

**THE IMPACT OF OWNERSHIP STRUCTURE AND CORPORATE  
GOVERNANCE ON CORPORATE SOCIAL REPORTING OF SELECTED  
PUBLIC LISTED COMPANIES IN MALAYSIA**

**CHEW KOOI PENG**

**Research report in partial fulfilment of the requirements for the  
degree of Master of Business Administration (Sustainable Development)**

**Universiti Sains Malaysia**

**2015**

## ACKNOWLEDGEMENT

First and foremost, I would like to express my sincere gratitude to my supervisor, Dr. Chu Ei Yet for all the guidance and encouragement he provided to me during the time I was working on the project. His comments were of very much value in the completion of the project.

I would also like to express my special thanks to all the lecturers that have taught me throughout my studies in USM— Associate Prof. Dr. Sofri Yahya, Dr. Yusliza Mohd Yusoff, Dr. Chu Ei Yet, Dr. Rajendran Muthuveloo, Dr. Yudi Fernando, Dr. Rosly Othman, Dr. Zurina Mohaidin, Prof. Dato' Ishak Ismail, Dr. Salmi Mohd Isa, Dr. Elisha Nasruddin, Dr. Suzari Abdul Rahim and Mrs. Junaimah Jauhar, thank you so much for your knowledge and guidance.

Special thanks to all my beloved friends for all those times they stood by me, for all their sincere help when I got stuck and for all their cheering-up when I was frustrated, Steven Choo Poh Wai, Alia Kamal, Fadzlina, Goh Jia Haur, Ng Hong Guan, Nur Aulia Fahada, Chong An Gee. I thank you all for the kind assistance, generosity, and understanding.

Last, but not least, I wish to thank my parents and family for their constant support and encouragement throughout that period that I was doing this project.

## TABLE OF CONTENTS

|  | <b>Page</b> |
|--|-------------|
| ACKNOWLEDGEMENT                        | i           |
| TABLE OF CONTENTS                      | ii          |
| LIST OF TABLES                         | vi          |
| LIST OF FIGURES                        | vii         |
| ABSTRAK                                | viii        |
| ABSTRACT                               | ix          |
| <br><b>CHAPTER 1 INTRODUCTION</b>      |             |
| 1.1 Introduction                       | 1           |
| 1.2 Background of Study                | 1           |
| 1.3 Problem Statement                  | 5           |
| 1.4 Research Questions                 | 8           |
| 1.5 Research Objectives                | 9           |
| 1.6 Significance of Study              | 10          |
| 1.6.1 Theoretical Significance         | 10          |
| 1.6.2 Practical Significance           | 11          |
| 1.7 Definition of Key Terms            | 11          |
| 1.8 Organization of Chapters           | 13          |
| 1.9 Chapter Summary                    | 14          |
| <br><b>CHAPTER 2 LITERATURE REVIEW</b> |             |
| 2.1 Introduction                       | 15          |
| 2.2 Theoretical Background             | 15          |
| 2.2.1 Stakeholder Theory               | 15          |

|                                       |  |    |
|---------------------------------------|--|----|
| 2.2.2                                 | Agency Theory  | 18 |
| 2.2.3                                 | Legitimacy Theory  | 20 |
| 2.3                                   | Corporate Social Reporting   | 22 |
| 2.3.1                                 | Rising of Corporate Social Reporting                                   | 24 |
| 2.3.2                                 | Corporate Social Reporting in Malaysia                                 | 27 |
| 2.4                                   | Ownership Structure in Malaysia  | 31 |
| 2.5                                   | Ownership Structure Variable   | 34 |
| 2.5.1                                 | Ownership Concentration  | 34 |
| 2.5.2                                 | Foreign Ownership  | 35 |
| 2.6                                   | Corporate Governance in Malaysia                                       | 37 |
| 2.7                                   | Corporate Governance Variable  | 40 |
| 2.7.1                                 | Board Independence   | 40 |
| 2.7.2                                 | CEO Duality  | 41 |
| 2.8                                   | Sizes of Company, Company's Profitability, Types of Industry Variables | 43 |
| 2.9                                   | Theoretical Framework  | 45 |
| 2.10                                  | Development of Hypotheses  | 47 |
| 2.10.1                                | Summary of Hypotheses  | 51 |
| 2.11                                  | Chapter Summary  | 51 |
| <br>                                  |  |    |
| <b>CHAPTER 3 RESEARCH METHODOLOGY</b> |  |    |
| 3.1                                   | Introduction   | 52 |
| 3.2                                   | Research Approach  | 52 |
| 3.3                                   | Research Design  | 53 |
| 3.3.1                                 | Population   | 53 |
| 3.3.2                                 | Unit of Analysis   | 54 |
| 3.3.3                                 | Sample Size & Sampling Method  | 54 |
| 3.3.4                                 | Data Collection Method   | 56 |

|       |  |    |
|-------|--|----|
| 3.4   | Measurement of Variables                                 | 57 |
| 3.4.1 | Measurement of Dependent Variable                        | 57 |
| 3.4.2 | Measurement of Independent Variables & Control Variables | 60 |
| 3.5   | Statistical Data Analysis                                | 61 |
| 3.6   | Chapter Summary  | 63 |

