

**THE RELATIONSHIP BETWEEN CORPORATE
GOVERNANCE MECHANISMS AND COMPANY
ATTRIBUTES AND ACCOUNTING CONSERVATISM OF
JORDANIAN LISTED COMPANIES**

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**THE RELATIONSHIP BETWEEN CORPORATE GOVERNANCE
MECHANISMS AND COMPANY ATTRIBUTES AND ACCOUNTING
CONSERVATISM OF JORDANIAN LISTED COMPANIES**

By

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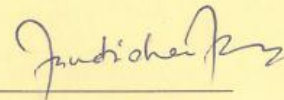
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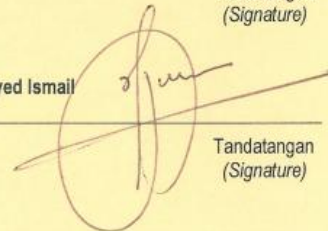
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ABSTRACT

This study examines the relationship between the corporate governance mechanisms related to the ownership structure, board of directors, audit committee and auditor quality along with company attributes and the accounting conservatism of Jordanian listed companies. The theoretical foundation of such a relationship was provided by five comprehensive theories which are the agency theory, the positive accounting theory, the resource dependence theory, stewardship and the signaling theory. The data were obtained from the annual reports of 348 Jordanian companies from 2009 to 2011. Upon using the multiple regression analysis, the results show that the relationship between the corporate governance mechanisms and accounting conservatism was somewhat varied. Fifteen hypotheses were developed in this study. Seven of them were significant while eight were not. For ownership structure, institutional and foreign ownership were significant while family and managerial ownership were not statistically significant. Board independence, financial expertise and board tenure were significant, while board size, CEO and multiple directorships were not significant due to the higher level of P-value compared to 0.05. On the other hand, audit committee and auditor independence were statistically significant to conservatism, while auditor brand name, company size and debt contract were reported to be negatively and not significantly related to conservatism. These results indicate that corporate governance plays a vital role in enhancing the level of conservatism and reducing agency conflict. Further, regulator bodies in Jordan should increase the effectiveness of corporate governance in Jordanian companies in order to enhance the quality of financial reports. In addition, this study opens up avenues for more studies on accounting conservatism not only in Jordan, but also in other countries where this area of study is lacking. Furthermore, it opens up opportunities and provides avenues for more in-depth research related to the quality of financial reports.

Keywords: corporate governance, accounting conservatism, board of directors, accrual-based, Jordan

ABSTRAK

Kajian ini mengkaji hubungan antara mekanisme tadbir urus korporat yang berkaitan dengan struktur pemilikan, lembaga pengarah, jawatankuasa audit dan kualiti juruaudit serta atribut syarikat dan konservatisme perakaunan syarikat-syarikat yang tersenarai di Jordan. Asas teori dalam perhubungan tersebut telah disediakan berdasarkan lima teori yang komprehensif iaitu teori agensi, teori perakaunan positif, teori pergantungan sumber, dan teori pengawasan dan pengisyaratan. Data diperolehi daripada laporan tahunan 348 buah syarikat di Jordan dalam tempoh 2009-2011. Dalam analisis regresi berganda, keputusan menunjukkan bahawa hubungan di antara mekanisme tadbir urus korporat dan konservatisme perakaunan adalah agak berbeza-beza. Lima belas hipotesis telah dibangunkan dalam kajian ini. Tujuh daripadanya adalah signifikan manakala lapan lagi didapati tidak signifikan. Bagi struktur pemilikan, pemilikan institusi dan pemilikan asing adalah signifikan manakala pemilikan keluarga dan pemilikan pengurusan didapati tidak signifikan secara statistik. Kebebasan lembaga pengarah, kepakaran kewangan dan tempoh lantikan lembaga pengarah adalah signifikan manakala saiz lembaga pengarah, Ketua Pegawai Eksekutif dan kepelbagaian jawatan pengarah didapati tidak signifikan kerana nilai P berada pada tahap yang lebih tinggi berbanding 0.05. Sebaliknya, jawatankuasa audit dan kebebasan juruaudit secara statistiknya signifikan kepada konservatisme, manakala penjenamaan juruaudit, saiz syarikat dan kontrak hutang dilaporkan negatif dan tidak signifikan dengan konservatisme. Keputusan ini menunjukkan bahawa tadbir urus korporat memainkan peranan penting dalam meningkatkan tahap konservatisme dan mengurangkan konflik agensi. Tambahan lagi, badan-badan pengawal selia di Jordan perlu meningkatkan keberkesanan tadbir urus korporat dalam syarikat-syarikat di negara tersebut bagi meningkatkan kualiti laporan kewangan. Di samping itu, kajian ini membuka ruang kepada lebih banyak kajian tentang konservatisme perakaunan bukan sahaja di Jordan, tetapi juga di negara-negara lain yang kekurangan kajian dalam bidang ini. Tambahan pula, kajian ini membuka peluang dan menyediakan ruang bagi penyelidikan yang lebih mendalam berkaitan kualiti laporan kewangan.

