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Corporate Governance Transparency in Small Listed Entities: The Case of Malta*

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Abstract:

Purpose: The objectives of this study are to examine whether a lack of transparency is a common corporate governance feature of listed entities (“MLEs”) in the small European state of Malta and, if so, to assess the possible implications of such a stance.

Design/Approach/Methodology: In order to achieve such research objectives, a predominantly qualitative mixed methodology was adopted. This involved carrying out thirteen semi-structured interviews with MLE and audit firm representatives, these being supported by an examination of the corporate governance statements of MLEs for the 2015-2017 periods.

Findings: Results show a general lack of transparency in corporate governance reporting, with a common MLE tendency to comply only at a superficial level with the principles of good corporate governance and thus to often fail to sustain an appropriate level of transparency and governance structures.

Practical Implications: It is recommended to increase company and shareholder awareness so as to help towards further improving current attitudes.

Originality/Value: The study is particularly envisaged to contribute towards encouraging stakeholders in small-state contexts to reassess their current perspectives towards corporate transparency.

Keywords: Corporate Governance, transparency, confidentiality, small European state.

JEL code: G34.

Paper type: Research article.

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1. Introduction

As a consequence of the global financial crisis and the demise of several well-known businesses such as Enron and Worldcom, for which frail corporate governance (CG) has been considered a causal element, a global awareness regarding efficient and effective CG has been revitalized (Khancel, 2007). Generally, CG is defined as “the system by which companies are directed and controlled” (Cadbury Report, 1992, p. 14). CG sets forth the relationship between the shareholders who own the entity, having an honest interest in the doings of the business, and the directors who are in charge of the entity’s assets and also mitigates the conflicts of interest which may arise between the two (Cadbury Report, 1992). CG is a mechanism which protects shareholder’s interest by virtue of proper practices and structures.

Calder (2008) claims that a sound CG framework is one which must evolve around three essential aspects of accountability, shareholder rights and transparency. In fact, the latter is nowadays generally considered to be the tool which mitigates distressed relationships between a company and its stakeholders through its perceived ability to create, maintain and repair trust issues (Fombrun and Rindova, 2000). In this context, the EU’s Transparency Directive specifies that the disclosure of proper information maintains investor confidence, market efficiency and investor protection (European Parliament and the Council of the European Union, 2013). Additionally, all existing CG frameworks adopt the comply-or-explain approach (CoE) except for the United States framework which adopts a rules-based approach. In this regard, Inwinkl *et al.* (2014) argues that the application of the CoE approach can only be successful if supported by high end and transparent reporting.

Notwithstanding the heightened awareness and improvement in CG during the last two decades, it is evident that several companies are still finding it challenging to entrench CG in their company culture and they tend to comply simply with the letter of the law and not with its spirit (Arcot *et al.*, 2010). Non-compliance with CG codes is still considered to be a persistent matter. Moreover, some companies are somewhat reluctant to provide adequate and substantial disclosure. They tend to cling to corporate confidentiality whilst hampering Corporate Transparency (CT). These concerns are also apparent in Malta. Both Azzopardi (2012) and Baldacchino *et al.* (2020) highlight the fact that MLEs do not provide adequate explanations as a justification for their non-compliance. Azzopardi (2012), also proves that the evaluation of the board of company is one of the weakest aspects of CG with companies claiming the unnecessary of such evaluation. Additionally, Bezzina *et al.* (2014) identified the disclosures of remuneration packages as one of the aspects of non-adherence by Maltese listed entities (MLEs) and areas of potential improvement.

In Malta, a number of recent studies addressing CG have been carried out. However, none of these has considered the possible linkage between CG and CT. Thus, the main objectives of this paper are to examine whether a lack of corporate

transparency is a relevant feature in the corporate governance of MLEs and, if so, to assess the possible reasons for such a corporate stance and its implications.

2. Literature Review

2.1 Corporate Governance in Malta

The emergence of CG in Malta traces back to 2001, when the Working Group set up by the Malta Stock Exchange was asked to give advice on matters relating to CG. One of the main recommendations was to establish a code of CG practices in order to enrich the quality as well as the transparency of corporate management. In response, the MFSA drafted the 'Code of Good Corporate Governance' and this has since then formed part of the Listing Rules (2018).

The proposed code was then revised in 2005 by the MFSA as a consequence of the international pressures on the concept of CG. The MFSA made some of its provisions mandatory such as the formation of an audit committee, the separation between the roles of the chairman and the chief executive and the inclusion of non-executive directors (NEDs) on the board (MFSA, 2005). Another revision was conducted in 2010 renaming the code as 'The Code of Principles of Good Corporate Governance for Listed Entities' (the Code), and dividing the Code into 12 main principles, supporting principles and provisions. The applicability of this Code was extended to include all listed companies, banks, trusts, finance companies but excluding collective investment schemes (Grima *et al.*, 2017; Grima and Thalassinos, 2020; Thalassinos *et al.*, 2015a; 2015b).

It is reasonable to say that the Code and all revisions followed developments that occurred within the United Kingdom (UK). Similar to the UK's Codes, the Code is based on the CoE approach, where entities are encouraged to comply with all the principles but if unable to do so an explanation is required (Bezzina *et al.*, 2014). In fact, the Code (2011) requires MLEs to include a CG statement (CGS) in the annual financial statements, which shall include two sections, the first section focusing on compliance with the Code and the mechanisms undertaken, whilst the second section addressing non-compliance. Moreover, the CGS shall be validated by auditors.