## **CHAPTER 4 DATA ANALYSIS AND RESULTS**

|       |   |    |
|-------|---|----|
| 4.1   | Introduction  | 64 |
| 4.2   | Sample Profile  | 64 |
| 4.3   | Descriptive Analysis  | 64 |
| 4.4   | Parametric Paired Sample T-Test                                   | 68 |
| 4.5   | Correlation Analysis  | 69 |
| 4.6   | Multiple Regression Analysis                                      | 72 |
| 4.6.1 | Regression Results  | 73 |
| 4.6.2 | Multicollinearity   | 76 |
| 4.6.3 | Diagnosis of Outlier, Normality and Linearity of the Relationship | 77 |
| 4.7   | Hypothesis Testing  | 80 |
| 4.7.1 | Summary of the hypotheses   | 82 |
| 4.8   | Chapter Summary   | 83 |

## **CHAPTER 5 DISCUSSION AND CONCLUSION**

|       |                           |    |
|-------|---------------------------|----|
| 5.1   | Introduction              | 84 |
| 5.2   | Recapitulation of Study   | 84 |
| 5.3   | Findings and Discussions  | 85 |
| 5.4   | Implications of the Study | 90 |
| 5.4.1 | Theoretical Implications  | 90 |
| 5.4.2 | Practical Implications    | 92 |

|                   |   |            |
|-------------------|---|------------|
| 5.5               | Limitations of the Study                        | 94         |
| 5.6               | Recommendations for Future Study                | 95         |
| 5.7               | Conclusion                                      | 95         |
| <b>REFERENCES</b> |   | <b>101</b> |
| <b>APPENDIX A</b> | <b>Corporate Social Reporting Checklist</b>     | <b>120</b> |
| <b>APPENDIX B</b> | <b>List of Selected Public Listed Companies</b> | <b>121</b> |
| <b>APPENDIX C</b> | <b>SPSS Outputs</b>                             | <b>124</b> |

## LIST OF TABLES

|  | <b>Page</b> |
|--|-------------|
| Table 3.1: Operationalization of variables   | 60          |
| Table 4.1: Sample's Composition by Types of Industry   | 65          |
| Table 4.2: Descriptive Statistics of companies' year 2011 corporate social reporting themes  | 65          |
| Table 4.3: Descriptive Statistics of companies' year 2013 corporate social reporting themes  | 65          |
| Table 4.4: Descriptive Statistics of companies' year 2011 and 2013 corporate social reporting length (CSRL)  | 65          |
| Table 4.5: Descriptive Statistics for ownership concentration (OC), board independence (BI), company's size (SIZE) in log form, company's profitability (ROE) in companies' year 2011 annual reports | 66          |
| Table 4.6: Descriptive Statistics for ownership concentration (OC), board independence (BI), company's size (SIZE) in log form, company's profitability (ROE) in companies' year 2013 annual reports | 66          |
| Table 4.7: Descriptive Statistics for foreign ownership (FO) and CEO duality (DUAL) variables, year 2011   | 67          |
| Table 4.8: Descriptive Statistics for foreign ownership (FO) and CEO duality (DUAL) variables, year 2013   | 67          |
| Table 4.9: Paired sample t-test for social reporting measures in PLCs in Malaysia  | 68          |
| Table 4.10: Correlation Matrix (year 2011)   | 70          |
| Table 4.11: Correlation Matrix (year 2013)   | 71          |
| Table 4.12: Regression Results (CSRL in year 2011 annual reports)  | 73          |
| Table 4.13: Regression Results (CSRL in year 2013 annual reports)  | 73          |
| Table 4.14: Collinearity Statistics (year 2011)  | 76          |
| Table 4.15: Collinearity Statistics (year 2013)  | 76          |
| Table 4.16: Summaries of the results for hypotheses testing  | 82          |

## LIST OF FIGURES

|   | <b>Page</b> |
|---|-------------|
| Figure 2.1: Stages of maturity of CSR activity    | 23          |
| Figure 2.2: A Model Process of CSR Implementation | 25          |
| Figure 2.3: Research Theoretical Framework        | 47          |
| Figure 4.1 P-P Plot (year 2011)                   | 79          |
| Figure 4.2 P-P Plot (year 2013)                   | 79          |

