implies institutional owners are aware of the demand for information from the retail investors who invest in their company provides sufficient pressure for the company to disclose integrated reporting information. The result for government ownership is consistent with Eng and Mak (2003), that government ownership influences voluntary disclosure positively. The government, who represent the community at large may demand information to be disclosed.

Table 5: Multivariate regression results

Variables	Predicted	Coefficients	t-Stats
Constant	?	0.125	7.524
MGROWN	-	0.254	0.845
FAMOWN	-	-0.225	-1.012
INSTOWN	+	0.463**	1.254
GOVOWN	+	1.551**	1.351
FMSIZE	+	0.125	2.542
LEV	+	0.024	0.271
FMAGE	+	-0.017	-0.589
R ² = 0.775			
Adjusted R ² = 0.540			
Highest VIF = 1.945			
F Stat = 5.362**			

Overall, these results imply that networks created from institutional ownerships and government ownership influences the behaviour of managers to disclose information as integrated reporting item. However, if the companies have large managerial ownership integrated reporting disclosure is expected to be reduced i.e. managerial ownership is found to have negative relationship with integrated reporting disclosure. The result

is found because share ownership by the management aligns the interest of shareholders with the management. As their interests are aligned, the necessity to provide additional disclosure is reduced, thus reducing the incentive for the managers to signal information through integrated reporting disclosure. Therefore, H₃ and H₄ are supported. The results however do not supported H₁, and H₂.

CONCLUSION

This study contributes to the literature by examining the relationship between selected corporate governance elements (such as the characteristics of ownership structure of companies) with an integrated reporting disclosure. These factors include managerial ownership, family ownership, institutional ownership and government ownership. Specifically, the study aims to figure out which of these factors are significantly related to increased voluntary disclosure (integrated reporting). The results from regression analysis show that institutional ownership and government ownership are associated with better integrated reporting disclosure. Managerial ownership, on the other hand reduces the incentives of the management to signal such information. In addition, we also find younger companies to have more incentives to disclose integrated reporting information compared to more established companies. The results enlighten us that important corporate governance determinants of integrated reporting disclosure can be predicted when signaling intention of the management. The findings of this study show that the existence of a ownership structure element such as institutional ownership in a company have implication to disclose financial information that is more relevant to investor decision making in a market. Our findings also may have implications for regulators in emerging countries characterized by highly networked economy, whereby, business and personal networks are important for company sustainability. However, specific character of different market may also affect the intention of the management. Therefore, further studies on other markets may enrich our understanding the applicability of these perspectives on disclosure.

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