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Internal corporate governance and board performance in monitoring roles

Evidence from Malaysia

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Abstract

Purpose – This paper aims to examine the relationship between internal corporate governance mechanisms and board performance in monitoring roles.

Design/methodology/approach – A survey questionnaire was used to gather data on board performance, while annual reports were employed to gather data on internal corporate governance mechanisms. Data for board performance were based on 112 directors who represent the companies.

Findings – Factor analysis extracted two dimensions of monitoring roles: management oversight roles and performance evaluation roles. Non-independent non-executive directors and managerial ownership were found to be positively related to both dimensions of monitoring roles, while the multiple directorships of non-executive directors were negatively related to management oversight roles.

Practical implications – The paper establishes the need for regulators to pay particular attention to multiple directorships, which are commonly practiced in public listed companies. The contribution of non-independent non-executive directors rather than independent directors in monitoring roles calls for further research. Regulators need to emphasize the performance evaluation roles of the board of directors (BOD), as much emphasis has been given to management oversight roles.

Originality/value – The study contributes to the literature concerning monitoring roles as it shows that management oversight roles and performance evaluation roles are differentiated. The findings provide an avenue for the contribution of non-independent non-executive directors and multiple directorships in monitoring roles.

Keywords Non-independent non-executive directors, Managerial ownership, Multiple directorships, Board performance, Monitoring roles, Boards of directors, Malaysia

Paper type Research paper

1. Introduction

Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders, and should facilitate effective monitoring (Organisation for Economic Co-operation and Development, 2003). Corporate governance mechanisms can be categorized into two controlling mechanisms: internal and external. The key external

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controlling mechanisms are managerial labor markets, the market for corporate control, debt, and concentrated shareholding by blockholders (Ali and Sanda, 2001). Two important internal corporate governance mechanisms are the Board of Directors (BOD) and directors' shareholding. However, due to the weak market control in emerging countries, internal corporate governance mechanisms play a vital role in the corporate governance of emerging markets (Lei and Song, 2004). Internal corporate governance mechanisms are considered to have influence on the decisions made by managers (Lemmon and Lins, 2003). A firm's ownership structure is also considered to be the primary determinant of the extent of agency problems between controlling insiders and outside investors.

Recent developments in the corporate governance literature highlight the concern about the effectiveness of the roles played by the BOD. Having board conformance to the governance structure does not necessarily ensure high board performance, as the design of the internal mechanisms of a firm is based on a company's need (Society of Management Accountants of Canada, 2002; Nicholson and Kiel, 2004). A focus on board performance is required, as several studies concerning the relationship between board performance and firm performance have shown a positive relationship (Brown, 2005; Judge and Zeithaml, 1992; Kula, 2005), which indicates the importance of the BOD in providing effective board performance to ensure higher firm performance (Chambers, 2002). It is expected that internal corporate governance mechanisms will have some impact on the roles played by the board of directors (as a proxy of board performance). Thus, the main objective of the present paper is to examine the influence of internal corporate governance mechanisms on board performance in executing monitoring roles in Malaysian public listed companies.

2. Review of the literature

2.1 Corporate governance in Malaysia

Efforts to improve corporate governance practices in public listed companies in Malaysia were undertaken prior to the Asian financial crisis of 1997, when the Kuala Lumpur Stock Exchange (KLSE) Listing Requirements of 1994 required companies to establish an audit committee. However, the emphasis on corporate governance practices was only highlighted after the crisis with the introduction of the Malaysian Code on Corporate Governance (MCCG Code) in 1999. The purpose of the code is to set out principles and best practices concerning the structures and processes that companies may use to achieve an optimal governance framework.

The MCCG Code requires public companies to adhere to the principles of the code based on the varying circumstances of individual companies. The code became effective for public listed companies after the revamp of the KLSE Listing Requirements in 2001. Accordingly, public companies need to adhere to Chapter 15 of Corporate Governance related to Directors, Audit Committee, Auditors and Corporate Governance Disclosure.