## ABSTRAK

Tujuan penyelidikan ini adalah untuk mengkaji kesan struktur pemilikan dan tadbir urus korporat pada tahap pelaporan sosial korporat dalam laporan tahunan syarikat tersenarai awam terpilih di Malaysia. Penyelidikan ini memberi tumpuan kepada maklumat laporan sosial korporat yang terkandung di dalam laporan tahunan tahun 2011 dan 2013 untuk 100 syarikat tersenarai di dalam Pasaran Utama Bursa Malaysia. Kepekatan pemilikan dan pemilikan asing digunakan sebagai proksi untuk struktur pemilikan. Pembolehubah di bawah tadbir urus korporat termasuk kebebasan lembaga pengarah dan CEO dualiti. 3 pembolehubah kawalan iaitu saiz syarikat, keuntungan syarikat dan jenis industri juga digunakan dalam penyelidikan ini. Pembolehubah bersandar, iaitu tahap laporan sosial korporat dalam laporan tahunan syarikat tersenarai awam di Malaysia, diukur dengan menggunakan analisis kandungan dari segi bilangan ayat. Analisis regresi berganda menunjukkan bahawa antara 4 pembolehubah bebas dan 3 pembolehubah kawalan yang diuji, hanya satu pembolehubah bebas (board independence) didapati mempunyai hubungan positif dengan tahap laporan sosial korporat dalam laporan tahunan syarikat untuk tahun 2011, manakala semua 4 pembolehubah bebas didapati tidak mempunyai hubungan dengan tahap pelaporan sosial korporat dalam laporan tahunan syarikat untuk tahun 2013. Antara ketiga-tiga pembolehubah kawalan, 2 pembolehubah kawalan (saiz syarikat dan keuntungan syarikat) didapati mempunyai hubungan positif yang signifikan dengan tahap pelaporan sosial korporat di dalam laporan tahunan syarikat untuk kedua-dua tahun 2011 dan 2013. Kajian ini berakhir dengan cadangan untuk memperbaiki amalan laporan yang sedia ada dan memberi cadangan untuk penyelidikan selanjutnya.

## **ABSTRACT**

The aim of this study is to examine the impact of ownership structure and corporate governance on the extent of corporate social reporting in the annual reports of selected public listed companies in Malaysia. This study focuses on the corporate social reporting information contained in the year 2011 and 2013 annual reports of 100 companies listed in the Main Market of Bursa Malaysia. Ownership concentration and foreign ownership are used as a proxy for ownership structure. Corporate governance characteristics include board independence and CEO duality. 3 control variables namely company's sizes, company's profitability and types of industry were used in this study. The dependent variable, the extent of corporate social reporting in annual reports of Malaysian public listed companies, is measured by content analysis in terms of number of sentences. The multiple regression analysis revealed that among 4 independent variables and 3 control variables tested in this study, only one of the independent variables (board independence) was found positively related to the extent of corporate social reporting in companies' year 2011 annual reports, while all 4 independent variables were found to have no relationship with the extent of corporate social reporting in companies' year 2013 annual reports. Among the three control variables, 2 control variables (company's sizes and company's profitability) were found to have significant positive relationship with the extent of corporate social reporting in both year 2011 and 2013 annual reports of the companies. The study ends with recommendations to improve the existing reporting practices and suggest areas for further research.

# **CHAPTER 1**

## **INTRODUCTION**

### **1.1 Introduction**

This chapter presents the main elements of this study. It starts with the discussions on the background of the study, in which consists of the overview on corporate social responsibility and adoption of corporate social reporting in Malaysia. It is then followed by problem statement, research questions and research objectives. Significant of study is also explained from two aspects including theoretical and practical contributions in this chapter. Lastly, definitions of key terms are provided at the end of this chapter.

### **1.2 Background of the Study**

The term of corporate social responsibility (CSR) has gained importance in business world as well as among media workers and academics from a wide range of discipline (Crowther and Aras, 2009). It indicates that although business corporations are primarily business oriented which run for the benefit of their shareholders, they also have a wide-ranging set of responsibilities to their stakeholders such as employees, customers, suppliers, communities as well as the society at large. In other words, businesses strive to balance the needs of society and environment against the need to make profit (Ihlen, Bartlett and May, 2011).

CSR is an emerging trend in developing countries such as Malaysia (Amran, Zain, Sulaiman, Sarker, and Ooi, 2013). Today, more and more companies in Malaysia are actively practicing CSR and the focus on CSR among companies in Malaysia has increased in line with international trends. The level of CSR-awareness and activities are really encouraging in Malaysia in recent years although some companies have CSR programs which date back many years, even decades. Due to Malaysian government played its role in ensuring the country remains competitive for both local as well as foreign investors, degree of awareness and commitment in CSR among Malaysian companies is not at an ignorance stage (Bryan Ching & Kim, 2011). The government's initiatives to further promote CSR among public listed companies (PLCs) is very encouraging in Malaysia (Said, Haron, Hj Zainuddin, Ibrahim and Saiful, 2008). For example, the launching of CSR Framework by Bursa Malaysia for PLCs and Silver Book for Government Linked Companies (GLCs) by Malaysian government in September 2006.

Besides that, there are also various speeches made by the members of the public through the authorities regarding the call for the adoption of good CSR leadership and practices. Prime Minister of Malaysia (The Honourable Dato' Seri Najib Tun Razak) in his keynote speech at the CSR Conference on 21 June 2004 mentioned that adoption of CSR helps to enhance companies' brand image, improve financial performance and increases the ability to attract and retain the best workplace that will have good influence to the market value of the company (Said et al., 2008). Again, the Prime Minister mentioned about CSR in the 2013 budget speech (Taha, 2013). The rise of CSR in Malaysia also closely linked

to the country's development plan. For example, Vision 2020 and the government's policy of enhancing standards of corporate governance and business ethics.

