THE QUALITY OF BOARD OF DIRECTORS, OWNERSHIP STRUCTURE AND LEVEL OF VOLUNTARY DISCLOSURE OF LISTED COMPANIES IN THAILAND

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by

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TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

KUALITI AHLI LEMBAGA PENGARAH, STRUKTUR PEMILIKAN DAN TAHAP PENZAHIRAN SUKARELA OLEH SYARIKAT-SYARIKAT YANG TERSENARAI DI PASARAN SAHAM THAILAND (SET)

ABSTRAK

Kajian ini menyelidik sama ada Lembaga Pengarah dan struktur pemilikan mempengaruhi indeks penzahiran sukarela dalam laporan tahunan 317 syarikat bukan kewangan yang tersenarai di SET tahun 2004. Dapatan kajian menunjukkan bahawa tahap penzahiran sukarela dipengaruhi oleh kualiti lembaga pengarah dan struktur pemilikan syarikat. Semakin tinggi kualiti lembaga pengarah, semakin tinggi juga tahap penzahiran sukarela. Tambahan lagi, hubungan ini nampak lebih lemah untuk syarikat yang mempunyai tahap penumpuan pemilikan ketua pegawai eksekutif (CEO) yang tinggi berbanding dengan penumpuan pemilikan CEO yang rendah. Kewujudan setiap satu indeks kualiti bagi setiap ahli lembaga pengarah, seperti kewujudan pemisahan Pengerusi Lembaga-pengarah urusan, perkadaran pengarah bukan-eksekutif yang bebas sebagai ahli lembaga, kewujudan jabatan audit dalaman syarikat, pengarah bukan-eksekutif yang bebas yang merupakan pengerusi jawatankuasa audit, bilangan bukan-eksekutif yang bebas dalam jawatankuasa audit, perkadaran kehadiran ke semua ahli jawatankuasa audit setahun berdasarkan jumlah mesyuarat jawatankuasa audit, jumlah ahli jawatankuasa audit yang merupakan pakar kewangan, seorang pengarah bukan-eksekutif yang bebas yang merupakan pengerusi jawatankuasa ganjaran, dan perkadaran pengarah bukan eksekutif dalam jawatankuasa ganjaran adalah faktor signifikan berhubungan dengan indeks penzahiran sukarela. Hasil dapatan ini menunjukkan hubungan di antara Ahli Lembaga Pengarah dan indeks penzahiran sukarela tidak semestinya sama di antara pemegang saham utama (disederhana secara positif dan negatif) dan pengurusan (disederhana secara negatif), antara pemegang saham utama yang bukan sebahagian daripada pengurusan

(disederhana secara positif) dan merupakan ahli keluarga (disederhana secara negatif), dan antara penumpuan pemilikan CEO yang tinggi (disederhana secara negatif) dan penumpuan pemilikan CEO yang rendah (disederhana secara positif). Akhir sekali, pembolehubah kawalan terdiri daripada saiz syarikat, jenis pengaudit, dan pulangan pendapatan didapati mempunyai pengaruh signifikan terhadap tahap penzahiran sukarela.

THE QUALITY OF BOARD OF DIRECTORS, OWNERSHIP STRUCTURE AND LEVEL OF VOLUNTARY DISCLOSURE OF LISTED COMPANIES IN THAILAND

ABSTRACT

This study investigates whether the quality of board of directors (i.e. each dimension and level of the board of directors' quality) and the ownership structure influence the voluntary disclosure index in the annual reports of 317 non-financial companies listed on the Stock Exchange of Thailand in 2004. The findings suggest that the voluntary disclosure index is influenced by the quality of board of directors and the ownership structure of the firm. The higher the board of directors' quality index, the higher is the voluntary disclosure index. Each dimension of board of directors' quality, namely, proxied by chairman-CEO separation, proportion of independent non-executive directors on the board, existence of internal audit department, an independent non-executive director who is an audit committee chairman, number of independent non-executive directors on audit committee, proportion of all audit committee members' attendance per year on total meetings of audit committee, number of audit committee members who are financial experts, an independent non-executive director who is a remuneration committee chairman, and the proportion of non-executive directors on remuneration committee, are significant factors associated with the voluntary disclosure index. These results show the relationship between the quality of board of directors and voluntary disclosure index will not necessarily be the same between companies with major shareholder owners (positively and negatively moderate) and those with managerial owners (negatively moderate), between companies with major shareholders who are not part of management (positively moderate) and those with family members (negatively moderate), and between companies with high concentration (negatively moderate) and those with low concentration (positively moderate) of CEO controlling ownership. Finally, control variables comprising company size, auditor type, and earnings return were found to have a significant influence on voluntary disclosure index.

CHAPTER 1

INTRODUCTION

1.1 Background of the study

Disclosure is the process through which an entity communicates with the outside world. The significance of proper and adequate corporate disclosure cannot be over emphasized in a free economy where the market allocates the resources to different sectors of the economy. Baumol (1965) reported that the lack of adequate disclosure can create ignorance in the securities market and can result in misallocation of resources in the economy (Chandra, 1974).