The MCCG Code underwent revision in 2007, which among other amendments placed importance on the process carried out by the nominating committee in evaluating the members of the board (Securities Commission Malaysia, 2007). According to the Code, the BOD should implement a process to be carried out annually for assessing the effectiveness of the BOD, committees of the board, and the contribution of each individual director. The revised code also provides criteria that should be considered by the nominating committee when recommending candidates for directorships. The proposed criteria include skills, knowledge, expertise and experience; professionalism; integrity; and the candidate's ability to discharge such responsibilities.

2.2 Theoretical perspectives on the monitoring roles of board of directors

Board performance refers to the ability of directors to perform board roles (Wan and Ong, 2005). According to Nicholson and Kiel (2004), an effective board is "one that can successfully execute the role set required of it" (p. 453). The ability of the board to execute these roles will determine how effectively the board governs the company. Wan and Ong (2005) classified board roles into four dimensions:

(1) monitoring roles;

(2) strategic roles;

(3) service roles; and

(4) resource dependency roles.

However, in the current study, the focus is on the monitoring roles as these roles are highly emphasized in Malaysia, as stated in the Companies Act 1965 and other directives such as the Malaysian Code of Corporate Governance (Finance Committee on Corporate Governance, 2001). In fact, the concentrated ownership in Malaysian public listed companies requires the practice of effective monitoring roles to avoid the expropriation of company assets by the majority shareholders at the expense of the minority shareholders.

From a theoretical perspective, agency theory recognizes the imperfection of existing governance structures in protecting shareholders' interests and concerns with the consequences from the conflict of interests between managers and shareholders (Jensen and Meckling, 1976; Fama, 1980; Fama and Jensen, 1983). Agency theory assumes that the interests of managers are not necessarily aligned with the interests of shareholders. The board of directors is considered to be an efficient mechanism for monitoring a firm's managers on behalf of its investors. Accordingly, the roles of the BOD are to maximize shareholders' wealth, reduce agency costs, select or dismiss the CEO, evaluate the CEO and company performance, and also participate in the strategic decision process and control. Table I provides the theoretical perspective and operationalization of the monitoring roles of the BOD from the agency theory perspective.

Theory	Agency theory
Board role	The primary role of boards is to monitor actions of agents (executives) to ensure their efficiency and to protect the interests of the principals (owners)
Operational definition of boards' role	Maximizing shareholders' wealth Reducing agency cost Selecting CEO and dismissing CEO Evaluating CEO and company performance Strategic decision making and control
Theoretical origins	Economics and finance

Sources: Zahra and Pearce (1989), Hung (1998)

Table I. Theoretical perspective and operationalization of monitoring roles of BOD

In Malaysia, the laws relating to the roles and responsibilities of directors can be found in the Companies Act 1965 and the Articles of Association. The Articles of Association contain regulations for the internal management of a company's affairs (Zainal Abidin, 2002). Detailed duties or responsibilities of directors are set out in Section (S) 122 to 141 of the Companies Act 1965. The duties can be classified into three, i.e. (1) fiduciary duty; (2) duty of care, diligence and skill; and (3) statutory duties (Ernst & Young, 1992). Fiduciary duty (S.132) refers to the duty to act honestly in the best interest of the company. Duty of care, diligence, and skill requires directors "to act with due care and diligence in the discharge of their duties as expected of a similar person (having the skill) in that position" (S.132 [1], p.146). Directors are also subject to statutory duty for various disclosure obligations (S.131 and S. 135), such as disclosure of directors' interests in the company and related company, and any changes in those interests. Accordingly, fiduciary duty, duty of care, diligence and skill, and statutory duties are related to monitoring roles.

