INTERNATIONAL JOURNAL OF BUSINESS AND MANAGEMENT STUDIES
Vol 5, No 2, 2013 ISSN: 1309-8047 (Online)

THE RELATIONSHIP BETWEEN CORPORATE GOVERNANCE AND TRANSPARENCY & DISCLOSURES IN STATE OWNED ENTERPRISES (SOEs): LITERATURE REVIEW

Sally Sayyed Hussien Ahmed

Accounting Department/American University in Cairo (AUC)

E-mail: sallyhussien@aucegypt.edu

Reem Sayyed Hussien Ahmed

Sadat Academy for Management Sciences (SAMS)

E-mail: reem.sayyed.hussien@gmail.com

─Abstract ─

This research aims to determine the relationship between Corporate Governance **(CG)** and Transparency & Disclosures **(T&D)** in State Owned Enterprises **(SOEs)**. Investigating this relationship is necessary as SOEs and Public-Private Joint ventures are continually increasing and they are facing many challenges which are different in nature from totally public or totally private sectors. In addition, they differ in many aspects like T&D requirements, and how they react to their societies. Enhancing T&D environment will lead to more positive impacts on societies. Moreover, assessing the adoption of the latest standards such as International Financial Reporting Standards **(IFRS)**, its impact on T&D environment focusing on SOEs is covered. To achieve the aim of this research, prior literature review is discussed in order to make the relationship between CG and T&D more understandable. The last section of the research offers some conclusions and recommendations.

Key Words: Corporate Governance (CG), Transparency & Disclosures (T&D), State Owned Enterprises (SOEs), International Financial Reporting Standards (IFRS)

JEL Classification: G34, H70, G32, M40, M41

1. INTRODUCTION

Due to globalization many developing countries face many challenges to build their competitive advantages in order to be able to participate in international trade and foreign investment so, the need for strong Corporate Governance (**CG**) is apparent. Moreover, the need to make harmonization between rules and standards (to make it easily to prepare unified financial statements) is necessary because different standards between countries make it more difficult to compare company's financial statements with its rivals. Therefore, the International Financial Reporting Standards (**IFRS**) were released. Accordingly, there must be strong CG system to guarantee the adoption of these international standards. To strengthen the country's economy, ensure its progress and make it capable of competing globally. Also, due to the increasing number of financial crisis and scandals a global awareness of the importance of CG is increasing. (Mousa, 2012)

This research examines the State-Owned Enterprises (**SOEs**) sector that can be defined as an entity which is created by the government in order to participate in commercial activities and one of its goals is to compete with the private sector. Conflicting interests exist between managers, employees and the state due to different objectives of the stakeholders in SOEs. Therefore, one fundamental issue that needs to be addressed here is the credibility and transparency of this sector as by enhancing T&D environment it will lead to more positive impacts on the society.

1.1. Research problem

SOEs face many challenges that are different in nature from totally public or totally private sectors. Simply state's objectives may differ from private sector objectives. Moreover, they differ in many aspects like the T&D requirements and how they react to the society as a whole (OECD, 2012). Therefore, the research problem can be summarized in the need for understanding the role of CG in enhancing T&D environment in SOEs.

1.2. Research importance

This research is very important for firms, investors, state and society as a whole to assure a transparent business environment.

1.3. Research objectives

This research aims to examine the relationship between CG and T&D in SOEs. This could be accomplished by the following sub-objectives:

- Discussing the difference between T&D and their relationship with CG.

- Exploring the literature review of CG and T&D in different countries to reach the research gap.

2. TRANSPARENCY AND DISCLOSURE (T&D)

Corporate T&D practices are a special issue of CG; they are considered the main pillars of CG quality (Mousa, 2012). CG is a dialogue between companies and their stakeholders with the purpose of paving the way for understanding the company's strategic and operational goals, and ways for achieving those goals (Parum, 2005 cited by Mousa, 2012). Moreover, companies are required to offer channels for disseminating information that will enable users to get relevant information equally, timely, and with an efficient cost (OECD, 2004).