This study focused solely on the disclosure found in the annual reports. It does not attempt to assess the quality of such disclosures or to identify incorrect or fraudulent disclosures. Other types of company disclosures exist and sources such as company websites and quarterly or half-yearly reports may provide useful information. However, this study focuses on annual report disclosures because they are the most important source of financial information to those outside a company (e.g. Botosan, 1997; Knutson, 1992; and Lang & Lungholm, 1993) and potentially facilitate comparable analysis.

There are two streams of disclosure literature, namely voluntary disclosure and mandatory disclosure. Voluntary disclosure can be defined as “disclosures in excess of requirements, representing free choices on the part of company managements to provide accounting and other information deemed relevant to the decision needs of users of their annual reports” (Meek et al., 1995, p.555). Mandatory disclosure refers to compliance with compulsory standards. If a disclosure item is mandatory, the assumption often made is that the item will definitely be disclosed; otherwise, the firm will receive a qualified audit report or some other regulatory sanctions. For that to happen standards must be rigorously enforced but in some countries, they are not.

Therefore, the adoption of high quality standards such as the International Accounting Standards (IAS) is one vital step, but it is not a sufficient condition for improved transparency (Ball et al., 2003).

Disclosure of information in the annual reports of companies is management's attempt to reduce information asymmetry. Investors would be able to make use of the information disclosed for decision making and for other investing activities. When management discloses more information than is mandated by law, it means that they are disclosing voluntary rather than mandatory information. Voluntary disclosure does provide useful information for investment purposes (Balachandran & Bliss, 2004).

Most of the research on voluntary disclosure to date has been conducted in the UK, the US, and Continental European countries (e.g. Adams & Hossain, 1998; Buzby, 1975; Cerf, 1961; Cooke, 1989; Depoers, 2000; Firth, 1979; Hossain et al., 1995; Inchausti, 1997; Malone et al., 1993; McKinnon & Dalimunthe, 1993; McNally et al., 1982; Raffournier, 1995; and Singhvi & Desai, 1971). Only a few studies (e.g. Balachandran & Bliss, 2004; Chau & Gray, 2002; Eng & Mak, 2003; Haniffa & Cooke, 2002; Hossain et al., 1994; and Rahman, 1998) have been conducted in Asian countries.

This study aims to examine the voluntary disclosure behavior of companies that are registered in the Stock Exchange of Thailand (SET). The SET has been categorized as an Emerging Capital Market or ECM, which is similar to the stock exchange in developing countries (Saudagaran & Diga, 1997). There are four reasons why the study of voluntary disclosure would prove to be significant in Thailand.

The first reason is because there is evidence that there is a low level of voluntary disclosure in Thailand. A study conducted by Center for International Financial Analysis & Research or CIFAR (1995) compared a point average of the information disclosure of the registered companies in an industrial group from 39 countries that consisted of the developed capital markets and the emerging capital markets. The study showed that countries in the emerging capital markets disclose less information than countries in the developed capital markets. Table 1.1 provides the ranking of information disclosed in 39 countries comprising 17 emerging and 22 developed capital markets.

Table 1.1
Disclosure levels of industrial companies in selected ECMs and developed capital markets

Rank	Country	Average Score of Disclosure
1	United Kingdom	85
2	Finland, Sweden	83
3	Ireland	81
4	Australia, New Zealand, Switzerland	80
5	*Malaysia**, Singapore, *South Africa**	79
6	*Chile**, France	78
7	USA	76
8	Canada, Denmark, Norway	75
9	Israel, Netherlands, *Sri Lanka**	74
10	Hong Kong, *Pakistan**	73
11	Spain, *Zimbabwe**	72
12	Japan, *Mexico**	71
13	*Nigeria**	70
14	*Argentina**, Belgium, *South Korea**	68
15	Germany	67
16	Italy, *Thailand**	66
17	*Philippines**	64
18	Austria	62
19	*Greece**, *India**	61
20	*Colombia**, *Taiwan**, *Turkey**	58

* *Emerging Capital Markets (ECMs)*

Source: CIFAR (1995), as cited in Saudagaran and Diga (1997)

In Table 1.1, six countries of the emerging capital markets are in the first 10, namely, Malaysia, Singapore, South Africa, Chile, Sri Lanka, and Pakistan. In contrast, nine countries are in the last five ranks. Thailand is ranked as number 16; the same level as Italy.

The ranking by CIFAR (1995) was based on 85 items. The items consisted of 67 items of mandatory disclosure and 18 items of voluntary disclosure. In Thailand, the Thai Accounting Standards or TAS provided the mandatory disclosure and any disclosure in addition to the mandatory disclosure is considered as voluntary. There is not much difference between TAS and the International Accounting Standards or IAS. Toplin et al. (2002) conducted a study on the mandatory disclosure based on a sample of 60 companies in Australia, Hong Kong, Malaysia, Phillipines, Singapore, and Thailand. It was found that the average level of mandatory disclosure of the sampled group is 95.5 percent, which was considered high. Interestingly it was found that the mandatory disclosure for Philippines and Thailand was much higher than Australia, Hong Kong, Malaysia, Singapore, and countries with British colonial links. This study differs from the CIFAR's (1995) study because CIFAR's list comprise majority of mandatory items as compared to voluntary items. It implies that in terms of mandatory disclosure, Thailand ranks high but it might not be the case for voluntary disclosure.