The Malaysian Code of Corporate Governance (Finance Committee on Corporate Governance, 2001) outlines the principal responsibilities of the board of directors in public listed companies, which are:

- to review and adopt a strategic plan for the company;
- to oversee the conduct of the company's business to evaluate whether the business is being managed properly;
- to identify principal risks and ensure the implementation of appropriate systems to manage these risks;
- to undertake succession planning, including appointing, training, fixing compensation, and replacing senior management (where applicable);
- to develop and implement an investor relations program or shareholder communication policy for the company; and
- to review the adequacy and the integrity of the company's internal control systems and management information systems, including systems for compliance with applicable laws, regulations, rules, directives and guidelines.

Most of the coverage of the principal responsibilities of BODs in the MCCG Code emphasizes the monitoring roles (items 2, 3, 4, 5 and 6), except for item 1, which concerns strategy roles. In fact the coverage in monitoring roles can be grouped into two kinds of role:

(1) management oversight roles (items 3, 5 and 6); and
(2) performance evaluation roles (items 2 and 4).

Several empirical studies have made attempts to operationalize items in the monitoring roles, such as the studies conducted by Wan and Ong (2005) and Brennan (2006). Wan and Ong (2005) identified ten items to represent monitoring roles in studying the influence of the board process on board performance. In their study, only one dimension of monitoring roles was tested. The items were as follows:

(1) monitor top management in decision-making;
(2) evaluate performance of top executives;
(3) has internal mechanism to evaluate performance yearly;

(4) member formally evaluated by others;
(5) analyze budget allocation versus performance;
(6) require information showing progress;
(7) review performance against strategic plan;
(8) review financial information for important issues/trends;
(9) engage in succession planning for CEO; and
(10) engage in succession planning for top managers besides CEO.

Another study by Brennan (2006) summarized items to be considered as monitoring roles based on findings from previous studies. Among the items identified were:

- setting the risk appetite of the organization;
- ensuring corporate survival;
- specifying lines of authority of the management and board;
- ensuring compliance with statutory and other regulations;
- reviewing social responsibilities;
- monitoring and evaluating management; and
- controlling operations.

It is noted that almost all the items used by Brennan (2006) emphasize management oversight roles rather than performance evaluation roles. Brennan (2006) also argues that none of the items ensure a positive effect on firm performance because exercising tight control by the board may function as constraints on management and limit managers to pursue shareholder value. The control mechanisms imposed with the intention of reducing self-serving behavior of managers might improve the accountability of the managers. However, at the same time the control mechanisms might reduce the efficiency of management.

Based on the above discussion, the current study produces comprehensive items that can be used to operationalize the concept of monitoring roles with the aim of enhancing the roles of BOD and also determining the factors that may influence their effectiveness.

2.3 Board of directors' (BOD) attributes

The attributes of BOD used in this study are based on the recommendations by Zahra and Pearce (1989). They identify four attributes of the BOD that could lead to superior performance of firms:

(1) composition;
(2) characteristics;
(3) structure; and
(4) process.

The board composition refers to the board size and the mix of director types (insiders versus outsiders). Board characteristics consist of two components:

(1) directors' background (age, educational background, values, and experience); and
(2) board personality.

Board structure refers to the dimensions of a board's organization, which include the type of committee, committee membership, flow of information, and board leadership. Board process refers to the approach the board takes in making decisions.

The board attributes that have been studied most in the corporate governance research are board composition and board structure. In management research, however, the focus of the studies is to link the CEO or executive directors' background and personalities with the firm's performance. The current study adopts all the board attributes suggested by Zahra and Pearce (1989), i.e. board composition (board size and director's type), board characteristics (knowledge/experience: tenure and multiple directorships), board structure (board leadership), and board process (frequency of meetings or percentage of meetings attendance), which are expected to provide more insights into the monitoring roles of boards of directors. The next part discusses the hypothesis development for each board attribute and managerial ownership in relation to board performance in the monitoring roles.