Kata kunci: tadbir urus korporat, konservatisme perakaunan, lembaga pengarah, asas keakruan, Jordan

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TABLE OF CONTENTS

TITLE	PAGE
TITLE PAGE	i
CERTIFICATION OF THESIS WORK.....	ii
PERMISSION TO USE.....	iv
ABSTRACT.....	v
ABSTRAK	vi
ACKNOWLEDGEMENT.....	vii
TABLE OF CONTENTS	ix
LIST OF TABLES	xviii
LIST OF FIGURES	xx
LIST OF ABBREVIATIONS	xxi
LIST OF APPENDICES	xxii
CHAPTER ONE:INTRODUCTION	1
1.0 Background of Study	1
1.1 Motivation for this Study	5
1.2 Problem Statement	7
1.3 Research Questions.....	11
1.4 Research Objectives.....	11
1.5 Significance of the Study	12

1.6 Scope of Study	18
1.7 Definitions of Terms	19
1.8 Organization of Study	20
CHAPTER TWO:LITERATURE REVIEW	22
2.0 Introduction.....	22
2.1 Accounting Conservatism.....	22
2.1.1 Definitions of Accounting Conservatism.....	23
2.1.2 The Importance of Conservatism	26
2.1.3 Theories of Conservatism.....	28
2.1.4 Accounting Conservatism Measurements	35
2.2 Overview of Corporate Governance	46
2.3 Overview of Jordan.....	56
2.3.1 Corporate Governance in Jordan.....	58
2.3.2 Empirical Evidences of Corporate Governance in Jordan	67
2.4 Underlying Theories	73
2.4.1 Agency Theory.....	73
2.4.2 Positive Accounting Theory.....	78
2.4.3 Resource Dependence Theory.....	78
2.4.4 Stewardship Theory.....	81

2.4.5 Signaling Theory	82
2.5 Corporate Governance and Accounting Conservatism.....	83
2.5.1 Ownership Structure.....	83
2.5.1.1 Institutional Ownership	84
2.5.1.2 Foreign Ownership	86
2.5.1.3 Family Ownership	88
2.5.1.4 Managerial Ownership	91
2.5.2 Board Characteristics	98
2.5.2.1 Independence.....	99
2.5.2.3 CEO Duality.....	110
2.5.2.4 Financial Expertise.....	115
2.5.2.5 Tenure	117
2.5.2.6 Multiple Directorships	120
2.5.3 Audit Committee	126
2.5.4 Auditor Quality.....	135
2.5.4.1 Independence.....	138
2.5.4.2 Brand Name	141
2.5.5. Company Attributes	146
2.5.5.1 Company Size	146
2.5.5.2 Debt Contracts.....	149

