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Board independence and corporate performance: Evidence from Malaysia

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One of the key provisions of the Malaysian Code on Corporate Governance is the requirement for inclusion of outside or independent directors on the board. The recent corporate scandals that have rocked the nation provide evidence of the failure of this provision to prevent these scandals from occurring. Though the Malaysian Code on Corporate Governance has been in place since 2000, it raises the question of the appropriateness of the provision as a bulwark against corporate misdeeds. The code is based on the United Kingdom's experience as set out in the Cadbury Report. Could a code based on the Anglo-Saxon experience suit the need of this country's business environment? This research, thus, addresses empirically, the effectiveness of the provision for outside or independent directors as provided for in the Malaysian Code of Corporate Governance on the governance of Malaysian firms. The analysis was performed by monitoring the changes in corporate performance with the inclusion of these outside directors. The sample for this study comprises of firms listed on Bursa Malaysia (formerly known as Kuala Lumpur Stock Exchange) for the year ending 2006. Results show that there is no convincing evidence that the provisions as outlined in Malaysian Code of Corporate Governance as regards outside directors have any positive effect on corporate performance.

Key words: Independent director, corporate performance, corporate governance, Malaysia.

INTRODUCTION

Much of the analysis into the causes of the Asian financial crisis of July 1997 use a macroeconomic and international finance theoretical approach (Hanazaki and Liu, 2003), citing reasons such as mid-term acceleration of external debt (from the private as well as the public sector), an aggravation tendency among economic fundamentals and panic fund recovery by some investors (Corsetti et al., 1999). Much has also been stated regarding the International Monetary Fund's role in accelerating the crisis by insisting on conditionality involving major structural reform in the midst of the crisis (Hanazaki and Liu, 2003).

However, Johnson et al. (2000) argued that the weaknesses and the failure of corporate governance mechanism in these affected countries should be honoured first as compared to other factors, since the economic and legal environments are important determinants of the extent of confidence of domestic and

foreign investors in a particular country or region. Empirical studies prove the existence of a relation between the state of corporate governance in an economy and the severity of crisis that it suffers (Johnson et al., 2000). This view is also taken by La Porta et al. (2000) who further illustrate that, across countries, corporate governance is an important factor in financial market development and the firm value. Recommendations such as the Treadway Commission (1987) and the Blue Ribbon Committee (1999) in the US, the Cadbury Committee (1992) and Higgs Committee (2003) in the UK and the Vienot Report (1995) in France, provide examples on the importance placed on corporate governance in different countries to protect the shareholder's wealth. Aligned with these efforts and in the wake of the Asian financial crisis, an initiative was started in Malaysia with the establishment of Finance Committee of Corporate Governance in 1998, which then released the Malaysian Code of Corporate Governance in March 2000 with a revised version in 2007, focusing primarily on board of directors, director's remuneration, shareholders and accountability and audit. This effort

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shows the importance placed by the Malaysian government on corporate governance. Though the code serves a guideline for effective corporate governance, the hybrid nature of the code makes it prone to misinterpretations and strategic manipulations. This is due the fact that it involves the use of broad principles that are applied flexibly to the varying circumstances of individual companies (Malaysian Code of Corporate Governance, 2001, 2007). The code states:

“It is not proposed that companies should be required to comply strictly with the prescriptions developed. Each company should have the flexibility to develop its own approach to corporate governance. And while the prescriptions establish a sound approach to corporate governance, companies may develop alternatives that may be just as sound. Nevertheless the prescriptions set the standard that companies must measure up to. Such a rule also ensures that the investment community receives an explanation for the company’s approach to governance so that it is in a position to support the approach or work to influence change”.

Obviously, the code serves only as a guideline to be implemented with the wise discretions of the board members; hence the stance of being an effective measure lies totally on the abilities and judgments of those that make the board. The question is how it is possible for a loosely outlined guideline coupled with the inherent weaknesses in human nature could ensure the integrity of a nation’s corporate governance.

The recent heavily publicized accounting fraud involving Transmile Sdn Bhd, together with the failure of the nation’s big players like Malaysian Airlines System (MAS) and Perusahaan Otomobil Nasional (PROTON) and also the scandals surrounding corporate figures like Tan Sri Halim Saad and Tan Sri Eric Chia, are just a few of the examples that can be attributed to the ineffectiveness of Malaysian Code of Corporate Governance. The argument on the precise nature of ineffectiveness, though yet to be identified, centered mainly on its implementation. However, the exact suitability of this code to Malaysia’s business environment should be studied first. This is because the code was an adaptation of the Hampel report and Cadbury report, which was actually formed based on the corporate governance experience of the United Kingdom to suit its working and living environment. However, the very nature of business being run in these two countries is different, besides the fact that the diversities could also be felt in different aspect like the political, cultural and legal arenas. This view is also supported by Cheung and Chan (2004), who argued that corporate governance is a product of a complex set of cultural, economic and social issues and