3. Literature review and development of hypotheses

3.1 Board size

Agency theory argues that smaller boards are more effective than larger boards in monitoring managers (Jensen and Meckling, 1976). Accordingly, as the board size increases, it may be difficult to reach timely decisions because of the existence of rival factions and cliques that may slow proceedings. Thus, large boards are less likely to function effectively because the CEOs have sufficient power to control operations and decisions (Jensen, 1993). A board size of more than ten directors is considered excessive (Lipton and Lorsch, 1992) and may have a negative effect on firm performance. Studies on the monitoring roles of the BOD in earnings management have shown the effectiveness of small boards (Abdul Rahman and Mohamed Ali, 2006). Previous studies in relation to firm performance have also shown the effectiveness of small board size (Yermack, 1996; Conyon and Peck, 1998; Mak and Li, 2001; Singh and Davidson, 2003). Thus, it is hypothesized that:

H1. There is a negative relationship between board size and board performance in monitoring roles.

3.2 Board leadership

Power plays a major role in strategic decision making and the board's power is limited compared to that of the CEO (Stiles, 2001) because the CEO has structural power and is an expert in the firm's operations compared to the outside directors. As the management team is usually headed by the CEO or Managing Director, who is responsible for the formulation of strategy (Van der Berghe and Baelden, 2005), having CEO duality would provide better strategy roles. However, independent leadership is expected to contribute to better monitoring of management and of strategy implementation. Boards are less likely to exert control over management when they lack independence from the management (Carpenter and Westphal, 2001).

Evidence concerning the relationship between CEO duality and earnings management activities is mixed. Deachow *et al.* (1996), who examined the relationship between earnings manipulation and weaknesses, showed that boards with CEO duality practices and boards dominated by management are more likely to manipulate earnings. However, Xie *et al.* (2003) found that CEO duality is negatively related to earnings management activities. As CEOs determine the agenda for board meetings and lead the discussion, having independent board leadership is critical as a check and balance before proposals are approved. In addition, Mohd Saleh *et al.* (2005) found that CEO duality firms are associated with earnings management activities and suggested that independent board leadership would promote audit committee effectiveness. Thus, it is hypothesized that:

H2. There is a positive relationship between independent board leadership and board performance in monitoring roles.

3.3 Board composition

Hermalin and Weisbach (1988) suggest that the effectiveness of board monitoring depends on the composition of the board, which refers to the composition of the outside directors on the board. Outside directors play an important role in ensuring that a company has an effective internal control system, which is carried out through their involvement in an audit committee in which they have a direct contact with the internal audit function and the external auditors.

Within the corporate governance structure, non-executive directors (NED) have an important position to monitor the management and executive directors. NEDs are seen as the check and balance mechanism to enhance a board's effectiveness. NEDs are expected to bring independence to the board and add to the diversity of skills and expertise of the directors (Abdullah, 2004). The business advisory role of the outside directors (non-executive directors; NEDs) on the BOD is vital. A special report on non-executive directors by The Economist Intelligence Unit (2003) highlights a special breed of non-executive directors who are non-independent – so-called "gray" or affiliated directors. Apart from being non-executive, an affiliated director is usually an ex-employee, related to the firm's controlling family, an interlocking director, or a professional with significant business or family ties with the firm (Klein, 1998). As most of the gray or affiliated directors own significant shares in the companies, their incentives to become involved and engaged in corporate governance are higher (Roberts *et al.*, 2005). In addition, since affiliated directors have a prior association with the firm, they often have a deeper knowledge of the firm and its industry than independent directors, and, thus, shareholders may feel that affiliated directors serve them better than independent directors. To be effective in monitoring strategic decisions, outside directors should be individuals from the business (CEO or executive directors from other companies) with relevant knowledge and related expertise (Pettigrew and McNulty, 1995). Thus, the hypothesis is developed as follows:

H3. There is a positive relationship between non-executive directors (NED) and board performance in monitoring roles.

