

UNIVERSITI TEKNOLOGI MARA

**CORPORATE GOVERNANCE AND
SOCIETY DISCLOSURE: THE
APPLICATION OF LEGITIMACY
THEORY**

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ABSTRACT

It is important for companies to adhere to society's values and norms by engaging in corporate social responsibility activities to remain legitimate, which in turn, translated into disclosures in annual reports. Corporate governance mechanisms have been used as explanatory factors in determining the level of CSR disclosures. This study aimed to investigate the corporate governance related motivating factors (audit committee, CSR committee, board size and independent directors) in influencing society disclosure in the Malaysian companies' annual reports using the legitimacy theory. The control variables examined were size, industry type and leverage. The level of society disclosure examined against the Modified Society Disclosure Index (MoSDI), which was comprehensively developed based on the society indicator of Global Reporting Initiative Version 4.0, preliminary observation on 2016 NACRA winners' annual reports and past literature. MoSDI comprises 50 items with nine main categories. The analysis involved 78 top companies' annual reports and sustainability reports from the year 2014, 2015 and 2016 respectively. Based on the findings, it was found that, on average for three years, society disclosure is relatively low at 34.75%, whereby out of 50 items examined, on average, the companies in Malaysia disclosed 17 items. Specifically, the extent of society disclosure for the year 2014, 2015 and 2016 were 33.64%, 36.00% and 34.61% respectively. The hierarchical regression analysis results found that independent directors and company's size were significantly associated with the level of society disclosure. By complying with good corporate governance practice, awareness can be raised and preventive measures can be taken in addressing society's issues through proper society disclosure. In addition, legitimacy gap can also be reduced via society disclosure. This study contributes to the CSR literature by specifically examining the relationship between corporate governance mechanisms and society disclosure using the legitimacy theory. Theoretical implication and implications on government and policy makers, companies, communities and education system are also provided in the thesis.

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CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Corporate social responsibility, or shortly known as CSR, has become a global trend since the last decades and this has marked an important area in business literature. Referred to as various names, namely, Sustainability, Corporate Citizenship, and Triple Bottom Line, CSR generally denotes dedications and efforts taken by firms to serve the rights of affected stakeholders, which covers non-financial aspects, such as environment and social disclosures. Caramela (2016, p. 1) defined CSR as “business practices involving initiatives that benefit society”. On the other hand, Janggu, Joseph and Madi (2007) viewed CSR as social activities undertaken by companies in order to fulfil social commitments towards employees and community. Social commitments can be conducted through scholarships, job opportunities, donations to the poor, charity events, and internship programmes.

It is maintained that, for CSR activities to be effective and transparent, they must be reported and disclosed. Environment, human capital and society disclosure are some examples of the CSR disclosures that are disclosed yearly by companies in their annual reports. Some companies take a more serious approach to report on CSR by having their own stand-alone CSR reports, such as standalone Nestle Society Report. This is a good initiative taken by companies, as nowadays, stakeholders demand for more fair and transparent disclosures. Furthermore, since annual reports are regarded as the main source of information, stakeholders, such as the community, investors and suppliers, are able to access the companies’ financial and non-financial information. Therefore, disclosures are essential for companies to meet stakeholders’ demands as a quest for sustainability. This is important because through disclosures in annual reports, greater transparency can be achieved, thus narrowing down the information gap as stakeholders’ information needs are fulfilled.

As mentioned above, there are several types of CSR disclosures. Similarly, there have been numerous studies on CSR disclosures carried out by scholars and researchers around the globe to grasp better understanding on issues regarding CSR (e.g. Alotaibi