that the governance structures of corporations differ from country to country, it is appropriate that corporate governance guidelines and practice codes be designed and adopted by each constituent country. In the end, corporate governance should produce an environment within each country that corporations identify with and can adhere to in their decision making process (Cheung and Chan, 2004). Certainly, this argument seems to be ignored in this country. The inherent flexibility in Malaysian Code of Corporate Governance (2000) makes effectiveness of its requirements highly questionable. Hence, this study was done to determine whether the requirements outlined in Malaysian Code of Corporate Governance (2000) have any significant impact on corporate performance of Malaysian Public Listed Companies. The study is narrowed down to the requirement on board independency and its supporting elements only. Malaysian Code of Corporate Governance (2000) recommends that to be ‘effective’, Independent Non-Executive Directors should make up at least one-third of the board membership. The code further explains that they should be able to bring an independent judgment to bear on the issues of strategy, performance and resources including key appointments and standards of conduct. Clearly, the term ‘effective’ here not only refers to the effectiveness of corporate governance but also to the effectiveness of the strategy, performance and resource managements of a company, which means that the Independent Non-Executive Directors are also held responsible for the firm’s performance. However, due to the flexibility of this code, companies can choose to have at least one third Independent Non Executive Directors as recommended or choose to report on why they did not comply with this requirement.

Therefore, this study was done to answer whether this requirement, which was mentioned earlier, adapted from the Cadbury and Hampel report, could actually benefit Malaysian Public Listed Companies in the long run. Besides that, the research also tries to address whether there are other elements that might bear significant impact on the role played by these Independent Non Executive Directors. However, this research is not going to look into all possible elements, rather only on their diligence and motivation as shown in Figure 1. Thus, the following was hypothesized and tested.

Hypothesis 1

H₀: There is a significant relation between proportion of Independent Non Executive Director and the corporate performance for Malaysian Public Listed Companies.

Hypothesis 2

H₀: There is a significant relationship between the Independent Non Executive Director’s diligence and the

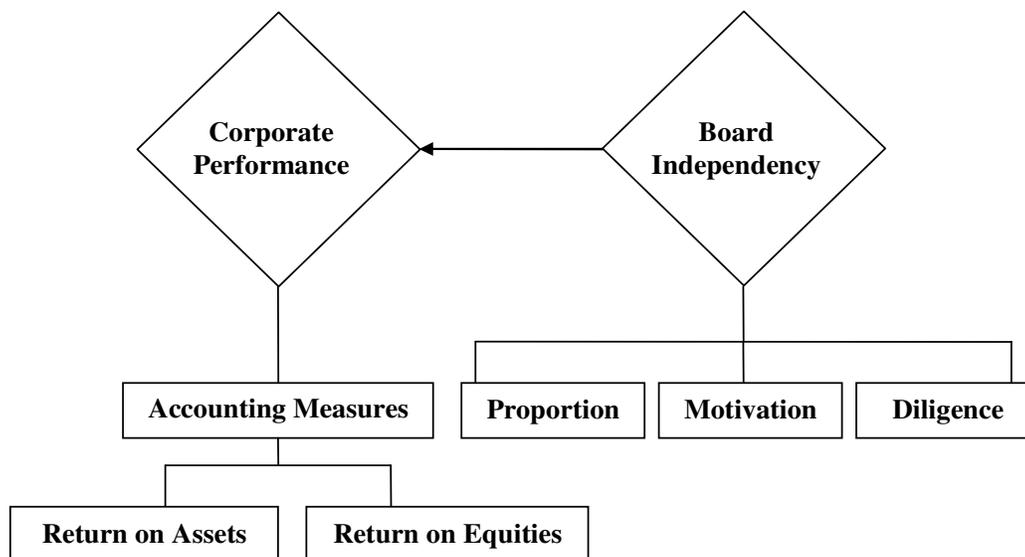


Figure 1. Theoretical framework.

corporate performance for Malaysian Public Listed Companies.

Hypothesis 3

H₀: There is a significant relationship between the Independent Non Executive Director's motivation and the corporate performance for Malaysian Public Listed Companies.

LITERATURE REVIEW

The board of directors has an important role in alleviating the agency costs that arise from the separation of ownership and decision control in corporations (Fama and Jensen, 1983). Short et al. (1999) also took this view and argued that the board of directors is the central corporate governance control mechanism responsible for monitoring the activities of managers, whilst Jensen (1993) describes the board of directors as the apex of the internal control mechanism in an organisation. Therefore, the sole existence of board of directors is to protect the interests of shareholders from where it receives its authority for internal control (Jensen, 1993). However, a board nominated by insiders, clearly would not be able to perform its supervisory functions properly, as personal relations make critical reflections of corporate policy less likely, given the fact that insiders are subordinates of CEO and they are not in a strong position either to monitor or discipline the CEO, (Daily and Dalton, 1993). However, this could be avoided with the adoption of outsiders in the board who could enhance the board's

monitoring power since they do not hold active role in the company except for their directorship which puts them in the best position to judge managerial decisions objectively (Fama, 1980). This view is also supported by Dare (1993), who believes that the outsiders become effective monitors when they question company's strategies and ask awkward questions, while at the same time being able to provide independent judgments to the board.