3.4 Multiple directorships

Multiple directorships refer to the number of external appointments held by corporate directors (Ferris *et al.*, 2003). Haniffa and Hudaib (2006) define multiple directorships as directors sitting on more than one board. Directors with more multiple directorships are expected to have more exposure to certain tasks and procedures that can be implemented in another company, making board performance more effective because fewer transaction costs are incurred (Beasley, 1996; Mohd Saleh *et al.*, 2005; Sarkar and Sarkar, 2009). They are expected to provide effective monitoring. Directors who have experience in related strategies are expected to be more capable of contributing to the strategic decision process (Carpenter and Westphal, 2001).

In the USA, it is often considered best practice for a director to hold less than three multiple directorships. "Busy directors" are defined as directors holding three or more directorships (Ferris *et al.*, 2003; Sarkar and Sarkar, 2009). According to the "busyness hypotheses", if directors have too many board assignments, their time and attention might be dissipated, and thus undermine their ability to discharge their roles.

In Malaysia, multiple directorships are found to be common among listed firms in Malaysia (Haniffa and Cooke, 2002). This practice is due to the high number of directorships allowed to directors. According to the KLSE Listing Requirements, BODs are allowed to have a maximum of ten directorships in public listed companies and 15 directorships in non-listed companies.

Following the "busyness hypotheses", directors with multiple directorships may have less time to scrutinize the internal control system closely, which lead to less effectiveness in monitoring managers. Thus, directors will put more reliance on the work of the internal audit (Fadzil *et al.*, 2005). It is hypothesized that:

H4. There is a negative relationship between multiple directorships and board performance in monitoring roles.

3.5 Board knowledge

Lorsch (1995) acknowledges that the board's ability to govern also depends on the knowledge of directors, which comes from their working experience. Fairchild and Li (2005) found that board knowledge in terms of directors' age and tenure had a positive relation to firm performance. Peasnell *et al.* (2001) found that the tenure of non-executive directors is negatively associated with the level of earnings of management activities, which indicates the importance of board tenure in performing effective monitoring roles. This suggests that NEDs with longer tenure have more knowledge about companies' operations, which assists them in overseeing management activities. However, longer board tenure may also result in declining performance due to impediments such as increased social cohesion between the CEO and board members and decreased innovation adaption (Bantel and Jackson, 1989; Westphal, 1999). Thus, the hypothesis is as follows:

H5. There is a relationship between the board tenure of non-executive directors and board performance in monitoring roles.

3.6 Board process

The board process refers to the decision-making activities of the board (Kula, 2005). It is assumed that the approaches taken by the board in making decisions are influenced by the frequency of board meetings, as all major issues and decisions are discussed and made at formal board meetings (Vafeas, 1999). More board committee meetings are required to focus on specific issues, especially when companies are performing poorly and require restructuring. Another measure of board process is to use the percentage of the meetings attended by the BOD. A high percentage of attendance would provide knowledge to directors about the business operations and contribute to monitoring the strategy implementation. Thus, it is hypothesized that:

H6. There is a positive relationship between board process and board performance in monitoring roles.

3.7 Managerial ownership

Shareholding in Malaysian PLCs is highly concentrated in the hands of a few shareholders (La-Porta *et al.*, 2000; Abdul Samad, 2002). Abdul Samad (2002) reported that the mean of the first largest shareholding was 30.30 percent and that of the five largest shareholdings was 58.84 percent, which accounted for more than half of the voting shares. About 71.4 percent of companies (Main Board and Second Board) were under majority ownership, having a shareholding of more than 50 percent, and were controlled by their five largest shareholders. The significant means of enhancing control in Malaysia is through pyramid-holding, cross-holding and managerial ownership (Claessens *et al.*, 2000). There is also a significant participation of owners in management, with 33 percent involved in management (Kuala Lumpur Stock Exchange and PricewaterhouseCoopers, 1999).