CSR is an activity the business attempts to negotiate its relationship to its stakeholders and the society at large (Ihlen et al., 2011). Thus, it includes mapping process and evaluation of stakeholders' demands, followed by the development and implementation of actions as well as policies to fulfill those demands. CSR communication is one of the way that business interacts with the stakeholders. One of the CSR communication tools is through nonfinancial reporting such as corporate social reporting or corporate social disclosure. Corporate social reporting is classified as voluntary disclosure as it is not essential of any financial disclosure regime, the Stock Exchange rules and regulations, accounting standards and the Companies Act in Malaysia. It delivers information to the society at large regarding companies' activities with community, environmental, employees, consumers as well as the companies' energy usage (Said et al., 2008).

Adoption of corporate social reporting is driven by few reasons (Saleh, Zulkifli and Muhamad, 2011; Grahovar, 2010). Saleh et al. (2011) investigated the impact of CSR on corporate financial performance among Malaysian's PLCs in an emerging market setting. Their study results of earlier estimation shown that there was a significant and positive relationship between CSR and corporate financial performance. The findings of their study proved that enhancing of financial performance is one of the drivers for practicing CSR among PLCs in Malaysia although the study results also indicated a limited evidence between CSR and corporate financial performance relationship in the long term.

According to Grahovar (2010), companies use CSR reporting to account for their responsibility, to establish a good reputation and to build a relationship with their stakeholders based on trust. The Malaysian former Prime Minister, Datuk Seri Abdullah Ahmad Badawi in the 2007 budget speech has emphasized the importance of CSR reporting by requiring companies to disclose their CSR activities in their annual reports (Said et al., 2008).

Malaysia as an industrialized country has experienced the presence of a larger number of giant local and multinational companies, which makes the importance for these companies to be responsible for their social and environmental impacts (Mustaffa & Rashidah, 2007). Hence, it shows that multinational companies' practices brought the concepts of CSR to Malaysia. According to Amran and Devi (2008), foreign influence is significant in the CSR development in Malaysia as Malaysia has high dependency on foreign investment. Besides that, majority of CSR consultants in Malaysia are foreign consultants such as CSR Asia and OWW Consulting. Although it is an encouraging development, it may not be adaptable to the needs and expectations of the local stakeholders.

There were literatures about the organization's internal factors and disclosure practices relationships over the years. In particular, ownership structure and corporate governance could be important determinants for CSR reporting since CSR reporting is affected by the choices, motives and values of the person who formulate and making decision in the organizations (Khan, Muttakin and Siddiqui, 2012). Transparency is one of the basic principles under corporate governance (Aras and Crowther, 2009). Adoption of

transparency would ensure that information is directly accessible and freely available to stakeholders who will be affected by such decision and their enforcement. Thus, corporate governance is a fundamental component for transparent disclosures, in which companies with good corporate governance will take good care of most CSR reporting issues (Sukcharoensin, 2012).

One of the drivers for CSR reporting in Malaysia is the introduction of Malaysia Code on Corporate Governance (Taha, 2013). Malaysian's code of corporate governance largely drew based on the recommendations of UK corporate governance, in which it focuses on the principles and best practice of corporate governance (Mallin, 2010). Majority of the PLCs in Malaysia are family-owned or controlled, with many developed from traditional family-owned enterprises. This may cause the issues of lack of responsive among the directors to the rights of minority shareholders. Thus, there is a need of good corporate governance to solve the issues and to protect the minority shareholders' rights.

Therefore, this research is intended to explore the potential determinants of CSR reporting among selected PLCs in Malaysia based on the prior literatures.

### **1.3 Problem Statement**

The private sector in Malaysia faced great pressures to accept social responsibility since the 1980s. It still has a long way to go although there are a lot of improvements in CSR disclosures. Studies have found that the CSR levels among Malaysian PLCs are still low. This might be caused by less intensive effort or motivation of top management of

companies in ensuring the companies play their part in disclosing CSR activities (Bryan Ching & Kim, 2011). According to Yusoff, Mohamad and Darus (2013), CSR awareness among companies in Malaysia in general can be observed as far lagging behind the global best practices benchmark. Yusoff et al (2013) found that precisely, a majority of the PLCs in Malaysia score low in CSR performance and disclosure practice. Abdul Razak and Mustapha (2013) stated that although the awareness level is high among managers and public demand for related information, there is still an uncertainty on what really motivates Malaysian companies to have disclosures of social and environment information. This is supported by Saleh, Zulkifli and Muhamad (2011) that stated that although Malaysian managers have high awareness level of CSR, this is not followed by CSR activities and disclosures.

Besides that, studies found that there are numerous of researches on CSR conducted in Western countries, but only little is concentrated on Asia, particularly in Malaysia. According to Ismail, Kassim, Amit and Rasdi (2014), CSR research seems to be limited in its coverage in Malaysia. Besides that, although Malaysia has experienced some significant improvements in regulatory changes as well as awareness programs toward CSR practices, a limited research has been carried out to evaluate CSR disclosures over time (Haniffa and Cooke, 2005; Esa and Mohd Ghazali, 2012).