Furthermore, according to the agency theory a higher proportion of outsiders on a board can better monitor and control the opportunistic behavior of the incumbent management, thus, minimizing the agency problem and maximizing shareholders' wealth (Fama and Jensen, 1983a, 1983b; Jensen and Meckling, 1976). Therefore, boards should have majority outside directors because a higher proportion of outsiders can strengthen a board's independence, provide greater breadth of knowledge and experiences and enhance the effective functioning of the board (Bacon and Brown, 1973; Williams and Shapiro, 1979). This was supported further by Fama and Jensen (1983), who provide the classic theoretical arguments that independent boards are more objective than non-independent boards at monitoring the firm.

However, this literature remained unconvinced that the presence of outsiders on the board could actually contribute to the well being of the company in the long run, since there is no convincingly solid evidences that they do improve the company's performance. Most of the empirical researches report contradicting and inconsistent outcomes. Examples of studies reporting a positive association include Baysinger and Butler (1985), who find weak evidence for the idea that firms with a higher percentage of outsiders on the board in 1970 had a

higher industry-adjusted return on equity in 1980. Schellenger et al. (1989) also show that outside director representation is positively related to return on assets and on risk-adjusted stock returns. A negative association is reported by Agrawal and Knoeber (1996), who find that more outsiders on the board negatively affect Tobin's q-ratio; they conclude that outsiders are added on boards for political reasons and they reduce performance directly or by proxy for the underlying political constraints that led to their board memberships. A further study is provided by Bhagat and Black (2002), who conclude that greater board independence is not correlated with various measures of long-term performance. The mixed empirical findings extend to the strategic management literature as well, where Dalton et al. (1998) provide meta-analyses of 54 empirical studies comprising 159 samples and 40,160 observations and conclude that there is still little evidence of a systematic relation between board composition and financial performance. Similarly, Rhoades et al. (2000) found evidence of a small, positive relation but however they added that the inconsistencies in how directors are defined and the ways performance is measured contribute to the ambiguity of results.

The uncertainties was observed with both the marketing and also the accounting measures of corporate performance as Hermalin and Weisbach (1991, 1998), Mehran (1995), Klein (1998) and Bhagat and Black (2002), all report insignificant relationships between accounting performance measures and the fraction of independent directors on the board, while Hermalin and Weisbach (1991) and Bhagat and Black (2002), again found no linkage between the proportion of outside directors and Tobin's Q, return on assets, asset turnover and stock returns. Meanwhile, Fosberg (1989) also finds no relation between the proportion of outside directors and multiple performance measures like sales, number of employees and return on equity.

Westpal (2002) concluded, that after nearly two decades of research by the corporate governance researchers to study the effect of outside directors on the performance find no convincing evidence that board independence enhances board effectiveness.

Due to the lack of consistent and conclusive evidence, corporate governance researchers turned back their attentions to the core of board process to identify the other elements of the board that can determine or contribute to the role and value of non-executive directors (Weir and Lang, 2001). Vafeas (1999) identified board diligence as an important determinant of the board's effectiveness, while Boumosleh (2007) believes that the extent to which directors perform their monitoring role depends on the incentives they receive. This obviously refers to the diligence and the motivation aspects of outside directors as possible elements that could determine the value of outsiders on the board.

DeZoort et al. (2002) suggest that the frequency of

meetings can be a proxy of diligence. Meetings are considered as important proxies for the time directors spend monitoring managerial performance (Vafeas, 1999) and also as an important resource in improving the effectiveness of a board (Coger et al., 1998; Lipton and Lorsch, 1992). Moreover, when boards hold regular meetings, they are more likely to remain informed and knowledgeable about relevant performance of the company leading them to take or influence and direct the appropriate action to address the issue (Blue Ribbon Committee, 1999; Abbott et al., 2003). This view is further supported by Adams (2000) and Vafeas (1999), who suggested that the number of board meetings is actually a very good proxy for the directors' monitoring effort.