Managerial ownership (MOWN) works as a direct incentive for managers to act in line with shareholders' interests (Jensen and Meckling, 1976). Accordingly, the greater the percentage of stocks owned by top managers, the more likely it is that managers will make decisions consistent with maximizing shareholders' wealth. High MOWN is expected to lead managers to maximize firm's wealth as the net effects will ultimately go to them. Ownership concentration by managers is a factor that has an impact on the monitoring potential of BODs (Nicholson and Kiel, 2004). The presence of controlling shareholders has been found to be associated with positive firm performance in Thailand (Wiwattanakantang, 2001). Companies with concentrated ownership might also be subjected to high monitoring activities, as the tendency for entrenchment is higher (Morck *et al.*, 1988; Mat Nor *et al.*, 1999; Ali and Sanda, 2001). It is hypothesized that:

H7. There is a positive relationship between managerial ownership (MOWN) and board performance in monitoring roles.

In the present study, firm size was considered a control variable as board performance may be affected directly or indirectly by factors related to the nature of the firm (Abdul Samad, 2002; Chee and Md Taib, 2005; Wiwattanakantang, 2001). Controlling for size is also necessary, as the percentage of managerial shareholding may be larger in small firms due to the small outlay required in small firms.

4. Research method

4.1 Population and data collection

The unit of analysis of this study is the company, and the BOD was taken to represent the company. The population of this study is companies listed on the main board of

Bursa Malaysia for the year 2006. Only the main board companies were selected in order to control for other factors that might influence the performance of companies on other boards, such as size differences and risks. As the population of companies listed on the main board in 2006 was around 520 (excluding finance companies, PN4, PN17, companies listed after 2004), the sample size was determined in line with Roscoe's (1975) recommendation – to have preferably one to ten (or more) for each variable tested for multivariate regression analysis. Thus, the study required a minimum sample size of 90.

A survey method was used to collect data on board performance from the BODs. Bearing in mind the poor response rate generally obtained in survey studies conducted in Malaysia, which is about 10 percent to 20 percent, questionnaires were sent to all 520 companies. Only BOD members were permitted to answer the survey questionnaire as the company's representative. To increase the response rate, follow-up letters were sent to non-respondents.

Data for board attributes, managerial ownership, and financial information were collected from companies' annual reports (Kuala Lumpur Stock Exchange, 2006).

4.2 Construction of questionnaire

The board performance in monitoring roles measures the extent of BOD participation or involvement in the monitoring functions. Items in the questionnaires related to the monitoring roles were adapted from Brennan (2006), Finance Committee on Corporate Governance (2001), and Wan and Ong (2005). Most items were adapted from Wan and Ong, except the item "evaluate the skill mix on the board", which was taken from the MCCG Code. The items "ensure corporate survival", "specify lines of authority of management and board", and "review social responsibilities of the company" were from Brennan (2006). Eleven items were considered to represent the monitoring roles.

In constructing the questionnaire, the content validity of the instrument was assessed based on the literature review and a pre-test study of the BODs and senior academics. In the actual survey, the BOD was required to indicate the extent of participation or involvement in the board roles of the company for the financial year 2006 using a five-point scale ranging from 1 (very little) to 5 (very much). See Appendix 1 for the monitoring items used in this study.

4.3 Data analysis

For board performance in monitoring roles, factor analysis was conducted to determine the clusters of items fitting into the board performance dimension. Reliability analysis was also run to determine the internal consistency (Cronbach's α) of items in a variable (Hair *et al.*, 2006). Regression analysis was conducted to examine the relationship between internal corporate governance mechanisms and each of the monitoring role dimensions. The regression function is as follows:

$$\begin{aligned}\mathrm{BP} = {} & b_0 + b_1(\mathrm{BSIZE}) + b_2(\mathrm{BLEAD}) + b_3(\mathrm{BCOM}) + b_4(\mathrm{MMDIR}) + b_5(\mathrm{TEN}) \\ & + b_6(\mathrm{BPROS}) + b_7(\mathrm{MOWN}) + b_8(\mathrm{LGTA}) + \varepsilon,\end{aligned}$$