2.2 The Comply-or-Explain Approach

Inwinkl *et al.* (2014) posited that at the heart of the EU's CG framework, which was introduced by Directive 2006/46/EC is the CoE approach. As a result of the transposition of EU directives into national law, the approach of CoE became evident in all EU member states as an obligatory disclosure rule of every CG code (Caspar, 2016). The CoE approach was originally put forward by the Cadbury Report of 1992 in the UK, which provided the first CG code and since then acted as an international benchmark of such practice (Keay, 2014). The purpose of the CoE

approach is to invite and encourage companies to comply with all the principles of the applicable CG code, but whenever they are not able to abide by certain provisions for one reason or another, companies are not expected to comply (Seidl *et al.*, 2013). In fact, the FRC (2018) suggests that a deviation from complying with a provision could be reasonable in specific settings based on a series of factors such as the size, history, complexity and structure of a company. The CoE has been designed to allow some flexibility to companies and to challenge the rigid hard law, acknowledged in the rigorous ‘one-size-fits-all’ approach, which seems unrealistic for the practice of CG (Kraakman *et al.*, 2004).

As mentioned, Inwinkl *et al.* (2014) claims that the application of the CoE approach can only be fruitful if maintained by blue-ribbon reporting, where non-compliant companies are required to provide sufficient and appropriate explanation for why they failed to conform with the provisions of the code. In this regard, Inwinkl *et al.* (2014) suggest that a proper explanation should provide (1) acceptable information about the areas of non-compliance, (2) an appropriate rationale for the non-conformity and (3) the actions the company is taking to solve the departure. Thus, the CoE approach contributes to increasing transparency and disclosure of how a company is governed (Sergakis, 2015). It also intends to “empower shareholders to make an informed evaluation as to whether non-compliance is justified, given the company’s circumstance” (Keay, 2014) as ultimately the primary objective of CG is the protection of the investor’s interest.

Having said that, Keay (2014) also points out that shareholders tend to lack participation with respect to the limited monitoring of the CoE approach and stick to the traditional channels of information such as the annual financial statements for decision making. On the other hand, studies show that certain companies are taking advantage of the flexibility of the approach by complying superficially with the set principles. Thus, both the unchallenging investor and the exploiting company are undermining the primary objective of the CoE principle.

2.5 Corporate Transparency

Over the years, a number of varying definitions for the concept of CT have been put forward by several researchers. For example, finance and accounting researchers define the concept as “the availability of specific information to those outside publicly traded firms” (Bushman *et al.*, 2004) and researchers of organisational behaviour describe it as “leader behaviors that are aimed at promoting trust through disclosures that include openly sharing information and expressions of the leader’s true thoughts and feelings” (Walumbwa *et al.*, 2011), thus indicating that the concept of transparency does not exist or operate merely in a particular field.

Despite the various approaches to explain the concept, it appears that there are some common surrounding aspects, firstly being that CT relates to information. In this regard, Fung (2014) argues that information is vital for investors to be able to make

well-informed judgments of the risk and rewards of a particular investment. Secondly, CT is deemed to be a perception of the information being received, such a perception can be highly influenced by an entity's information sharing performance (Schnackenberg and Tomilson, 2016) and thirdly is the quality of information made available (Bushman *et al.*, 2004).

Schnackenberg and Tomilson (2016) mentioned three distinct dimensions which contribute to the general perception of CT by improving stakeholder confidence in the quality of information being received, namely (1) disclosures, (2) clarity and (3) accuracy. Haely and Palepu (2001) define corporate disclosures as a means of communicating company performance and governance to the outside stakeholders. The concept of corporate disclosures entails information to be freely and openly distributed in order to be treated as transparent while warranting the availability of relevant information thereof.

Farvaque *et al.* (2011) mention two important distinctions. The first is that between financial and non-financial corporate disclosures. The former generally relates to information about the financial performance and position of a company included in the financial statements whereas the latter mainly involves information about the company's social and CG. The second distinction is that between mandatory and voluntary disclosures. Mandatory disclosures relate to what is required by laws and regulations while voluntary disclosure is generally supplementary information, which is even more expected in today's contemporary world.

A company can increase its level of disclosure by disclosing further volumes of information in more frequent intervals through the use of open information systems on the one hand or it can reduce it through keeping secrets (Schnackenberg and Tomilson, 2014). Most of the time, secrets are linked with negative connotations; however, there are times where secrets are considered to be legitimate and ethical within the parameters of confidentiality and necessary for sustaining the competitive advantage of a firm, such as product ingredients. Nonetheless, the intended concealment of information from external stakeholders is considered both illegitimate and unethical (Anand and Rosen, 2008; Bennis and O'Toole, 2009). Another pivotal dimension of CT is clarity.

Schnackenberg and Tomilson (2014) define clarity as the degree of rationality and directness of the information shared by organisations. In this context, Winkler (2000) explained that companies are expected to deliver clearer information so as to reflect transparency while Street and Meister (2004) emphasised that such information must be understandable. Wolfe and Putler (2002) explained that companies could influence and communicate more clearly with stakeholders by delivering the message which is fit for their knowledge, interests and requirements, avoiding any unnecessary ambiguous linguistics and formality. Lastly, accuracy is considered to have an essential role in enhancing CT and preventing corporate

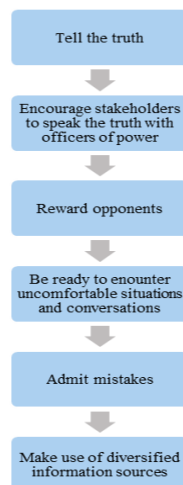
scandals (Akhigbe and Martin, 2006). Information is required to be valid (Bushman *et al.*, 2004) and reliable (Williams, 2005) in order to be transparent.