2.1. Disclosure

There is no strict definition of disclosure but generally speaking it can be defined as a "display of important information to investors, creditors, and others in a way that allows the prediction of the company's ability to achieve profits in the future and to pay off their liabilities or obligations." (Mohamed, 2012)

It can be classified according to the degree of obligation to:
2.1.1. *Mandatory disclosure:* refers to the accounting information that must be disclosed to investors when preparing the financial statements.
2.1.2. *Voluntary disclosure:* refers to the self-disclosure of company's information to investors, without a legal requirement. (Mohamed B. H., 2012)

2.2. Transparency

Transparency can be defined as, "sharing information and acting in an open manner and transparency allows stakeholders to gather information that may be critical in detecting and defending their interests." (Burch Adiloglu, 2012)**.** It differs from disclosure in going beyond following the standards of reporting to provide users with all the information needed to help them taking rational investment decisions.

2.3. Difference between T&D

In summary, Disclosure is a legal obligation, while Transparency is an ethical obligation (Steve Lee, 2011). Consequently Both T&D keep corporate stakeholders better informed about the way a company being managed, governed. (Burch Adiloglu, 2012)

3. LITERATURE REVIEW

The literature related to this research can be divided into 3 categories:

- Studies on the relationship between CG and T&D
- Studies on IFRS and its impact on the firm performance
- Studies on the role of CG in SOEs

3.1. Studies on the relationship between CG and T&D

Table 1

Author(s), year	**Objectives**	**Methodology**	**Findings**
Teresa Conover and Khaled Dahawy, (2007)	The study measured the degree of compliance with International Accounting Standards (**IAS**) required disclosures. Furthermore, compared empirically the degree of compliance of each company and located some of the special characteristics that might relate to companies with different degrees of compliance.	The methodology of the study was based on a disclosure checklist created by the Capital Market Authority (**CMA**) to measure the degree of compliance of the most active companies in the Egyptian stock market with the required disclosures.	The findings can be divided as follows: Theoretically, the study documented that IAS were in some parts inconsistent with Egypt culture. Practically, the results showed also that the average compliance rate was 61% which indicated that these companies did not comply with the requirements of disclosures as mandated by the CMA, based on international standards. Also, the compliance with IAS was selective in Egypt.
Laksmana, (2007)	The study examined whether certain board and compensation committee characteristics were associated with the extent of board disclosure.	The methodology of the study was based on a sample of six major industries. To measure the extent of board disclosure, a database of disclosure index based on information reported in compensation committee reports was	The results indicated: First, boards with the ability to exercise independent judgment would make decisions that are in the best interests of shareholders when having disagreements with management. Second, the study suggested that firms needed to consider limiting Chief Executive Officer **(CEO)** influence in

		constructed.	shaping board/committee meeting agendas to obtain stronger boards that would perform their monitoring duties more effectively.
Nick Lin-Hi, (2011)	The study constructed a theoretical framework that captured the relationship between CG and global one. This framework identified an interaction between corporate and global governance that allowed corporations to bring good CG to life.	British Petroleum **(BP)** case was investigated to show a real disaster in the oil and gas industry.	The findings indicated that the main problem of adapting the rules of CG was concentrating on the short-term benefits "quick-wins" instead of long-term benefits like sustainability. It suggested increasing managers' compensations and bonuses as, it might be beneficial to the organization as a whole and don't allow them to make dysfunctional decisions that harm the organization, environment and society.
Khaled Samaha, (2012)	The study examined the impact of a comprehensive set of CG attributes (board composition, board size, CEO duality, director ownership, blockholder ownership and the existence of audit committee) on the extent of CG disclosure in Egypt.	The measurement of the study was based on published data created from a checklist developed by the United Nations, which was gathered from a manual review of financial statements and websites of a sample of Egyptian companies listed on Egyptian Stock Exchange (**EGX**).	The findings indicated that the extent of CG disclosure was lower for companies with duality in position and higher ownership concentration as measured by blockholder ownership. Also, increased with the proportion of independent directors on the board and firm size.

Prior studies related to the relationship between (**CG**) and (**T&D**) examined the impact of some CG mechanisms on the extent of disclosures. Some of them indicated that there was a positive relationship between some of CG mechanisms and the extent of disclosures (e.g. board independence, board size, internal audit department). On the other hand, some studies showed contradict results.