Ownership structure is an important mechanism which plays a critical role in influencing a company's social responsibility information disclosure practices (Sukcharoensin, 2012). It still remains as an issue of concern in most of the emerging markets such as Malaysia,

where there are issues of concentrated ownership and companies are controlled by major owners, either family or state (Jalila and Devi, 2012). It is viewed that a company's ownership structure adequately reflects the influence of the majority shareholders on the decisions of information disclosures. Hence, a company's level of information disclosures are expected to vary systematically with the level of ownership composition of the company (Akhtaruddin and Haron, 2010). According to Taha (2013), whether the level of ownership concentration has impact or no impact at all on a company's level of voluntary disclosure, it is up to the decision of the company's high ownership. Furthermore, types of ownership also have influences on a company's level of information disclosures. According to Reverte (2009), the chances of managerial opportunism and conflict of interest between principal and agent are higher in a company with more dispersed ownership structure. Thus, higher level of disclosures are expected to reduce the issues of agency problem and information asymmetries in a dispersed ownership structure company. One of the examples of dispersed ownership structure is foreign ownership with separation of management and their owners geographically.

Corporate governance is another important mechanism which also has influence on a company's social responsibility information disclosure practices. According to Said, Zainuddin and Haron (2009), an effective corporate governance will ensure that shareholders' interests are looked after. In Malaysia, there are a lot of efforts by the government and private sectors to enhance the corporate governance standard. The introduction of Malaysia Code on Corporate Governance (MCCG) was one of the drivers for social reporting in Malaysia. Board independence is an example of good governance.

Existing of independent non-executive directors in a company is expected to have more impacts on a company's social disclosure practices (Haniffa and Cooke, 2005). While CEO duality is an example of weak governance. Existing of CEO duality is expected to have negative influences on a company's social disclosure practices as it represents a conflict of interest (Michelon and Parbonetti, 2008).

The above issues show that the CSR implementation and reporting among the PLCs in Malaysia still have spaces for improvement. Thus, this study intends to fill up the gap by examine the influences of ownership structure and corporate governance on corporate social reporting in year 2011 and 2013 annual reports of selected PLCs in Malaysia. Four determinants for corporate social reporting have been chosen under ownership structure and corporate governance, which are ownership concentration and foreign ownership under ownership structure; board independence and CEO duality under corporate governance. Control variables for this study are company's sizes, company's profitability and types of industry.

#### **1.4 Research Questions**

Below are the questions that this research attempts to answer:

- 1) What is the overall level and trend of corporate social reporting in annual reports of Malaysian public listed companies?

- 2) What is the relationship between ownership structure (ownership concentration and foreign ownership) and the extent of corporate social reporting in Malaysian public listed companies' annual reports?
- 3) What is the relationship between corporate governance (board independence and CEO duality) and the extent of corporate social reporting in Malaysian public listed companies' annual reports?
- 4) Can the extent of corporate social reporting among Malaysian public listed companies be linked to factors such as sizes of company, company's profitability and types of industry?

## **1.5 Research Objectives**

The objectives of this research are:

- 1) To examine the overall level and trend of corporate social reporting in annual reports of Malaysian public listed companies.
- 2) To study whether there is a relationship between ownership structure (ownership concentration and foreign ownership) and the extent of corporate social reporting in Malaysian public listed companies' annual reports.
- 3) To study whether there is a relationship between corporate governance (board independence and CEO duality) and the extent of corporate social reporting in Malaysian public listed companies' annual reports.

- 4) To evaluate whether factors such as sizes of company, company's profitability and types of industry linked to the extent of corporate social reporting among Malaysian public listed companies.

## **1.6 Significance of Study**

This section presents the theoretical and practical significance of this study.

### **1.6.1 Theoretical Significance**

A broader gap in literature will exist along with the evolving of corporate social reporting. However, the barrier to strengthen this gap is still remain unexplored. Thus, the outputs of this study may give contribution to the disclosure literatures by filling the knowledge gap.

This study attempts to extend upon existing literatures by addressing specific attributes of ownership structure, corporate governance and voluntary disclosures in the context of Malaysia. Findings from this study will increase the researchers' and students' understanding on CSR practices in Malaysia through demonstrating that extent of a company's corporate social reporting practices could be influenced by its characteristics such as ownership concentration, types of ownership, board independence, company's sizes and profitability. In other words, the findings from this study will help to extend the previous studies' findings in Malaysia.

## **1.6.2 Practical Significance**

As mentioned, CSR implementation and reporting among the PLCs in Malaysia still have more spaces for improvement. Thus, in terms of benefits to the companies, the findings from this study may provide insights as well as practical suggestions, in which Malaysian companies can implement to improve their CSR practices and reporting. It is also hope that the study will act as a motivation for the companies' management as well as the shareholders to integrate CSR approaches as one of their strategies to gain competitive advantage while fulfilling the society needs.

Besides that, studies found that there are numerous of researches on CSR conducted in Western countries, but there is scarce academic research in Asia, particularly in Malaysia (Ismail et al., 2014). This may cause limited understanding on practices of the CSR and corporate social reporting in this country. This study attempts to fill the existing gap and develop a practical guideline in assisting the companies to prepare better and more credible corporate social reports in their annual reports.

## **1.7 Definition of Key Terms**

**Corporate Social Responsibility** (CSR) is related to the three areas of a company's integrated responsibility namely environment, working conditions and human rights (Jutterstrom and Norberg, 2013). UNIDO - United Nations Industrial Development Organization (2014) defined corporate social responsibility as a company's achievement of "Triple Bottom Line" (a balance of economic, environmental and social imperatives),

while addressing the shareholders' and stakeholders' expectations at the same time. In other words, corporate social responsibility is a management concept in which social and environmental concerns are integrated in a company's business operations and relations with the stakeholders.