Similarly, this literature is faced with unconvincing and inconsistent evidence in regards to the relationship between board meetings and the performance of a firm. Vafeas (1999) finds a negative correlation between the number of board meeting and performance, which means that boards that meet more frequently are, valued less by the market. Vafeas (1999) note that this due to the notion that an increase in board meetings actually is due to poor performance, confirming with Jensen (1993) suggestion that meetings were a reactive response and not a proactive measure. However, Vafeas (1999) also find that boards meet more frequently after crises and thus improving the company's performance. Karamanou and Vafeas (2005) also examine the impact of board meetings on management earnings forecasts and find weak evidence of a positive relationship. This view is also taken by Menon and Williams (1994), who argued that number of meetings is only a rough proxy for activity since it does not provide any indication of the work accomplished during these meetings.

Next, in regards to independent directors' remuneration, a direct relationship is expected between the pay and the corporate performance since the independent directors are also an instrument of the shareholders. This view supported by a number of studies, using different performance measures, which found significant, positive relationship between pay and performance. For example, Ciscel and Carroll (1980) using changes in performance and changes in pay, Main et al. (1995) using accounting measures, Conyon and Leech (1994) and Main et al. (1996) using share price analysis and Jensen and Murphy (1990) using both approaches all found a weak, positive link between performance and executive pay. Harford (2003) on the other hand uses a sample of hostile target firms over the period 1988 and 1991 and finds that directors' financial compensation is relatively small and unlikely to affect board decisions. Meanwhile Hermalin and Weisbach (1998), suggest that the equity-based compensation is a mechanism that aligns directors' interests with shareholder's shareholders' and can motivate directors to increase monitoring. In other words, directors' equity-based compensation leads to more independent boards.

However, Fama and Jensen (1983) argued that directors' major motivation is their interest in reputation building and that this incentive is better achieved when director compensation is small. Harford (2003) provides evidence supporting Fama and Jensen's argument.

Clearly, it is hard to determine the exact nature of outsiders' role in a corporate board with all the unconvincing and contradicting evidences from past studies. These studies also fail to highlight the internal elements that could actually influence the contributions of outside directors towards corporate performance. Evidence in regards to their involvement in board meeting together with the compensation paid to them, are also inconclusive. One reason for these uncertainties could be attributed, as argued by Shleifer and Vishny (1997) and Gibson (2003) to the differences inherent in the economic conditions and institutional influences, such as variations in capital markets, political and legal systems that may influence agency costs arising from different ownership structures, thus the effect of corporate governance structures may also be different (Haniffa and Hudaib, 2006).

RESEARCH METHODOLOGY

Selection of measures

Corporate performance

The dependent variable – corporate performance was measured using two accounting proxies: Return on Assets (ROA) and Return on Equities (ROE). As an accounting measure of performance, these two proxies are commonly employed and generally accepted by the corporate governance researchers, though some researcher prefers to use the market measures. The two measures, which represent different perspectives of how to evaluate a firm's financial performance, have different theoretical implications (Hillman and Keim, 2001) and each is subject to particular biases (McGuire et al., 1986). Although accounting measures of performance have been criticized in the past, they have recently been defended on a number of grounds (Bromily, 1986; Jacobson, 1987; Long and Ravenscraft, 1984). These variables are considered robust measures of performance by a number of scholars (Bettis, 1981; Bass et al., 1978). Hence, this research would also be employing the accounting measures of performance to test all the hypotheses. Return on Assets was calculated as the ratio of net income to the book value of assets, while Return on Equities was calculated as net income divided by book value of equity.

Board independence

The independency of the board was measured through three proxies - the proportion, motivation and diligence of Independent Non Executive Directors.

Proportion of Independent Non Executive Directors was measured as the overall percentage of Independent Non Executive Directors on the board to the board size, while the diligence was measured as the average participations of Independent Non Executive Directors in annual meetings. The proportion on Independent Non Executive Directors was grouped into two categories. The first one for companies that have less than the recommended requirement of at least one third of Independent Non

Executive Directors while the second group for companies that did not comply with this requirement. Meanwhile, the diligence proxy was categorized into three subgroups. Companies that have at least two third average participations of Independent Non Executive Directors in board meeting as 'High' and those with less than one third as 'Low' while the rest as 'Medium'. Finally, the third proxy, motivation, was measured as the average compensation or monetary fees, including salaries and bonuses paid to Independent Non Executive Directors in a year.

Control variables

Besides the three main proxies of board independency, this study also focused on other elements of a board that could bring significant impacts on firm performance like board size, frequency of board meetings and the industry in which the company was involved. Prior studies have suggested that the size of a board is an important element contributing towards board effectiveness (Jensen, 1993; Yermack, 2004; Dalton et al., 1998). Besides that, empirical studies also have shown that the size of the board is positively linked with the firm's performance (Karamanou and Vafeas, 2005; Haniffa and Hudaib, 2006). Another important element considered was the frequency of board meetings conducted in a year. Though the result from prior studies is inconclusive, the board meeting time is deemed as important resource in pushing a company for an improved performance (Lipton and Lorsch, 1992). Furthermore, according to Vafeas (1999), the frequency of board meetings is a proxy for the time directors spend monitoring managerial performance. The last element considered was the industries in which the companies were involved. Prior studies have indicated that the industry sector is also a significant determinant of a firm's performance (Short et al., 1999).