Given the volatility of today's financial markets and the increase in scrutiny, transparency is no longer viewed as a luxury but has become a necessity in a system of governance (Borgia, 2005). Borgia (2005) continues to explain that CT may not lead to instant corporate success, but the absence of which may be a burden on the company's performance and reputation and yet some companies may choose to set aside such requirements. In this regard, Bennis and O'Toole (2009) suggested a process involving a number of stages or practices that a company should incorporate in its CG framework in order to develop the concept of CT and improve the management of the firm. Figure 1 provides an illustration of this process.

3. Research Methodology

In order to achieve the objectives of this research study, a predominantly qualitative mixed methodology was adopted. Primary data was obtained from two different sources. Initially, semi-structured face-to-face interviewees were carried out. Interview questions were directed towards two interviewee categories: (1) MLEs representatives and (2) Big 4 audit firms representatives, with the aim of obtaining varying views from different professionals. In total, thirteen interviews were conducted, nine of which were carried out with MLEs representatives and the remaining four with representatives of audit firm. The interview schedule prepared for the purpose of this study comprised a combination of closed-ended and open-ended questions. It was aimed towards equity MLCs and Corporate Governance Experts ('CGEs'). A five-point Likert scale, with '1' being strongly disagree and '5' being strongly agree, was used for the closed-ended questions

Figure 1. The process of developing the concept of corporate transparency in corporate governance



Source: Adapted from Bennis and O'Toole (2009).

To further support this study, we also conducted a detailed examination of the CGS of MLEs for three consecutive years, between 2015 and 2017. As at 23rd August 2018, the Malta Stock Exchange (MSE) consisted of 23 equity listed entities: three of these entities were admitted to the MSE in 2017 or subsequent to this year. In total, the examination was conducted on 61 annual reports. The focus of such examination was on the adequacy of explanations disclosed in the non-compliance section of such statements.

4. Findings and Discussion

4.1 The Maltese Regulatory Framework

(i) *Is the CGS a sufficient mechanism for CT?*

As already mentioned constructing a regime of CT has become an elementary first step in attaining trust and confidence in today's contemporary environment. All respondents (11) suggested that honest and "*open communication*" contribute significantly to the generation of stakeholder trust and confidence in public entities and consequently in the financial market. Research participants marginally agreed ($\bar{x} = 3.54$) that a lack of CT and dialogue shatter shareholder/stakeholder trust as the concept of secrecy generally creates suspicions and conspiracy theories. Additionally, participants themselves emphasized that CT materialize only when a company has the ability to produce a system of fairness and respect, where the board and management of the company are willing to speak the truth to relevant stakeholders and vice versa.

Moreover, if company directors and executives are inclined to listen to opposing arguments to those put on the table and guarantee to take notice of such viewpoints, they open the way for the creation of a transparent environment. Such conduct is in accord with Walumbwa *et al.*'s (2011) definition of CT, where CT is defined as the extent to which information disseminates freely between the company and all its relevant stakeholders irrespective of their power of influence on the company's performance.

As stated in the literature, Bennis and O'Toole (2009) suggested a process involving a number of stages or practices that a company should incorporate in its CG framework in order to be able to produce a higher degree of transparency to improve disclosures. This process is being referred to in various parts of this discussion. Bennis and O'Toole (2009) recommended that a company should initiate this concept building by always telling the truth, while avoiding picturing situations rosier than they actually are with the primary aim to mislead the market. Therefore, the question arises whether MLEs are being transparent enough in their CGSs by telling the truth.

The examination of the CGSs revealed a number of issues relating to the adequacy of explanations provided. Although a number of companies are showing progress in their disclosures over the years, others significantly fail to do so. As also found in other foreign studies of Arcot *et al.* (2010) and Sergakis (2015), such failures mostly relate to explanations for non-compliance being inadequate, superficial or even non-existent. In this context, the findings in this study confirm a number of previous recent studies also held in Malta such as Debono (2016).

This study found that generally most companies do recognise their non-compliance with the principles or supporting provisions of the Code. However, as per the examples illustrated in Table 1, a number of companies simply identify such departure/s and fail to provide any valid reason or explanation for their actions, at times even attempting to justify this by depicting the other measures put in place instead of complying.