The Asian financial crisis in 1997 has led to the realization that greater adequate disclosure of company was essential to protect investors' interest (Balachandran & Bliss, 2004). This led to the second reason why the study should be conducted. The lack of good corporate governance and lack of adequate disclosure and transparency by Thai listed companies on the SET resulted in a loss of investor's confidence (Paweewun, 2003). Trairatvorakul (1998) reported that adequate disclosure and transparency is a key to promote investors' confidence and market efficiency. He suggested that SET should require listed companies to disclose both financial and non-financial information in their annual reports. Since January 1998, the SET has required listed companies to set up an audit committee comprising at least three members to review the company's annual report to "ensure accuracy and adequate disclosure" (SET, 1999a, p. 7). This requirement is encapsulated in the Best Practice Guidelines for Audit Committee (SET, 1999a).

According to McKinsey & Company Investor Opinion Survey (2000) investors do not mind paying a 25.7 percent premium for Thai listed companies that comply with the principles of good corporate governance. In addition, the McKinsey & Company Investor Opinion Survey (2000) found that although there was a significant improvement in the principles of good corporate governance, but their corporate information disclosure and transparency, equal treatment for both major and minor shareholders, and the role of stakeholders, needed to be improved.

The third reason for why this study should be undertaken is the unique feature found in Thai companies which is not found in other countries. Most Thai companies are usually run by Chinese family members and is thus based on the Chinese family values. This value allows one to only disclose information that is necessary as disclosing more information would be considered as revealing the "family secret". This practice is supported by Jelatianranat's (2000)' study while Gray (1988) and Radebaugh and Gray (1997) confirmed this finding and concluded that in Asian environment the culture of the countries will shape the practice of the companies. Ball et al.'s (2003) recommended that companies in the Asia should be encouraged to disclose more voluntary information as for the benefit of their investors and users of the financial statements.

The fourth and final reason as to why the study should be undertaken is based on the study by Limpaphayom (2000). This study found that the management and the ownership structure of a company will influence the information disclosed. Wiwattanakantang (2000) found that companies registered in Thailand - in addition to being controlled by the family system - usually their top management owns the largest shares. Top management and the first largest shareholder often one and the same person and this therefore indicate the presence of managerial ownership.

Previous studies have examined some corporate governance mechanisms that may influence voluntary disclosure practice (e.g. Balachandran & Bliss, 2004; Eng & Mak, 2003; Evans, 2004; Haniffa & Cooke, 2002; Ho & Wong, 2001; and Willekens et al., 2004). However, the studies examined the effect of the corporate governance mechanisms such as board of directors, audit committee, remuneration committee, etc individually and did not examine the effect of the corporate governance mechanisms in aggregate characteristics. This study will only be focusing only on one corporate governance mechanism, namely the board of directors. This study will also be developing an index to measure the quality of the board of directors. To date, this is the first study that will be using an index to measure the quality of the board of directors. The reason why only the board of directors is studied is because the board of directors acts as the top management of the company and has the final say in all decisions that will be made by the company.

The main objective of this study is therefore to examine the relationship between the level of the board of directors' quality with the level of voluntary disclosure of listed companies in Thailand. Under the implicit assumption of Jensen and Meckling's (1976) positive agency theory, the study hypothesized that an improved quality of the board of directors would lead to more voluntary disclosure practices. The index of the quality of the board of directors developed for this study can be adapted to other countries or economies with similar institutional backgrounds as the Emerging Capital Markets (ECMs)[1].

The board of directors of the companies is chosen as it is an important tool to protect shareholders' assets and to control the management of the company. The board of directors is also the main policy making body, strategic planner, and acts as the authority of the company. In Thailand, the board of directors of most the listed

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[1] ECMs are made up of 47 countries (IFC, 1994, as cited in Saudagaran & Diga, 1997). comprising 14 countries in Africa i.e. Botswana, Cote d'Ivoire, Cyprus, Egypt, Ghana, Kenya, Mauritius, Namibia, Nigeria, South Africa, Swaziland, Trinidad and Tobago, Tunisia, and Zimbabwe; 11 countries in Asia i.e. Bangladesh, China, India, Indonesia, Korea, Malaysia, Pakistan, Philippines, Sri Lanka, Taiwan, and Thailand; 5 countries in Europe i.e. Greece, Hungary, Poland, Portugal, and Turkey; 13 countries in Latin America i.e. Argentina, Barbados, Brazil, Chile, Colombia, Costa Rica, Ecuador, Jamaica, Mexico, Panama, Peru, Uruguay, and Venezuela; and 4 countries in the Middle East i.e. Iran, Jordan, Morocco, and Oman.

companies on the SET are controlled by the largest shareholders. As a result of this, the interests and participation of the minority shareholders are being undermined (Limpaphayom, 2000). An important tool for the protection of the minority shareholders is the ownership structure in the companies. Generally, the ownership structure of the top five largest shareholders in the company from 1990 to 1998 and 2003 shows an increasing trend. Please refer to Table 1.2 for details.