3.2. Studies on IFRS and its impact on the firm performance

Table 2

Author(s), year	**Objectives**	**Methodology**	**Findings**
Pamela Kent, (2008)	The study investigated the association between the level of disclosure and CG quality.	The methodology of the study was based on a sample of all Australian public companies (1000) listed on the Australian Stock Exchange **(ASX)**.	The results indicated that the quantity of disclosure was positively related to some aspects of superior CG, such as the frequency of board and audit committee meetings and the choice of auditor.
Kholeif, (2008)	The study examined the symbolic use of IFRS in an Egyptian state-owned company that was partially privatized by drawing on new institutional sociology and its extensions.	The methodology of the study was based on using an intensive case study. Data were collected from multiple sources, including unstructured and semi-structured interviews, direct and participative observations, discussions and documentary analysis.	The findings revealed that the company faced conflicting institutional demands from outside. To meet these conflicting institutional demands, the company adopted loosely coupled accounting rules, routines, and Information Technology **(IT).**
Yip, (2012)	The study examined whether the mandatory adoption of IFRS in the European Union **(EU)** significantly improved information comparability in 17 European countries.	The methodology of the study was based on three proxies: The similarity of accounting functions that translate economic events into accounting data, the degree of information transfer, and the similarity of the information content of earnings and of the book value of equity- to measure information comparability.	The findings were consistent with the view that mandatory IFRS adoption improved information comparability across countries. However, it addressed that the mandatory IFRS adoption was not sufficient to achieve a full enhancement in comparability in the EU. Further it indicated that comparability improvement was more likely to occur among firms from similar institutional environments than among firms from different institutional environments.

Previous studies related to the adoption of IFRS and its impact on the firm performance revealed that the IFRS adoption increased the comparability of financial statements but there were some obstacles for the right adoption accordingly, companies adopt loosely coupled accounting rules.

3.3. Studies on the role of CG in SOEs

Table 1

Author(s), year	**Objectives**	**Methodology**	**Findings**
Cornett, et. al, (2005)	The study examined performance differences between privately-owned and state-owned banks by employing cash flow and accounting based measures of performance.	The methodology of the study based on banks in 16 East countries from 1989 through 1998.	The findings indicated that state-owned banks generally operated less profitably, efficiently than privately-owned banks over this period. Also, performance differences were significant in those countries where government involvement in the banking system was the greatest. Differences in CG, managers' incentives, and objectives were offered as explanations for the results.
Musa Mangena, (2007)	The study investigated the association of foreign share ownership with firm-level disclosure and CG structures in Zimbabwe. In addition, it examined the effect of disclosure and CG on foreign share ownership.	The methodology of the study was based on data drawn from companies listed on the Zimbabwe Stock Exchange.	The results indicated that disclosure, proportion of non-executive directors, institutional share ownership and audit committee independence were all positively and significantly associated with foreign share ownership. These results were consistent with the notion that foreign investors had a preference for companies with effective CG structures and less information asymmetry.
Bremer, (2012)	The study examined a part of the SOE sector which is public-private joint ventures in Egypt and Middle East and	The database was based on corporate websites for a sample of 12 holding companies	The findings indicated that firms with a higher share of public ownership and those listed on the stock exchange were more likely to score well on both measures of

	North Africa region (**MENA**). It focused on T&D practices.	and 100 public-private joint ventures.	disclosure; that was, on having a website and on providing comparatively complete disclosure.

Most previous studies related to the role of CG in SOEs and Private-Public JVs addressed many differences among countries in governing the SOEs. Also, in some countries state or government ownership whether partially or totally had positive impacts on the performance of companies while in other countries it had negative impacts.

4. SUMMARY AND CONCLUSIONS

CG has been examined in many studies all over the world. The role of CG in enhancing company's performance is increasingly important. T&D are considered the main components of CG. It can be argued that T&D helps in strengthening and increasing the effectiveness of CG. Most of studies examined the relationship between CG and T&D. Some of them indicated that there was a positive relationship between some of CG mechanisms and the extent of disclosures. Consequently, they can lead to more transparent environment while others can be misused and mislead the investors.