Despite the free-hand report writing mechanism granted by the CoE approach embedded in the Code it is evident that in a number of instances, different companies tend to provide the same type of explanations, at times with slight variations. Table 2 presents some illustrations:

Table 1. Justifications for non-compliance

Grand Harbour Marina plc 2015: Provision 9.3
<i>"The Company does not have a formal mechanism in place as required by Code provision 9.3 to resolve conflicts between minority shareholders and controlling shareholders and no such conflicts have arisen". (p.19)</i>
Medserv plc 2016: Principle 3
<i>"In accordance with Code Provision 3.1, where the roles of the Chairman and the Chief Executive Director are combined, the Board should appoint one of the independent non-executive directors to be the senior independent director. The Board has not appointed one of the independent non-executive directors to be the senior independent director". (p.21)</i>
Plaza Centres plc 2017: Provision 6.4
<i>"With respect to Code Provision 6.4, the Board notes that professional development sessions were not organised for the period under review". (p.15)</i>
HSBC Bank Malta plc 2015: Provision 4.2.7
<i>"Code Provision 4.2.7 recommends 'the development of a succession policy for the future composition of the Board of Directors and particularly the executive component thereof, for which the Chairman should hold key responsibility'. The bank discloses that it never formalized a Board succession policy. However, in practice the REMNOM Committee is actively involved in the board succession, specifically in recommending the appointment of new members and also by evaluating any newly proposed appointees". (p.34)</i>

Table 1. Explanations with minor inter-company variations

Plaza Centres plc 2016: Provision 9.4
<i>“Plaza does not have a policy in place to allow minority shareholders to present an issue to the Board”. (p.15)</i>
Malta International Airport plc 2017: Provision 9.4
<i>“The Company does not have a policy in place to allow minority shareholders to present an issue to the Board”. (p.22)</i>
GO plc 2015: Principle 3
<i>“As explained in Principle 3 in Section B, the Board is composed entirely of non-executive Directors. Notwithstanding this, it is considered that the Board, as composed, provides for sufficiently balanced skills and experience to enable it to discharge its duties and responsibilities effectively. In addition, no cases of conflict of interest are foreseen”. (p.32)</i>
Malta Properties Company plc 2015: Principle 3
<i>“As explained in Principle 3 in Section B, the Board is composed entirely of non-executive Directors. Notwithstanding this, it is considered that the Board, as composed, provides for sufficiently balanced skills and experience to enable it to discharge its duties and responsibilities effectively. In addition, no cases of conflict of interest are foreseen”. (p.16)</i>

Table 2. Explanations with no intra-company variations

RS2 Software plc 2015: Provision 4.2.7
<i>“The Code recommends the development of a succession policy for the future composition of the Board of Directors. The Company does not consider this principle to be applicable to it on the basis that appointment of directors is a matter which is reserved exclusively to the Company’s shareholders (except as specified herein)”. (p.31)</i>
RS2 Software plc 2016:
<i>“The Code recommends the development of a succession policy for the future composition of the Board of Directors. The Company does not consider this principle to be applicable to it on the basis that appointment of directors is a matter which is reserved exclusively to the Company’s shareholders (except as specified herein)”. (p.13)</i>
RS2 Software plc 2017:
<i>“The Code recommends the development of a succession policy for the future composition of the Board of Directors. The Company does not consider this principle to be applicable to it on the basis that appointment of directors is a matter which is reserved exclusively to the Company’s shareholders (except as specified herein)”. (p.40)</i>

Furthermore, similarities are also evident with companies continuing not to adhere to a principle or provision of the Code, often providing the same exact explanations from year to year. Table 3 gives some examples of this. This could indicate that few

companies are trying to solve such departures, and also that little, if any, effort is being made to improve compliance.

Albeit the fact that research participants did agree ($\bar{x} = 4.08$) that the CoE approach for the CGS requires sufficient and appropriate explanations to be effective, it is clear that some MLEs are in practice not bothered to provide such explanations and improve the situation. At the same time, a general denial persists with respect to any link between such low-quality explanations and a lack of CT. This is also indicative of corporate agents such as directors and managers being more intent on paying “lip service” to CG through politically correct explanations to complement their needs rather than telling the truth. This is an illustration of the agency problem. With such attitudes towards the CGS it can hardly be claimed that such a statement conveys a proper reflection of CT within the local context and therefore further guidance to MLEs may be required regarding the preparation of such a statement.

(ii) Is the Code to be legally enforceable?

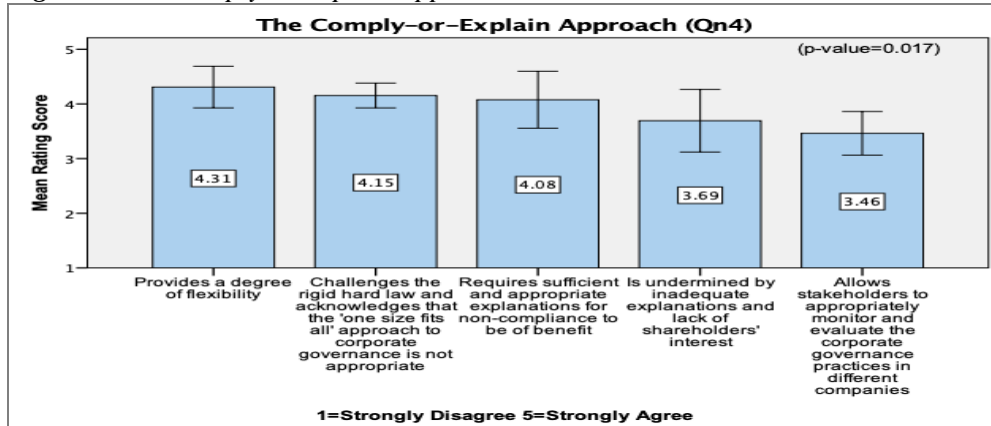
As claimed by Inwinkil *et al.* (2014), CG and the CoE approach are perceived to do their trick only if supported by high-quality reporting. In this context, MLEs seem to be decently aware of what is expected of them, and yet the issue of a lack of explanations persists with companies evidently exploiting the flexibility provided by the CoE. Research participants were asked to provide the extent of their agreement to five statements relating to the CoE as illustrated in Figure 2.