where BP is the board performance dimensions in monitoring roles, BSIZE is the number of board members, BLEAD is board leadership (dummy 1 for CEO $\neq$ Chairman, and 0 otherwise), BCOM is the board composition, the proportion of independent directors to board size (INE) or non-independent non-executive directors to board size (NINE) or non-executive directors to board size (NED), MMDIR is the directorships per non-executive director, TEN is the average of non-executive directors' tenure, BPROS is the frequency of board meetings (FMEET) or percentage of directors' meeting attendance (PMEET), MOWN is the percentage of executive directors' shareholdings (direct and indirect shareholding), and LGTA is the logarithm of total assets.

Previous studies seem to consider NEDs as independent directors, and sometimes they are used interchangeably. For the current study, we differentiated NEDs into independent directors and non-independent non-executive directors to identify the impact of each on the monitoring roles. At the same time, we also considered NEDs as a whole (both independent and non-independent), and this has been used in previous studies (Haniffa and Hudaib, 2006; Weir *et al.* 2002).

5. Results and discussion

5.1 Sample profile

Out of 520 questionnaires sent, only 112 were usable, which represents a response rate of 21.54 percent. With respect to sector, almost all sectors (industries) are covered in this study. Table II shows the profile of respondents in the study. For the composition of respondents, CEO/Managing Director represents the highest frequency of 36 (32.14 percent), followed by executive director with 30 (26.79 percent). The non-executive directors, comprising independent directors and non-independent non-executive directors were 24 (21.43 percent). Eleven (9.82 percent) company secretaries participated in the study. Responses from the company secretaries were also included in this study, as they are key management positions akin to the CEOs (Zainal

	Frequency	Percentage
Position		
Chairman	11	9.82
CEO/Managing director (MD)	36	32.14
Executive director (ED)[a]	30	26.79
Non-executive director (NED)[b]	24	21.43
Company secretary (CS)	11	9.82
Director type		
Executive director (ED)	68	60.71
Independent director (INE)	20	17.86
Non-independent non-executive director (NINE)	13	11.61
Industry type		
Consumer product (CP)	9	8.00
Industrial product (IP)	28	25.00
Trading and services (TS)	28	25.00
Technology (TECH)	3	2.70
Infrastructure (INFRA)	1	0.90
Construction (CONST)	17	15.20
Property (PROP)	15	13.40
Plantation (PLT)	11	9.80

Notes: [a]Executive directors other than the Chairman or the CEO/MD; [b]non-executive directors other than the Chairman

Table II. Profile of respondents from the survey questionnaire

Abidin, 2002). In total, based on the type of director, 60.71 percent of the respondents represent the executive directors, while 29.47 percent were non-executive directors.

The response bias analysis (t-test) for the dimensions of monitoring roles data was conducted for two groups of respondents to examine the homogeneity of samples. The first group is early ($n = 63$) versus late ($n = 49$) responses. Late responses refer to responses received after the follow-ups were done. The second group is non-executive directors ($n = 33$) versus executive directors or other responses ($n = 79$). The results show no significant difference between early and late responses for the dimension of monitoring roles, as shown by the insignificant t-value of each factor (MONITOR1 ($t = -0.839$), MONITOR2 ($t = 0.099$)). The result for the second group also shows no significant difference between non-executive directors' and executive directors' responses (MONITOR1 ($t = 0.973$), MONITOR2 ($t = 0.551$)). Thus, the response bias is not considered a significant issue in this study.

5.2 Board performance of monitoring roles

Results from the factor analysis extracted two dimensions of monitoring roles. These are named management oversight roles (MONITOR1) and performance evaluation roles (MONITOR2). Details of items in each factor are given in Appendix 2. The finding is somewhat different from that of Wan and Ong (2005) because they only managed to identify one dimension of monitoring roles. The difference may be due to the instruments used to capture board performance items.