**Corporate social reporting** is a company's approach to report its activities, in which the report identifies, measures and reports on the company's socially or environmentally relevant behavior (Benn and Bolton, 2011). KPMG survey (2013) defined corporate social reporting as the means by which a business identifies both its potential risks and opportunities due to changing of social conditions and expectations. In other words, corporate social reporting is the process by which a company create long term value and resilience to environmental and social change through collecting and analyzing of data.

Encycogov - Encyclopedia of Corporate Governance (2014) defined **ownership structure** by the distribution of equity with respect to votes and capital as well as by the equity owners' identity.

**Ownership concentration** refers to the quantity of stock owned by individual investors and large-block shareholders (investors with at least 5 per cent of equity ownership within the company). Higher level of ownership concentration or more block shareholders indicate that shareholders have stronger monitoring power over a company's managerial decisions while lower level of ownership concentration or less block shareholders might

indicate weaker governance power over a company's managerial decisions (Financial Times, 2014).

**Foreign ownership** refers to a kind of ownership, in which there are certain percentage of foreign shareholders in the companies investing in the local market (Jalila and Devi, 2012).

**Corporate governance** refers to the clarification of a corporate perspective on the companies' purpose, on who owns them, who should manage them, and how to manage them (Benn and Bolton, 2011). In other words, it is about how a company is governed.

**Board Independence** refers to a state in which other than their directorship, majority of board members do not have any other relationships with the company (Rezaee, 2009).

**CEO Duality** indicates that the CEO of company holds both the chief executive and the chair of the board directors' position (Rezaee, 2009).

## **1.8 Organization of Chapters**

This study consists of five chapters. Chapter one provides an overview and background of this study. Chapter two is the backbone of this study, in which it consists of the discussion on the theoretical background and literature review on the independent variables, control variables and dependent variable. Discussion on theoretical framework and hypothesis development also included in this chapter. Chapter three presents the

research methodology of this study in terms of research design, sampling procedures, data collection method, measurement of variables and data analysis technique. Chapter four illustrates the results for the data collected using statistical analysis. Last chapter (chapter five) presents a discussion on the overall findings and implications of the research based on the study. This chapter also provides the limitation of the study as well as a suggestion for future research and conclusion to wrap up the study.

## **1.9 Chapter Summary**

This chapter has provided the discussions on the background of study, problem statement, research questions and research objectives as an opening of this study. It continued with the explanation of the contribution of study and definition of key terms. The next chapter would provide discussions with regard to two main independent variables (ownership structure and corporate governance) and corporate social reporting based on previous literature.

## **CHAPTER 2**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

This chapter provides the reviews of the underlying theories, rising of corporate social reporting, corporate social reporting in Malaysia and corporate governance in Malaysia. Then, it provides a review of the past literature on ownership structure variables (ownership concentration and foreign ownership) and corporate governance variables (board independence and CEO duality). Next, it shows the theoretical framework of this study and development of hypotheses. Finally, a summary of the chapter is provided at the end of this chapter.

#### **2.2 Theoretical Background**

There are three theories applied in this study, which are Stakeholder theory, Agency theory and Legitimacy theory. These three theories show how corporate social reports create pressure on the companies to be more responsible, with each of them varies in terms of refinement level in approaching the reporting issue.

##### **2.2.1 Stakeholder Theory**

Stakeholder theory is one of the widely used concepts in business and society literature in recent years (Jamali, 2008). Stakeholder theory takes account of a broader group of

constituents other than shareholders. The theory attempts to describe the nature of relationships between organizations and those with a 'stake' in the organizations' operations as well as the outcomes of business activity (Benn and Bolton, 2011). In other words, stakeholder theory aims to identify diverse groupings within society that the organizations have some responsibility to them. There are four categories of stakeholders – investors, suppliers, employees and customers acknowledged in the classical model of the theory of the firm (Figar and Figar, 2011). Apart from the four categories of stakeholders, Freeman (1984) gave a wider definition of stakeholders as any person or group that 'can influence or is influenced by the achievement of an organization's objectives' by introduced another four groups of stakeholders - governments, communities, politicians and trade associations (Benn and Bolton, 2011; Figar and Figar, 2011).

As mentioned, stakeholder theory focuses on the way a business manage its stakeholders. Thus, it has close relationship with the concept of corporate social responsibility (CSR) due to business is expected to carry out its responsibility towards society (Raupp, 2011). According to stakeholder theory, the decision makers need to reflect on the company's purposes, especially on the company's nonfinancial role (Raupp, 2011). In other words, stakeholder theory can resulting in well-supported decisions regarding of what kind of social responsibilities a firm should participate. Ullmann (1985) further developed concepts of stakeholder theory by Freeman (1984) with his three-dimensional framework (Elijido-Ten, 2013). With the three dimensions namely stakeholder power, strategic posture, and past and current economic performance, Ullmann suggested that social

reporting were used as a means by firms for stakeholders and the external environment relationship management (Elijido-Ten, 2013).