Sampling design

The sample was derived from Kuala Lumpur Stock Exchange for the year 2006, with the unit of analysis being the Malaysian Public Listed Companies. A total of 115 companies were sampled covering more than eight different industries from the three main boards of Kuala Lumpur Stock Exchange – the First Board, Second Board and MESDAQ. The sampling was done on a probability basis using the simple random sampling method.

Data analysis techniques

The statistical analysis was performed using the statistical software, SPSS version 15.0. First, a descriptive analysis was performed to observe the board characteristics of the sample. Then, a normality test was performed to determine that the dependent variables were normally distributed. Kolmogorov-Smirnov normality test was chosen as the appropriate test since the size of sample was larger than 50. Next, a reliability test was performed to determine internal consistency of the corporate performance measure. The consistency of this measure need to be determined first, before any further analysis could be performed, since both of the proxies was manually derived and computed from multiple secondary sources. It was predetermined that the measure will only be accepted if the resulting Cronbach Alpha coefficient is more than 0.60, the threshold recommended by Nunnally (1967) for exploratory research. This was followed with a bivariate correlation analysis to avoid the issue of multicollinearity.

Finally, all the three main hypotheses were tested by comparing their respective means. The first hypotheses were tested through Independent Sample t-Test because of the nominal nature of the

independent variable and also because the independent variable had only two levels, that is, "At Least One Third" and "Less than One Third". The second and third hypotheses were tested through multiple One-way ANOVAs. The supporting three hypotheses were also tested using multiple One-way ANOVAs.

RESEARCH FINDINGS

Characteristics of the sample

The sample was derived randomly on a probability basis from the Kuala Lumpur Stock Exchange. Tables 1-7 show the characteristics of the sample. It can be observed from Table 1 that the majority of the sample was represented by companies listed in the First Board with 57.4%, followed by those in Second Board with 31.3%, while the rest at 11.3% in MESDAQ.

The sample was derived from more than eight different industries. The industries were classified as Construction, Consumers Products, Finance, Industrial Products, Plantation, Properties, Trading and Services and Technology. The rest of the minor industries were group together as 'Others'. It can be observed from Table 2 that companies involved in producing industrial products makes up the bulk of the sample at 29.6%, followed at a far distant by companies specializing in consumer products at 15.7%. Third in the hierarchy, resting at 13.9% were the companies whose major business revolved around properties. Following next, with an exact identical representation, were the companies focused on technology and, on the trading and services industry, with 11.3% each, while companies from the plantation, construction and finance industries occupying the lower part of the distribution with the plantation were occupying 5.2%, while construction and finance industries each occupying 4.3%. The rest of the sample, at 5.2% was represented by 'Others'.

An important component of the board's characteristic is board size. The maximum observed size was fourteen while the minimum was four, with an average size of 7.15. As shown in Table 3, the majority of the companies, at 46.1% had a board of size between 4 to 6, followed closely by board of size between 7 to 9 at 40.9%, with a minority of 10.4% had board of size between 10 to 12 while the remaining 2.6% of the companies had board of size between 13 to 15.

In regards to the proportions of Independent Non Executive Directors, it can be seen from Table 4 that a huge majority, at 80% complied with the requirement set by Malaysian Code of Corporate Governance, by having at least one third Independent Non Executive Directors on their boards. The average representation of Independent Non Executive Directors on the board was 40%, with minimum representation being 16.67% and maximum being 75%.

Most companies were seen having between three to six meetings in a year. It can be seen from Table 5 that 51.3% of companies sampled, conducted between five to

six meetings per year and 36.5% of them having between three to four meetings per year. Only 3.5% had one to two meetings in a year with another 2.6% had nine to ten meetings, while the rest, at 6.1% had seven to eight meetings per year.

In regards with the Independent Non Executive Directors' participations in the meetings, it can be seen from Table 6 that almost all of them, at 91.3% show high level of participation. Only 6.1% of these companies had medium participations, while the rest, a small minority, at 4.3% had low participations by their Independent Non Executive Directors in all meetings conducted in the year 2006.

Based on the five predefined remuneration ranges, it can be seen from Table 7 that majority of the Independent Non Executive Directors, at 74% were being paid an average remuneration fees of RM50, 000 and below. A detailed breakdown showed that the majority of 38.3% were getting paid between RM25, 001 to RM50, 000 per annum while another 35.7% were getting paid between RM25, 000 and below. Another 12.2% of the companies were paying between RM50, 001 to RM75, 000 per annum and a small portion, at 6.1% were paid a huge sum between RM75, 001 to RM100, 000 per annum. The rest of the companies were having really good remunerations packages – which exceeded RM100, 000 per annum. 9.6% of the companies sampled were seen providing this luxury.