The findings of this study indicate that companies do acknowledge the fact that the CoE is the main characteristic of the Code which enables them not to be unduly burdened by regulations, as the two most agreed statements are that it provides a degree of flexibility ($\bar{x} = 4.31$) and it manages to challenge the rigid hard law ($\bar{x} = 4.15$). A number (5) of respondents stated that it allows them to justify themselves in light of the characteristics of their operations (5/13). Yet, the examination of the CGS confirms that despite having been given such flexibility, some MLEs remain reluctant to refrain from any sort of exploitation.

One of the main objectives of the CoE approach is to contribute towards increasing CT and disclosure. The notion is to protect the interest of shareholders which could be threatened by the separation of ownership and control, as such an approach helps to empower them to make better-informed decisions. Fung (2014) supports this idea of empowerment and adds that, if used appropriately, CG could also be an effective investment valuation tool. Yet, the findings indicate ($\bar{x} = 3.69$) that the lack of sophistication and the financial illiteracy of most Maltese shareholders, particularly the minority ones, too often render them uninterested or even incompetent in exerting any pressures for CT or any other CG issues beyond the distribution of dividends. It is the majority shareholder who typically shows interest in such issues

and, as a result, overall shareholder monitoring may be lacking and undermining the whole concept.

Figure 2. *The comply-or-explain approach*



Source: Authors' Compilation.

Therefore, it is natural that these arguments give rise to the debate over whether the Code needs to be legally enforceable if it is to ensure adherence to regulations of CG CT best practices. Most respondents (8) indicated that MLEs would resist the legal enforceability of the Code) and that, therefore, one would need to proceed cautiously on this matter. On the one hand, legal enforceability of CG provisions could result in a one-size-fits-all effort which does not leave enough room for maneuvering in different companies in a dynamic and complex market. In fact, two research participants pointed out that if the Code is compelled, it would merely drive companies in improving their CG and CT, but will possibly reduce their efforts to a symbolic box-ticking exercise. Also, one emphasized that CG is a matter of “ethics” while pointing out that it would be better if a “name-and-shame policy” had to be adopted for defaulter rather than legally enforce the Code.

On the other hand, it is clear from the literature (Baldacchino, 2007) that, within the Maltese CG culture, unless there is legal enforceability there will be too few adherents to best practices even if recommended by a CoE code. There is also the issue of the extent to which CG matters, most of which fall under the umbrella of corporate ethics, may be regulated directly and effectively by any laws. Translating into legislation such matters which are considered part of ethical morals may also be highly controversial. Therefore, legal enforceability of CG/CT matters may have the reverse effect to the legislators’ intent in that companies may attempt only to observe the letter, rather than the spirit, of the law.

Taking both sides of the argument into consideration, one possible compromise that emerges is the introduction of structured requirements in a part of the CGS. By going through the answers to the structured questions stakeholders may come to

know clearly whether CG/CT requirements are being met. However, so as not to render the CGS as a mere box-ticking exercise any structured part could be followed by another semi-structured part made up of more open-ended questions, wherein the company may explain with some flexibility the extent to which it is adhering to CG/CT practices.

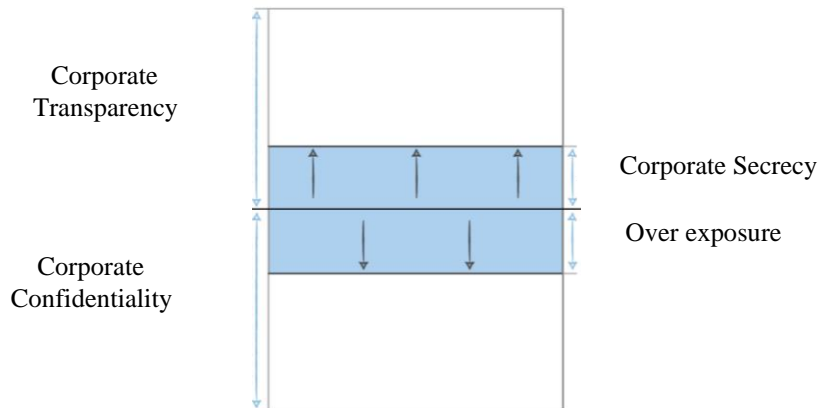
4.2 The Dysfunctional Corporate Governance Practices and Corporate Transparency: The Links

(i) Where is the line to be drawn between corporate confidentiality and transparency?

The appropriate level of CT emanates from a balance between the stakeholders' right to have information and the companies' right to privacy with respect to confidential and sensitive matters. On the one hand, stakeholders have a legitimate right to receive detailed information which is transparent enough as to allow them to form a valid opinion on the past, present and future direction of the company. In this context, the Code (MFSA, 2011) recommends for MLEs to *"give shareholders a clear and comprehensive picture of a company's governance arrangements"* (p.1) and to communicate effectively by providing *"regular, timely, accurate, comprehensive and comparable"* (p.15) information. On the other hand, companies' right to privacy refers to their right to control the supply of information and disclosures in such a way that they retain confidential and sensitive material as a protection of their competitive advantage as claimed by the OECD (2015).