Table 1.2
Top Five Ownership Concentration for Public Companies Limited
(Unit: percent of total outstanding shares)

Largest	1990	1991	1992	1993	1994	1995	1996	1997	1998	2003
First	26.18	26.35	26.79	32.28	26.36	27.66	28.05	28.50	28.86	35.58
Second	11.44	11.43	10.99	16.52	10.67	11.26	11.69	11.70	12.07	14.47
Third	6.61	6.80	7.08	9.89	6.89	6.99	7.12	7.35	7.27	7.72
Fourth	4.93	5.00	5.18	6.39	4.85	5.00	5.06	5.12	5.18	4.83
Fifth	3.85	3.91	3.98	4.57	3.85	3.91	3.88	4.07	4.18	3.30
Top Five	53.01	53.49	54.02	69.65	52.62	54.82	55.80	56.74	57.56	65.90

Source: 1990-1998, as cited in Limpaphayom (2000), and 2003 from the report on the disclosure of additional information (Form 56-1) and annual reports (Form 56-2) of all Thai public limited companies in the SET

Although the Public Company Act of 1992 and The Securities and Exchange Act of 1992 permitted shareholders to hold a minimum proportion of shareholdings per person but in practice this could not be enforced. This was because the large shareholders were family' members or are the management of the company. As a result there was minimal legal protection for minority shareholders.

1.2 Problem statement

The study by CIFAR (1995) ranked Thailand as number 16 from 20 which showed that the information disclosed in the annual reports of Thai companies was not adequately disclosed. Standard & Poor and the National University of Singapore (S&P

& CGFRC, 2004) in their studies recommended that Thai listed companies had to improve transparency and provide more information disclosure.

Thai listed companies were mostly controlled by family members, the CEO and the CFO who were large shareholders or representatives of large shareholders. In addition, Wiwattanakantang (2000) stated that most listed companies in the SET were controlled by a few large shareholders and the percentages of total share were also high. Minority shareholders held a small percentage of shares and thus had less influence to control and make decisions about the administration. Consequently, Thai listed companies do not prefer to disclose the information as investors in the stock exchange expected (Jelatianranat, 2000).

From the problem above, the important element to be present in the company that could lead to a better transparency in the annual report is the board of directors' quality. Levitt (1999) found that, when corporate governance was not good, there is a lower level of transparency in the annual report, profit manipulation, and there is a weakness in internal control. One of the recommendations made by Levitt to overcome this problem was to have the board of directors' quality for ensuring the integrity of financial reports.

Previous research examining board of directors' characteristics have studied the following dimensions: (1) the board's leadership structure (e.g. Evans, 2004), (2) board's composition (e.g. Vafeas, 1999; and Willekens et al., 2004), (3) board's meetings (e.g. Evans, 2004; and Vafeas, 1999), (4) board's controlling system and internal audit (e.g. Willekens et al., 2004) and (5) board's committees such as audit committee. Pertaining audit committee characteristics, the following dimensions were examined in previous research (1) audit committee's leadership structure (e.g. Haniffa & Cooke, 2002), (2) audit committee's composition (e.g. Ho & Wong, 2001; and Willekens et al., 2004), (3) audit committee's meetings (e.g. Evans, 2004; and Liu, 2004) and (4) audit committee's knowledge and expertise (e.g. Mangena & Pike, 2005). Haniffa and Cooke (2002) and Vafeas and Theodorou (1998) have examined another committee set up by board of directors, that is the remuneration committee. Dimensions of the remuneration committee examined were (1) leadership structure (e.g. Haniffa & Cooke, 2002) and (2) composition (e.g. Vafeas & Theodorou, 1998).

In Thailand, there have not been many researches examining the relationship between the quality of the board of directors and the level of voluntary disclosure in the annual reports of listed companies in the SET. SET emphasized the role of the board of directors, the audit committee and the remuneration committee, to ensure that the annual financial reports of the company is reliable and ensure that there is disclosure of information that would prove beneficial to the users of the financial statements.

However, it should be noted that even with quality board of directors overseeing that there is transparency in the annual reports, this could still not be achieved. As discussed earlier, Thai listed companies are usually owned by family members of the company and also by the five largest shareholders of the company. As such, this may not be possible under very high ownership concentration, large shareholders who have access to corporate information are less motivated to disclose private information to external shareholders. The result is weak overall corporate governance and inadequate protection of small shareholders' rights. Thus this study introduces ownership structure as the moderator variable which could influence the relationship of the quality of the board of directors to level of voluntary disclosure of the annual reports of the companies.

Thus, this study aims to investigate the influence of the board of directors' quality, on the level of voluntary disclosure of listed companies in Thailand. In addition, it aims to ascertain the role of ownership structure as a moderator variable on the relationship between the board of directors' quality and the level of voluntary disclosure of listed companies in Thailand.

1.3 Research questions

On the basis of the research background, this study will be guided by seven major research questions:

(1) What is the level of the board of directors' quality of Thai listed companies?

(2) What are the dimensions of the construct referred to as "board of directors' quality" (i.e. the quality of the board's leadership structure, composition, meetings, controlling system, committees, audit committee and remuneration committee) of Thailand's listed companies?

(3) What is the level of voluntary disclosure of Thailand's listed companies?

(4) What is the relationship between the level of the board of directors' quality and the level of voluntary disclosure in Thailand's listed companies?