2.6 Chapter Summary	156
CHAPTER THREE: RESEARCH FRAMEWORK AND METHODOLOGY	157
3.0 Introduction.....	157
3.1 Research Framework	157
3.2 Hypotheses Development	161
3.2.1 Ownership Structure	161
3.2.1.1 Institutional Ownership	161
3.2.1.2 Foreign Ownership	162
3.2.1.3 Family Ownership	163
3.2.1.4 Managerial Ownership	165
3.2.2 Board Characteristics	166
3.2.2.1 Board Independence	167
3.2.2.2 Board Size	168
3.2.2.3 CEO Duality	169
3.2.2.4 Board Skill (Financial Expertise, Tenure, Multiple Directorships) ...	170
3.2.3 Audit Committee	173
3.2.4 Auditor Quality.....	175
3.2.4.1 Independence	175
3.2.4.2 Brand Name	176
3.2.5 Company Attributes	177

3.2.5.1 Company Size.....	178
3.2.5.2 Debt Contract.....	178
3.3 Methodology.....	180
3.3.1 Research Design.....	180
3.3.2 Sample and Data Collection.....	180
3.3.2.1 Sample.....	180
3.3.2.2 Data Collection.....	181
3.3.3 Unit of Analysis.....	182
3.3.4 Method of Data Analysis.....	182
3.3.4.1 Descriptive Analysis.....	183
3.3.4.2 Inferential Analysis.....	183
3.3.4.2.1 Correlation Analysis.....	183
3.3.4.2.2 Multivariate Analysis.....	183
3.4 Operation Definitions and Measurement of Variables.....	185
3.4.1 Corporate Governance.....	185
3.4.1.1 Ownership Structure.....	185
3.4.1.1.1 Institutional Ownership.....	186
3.4.1.1.2 Foreign Ownership.....	186
3.4.1.1.3 Family Ownership.....	186
3.4.1.1.4 Managerial Ownership.....	186

3.4.1.2 Board Characteristics.....	187
3.4.1.2.1 Independence	187
3.4.1.2.2 Size.....	187
3.4.1.2.3 CEO Duality.....	188
3.4.1.2.4 Financial Expertise.....	188
3.4.1.2.5 Tenure	188
3.4.1.2.6 Multiple Directorships	189
3.4.1.3 Audit Committee	189
3.4.1.4 Auditor Quality.....	189
3.4.1.4.1 Auditor Independency.....	189
3.4.1.4.2 Brand Name	190
3.4.1.5 Company Attributes.....	190
3.4.1.5.1 Company Size	191
3.4.1.5.2 Debt Contract	191
3.4.2 Measurements of Accounting Conservatism.....	191
3.4.2.1 Accrual-Based Conservatism (ACCR).....	192
3.5 Chapter Summary	193
CHAPTER FOUR: ANALYSIS AND FINDINGS	195
4.0 Introduction.....	195
4.1 Regression Assumptions.....	195

4.1.1 Outliers Detecting.....	196
4.1.2 Normality.....	197
4.1.3 Linearity	199
4.1.4 Multicollinearity.....	200
4.1.5 Autocorrelation.....	203
4.1.6 Heteroscedasticity	204
4.2 Descriptive Statistics.....	205
4.3 Correlation Analysis	212
4.4 Multiple Regression Analysis.....	213
4.5 Hypotheses Testing.....	216
4.5.1 Ownership Structure and Accounting Conservatism	218
4.5.2 Board Characteristics and Accounting Conservatism	220
4.5.3 Audit Committee and Accounting Conservatism.....	224
4.5.4 Auditor Quality and Accounting Conservatism	224
4.5.5 Company Attributes and Accounting Conservatism	226
4.6 Summary of Hypotheses Testing	229
4.7 Robustness Tests.....	230
4.7.1 Institutional Ownership Measured Using Binary Variables.....	231
4.7.2 Managerial Ownership Measured Using Binary Variables.....	234
4.7.3 Board Independence Measured Using Binary Variables	236