In short, one may synthesise this as the dilemma between the two requisites of CT and corporate confidentiality, both essential for a business to be successful. Figure 3 illustrates that there needs to be a line drawn between these two opposites. If such a line is not appropriately drawn, corporate secrecy will start to infringe on CT. Therefore, the main concern and responsibility of those in charge of CG are to ensure that such a line is legitimate and that no corporate secrecy infringement occurs. Becoming too focused on confidentiality may result in unneeded secrecy with its negative implications. On the other hand, even focusing on transparency may result in undue damage to the company within its market in view of its overexposure.

The findings of this study indicate that a number of MLEs may be finding it difficult to draw such a legitimate line. In fact, when faced with four different dysfunctional CG practices which were indicative of possible suppression of CT, a controversy arose among interviewees. While about half (6) recognised that such practices are possibly secretive, others (7) rationalised that they are not so but that, rather, they have more to do with the need for corporate confidentiality as further explained below.

Figure 3. *The corporate dilemma*

Source: Authors' Compilation.

▪ ***Insufficiently detailed disclosures relating to director compensations***

When asked about the insufficient detailed disclosures relating to director compensations most participants (10) opposed any relation to a lack of CT. On the contrary, they attributed this to the perceived “commercial sensitivity” with respect to any information being published and the legal need for personal privacy, which are even more prevalent given the smallness of the state of Malta. A number (6) of participants felt deeply that given such smallness, it is safer for MLEs to limit this to an aggregate figure of remuneration. One interviewee deliberated that there is no “added value” in individualised disclosure but only in aggregate disclosure of remuneration, which on its part could be overseen by an appropriate remuneration committee.

Conversely, a minority of research participants (3) acknowledged the possible link between the practice of aggregated remuneration and a lack of CT. They found such a practice as originating from the perceived need to conceal the amounts earned at the top level and their remuneration thereof. One interviewee mentioned that this practice is most evident in debt-listed companies, which are not subject to as much stakeholder scrutiny as equity-listed companies. One of these interviewees claimed that this practice is indeed dysfunctional but that such practice is on the decline.

In this context, the examination of the annual reports revealed that in the CGSs for the three financial years ending 2015 to 2017, there were only nine cases of non-compliance relating to the setting up of a remuneration committee. Moreover, despite the fact that the Code limits its requirement to an aggregated disclosure of remuneration and most of the interviewees considered that such aggregation is sufficient, there were still 25 cases over the three years where companies went beyond the Code requirements to disclose individualised remuneration. Companies providing such individualised remuneration information included Bank of Valletta plc, HSBC Bank Malta plc, MaltaPost plc and Plaza Centres plc.

▪ ***Non-evaluation of the performance of the board***

With respect to the non-evaluation of the performance of the board of directors, most participants (9) maintained that there is probably little, if any, link between such non-evaluation and corporate attitudes against CT. Such links may, however, arise from the fact that an appreciable number of directors may not be willing to subject themselves to such an exercise. This might be because the results of this exercise may have adverse implications beyond the company performing such an evaluation. Malta is a country where many directors have multiple “positions” in different companies and where the place is “too small” for any undesirable results of the performance evaluation of the directors whether published or also not to become known elsewhere. It is evident that companies prefer to come to know about performance only informally and without any structure. Possibly the regulator requiring structures, such as a robust and detailed questionnaire, an interview, a review of the board minutes as well as the engagement of independent consultants, are the only ways for CT in this context to become implemented.

▪ ***Inadequate explanations for non-compliance***

When asked about the inadequacy of explanations for non-compliance with the Code, responses were balanced as to whether there is a link between such explanations and the lack of CT with slightly more responses (7) to such no link. The main reason forwarded by those who stated that there is no such link is that the preparers of explanations have legitimately considered the competitiveness of the company. Furthermore, giving more detailed explanations would be dangerous as it would breach confidentiality. This study indicated that in Malta, a satisfactory level of confidentiality and the right accounting numbers were significantly more important than CT. Moreover, both an inappropriately structured Code and the Maltese culture commonly override any consideration towards more transparency. On the other hand, participants maintaining that there is a link (6) between CT and inadequate explanations emphasised that a number of company boards were ready to “skew the picture” in order to stick to “political correctness”. The latter attitudes lead such directors to consider and evaluate each and every word and resort to a “copy-and-paste” from similar reports method.

▪ ***Communication with shareholders and the market***

Regarding the lack of communication with shareholders and the market and its link to company attitudes against CT a minority (5) of research participants all company representatives, emphasised that there is no such lack of communication. Communication with shareholders includes not only the AGM but also company announcements, company’s newsletters, the annual report, e-mails and meetings with the Malta Association of Small Shareholders (MASS). Therefore, in their opinion there was no question of any link with CT.

On the contrary, most participants (8) stated that a lack of communication with shareholders and the market do exists with most of these (6) also pointing out that there is a link to attitudes against CT. In their view, adverse CT attitudes were

evident from the lack of meaningful communication with all shareholders particularly in the AGM which they described as often being “stage-managed”, a “fancy reception” and of “inconvenience to directors”. A number of interviewees (3) referred to the implication of there being no CT by the fact that a number of directors do not feel any sense of accountability. A common cause of the situation is that many shareholders are not sophisticated enough to exert pressure on their directors at the AGM, which they may view as entertainment.