(5) What is the relationship between each dimension of the board of directors' quality (i.e. the quality of the board's leadership structure, composition, meetings, controlling system, committees, the audit committee and the remuneration committee) and the level of voluntary disclosure in Thailand's listed companies?

(6) What is the effect of ownership structure on the relationship between the level of the board of directors' quality and the level of voluntary disclosure in Thailand's listed companies?

(7) What is the effect of ownership structure on the relationship between each dimension of the board of directors' quality (i.e. the quality of board's leadership structure, composition, meetings, controlling system, committees, audit committee and remuneration committee) and the level of voluntary disclosure in Thailand's listed companies?

1.4 Research objectives

This study will present empirical evidence that relationships exist and will among the board of directors' quality, the level of voluntary disclosure and ownership structure. The objectives of this study are:

(1) To determine the level of the board of directors' quality which is associated with the quality of the board's leadership structure, composition, meetings, controlling system, committees, the audit committee and the remuneration committee in compliance with SET's Code of Best Practice for Directors of Listed Companies, Best Practice Guidelines for Audit Committee, and the Principles of Good Corporate Governance of the Thai listed companies.

(2) To determine each dimension of the board of directors' quality which is associated with the quality of the board's leadership structure, composition, meetings, controlling system, committees, the audit committee and the remuneration committee of the Thai listed companies.

(3) To determine the level of voluntary disclosure of all information in the corporate annual reports of the Thai listed companies.

(4) To determine the relationship between the level of the board of directors' quality and the level of voluntary disclosure of the Thai listed companies.

(5) To determine the relationship between each dimension of the board of directors' quality which is associated with the quality of the board's leadership structure, composition, meetings, controlling system, committees, audit committee and remuneration committee and the level of voluntary disclosure of the Thai listed companies.

(6) To determine whether the ownership structure moderates the relationship between the level of the board of directors' quality and the level of voluntary disclosure of the Thai listed companies.

(7) To determine whether the ownership structure moderates the relationship between each dimension of the board of directors' quality and the level of voluntary disclosure of the Thai listed companies.

1.5 Significance of the study

1.5.1 Theoretical

Eisenhardt (1989, p.59) argued that the agency theory has developed into positive agency theory which "the principal and agent are likely to have conflicting goals and then describing the governance mechanisms that limit the agent's self-serving behavior".

Under the implicit assumption of Jensen and Meckling's (1976) positive agency theory, the study hypothesized that an improved quality of the board of directors would lead to better governance that enhances more voluntary disclosure practices, and that voluntary disclosure practices are used as a means to reduce information asymmetry (e.g. Petersen & Plenborg, 2006) and agency problems.

Leftwich et al. (1981) argued that the larger the proportion of independent directors on the board, the more effective it will be in monitoring managerial opportunism, and thus firms whose boards are dominated by outside directors are expected to disclose more voluntary information.

Fama and Jensen (1983a) indicated that a higher proportion of independent non-executive directors on the board should result in more voluntary corporate disclosure. They have suggested that once the firm's capital is widely held, the potential of conflicts between principal and agent is greater than in family-controlled firms. To reduce these conflicts some shareholders, especially institutional ones, force managers to disclose more corporate information for the accurate evaluation of the firm's performance. As a result, information disclosure is likely to be more intensive in widely held firms.

The prevalence of family-controlled firms listed on a stock exchange, which is the case in the SET, may result in less demand for corporate disclosures (Dhnadirek and Tang, 2003). Furthermore, Wiwattanakantung (2000) found that Thai listed companies' ownership is highly concentrated and most of the shares are owned by executive directors. As a result, managers and owners are of the same person.

Consequently, “ownership is highly concentrated, the nature of the agency problem shifts away from manager-shareholder conflicts to conflicts between the controlling owner and minority shareholders” (e.g. Berle & Means, 1932 and Fan & Wong, 2002 as cited in Hope, 2003, p.10). It is important, then, to investigate whether controlled firms and family ownership are associated with lower incentives of independent directors for voluntary earnings disclosures.

It is difficult or expensive for the minority shareholders to verify what the controlling owner is actually doing with independent directors. Thus, the theoretical contribution of this study extends the positive agency theory to include ownership structure as moderator variables.

Ownership structure has often been considered as an independent variable that influences the level of voluntary disclosure in previous research. In this study, the role of ownership structure as moderator variable is investigated as appose to its role as independent variable as in previous research. This is an additional contribution to the positive agency theory. Ownership structure has been treated as moderator variables in this study as previous studies (Chen & Jaggi, 2000; and Forker, 1992) have shown that the quality of board of directors in the firms with managerial and family controlling ownership may become impaired and their influence on the disclosure quality of a firm’s financial reporting may be weaker than in firms without managerial and family controlling ownership. In addition, Hill (1999, p. 1127) argues that the role of managerial and family controlling ownership should be examined when corporate governance studies are undertaken as findings in corporate governance studies are not consistent.

1.5.2 Practical

The practical contribution of this study will assist the Stock Exchange of Thailand (SET) to understand the level of voluntary disclosure. The determining factor is the board of directors’ characteristics that influence the level of voluntary disclosure.