Analysis of measures

Normality test

The Kolmogorov-Smirnov normality test (Table 8) revealed that both corporate performance measures were not normally distributed with the significant values for both Return on Assets and Return on Equities were less than 0.05. In general, significant values less than 0.05 is considered as good evidence that the data set is not normally distributed.

Since both of the measures were slightly skewed, a logarithmic (base 10) transformation was performed:

$$\begin{aligned} \text{Return on Assets} &= \text{Log}_{10} (\text{Return on Assets}); \\ \text{Return on Equities} &= \text{Log}_{10} (\text{Return on Equities}); \end{aligned}$$

Another normality test (Table 9) revealed that the transformed measures both produced normal distributions with significant values well above 0.50. (Return on Assets $p=0.200$; Return on Equities $p=0.200$).

Furthermore, the values for the skewness and kurtosis were both within the permitted range of below two. This provides more concrete evidence that the transformed values were normally distributed.

Consistency assessment

Next, it was observed the Cronbach Alpha coefficient for

Table 1. Characteristics of the sample: Board listings.

| Board | Frequency | Percent |
|--------------|-----------|---------|
| First board | 66 | 57.4 |
| Second board | 36 | 31.3 |
| MESDAQ | 13 | 11.3 |
| Total | 115 | 100.0 |

Table 2. Characteristics of the sample: Industries.

| Industries | Frequency | Percent |
|----------------------|-----------|---------|
| Construction | 5 | 4.3 |
| Consumer products | 18 | 15.7 |
| Finance | 5 | 4.3 |
| Industrial products | 34 | 29.6 |
| Plantation | 6 | 5.2 |
| Properties | 16 | 13.9 |
| Trading and Services | 13 | 11.3 |
| Technology | 13 | 11.3 |
| Others | 5 | 4.3 |
| Total | 115 | 100.0 |

Table 3. Characteristics of the sample: Size of boards.

| Size of the boards | Frequency | Percent |
|--------------------|-----------|---------|
| 13 - 15 | 3 | 2.6 |
| 10 - 12 | 12 | 10.4 |
| 7 - 9 | 47 | 40.9 |
| 4 - 6 | 53 | 46.1 |
| 1 - 3 | 0 | 0 |
| Total | 115 | 100.0 |

Table 4. Characteristics of the sample: Proportion of independent non executive directors.

| Proportion of independent non executive directors | Frequency | Percent |
|---|-----------|---------|
| At least one third | 92 | 80.0 |
| Less than one third | 23 | 20.0 |
| Total | 115 | 100.0 |

the reliability test was 0.923 (Table 10), well above the threshold recommended by Nunnally (1967) for exploratory research at 0.60. The result indicated that the accounting measures of corporate performance calculated from the sample, was consistent and reliable.

Correlation analysis and multicollinearity

It was also observed (Table 11) from the bivariate

Table 5. Characteristics of the sample: Frequency of board meetings.

| Frequency of board meetings | Frequency | Percent |
|-----------------------------|-----------|---------|
| 1 - 2 | 4 | 3.5 |
| 3 - 4 | 42 | 36.5 |
| 5 - 6 | 59 | 51.3 |
| 7 - 8 | 7 | 6.1 |
| 9 - 10 | 3 | 2.6 |
| Total | 115 | 100.0 |

Table 6. Characteristics of the sample: Participation of independent non executive directors in board meetings.

| Participation of independent non executive directors in board meetings | Frequency | Percent |
|--|-----------|---------|
| Low | 3 | 2.6 |
| Medium | 7 | 6.1 |
| High | 105 | 91.3 |
| Total | 115 | 100 |

Table 7. Characteristics of the sample: Remuneration paid to the independent non executive directors.

| Remuneration | Frequency | Percent |
|--------------------------|-----------|---------|
| RM 1 - RM 25, 000 | 41 | 35.7 |
| RM 25, 001 - RM 50, 000 | 44 | 38.3 |
| RM 50, 001 - RM 75, 000 | 14 | 12.2 |
| RM 75, 001 - RM 100, 000 | 7 | 6.1 |
| More than RM 100, 001 | 9 | 7.8 |
| Total | 115 | 100 |

correlation analysis that these two variables of corporate performance were highly correlated. The observed significant value was less than 0.001 with the Pearson correlation coefficient at 0.858. The positive value of the coefficient indicates that a direct or positive relationship exist between these variables. However, the high coefficient value, at 0.858, which is almost close towards the perfect 1, implied that each of the variables explains the other very well, means there exist a multicollinearity between the dependent variables, hence it is adequate if either one of them was utilized in the proceeding analysis. Therefore, the remaining statistical analysis was performed using only Return on Equities as the dependent variable. Return on Equities was chosen randomly to avoid any bias.