One auditor pointed out that in his/her experience, the link between a company’s attitudes and a lack of CT becomes more evident whenever a company is not performing well and even more when in distress. On the other hand, a company enjoying boom performance is much more prone to be transparent. Two other participants (2) claimed that although a lack of communication exists, it can’t be directly linked to a lack of CT. In their view, such a lack of communication exists because of shareholder indifference, thus rendering it unviable for companies to invest in more disclosures than at present.

As seen in the literature and from the various findings of this study, two major pillars in developing the concept of CT are the readiness to encounter uncomfortable situations and to admit mistakes – two pillars which, unfortunately, seem to be frail in the Maltese corporate culture.

4.3 Possible Reasons for Lack of Corporate Transparency

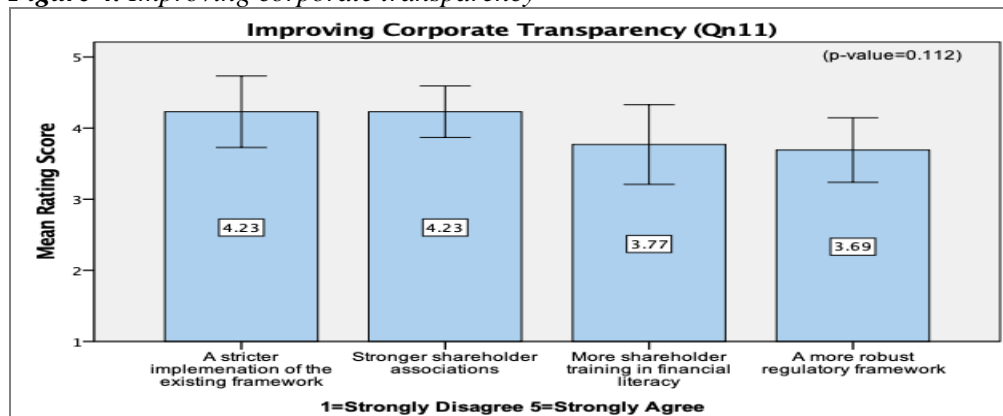
(i) Is the regulator to be more involved?

When asked how valid the Code is in encouraging good CG practices, few research participants (2) highlighted the detail that issues relating to CG arise not specifically because of the Code itself, but more as a result of its weak implementation. This explains that the current situation considerably lacks the involvement of the regulatory authority. More precisely, the MFSA is not placing much pressure on those companies failing to comply with the Code. In particular, the regulator generally does not review the substance of the disclosures provided in the CGS. In the experience of some of the company representatives (3), very few MFSA inspections have been held in this context and even where inspection does materialise, regulator feedback is often delayed, and hence rarely relevant. Unfortunately, few interviewees (2) agreed that the MFSA tends to focus more on somewhat trivial matters such as requiring the provision of the annual report not through a hyperlink. This situation could be permitting companies to provide superficial disclosures and withhold useful information from the users.

In a similar vein, research participants highly agreed ((Figure 4), that in order to improve CT, a stricter implementation of the existing regulatory framework is needed. Most (8) claimed that the MFSA could take up a more “proactive supervision” stance. In these circumstances, the Code needs to be clearer so that inspectors will be able to act where appropriately required. An effective regulator

needs to be provided with appropriate resources and while audit firms could lend a helping hand to the regulator, it ultimately remains the regulator's responsibility to inspect properly.

Figure 4. Improving corporate transparency



Source: Authors' Compilation.

More regulatory involvement is probably required, not only with respect to monitoring and inspection, but also in terms of better guidance to MLEs in preparing their CGS. Such increased involvement does not necessarily lead to stricter fines but may also involve the introduction of policies such as a name-and-shame one. With the increased stakeholder use of social media sources, a name-and-shame policy could render companies highly concerned with potential damages that any regulator announcement in their regard could have on the reputation, credibility, financial support, trust and competitive advantages of the company. A stronger level of regulation does not have to be overstretched and will not be so if the focus is on improving communication lines between the regulator and MLEs. In this context, provisional guidelines on CG matters such as transparency and confidentiality could go a long way.

(ii) Are stakeholders contributing to less corporate transparency?

The shareholder who exercises his own right as the owner of the company can exert significant influence on the company's CG. However, the indications are (5) that most shareholders do not value the information provided in the CGS and any analysis therein is carried out either by institutional shareholders or financial intermediaries. A related issue is that even if they are willing to, most shareholders are not themselves competent and sophisticated enough to analyse the financial statements. Nowadays, the financial statements persistently include much more complexities and technicalities which increases the difficulty of interpretation especially for the individual shareholder who is less familiar with finance and tend to be only interested in the distribution of dividends. One research participant declared that the CGS together with the Chairman's and the CEO's statements could become even more popular than the financial statements themselves as sources of

reference to individual shareholders. Likewise, another interviewee pointed out that the CGS is one of the simplest in the annual report, she/he still doubts whether stakeholders actually appreciate its value enough.

Considering this lack of interest and competence, such statements may easily turn out to be a waste of resources if left unread by most shareholders. After all, it is of little use for companies to improve the level of CT if doing so leaves hardly leaving any impact on most corporate stakeholders. In this connection, the MASS may play its part in helping its members achieve better training and understanding and possibly acting as an intermediate for them in dialogues with companies. Figure 4 shows that having stronger shareholder associations could be the way forward for improving current CT situation locally. Research participants (8) pointed out that collective action is much more effective than individual initiative.