The SET can then monitor the board of directors' characteristics that influence the level of voluntary disclosure in its quest for improved the transparency and the accountability of the corporate annual reports of the companies listed on the SET.

1.6 Definition of key terms

For the purpose of this study, the following terms will be utilized:

1.6.1 The quality of the board of directors

The quality of the board of directors in this study includes the dimensions of (1) the quality of the board of directors' leadership, (2) its composition, (3) meetings, (4) the controlling system, (5) the committees, (6) the audit committee and (7) the remuneration committee. The criteria are obtained from the SET's Code of Best Practice for Directors of Listed Companies (SET, 1999b), Best Practice Guidelines for Audit Committees (SET, 1999a), and the Principles of Good Corporate Governance (SET, 2001). Board of directors' quality are measured based on eleven dimensions and eleven items. Description of the dimensions and items are as follows:

1.6.1.1 Quality of board

The quality of board in this study includes five dimensions of (1) quality of board's leadership structure measured by the existence of titles and authority of the board's chairman and head of management team are clearly separated in compliance with No.9 of the Principles of Good Corporate Governance, (2) quality of board's composition measured by more than half of the directors on the board are independent non-executive directors (INDs) in compliance with No.8 of the Principles of Good Corporate Governance. In addition, board's composition in this study is referred to as the company committees should consist of members of the board of directors into one of three categories namely, (i) executive directors who are concerned with the administration or committees that are authorized to sign; (ii) non-executive directors such as independent non-executive directors who are not placed in any position and are not authorized to sign and are independent from the largest shareholders, the management, and other concerned persons and are not own more than 0.5 percent of direct outstanding shares and outside non-executive directors (all those not included in executive directors and independent non-executive directors) are those members the board who did not have any position in the company and were not representatives of the largest shareholders but they might be the representatives of customers, suppliers, or the creditors, etc (SET, 1999b), (3) quality of board's meetings measured by all directors are to attend every board meeting in compliance with No.11 of the Principles of Good Corporate Governance, (4) quality of board's controlling system and internal audit measured by the existence of internal audit department in the company in compliance with No.13 of the Principles of Good Corporate Governance, and (5) quality of board's committees measured by audit committee (AC) and remuneration committee (RC) are established in compliance with No.13 of the Principles of Good Corporate Governance.

1.6.1.2 Quality of audit committee (AC)

The quality of audit committee in this study includes four dimensions of (1) quality of AC's leadership structure measured by the existence of AC's chairman is an IND in compliance with No.12 of the Principles of Good Corporate Governance, (2) quality of AC's composition measured by at least three AC members are INDs in compliance with No. 3.1 of Best Practice Guidelines for Audit Committee, (3) quality of AC's meetings measured by all AC members are to attend every AC meeting in compliance with No.11 of the Principles of Good Corporate Governance, and (4) quality of AC's knowledge and expertise measured by at least one AC member is a financial reporting expert such as CPA in compliance with No. 3.3 of Best Practice Guidelines for Audit Committee.

1.6.1.3 Quality of remuneration committee (RC)

The quality of remuneration committee in this study includes two dimensions of (1) quality of RC’s leadership structure measured by the existence of RC’s chairman is an IND in compliance with No.12 of the Principles of Good Corporate Governance and (2) quality of RC’s composition measured by more than half of the RC members are non-executive directors in compliance with No.12 of the Principles of Good Corporate Governance.

1.6.2 A high concentration of CEO’s ownership

A high concentration of CEO’s ownership is referred to as the percentage of shares held by a CEO and includes his family as a single unit; adapted from McClelland and Barker III (2004); transform recode by median of all sample companies, if more than median is high concentration and at most median is low concentration.

1.6.3 The largest shareholder controlling ownership

The largest shareholder controlling ownership in this study is referred to as the percentage of direct ownership’ share held by the largest shareholder (the percentage of shares held by shareholders who have the same family name will be combined as a single unit). The definition of a controlling ownership is adopted from the Stock Exchange of Thailand (SET) and this has been used in Wiwattanakantang’s study (2000). In Thailand, the shareholder who controls at least 25 percent of outstanding shares will have adequate controlling rights on the firm’s management.

1.6.4 The non-executive director, largest shareholder-controlling ownership

The non-executive director, largest shareholder-controlling ownership is referred to as the percentage of direct ownership’s share, at least 25 percent of direct outstanding shares, held by the largest shareholder who is non-executive director; adapted from Chen and Jaggi (2000).

1.6.5 The family member, largest shareholder-controlling ownership

The family member, largest shareholder-controlling ownership is referred to as the percentage of direct ownership share, at least 25 percent of direct outstanding shares held by the largest shareholder who is a family member; adapted from Chen and Jaggi (2000).

1.6.6 Minority shareholders

Minority shareholders in this study are referred to as shareholders though larger in number, hold only a small portion of total shares. They have very little influence over management decision-making and control (Wiwattanakantang, 2000).

1.6.7 Firm characteristics

This study will control the firm characteristics. Three firm characteristics (1) performance variables, (2) structure variables, and (3) market variables will be controlled. These categories are based on Chen and Jaggi (2000), Lang and Lundholm (1993), and Wallace et al. (1994).