Stakeholder theory is prominent in researches exploring stakeholder powers in the social and environmental disclosure. Ali and Ridwan (2013) stated that different stakeholders will have different expectations from the company. Disclosing of social and environment information in conflicting situation will need to comply with the interest of powerful stakeholders such as government, shareholders, and international buyers etc. (Deegan and Jeffrey, 2006).

According to Amran et al. (2013), transparency issue is the most recent trend in business, in which companies needed to produce CSR reporting, that is also reflected as an action to empowering the stakeholders. Through CSR reporting, it will give a good stage for the communication of stakeholders' concerns and expectations to the companies for improvement of their CSR practices. Dincer (2011) suggested that the most used viewpoints explaining CSR reporting and disclosures are: 1) the importance of CSR information to shareholders, 2) the connection between social reporting and social performance, 3) the factors affecting companies' decisions to have disclosures of corporate social information. Dincer (2011) found that in order to achieve a long term and mutually beneficial relationship, the stakeholders need to be satisfied at optimum levels. Besides that, stakeholder power which come from the control over the resources critical to the organization, is important for the company. Dincer (2011) further stated that determinants for the social expectations and authorizations to carry out larger social

programs are the economic performance of the company and the key decision makers' attitude towards the stakeholders' demand.

### **2.2.2 Agency Theory**

One of the main theories affecting the development of corporate governance is agency theory (Benn and Bolton, 2011; Mallin, 2010). As corporate governance often linked to principal-agent relation, the theory identifies the important role of agency relationships management in corporate governance (Germanova, 2008). Agency theory looks into the principal-agent relationship, in which the principal hires the agent to perform on behalf the principal, the agent was expected to advance the principal's goals when both of them enter into the contracts. The primary agency relationships were the shareholders as the principal and the managers as the agent in the business corporation context (Benn and Bolton, 2011; Mallin, 2010; Germanova, 2008).

Agency theory also identifies the conflicting of interests among the principals and agents. The key issue is opportunism or self-interest is present in any principal-agent relationships through moral hazard and adverse selection (Figar and Figar, 2011). This is due to the reason that the principal do not have proper observation on the agent's effort. Furthermore, as contracts between the principal and agent are established in the situation which the issues of uncertainty and information asymmetry exist, the contractual relationships will have potential agency problem (Germanova, 2008). Jensen and Meckling's (1976) discussion on agency theory based on agency costs and ownership structure shows the central conflict of interest between managers and owners (Laiho,

2011). The main idea in Jensen and Meckling's model is that the issue of conflict of interest occur because the agents do not bear the full costs of their actions. In other words, agency problem occurred due to separation of ownership and control.

Agency costs tend to arise when agency problem occurs (Germanova, 2008). According to Laiho (2011), maximization of utility by self-interested manager will lead to problem of agency costs. However, David et al (1997) as cited in Benn and Bolton (2011) argue that agency costs can also arise from other factors such as lack of information or managerial skill deficits other than self-interest. Nesvadbová (2009) suggested that arising of agency costs are due to separation of ownership from control. Agency costs are mainly related to public listed companies than small family owned business because of separation of the owners from the companies' management.

Two main ways to alleviate agency problems are through transparency and monitoring (Healy and Palepu, 2001). Transparency mechanisms identify the need to have disclosure of relevant information in order for the shareholders to make evaluation about the management of the companies' resources (Sartawi et al., 2014). However, there is also a need for the implementation of monitoring mechanisms due to the connection between transparency and monitoring (Germanova, 2008). Establishment of corporate governance was to assure maximization of the firm value and as a form of protection to the investors (Navarro and Urquiza, 2010), while disclosures were a part of the monitoring mechanisms to mitigate lack of information and agency problems (Sharma, 2013). Hence, complementary mechanisms to mitigate agency problems consisted of voluntary

disclosure and corporate governance, in which adoption of more governance controls will lead to the increase of disclosure (Cerbioni and Parbonetti, 2007).

### **2.2.3 Legitimacy Theory**

Legitimacy theory is frequently used in the field of corporate social reporting (Grahovar, 2011). However, legitimacy theory has different viewpoints as compared to stakeholder theory and agency theory. As compared to agency theory, legitimacy theory suggests that companies need to fulfill not only the requirements of the owners or investors, companies also need to satisfy the expectations of the society. While for stakeholder theory, legitimacy theory further expands stakeholder theory by stressing that there is also a need for legitimization process engagement besides of the society's expectations on accountability (Fernando and Lawrence, 2014).

According to legitimacy theorists, an organization will do its best to legitimize its business in order to survive (Fernando and Lawrence, 2014). Dowling and Pfeffer (1975) brought legitimacy theory into mainstream of management by stated that companies seek for legitimacy by ensuring that their values system is in accordance with the society's value systems (Dobbs and Staden, 2009; Fernando and Lawrence, 2014; O'Donovan, 2000; Grahovar, 2011). Hence, management of legitimacy – desire of companies to manage changes in others' perceptions of the companies is the key element of legitimacy theory (O'Donovan, 2000).