For such actions to become possible, it is essential for minority shareholder associations to place more importance on the protection of shareholders' interests without sharing the common current disinterested mindset (i.e., mostly focused on the distribution of dividends) of most minority shareholders and prioritises the educational aspect. Companies may also play their part to encourage both internal and external stakeholders to participate more in CG/CT matters. In this context, Bennis and O' Toole's (2009) process includes encouraging stakeholders to speak the truth with high ranking individuals within their company. In the Maltese corporate context, this study indicates that companies often discourage shareholders from participating by measures such as allowing too short a time for questioning in the AGM or using too technical a language for the ordinary minority shareholder to be engaged.

(iii) How relevant is the small state environment?

This study indicates that within the Maltese small state environment, corporate disclosures may lead to wider damages to those in charge of CG as the corporate community is smaller and most people are easily accessible and know each other. This is also in line with the literature. Furthermore, corporate competitors may be watching company developments more closely and intensely and therefore rendering directors more prone to withholding information. Probably, such an innate issue cannot be easily resolved at least not until there is more integration between Maltese industries and its European counterparties.

4.4 Possible Implications on the Corporate Governance of Maltese Listed Entities

(i) Will investor trust be diminished?

As stated earlier, owing to the volatility in the international financial markets, the need and demand for the proper level of CT have been on the rise. Corporate information and disclosure are considered to be integral components for both existing and potential investors in their investment decision making. CT and a more

robust disclosure regime which demand accurate and detailed information on financial matters and other non-financial matters, such as the entity's goals for the future, related party transactions, conflicts of interests and governance structures are expected. This would enable investors, along with other market participants, to much more accurately evaluate the position and activities of the company. As such, this would lead to the generation of more trust and confidence and even facilitate external financing to the company. In this context, research participants agreed marginally ($\bar{x}=3.77$) that a lack of CT may result in diminished investor trust in the entity and the financial market. Most participants (7) claimed that the investor is required to be treated fairly and provided with all relevant information required to make informed decisions. If this is not the case, one cannot expect that the existing/potential investor to be "totally confident" and provide the necessary support.

On the contrary, some participants (6) clarified that in Malta such diminished investor trust could possibly not take place since the Maltese investor's trust in the market is mainly driven by "*high rates of return*", "*dividends*", "*bonds income*" and "*shares price volatility*" rather than the lack of CT or anything related to CG. A few of them (2) pointed out that the possible reason behind this deficiency of awareness about the CG concept maybe the fact that, until today, every bond issued has been paid back and none of the MLEs has failed. Therefore, investors do not easily "*get alarmed*". However, such a lack of sensing alarm as long as they receive their return may prove itself to be dangerous.

Therefore, in order to restrain a closed and opaque corporate culture which usually lead to increased negative consequences, the annual report possibly require to commission more importance on the CG aspects beyond the financial ones. Hopefully, minority shareholders will, in time, be better financially educated and further appreciate both aspects and stop limiting themselves to what directly concerns them.

(ii) *Will false information and rumours be spread in the market?*

The findings of this study demonstrate a marginal agreement ($\bar{x} = 3.62$) that any lack of information, direct dialogue and CT may easily create suspicions even when circumstances do not warrant this. Moreover, such lack may also result in the spread of false rumours in the market as it may act as a motive for people to draw their own conclusions.

This practice can negatively impact both the company which is not disclosing the required detailed information and its stakeholders. External stakeholders such as investors and creditors may end up being misled into taking the wrong decisions. The company's reputation, which may have taken a long time to build, may easily become susceptible to destruction, thus leading to the creation of further investment barriers. Furthermore, at a point in time companies involved in any market rumours

will have to react to set the “*record straight*” subjecting themselves to unnecessary costs which could be avoided through appropriate foresight.

CT and information sharing should push the company not only towards correcting wrong impressions but also to be more proactive and generate market confidence. Indeed, in the real-world information may flow quickly but not necessarily smoothly. The management of a company usually have greater access to information than its owners and therefore are more aware of the functioning of the business. The impact of CT is that of minimising such information asymmetry. The more companies manage to be transparent without breaching any legitimate confidential matters, the more they push towards problem-solving and ensure that any wrong doing if committed in the past will not be repeated in the future.

5. Conclusion

This study concludes that, at present, CT is not sufficiently entrenched within the CG culture of several MLEs, as the latter are still facing difficulties in achieving and maintaining a legitimate balance between corporate confidentiality and transparency. In this regard, the Maltese Code may be more supportive by providing more detailed and clearer guidelines on CT. In particular, the Code does not specify how the CGS may properly reflect the appropriate level of CT. This is evidently contributing to the tendency of some MLEs to render the CGS as a merely politically correct necessity and only complying to an artificial symbolically level, despite not being strangers to what it is and what it should entail.

In addition, insufficient regulatory enforcement maybe another major factor contributing to a lack of CT. In this context, more regulatory involvement is clearly required in terms of monitoring and inspections. Such increased enforcement may do away with inadequate explanations for non-compliance with the provisions of the Code. Furthermore, this study concludes that shareholders, in particular minority shareholder, often lack the necessary level of sophistication and financial education to render them competent to challenge those charged with CG. The tendency is therefore for them to be merely interested in the return of their investment. As a small island state, Malta may also be contributing to the reluctance of corporate directors to be more transparent.

The implications of the above are that both the regulator and the regulated need to be taking the appropriate action as otherwise one cannot ensure adequate investor confidence and protection against future corporate scandals.

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