The performance variables controlled in this study are: (1) profitability, defined as the ratio of income before extraordinary items (IBEX) over net sales (profit margin) and IBEX over book value of equity for the beginning of the period (earnings return); and (2) liquidity ratio, defined as the ratio of current assets over current liabilities.

The structure variables controlled in this study are: (1) debt-equity ratio, defined as the ratio of long-term debt over book value of common equity; and (2) firm size, defined as the natural logarithm of total assets, net sales, and market capitalization.

The market variables controlled in this study are: (1) scope of business operations, defined as conglomerate or non-conglomerate firms; and (2) type of audit firm, defined as the Big4 international independent audit firms (i.e. PriceWaterhouseCoopers, Ernst & Young, Deloitte and Touche, and KPMG).

1.6.8 Voluntary disclosure

Voluntary disclosure in this study are the external reporting done beyond what is mandated (Meek et al., 1995, p.555) and voluntary disclosure covers all data which concerns both the subsidiaries and the group itself (Depoers, 2000). The checklist of voluntary disclosure items in this study as a dependent variable comprising 70 items in annual reports of sample companies i.e. overall voluntary disclosure of general corporate information, corporate strategy, research and development (R&D), future prospects, employee information, social policy and value-added information, segment information, financial review, foreign currency information, and stock price information which was adopted from Meek et al. (1995) and Chau and Gray (2002). The scoring of voluntary disclosure items under the unweighted voluntary disclosure index was adopted from Cooke (1989).

1.7 Organization of the thesis

This thesis is organized into six chapters. Chapter 1 provides the background, problem statement, research objectives, research questions, definitions of key terms, significance of the study, and the organization of the remaining chapters.

Chapter 2 is divided into fourteen sections and comprises the background, the legal framework of the board of directors, the board of directors’ composition, roles and responsibilities of the directors, the collective responsibility of the directors, conflict of interest, appointments to the board of directors, holding a director’s position, directors’ remuneration, board of directors and shareholders’ meetings, directors’ reporting, relationship among members of the board of directors and relationship with investors. It ends with a summary of the chapter.

Chapter 3 presents a review of the literature, previous research, the theoretical framework and the hypotheses that are related to this study. The review presented includes the positive agency theory, voluntary disclosure, disclosure criteria and corporate governance mechanisms. This chapter also includes the theoretical framework and discusses the hypotheses of the study and the control variables. It ends with a chapter summary.

Chapter 4 is divided into seven sections and comprises research design, measurement of variables of the study, population and sample of the study, data collection method, explanation of data analyses that will be taken and a summary of the chapter.

Chapter 5 presents the results of the data analysis. Firstly, this chapter describes the sample. Secondly, it describes the demographic information of the sample in terms of level of board of directors' quality, level of voluntary disclosure items, ownership structure's demographic information, and firm characteristics' demographic information. Thirdly, this chapter presents the analysis of the dependent variables, including goodness of measures using reliability analysis. Finally, the results of hypotheses testing are presented.

Finally, Chapter 6 recapitulates the major findings of this study and discusses the interpretation of the results. The implications of the findings are also discussed, together with limitations and suggestions for future research. This chapter concludes by reference to the findings.

CHAPTER 2

THE BOARD OF DIRECTORS IN THAILAND

This chapter is divided into fourteen sections and comprises the background, the legal framework of the board of directors, the board of directors' composition, roles and responsibilities of the directors, the collective responsibility of the directors, conflict of interest, appointments to the board of directors, holding a director's position, directors' remuneration, board of directors and shareholders' meetings, directors' reporting, relationship among members of the board of directors and relationship with investors. It ends with a summary of the chapter.

2.1 Background

The Public Company Act of 1992 superseded the Public Limited Company Act of 1978. According to Limpaphayom (2000) the new act was established to overcome the shortfalls of the previous act. The Public Limited Company Act of 1978 did not allow having cumulative voting because this could lead to the frequent changes of the board of directors, which could cause disunity in the company administration. The law also forbade the largest shareholders to hold shares which are more than 50 percent of paid-up capital and forbade other shareholders to hold shares which are more than 10 percent of paid-up capital. In addition, the law discouraged companies whose owners were family members to be listed companies on the SET. As a result of the new Public Company Act of 1992 the ownership structure of the five largest shareholders was increased from 50 to 70 percent of paid-up capital from 1990 to 1998 and 2003 (Limpaphayom, 2000). There were also more companies listed on the SET as a result of the new Act.

To cater for the increase in companies listed on the SET, Securities and Exchange Commission (SEC) of Thailand and the Stock Exchange of Thailand (SET) have recommended some good principles for the board of directors of the listed companies (SET, 1999b) and for the audit committees (SET, 1999a) to effectively carry out their duties. One phenomenon that can be observed in Thai listed companies, according to Claessens et al. (2000) was that more than 60 percent of the listed companies were family-owned. Although over many years the family-owned style tended to decrease in some part, it still remained a significant portion. As a result of this family owned nature, there were lack of compliance with some of the principles suggested (SET, 2001).

The Corporate Governance Center of the Stock Exchange of Thailand or the SET (SET, 2003) found that 98 percent of the listed companies were able to comply with the following principles: proxy of voting; the rights of the stakeholders; the protection of inside information; the remuneration of the directors and the management; and the audit committees. Three of the principles that were not complied with were: a written policy on corporate governance, having a remuneration committee, and an independent chairman of the board of directors.