4.7.4 Board Size Measured Using Binary Variables	237
4.7.5 Company Size Measured Using Binary Variables	239
4.7.6 Debt Contract Measured Using Binary Variables	240
4.8 Chapter Summary	242
CHAPTER FIVE:DISCUSSION AND CONCLUSION.....	243
5.0 Introduction.....	243
5.1 Overview of the Study	243
5.2 Discussions of Hypotheses	245
5.2.1 Ownership Structure.....	246
5.2.1.1 Institutional Ownership	246
5.2.1.2 Foreign Ownership	246
5.2.1.3 Family Ownership	248
5.2.1.4 Managerial Ownership	249
5.2.2 Board Characteristics	250
5.2.2.1 Independence	250
5.2.2.2 Size	251
5.2.2.3 CEO Duality	252
5.2.2.4 Board Financial Expertise, Tenure and Multiple Directorships	253
5.2.3 Audit Committee	254
5.2.4 Auditor Quality.....	254

5.2.4.1 Auditor Independence.....	254
5.2.4.2 Auditor Brand Name	255
5.2.5 Company Attributes	256
5.2.5.1 Company Size.....	256
5.2.5.2 Debt Contract.....	256
5.3 Implications of the Study	257
5.4 Limitations of this Study.....	263
5.5 Suggestions for Future Research	265
5.6 Conclusion	267
REFERENCES.....	268
APPENDICES.....	330

LIST OF TABLES

Table		Page
2.1	Summary of Major Previous Studies that Examining Ownership Strictures and Accounting Conservatism	95
2.2	Summary of Major Previous Studies that Examining Board Characteristics and Accounting Conservatism	123
2.3	Summary of Major Previous Studies that Examining Audit Committee and Accounting Conservatism	132
2.4	Summary of Major Previous Studies that Examining Auditor Quality and Accounting Conservatism	144
2.5	Summary of Major Previous Studies that Examining Company Attributes and Accounting Conservatism	152
4.1	Mahalanobis Distance Test and the Value of Cook's Distance	197
4.2	Normality Test	198
4.3	Pearson Correlation Coefficients	202
4.4	Testing for Multicollinearity	203
4.5	Autocorrelation Test	204
4.6	Descriptive statistics	211
4.7	Variables Description and Expected Direction for the research Model	214
4.8	OLS Regression Result	217
4.9	Summary of Regression Analysis of Study Model	227
4.10	Results Summary of Hypothesis 1 to Hypothesis 5	229
4.11	Variables Description and Expected Direction for the research Model	231
4.12	Multiple Regression Results: Institutional Ownership Measured Using Binary Variables	233

4.13	Multiple Regression Results: Managerial Ownership Measured Using Binary Variables	235
4.14	Multiple Regression Results: Board Independence Measured Using Binary Variables	236
4.15	Multiple Regression Results: Board Size Measured Using Binary Variables	238
4.16	Multiple Regression Results: Company Size Measured Using Binary Variables	239
4.17	Multiple Regression Results: Debt Contract Measured Using Binary Variables	241

LIST OF FIGURES

Figure		Page
3.1	Framework of the study	160
4.1	Histogram	199
4.2	Normal P-P Plot of Regression Stand (DV: Accrual)	200
4.3	Scatter Plot (DV: Accrual)	205

LIST OF ABBREVIATIONS

AC	Audit Committee
ASE	Amman Stock Exchange
BCBS	Basle Committee on Banking Supervision
CEO	Chief Executive Officer
IFRS	International Financial Reporting Standards
JACPA	Jordanian Association of Public Accountants
JSC	Jordan Securities Commission
OECD	Organization for Economic Cooperation and Development
OLS	Ordinary Least Square
PCAOB	Public Company Accounting Oversight Board
SOX	Sarbanes Oxley
VIF	Variance Inflation Factors

LIST OF APPENDICES

Appendix	Page
Appendix A Definitions for the Abbreviations of the Initial Model	331