Testing of hypotheses

The first hypothesis states that there is no significant relationship between the proportion of independent non

Table 8. Tests of normality.

| Returns | Kolmogorov-Smirnov(a) | | | Shapiro-Wilk | | |
|--------------------|-----------------------|-----|------|--------------|-----|------|
| | Statistic | df | Sig. | Statistic | df | Sig. |
| Return on assets | .188 | 115 | .000 | .740 | 115 | .000 |
| Return on equities | .205 | 115 | .000 | .709 | 115 | .000 |

a, Lilliefors significance correction.

Table 9. Tests of normality after logarithmic transformation.

| Returns | Kolmogorov-Smirnov(a) | | | Shapiro-Wilk | | |
|--------------------|-----------------------|-----|---------|--------------|-----|------|
| | Statistic | df | Sig. | Statistic | df | Sig. |
| Return on assets | .067 | 110 | .200(*) | .992 | 110 | .746 |
| Return on equities | .062 | 111 | .200(*) | .984 | 111 | .226 |

*, This is a lower bound of the true significance.

a, Lilliefors significance correction.

Table 10. Reliability statistics.

| Cronbach's Alpha | No. of Items |
|------------------|--------------|
| .923 | 2 |

executive directors and corporate performance for Malaysian Public Listed Companies.

The hypothesis was tested using independent sample t-test, with the confidence level at 95%. Independent sample t-test makes the assumption that the mean value for two independent group will be statistically different. Table 12 shows the result of the independent sample t-test conducted, with the corporate performance measure – Return on Equities as the dependent variables while the proportion of Independent Non Executive Directors being the independent variable.

The test reveals that the homogeneity of variance assumption had been violated, hence the t-test with equal variances not assumed were taken for further interpretation. The observed significant values was more than the accepted alpha value at 0.05 ($p = 0.166$), thus preventing the null hypothesis to be rejected and concluded that there is no relationship between the proportion of Independent Non Executive Directors and corporate performance of Malaysian Public Listed Companies.

The result of the One-way ANOVA revealed (Table 13) that the observed significant value was again more than accepted alpha value of 0.05; $F(2,108) = 0.200$; $p = 0.819$, thus again prevented the null hypothesis to be rejected and concluded that there is no significant relation between the Independent Non Executive Directors' diligence and corporate performance for Malaysian Public Listed Companies.

The result of the second One-way ANOVA reveal (Table 14) an almost identical result with the significant value again more than the accepted alpha value of 0.05; $F(4,106) = 1.547$; $p = 0.194$.

This result indicated that there is again no relationship between the Independent Non Executive Directors' motivation and the corporate performance of Malaysian Public Listed Companies.

Other findings

The result from other analysis revealed (Table 15) that there was no relationship between board size and the frequencies of meetings conducted and corporate performance of Malaysian Public Listed Companies.

However, it was observed through One-way ANOVA that there is a significant relationship between the industries in which the companies were involved and their performance. ($F(8,102) = 2.286$; $p = 0.027$);

Summary of findings

Malaysian Code of Corporate Governance (2000) emphasized on the importance of outsider on the board to bring an independent judgment to the board and to enhance its effectiveness. However, the findings from this study revealed that the number of outsider did not bring any sort improvement towards the performance of a firm. Similarly, the size of board also did not play any significant role in improving the performance of the company.

It was also observed that the diligence of the Independent Non Executive Directors seems insignificant to the well being of the firm. There participations of the board meetings were not empirically related towards the

Table 11. Correlation analysis between the dependent variables.

| | | Return on equities | Return on assets |
|--------------------|---------------------|--------------------|------------------|
| Return on equities | Pearson correlation | 1 | .858(**) |
| | Sig. (2-tailed) | | .000 |
| | N | 111 | 108 |
| Return on assets | Pearson correlation | .858(**) | 1 |
| | Sig. (2-tailed) | .000 | |
| | N | 108 | 110 |

** Correlation is significant at the 0.01 level (2-tailed).

Table 12. Independent samples t-test's output for the testing of the first hypothesis.

| | | Levene's test for equality of variances | | t-test for equality of means | | | | | | | |
|--------------------|-----------------------------|---|------|------------------------------|--------|-----------------|-----------------|-----------------------|---|--------|-------|
| | | F | Sig. | t | df | Sig. (2-tailed) | Mean difference | Std. error difference | 95% confidence interval of the difference | | |
| | | | | | | | | | | Lower | Upper |
| Return on equities | Equal variances assumed | 1.250 | .266 | -1.252 | 109 | .213 | -.13958 | .11148 | -.36052 | .08137 | |
| | Equal variances not assumed | | | -1.410 | 41.060 | .166 | -.13958 | .09897 | -.33945 | .06030 | |