2.2 Legal framework of the board of directors

The Public Company Act (PCA) of 1992 allows public companies to have many directors but not less than five persons. To qualify as directors one (1) must be at least eighteen years of age; (2) must not be a bankrupt; (3) must not have been imprisoned for fraud or embezzlement; and (4) must not be removed from the government office for fraud. Additionally, the directors must not be the shareholders in the companies but could be the representatives of the major shareholders from various groups.

The Public Company Act of 1992 has defined the regulations for the appointment procedure, qualification, roles, duties, and the responsibility of the directors in a listed company. Besides, the directors would be selected by the shareholders in the annual meeting. In business, directors were required to work with care and honesty according to the law and regulations for the best benefit of the companies. On the other hand, if the directors were found to have disobeyed the rules and regulations, they can be imprisoned or be asked to pay a fine. Generally, many listed companies established a code for their companies regarding the best principles/code of corporate governance and business ethics (Limpaphayom, 2000a).

Nikomborirak (2001) stated that shareholders are allowed to vote to determine who should be the director of the company in the annual general meeting. A holder of one share is allowed to cast one vote. In Thailand, cumulative preference shareholders are also allowed to vote. This is not in line with the practice in many Asian countries. The problem occurs from shares that had cumulative voting or which disregard the voting plan according to the regulations in the Public Company Act of 1992, that is, one share one vote; however, a few companies permitted cumulative voting. In Thailand, the term for a directorship is between 2 to 4 years. To stay compliant with the regulations, what happens in practice is that the companies will randomly select their directors and reappoint one third of them who are terminated each year. The Public Company Act of 1992 did not require independent directors to be board of directors of a company. However, in 1999, the SET introduce a new requirement which required that the board of directors of a listed company must comprise of at least two independent directors. The role of the independent directors was to ensure there was no biasness in decisions made by the board of directors and that the interests of minority shareholders were protected.

2.3 Board of directors' composition

The SET (1999b) requires the board of directors to comprise of the following: (1) directors who were involved with routine administration who have an authority to approve activities of the company; (2) non-administrative directors who were independent and did not hold any position in the administration or did not work as employees of the companies. They do not have an authority to approve activities of the company. They must also be independent from the large shareholders, the management, and related parties persons. They should be able to look after the interest of the shareholders and should prevent any form of occurrence of conflict of interest; and (3) outside directors who did not hold any position in the administration and are not employees of the companies. They must not be the representative of large shareholders; nevertheless, they might be the representative of stakeholders such as customers, suppliers, or creditors. The proportion of independent board of directors should include number of independent non-executive directors more than the number of the outside non-executive directors adds to executive directors and at least three independent non-executive directors as audit committee members on the board.

The directors are responsible to ensure that the financial and non-financial data are disclosed in the annual reports. The board of directors is considered as the highest decision making committee in a company. The board of directors should be able to voice out their opinions freely. The chairman of the board should be an independent director and should not be the same person as the managing director (SET, 1999b).

With respect to audit committee, SET (1999a) requires that every listed company must have at least three independent non-executive directors as audit committee members. Nikomborirak (2001) defines independent non-executive directors as follows: (1) must not be employees of the companies, subsidiaries, or conglomerates; (2) do not hold shares that are more than 0.5 percent of the paid-up capital of the company; and (3) do not have any benefit or interest, directly or indirectly in the company, its subsidiaries, or its conglomerates.

In a study conducted by SET (2003), it was found that 73 percent of the listed companies comply with the requirement of having at least three independent non-executive directors in the board. Out of this percentage, it was found that 67 percent of the companies had at least three independent non-executive directors; while 31 percent had four to 14 independent non-executive directors and two percent had less than three independent non-executive directors on their board.

SET (2003) analyzed the possible reasons for non-compliance, as follows: (1) a lot of directors in the board of directors did not understand the definition of the independent non-executive directors, (2) difficult to find independent non-executive directors to sit on the board, and (3) the companies did not want to incur further expense, especially the smaller companies to remunerate the independent board of directors.

An interesting finding from the study has shown that although on average, the board size was 11 people and the smallest size was 5 people (which were the minimum requirement of the Public Limited Company Act 1992), the actual size of the board of directors could go to as high as 25 people. The textile and clothing sector had the largest board size with an average of 15 people.

2.4 Roles and responsibilities of board of directors

The SET (1999b) has listed the roles and responsibilities of the board of directors. Directors are required to be competent, knowledgeable, and experienced to run a business. They must also have an interest to serve the company. In addition, they must be honest. Directors are to accept the resolutions of the shareholders' meetings and must at all times look after the interest of the company. They are responsible to implement and monitor policies of the companies so that economic value and shareholders' wealth are maximized. Directors must manage the company according to the laws and regulations. They should also ensure an efficient and sound system of internal control and internal audit in the company. In carrying out their duties, directors might seek professional advice from outside parties for assistance at the company's expense. A company secretary should be appointed to assist the directors in carrying out their duties. Finally, the directors should establish and implement a Code of Corporate Conduct and a Code of Ethics for the companies.