In addition, studies on IFRS are rapidly increasing. Prior studies related to IFRS revealed that its adoption in some countries increased the comparability of financial statements but the case was different in other countries. Also, there were some barriers for its successful adoption especially in the developing countries. Finally, after the investigation of the literature review, it can be concluded that there is a shortage in studies that handled the CG mechanisms and its role in enhancing T&D in SOEs. The efforts that were exerted to ensure and enhance the T&D environment cannot be neglected. However, they were insufficient regarding SOEs in developing countries like Egypt and other Middle East countries.

5. RECOMMENDATIONS

- Government should increase companies' awareness of T&D and their positive impacts on the financial performance and on the society as a whole.
- State should participate in a lot of projects that will make it capable of competing with the private sector more effectively.
- Appropriate guidelines and regulations should be developed for SOEs and other types of joint ventures due to their mixed objectives.

6. FUTURE RESEARCH

Investigating the role of CG in SOEs in developing countries empirically would be a fruitful idea for future research. Also, further studies could focus on the role of non-traditional CG mechanisms (e.g. Chief Compliance Officer **(CCO),** Chief Risk Officer **(CRO),** and Chief Ethical Officer **(CEO)**) in enhancing the company's performance.

BIBLIOGRAPHY

Allan Sloan of Fortune (2011), *The Difference in Transparency and Disclosure*,

http://blog.smu.edu/maguireethics/2011/11/01/the-difference-in-transparency-and-disclosure-from-allan-sloan-of-fortune/, [Accessed 11/2/2011]

Bremer, J. (2012), "Transparency of Egypt's public-private joint ventures", *Towards New Arrangements for State Ownership in the Middle East and North Africa*: OECD, pp.117-144.

Burch Adiloglu, B. V. (2012), "The Relationship between the Financial Ratios and Transparency Levels of Financial Information Disclosures Within The Scope of Corporate Governance: Evidence from Turkey", *The Journal of Applied Business Research ,Vol. 28*, No. 4, pp.543-554.

Khaled Dahawy, T. C. (2007), "Accounting Disclosure in Companies Listed on the Egyptian Stock Exchange" *Middle Eastern Finance and Economics journal, Issue* 1.

Khaled Samaha, K. D. (2012), "The Extent of Corporate Governance Disclosure and its Determinants in a Developing market: The case of Egypt", *Advances in Accounting, Vol.28, Issue* 1, pp.168-178.

Kholeif, A. (2008), "A New Institutional Analaysis of IFRS Adoption in Egypt: A Case Study of Loosley Coupled Rules and Routines" *Working Paper No. 08/0.*

Laksmana, I. (2007), "Corporate Board Governance and Voluntary Disclosure of Executive Compensation Practices", Ken State University.

Marcia Millon Cornett, L. G. (2005), "The Impact Of Corporate Governane On Performance Differences In Privately-Owned Versus State-Owned Banks: An International Comparison", *Journal of Financial Intermediation*, Vol. 19, Issue 1, pp.74-94.

Mohamed, B. H. (2012), "Examine the impact of Corporate Governance on Transparency and Disclosure and the Quality of Financial statements in light of the Financial Accounting System", *Corporate Governance as a tool to limit the Administrative and Financial Corruption.* Sakra City: Mohamed Khedir University.

Mousa, A. M. (2012), " Corporate Governance Practices: Transparency and Disclosure- Evidence from the Egyptian Exchange" , *Journal of Accounting, Finance and Economics*, Vol. *2*, No. 1, pp.49-72.

Musa Mangena, V. T. (2007), "Disclosure, Corporate Governance and Foreign Share Ownership on the Zimbabwe Stock Exchange", *Journal of International Financial Management & Accounting,* Vol. 18, No. 2, pp.53-85.

Nick Lin-Hi, I. B. (2011), "The Relationship between Corporate Governance, Global Governance, and Sustainable Profits: Lessons learned from BP", *Corporate Governance*, Vol. 11, No. 5, pp.571-584.

Pamela Kent, J. S. (2008), "Corporate Governance and Disclosures on the transition to International Financial Reporting Standards", *Accounting & Finance,* Vol. 48, No. 4, pp.649-671.

Yip, R. W. (2012), "Does Mandatory IFRS Adoption Improve Infomration Comparability?", *The Accounting Review,* Vol. 87, No. 5, pp.1767-1789.

Investopedia, http://www.investopedia.com/terms/s/soe.asp