CHAPTER ONE

INTRODUCTION

1.0 Background of Study

Accounting conservatism is considered as the most effective principle underpinning accounting valuation and has a lengthy historical application to financial accounting exceeding, five centuries (Basu, 1997; Sterling, 1970). Nonetheless, the concept of conservatism faces significant criticism by academics, capital market regulators and standards-setters. Critics such as LaFond and Watts (2008) argued that conservatism leads to understate of net assets in the present period leading to overstate of earnings in the future periods due to the understate of future expenses. Despite heavy criticism, previous empirical studies reported that conservatism has increased during the past decades (Givoly & Hay, 2002; Lobo & Zhou, 2006). This suggests critics may overlook major benefits of conservatism. The lengthy persistence and resilience to criticism of accounting conservatism are intriguing empirical impasses producing a number of significant unanswered questions.

Previous studies have defined conservatism by the aphorism “anticipate no profit, but anticipates all losses” (Watts, 2003a). Basu (1997) defined accounting conservatism as earnings asymmetric timeliness that requires high level of verification for recognizing of good news as an economic profit than recognizing bad news as an economic loss. Givoly and Hayn (2000) defined accounting conservatism as a choice between the principles of accounting that lead to decrease the cumulative earnings by slower recognition of

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APPENDICES

APPENDIX A

Definitions for the Abbreviations of the Initial Model

Definitions for the Abbreviations of the Initial Model

Symbol	Variables	Description and Measurement	Predicted Direction	Relevant Hypotheses
	Dependent Variable			
ACCR	Accounting Conservatism	ACCR= [(income +depreciation expenses– operating cash flows)] ÷Total assets. ACCR = (Accruals / 3 years) X (-1).		
Symbol	Variables	Description and Measurement	Predicted Direction	Relevant Hypotheses
	Ownership Structure			
OWINST	Institutional Ownership	Institutional ownership measured as ratio, “by dividing the number of shares held by the institutions to the total number of firm's shares.	+	H1a
OWFOREI	Foreign Ownership	Foreign ownership measured as the percentage of shares held by foreigners to total number of firm's shares.	+	H1b
OWFAM	Family Ownership	Family ownership measured as the percentage of shares held by families to total number of firm's shares.	+	H1c
OWMAN	Managerial Ownership	Managerial ownership calculated as the percentage of shares held by directors on the board to the total number of firm's shares.	–	H1d
BIND	Independence	Board independence measured proportion of independent directors to total directors on board.	+	H2a
BSIZ	Size	Board size is the natural logarithm of total number of board members.	+	H2b
BCEO	CEO Duality	Dummy variable = 1 if CEO/Chairman roles combine;0 if separate.	+	H2c
BFI	Financial Expertise	Percentage of board members with financial expertise to total directors on board.	+	H2d
BTEN	Tenure	Average years the independent directors served on the firm’s board.	+	H2e

Symbol	Variables	Description and Measurement	Predicted Direction	Relevant Hypotheses
BMULT	Multiple Directorships	Percentage of board members with more than two outside directorships to total directors on board.	+	H2f
	Audit Committee	Dummy variable = 1 if company has audit committee and 0 otherwise.	+	H3
ACIND	Audit committee independence	The proportion of independent members in the audit committee		
ACFE	Financial expertise	The total number of audit committee Members with financial expertise divided by the total number of audit committee members.		
ACD	Diligence	Diligence, awarding a score of 1 if the audit committee meets at least four times or more in financial year; and 0 otherwise		
	Auditor Quality			
AUIND	Independence	Measured by non-audit fee/total fee ratio.	+	H4a
AUBRAN	Brand Name	Dummy variable = 1 if the external auditor engaged by Big 4 firm, and 0 otherwise.	+	H4b
	Company Attributes			
CSIZE	Size	Company size measured by log of total assets.	+	H5a
CDEBT	Debt Contract	Noncurrent liabilities/total assets.	+	H5b