Before legitimacy was brought into question due to some incidents, a company is considered legitimate. However, as the nature of legitimacy is based on social views which can and do change over time, any company's state as being legitimate or illegitimate is not static. Any sensitive social issues which are publicly linked to a company can change the social views and in turn change the legitimate state of the company (O'Donovan, 2000). According to Grahovar (2011), legitimacy gap may arise due to no correspondence between companies' activity and social values. The occurring of legitimacy gap may be due to reasons such as 1) social expectations remain the same whereas company changes 2) company's performance remains the same whereas social expectations change 3) both company and social views change but in opposite directions.

In order to reduce legitimacy gap and ensure the company's survival, a company will use CSR performance and disclosures as the strategies in the process of legitimization (Fernando and Lawrence, 2014), in which a company will receive legitimate advantages through the use of CSR reporting according to legitimacy theory. There are four tactics which a company might use to gain legitimacy (Dowling and Pfeffer (1975) and Lindblom (1994) as cited in Dobbs and Staden, 2009). The tactics are 1) informing the society about the actual changes in the company's behavior 2) changing the society's views without changing the company's actual behavior 3) manipulating the society's views through deflection of attention to another issue from an issue of concern 4) changing the external expectations of the company's behavior. All these tactics can be implemented through the use of voluntary disclosures.

Legitimacy literature, Yao, Wang and Song (2011) studied corporate social responsibility reporting (CSR) determinants in China. Their study reviewed and analyzed annual reports of over 800 listed companies on the Shanghai Stock Exchange in year 2008 and year 2009. One of their study's findings indicated that disclosure of environmental responsibility information tend to be higher among companies in environmentally sensitive industries. In Chu, Chatterjee and Brown (2013)'s study, legitimacy theory were tested through investigation of the factors that motivate greenhouse gas reporting among Chinese companies listed on Shanghai Stock Exchange. They analyzed annual reports and CSR reports of the top 100 A-share companies. Their study showed that although larger companies tend to have higher levels of greenhouse gas disclosures due to higher levels of carbon dioxide emissions, most of the companies tend to report only neutral and good news instead of negative news. Both of the literatures support the views that CSR reporting were used as a tool for companies to reduce legitimacy gap.

### **2.3 Corporate Social Reporting**

A company's practices of financial data measurement and reporting has long been seen as an essential element of corporate accountability. However, in relatively recent times, it is no longer restricted for a company to have financial reporting only, in which it also needs to have reporting of non-financial performance as well. Benn and Bolton (2011) defined corporate social reporting as an approach that a company has reporting of its activities, in which it involves identification, measurement and reporting on the company's socially or environmentally relevant behavior. According to Blowfield and Murray (2011), corporate social reporting is a part of corporate reporting process, in

which a company demonstrates its accountability to shareholders as well as other stakeholders. Figure 2.1 shows stages of CSR development as proposed by Crowther (2006). Corporate social reporting fall into stage 4 (measurement and reporting). For most organizations, stage 4 is the current stage of development, that organizations tend to have reports on different things as there are no standards of what to report at the moment (Crowther and Aras, 2009).

| <b>Stages of development</b> | <b>Dominant feature</b>   | <b>Typical activity</b>                                    | <b>Example</b>   |
|------------------------------|---------------------------|--|--|
| 1                            | Window dressing           | Redesigning corporate reporting                            | Changed wording and sections to reflect CSR language         |
| 2                            | Cost containment          | Re-engineering business processes                          | Energy efficiency programmes                                 |
| 3                            | Stakeholder engagement    | Balanced scorecard development                             | Customers/employees satisfaction surveys                     |
| 4                            | Measurement and reporting | Sophisticated tailored measures                            | CSR reports  |
| 5                            | Sustainability            | Defining sustainability: re-engineering processes          | Sustainability reporting                                     |
| 6                            | Transparency              | Concern for the supply chain: requiring CSR from suppliers | Human rights enforcement: eg. child labour                   |
| 7                            | Accountability            | Reconfiguration of the value chain                         | Relocating high value added activity in developing countries |

*Source: Crowther (2006)*

*Figure 2.1: Stages of maturity of CSR activity.*

### **2.3.1 Rising of Corporate Social Reporting**

There is an increasing number of companies in most of the countries chosen to have non-financial information reporting over the last thirty years or so, such as their stand on corporate responsibility and sustainability. The term “social accounting” has gained prominent due to this emerging trend. As defined by Blowfield and Murray (2011), social accounting is a company’s practice of accounting for non-financial parts of its performance, in which it also refers to a company’s action of extending its accountability to a broader range of stakeholders within the society. As an important component of social accounting, corporate social reporting has earned concerns since 1970s (Noronha, 2014), as prompted by several issues such as company collapses and scandals. Also due to establishment of new laws in 1970s in different countries, that companies were required to have reporting on their performance aspects such as employment practices, impacts of companies’ operations on the environment, consumer policies, and the like (Blowfield and Murray, 2011).

Followed by the emergence of corporate social reporting in 1970s, rapid globalization during 1980s and 1990s has urged companies to aware that their operations and activities have great influences on local as well as global context. A very clear upward trend in social reporting started to arise in the late 1990s, despite of the varying patterns in corporate social and environmental reporting. There are two trends which arise in 1990s that still continue today. First, separation of the environmental aspects from the social aspects of company performance. As compared to the reports in 1970s, the reports in