Table 13. One-way ANOVA's output for the testing of the second hypothesis.

| Return on equities | | | | | |
|--------------------|----------------|-----|-------------|------|------|
| | Sum of squares | df | Mean square | F | Sig. |
| Between groups | .093 | 2 | .046 | .200 | .819 |
| Within groups | 24.962 | 108 | .231 | | |
| Total | 25.055 | 110 | | | |

Table 14. One-way ANOVA's output for the testing of the third hypothesis.

| Return on equities | | | | | |
|--------------------|----------------|-----|-------------|-------|------|
| | Sum of squares | df | Mean square | F | Sig. |
| Between groups | 1.382 | 4 | .345 | 1.547 | .194 |
| Within groups | 23.673 | 106 | .223 | | |
| Total | 25.055 | 110 | | | |

Table 15. Summary of other findings.

| Null hypothesis | One-way ANOVA |
|--|---|
| There is a significant relationship between the board size and corporate performance. | Return on equities: F(3,107)=0.306;p=0.821; Failed to reject the null hypothesis. |
| There is a significant relationship between the industry and corporate performance. | Return on equities: F(8,102)=2.286;p=0.027; Rejected the null hypothesis. |
| There is a significant relationship between the frequency of board meetings and corporate performance. | Return on equities: F(4,106)=2.047;p=0.093; Failed to reject the null hypothesis. |

corporate performance. Besides that, the frequency of board meetings also seems to be insignificant towards corporate performance. The same was observed with the compensation or the remuneration paid to these Independent Non Executive Directors. Surprisingly they were not extrinsically motivated by the remuneration paid by the companies.

However, it was observed that the industries in which the companies were involved seemed to have an impact on their corporate performance. This could be due to the fact that the performance could be influenced by the sensitivity of certain industries to macroeconomic, as well as to political factors.

LIMITATIONS AND SUGGESTIONS

The study was focused on a single financial year. The outcome could be biased by the annual economical fluctuation and also by the influence of the legal and political environment surrounding the nation at the time of study. A more accurate and precise result could be obtained if the sample were driven from multiple financial years since this would reflect the performance of a listed company over a period time and be independent of external factor.

The sheer number and presence of Independent Non-Executive Directors could not be used to determine their contributions towards the well being of an organization. There are other factors, in regards to Independent Non Executive Directors, which might have impacted their contributions. The research should have focused also on related factors such as qualifications, previous work experience and age and work tenure.

The study also did not address the role played by the Independent Non Executive Directors in audit and remuneration committee. The research had been narrowed down only to the role they played in the board meetings. The result from this research could be attributed to the fact that maybe the Independent Non Executive Directors role are more into governance perspective, rather into corporate strategy planning or the allocation of resources. Future studies, if taken, should address in depth the role played by them in relevant committee.

Besides that, the research was also focused on only accounting measures of performance. However, the accounting measures capture only historical aspects of firm performance (McGuire et al., 1986) and they are subject to bias from managerial manipulation and differences in accounting procedures (Branch, 1983; Brillloff, 1972). Market measures on the other hand are forward looking and focus on market performance. They are less susceptible to different accounting procedures and represent the investor's evaluation of the ability of a firm to generate future economic earnings (McGuire et al., 1988).

Conclusion

The Cadbury Report and the Hampel Report were developed based on experience in United Kingdom. It was designed to suit the political, economical and cultural needs of this country. The rationale beyond the decision to adapt these reports into Malaysian Code of Corporate Governance (2000) seems totally unjustifiable. The recommendation and the requirements, at least on matters related to board compositions, board meetings, the role of outsiders and the remuneration packages seemed not to benefit Malaysian Public Listed Companies. Though it is hard to identify the exact reason for this, one obvious issue need to be addressed now, is that the code need to be revised again by taking into consideration the external factors influencing or affecting our companies, which includes the political, economic and cultural factors in Malaysia. A code developed for an Anglo-Saxon business model definitely would not suit the Asian business model.

The hybrid nature of the code also needs to be addressed. Flexibility of corporate guidelines means the door has already been open for manipulations. This is evident with the recent outbreak of corporate scandals.

In a time where the world is rocked by corporate scandals, there exists a need for the government to play a more crucial role in preventing the reoccurrence of these scandals. Government needs to provide much more stringent guidelines while ensuring the enforcement is closely monitored. Existence of a code without proper implementations will definitely prove to be futile. The current scenarios show that enforcements only take place when a new scandal is discovered.

Malaysian Code of Corporate Governance (2000) has been in place since the year 2000. However, it is quite clear that there are a lot of loopholes in term of its guidelines and also in its implementation. The responsibility now is solely on the shoulders of the government to ensure effective corporate governance is maintained throughout the nation, for as far as businesses are concerned, though many like deny it, the main priority is to maximize profit with ethical codes taking a back seat.

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