5.3 Descriptive statistics of variables

Based on the common definition of board leadership (BLEAD), Table III shows that about 83.9 percent of the sample companies have different persons acting as the CEO/MD and the chairman of the companies. Even though the MCCG Code recommends that companies have independent leadership, some companies (about 16.1 percent) still choose a combined leadership structure.

Table IV reports the descriptive statistics of continuous variables. The average board size (BSIZE) is 7.66 with a minimum of four directors and maximum of 13 directors. The board size of the sample companies in this study is not much different from that in the study by Kuala Lumpur Stock Exchange and PricewaterhouseCoopers (1999) of eight directors. On average, the companies have a higher proportion of independent directors (0.42), meaning that one third of the directors or two members should be independent directors (Finance Committee on Corporate Governance, 2001). The average proportion of non-independent non-executive directors (NINE) in a company is 0.24 (which is about two directors). The proportion of NINE in this study is quite low compared to that in the study by Kuala Lumpur Stock Exchange and PricewaterhouseCoopers (1999), which found an average of three NINE in a public listed company.

Table III.
Descriptive statistics of categorical variable

BLEAD	Frequency	Percentage
CEO = Chairman (0)	18	16.1
CEO ≠ Chairman (1)	94	83.9

Note: $n = 112$

Variables	Mean	SD	Skewness	Kurtosis	Minimum	Maximum
BSIZE	7.66	1.79	0.47	−0.22	4	13
INE	0.42	0.11	1.01	0.97	0.30	0.83
NINE	0.24	0.18	0.27	−0.93	0.00	0.67
NED	0.66	0.19	−0.04	−1.13	0.30	1.00
FMEET	5.79	2.20	1.90	4.15	4	15
PMEET (percent)	93.70	5.48	−1.15	1.35	75.00	100.00
TEN (years)	6.78	3.54	0.94	0.91	1.33	18.00
PMDIR (percent)	56.79	31.22	−0.18	−1.00	0.00	100.00
MMDIR	1.73	1.34	0.91	0.58	0.00	6.50
MOWN (percent)	23.80	23.06	0.34	−1.32	0.00	79.10
MONITOR1	4.11	0.61	−0.38	−0.18	2.33	5.00
MONITOR2	3.74	0.80	−0.53	−0.12	1.50	5.00
LGTA	20.40	1.25	0.70	0.26	17.93	24.46

Note: $n = 112$

Table IV. Descriptive statistics of continuous variables

The frequency of meetings (FMEET) conducted is about 5.79 times per year with a minimum of four times to a maximum of 15 times. The percentage of attendance in meeting of directors (PMEET) is quite high with an average of 93.70 percent. By company, the average tenure (TEN) of non-executive directors serving on the board is about 6.78 years with a minimum period of 1.33 years and a maximum period of 18 years. For multiple directorships (PMDIR), on average, more than 50 percent of the non-executive directors in a company have at least one additional directorship in other PLCs. Multiple directorships per non-executive director (MMDIR) in a company are 1.73 with a maximum of 6.50. Individually, the maximum multiple directorships held by directors reached the maximum limit of ten directorships in PLCs. Some of them even have additional directorships in non-public listed companies, societies and government agencies. For managerial ownership (MOWN), on average, executive directors hold 23.80 percent shareholdings. For board performance, on average, the means are more than 3.00 with MONITOR1 (management oversight roles) having higher scores than MONITOR2 (performance evaluation roles).

5.4 Correlations among variables

Table V reports the correlations among the variables of the study. In general, most correlations are less than 0.80, except for the correlation between the non-independent non-executive directors (NINE) and the non-executive directors (NED). Board size (BSIZE) is found to be positively correlated with firm size (LGTA) and the proportion of non-independent non-executive directors (NINE). However, board size is negatively correlated with the percentage of attendance at meetings (PMEET) and the proportion of independent directors (INE). This means that companies with a larger board size tend to have a lower percentage of board attendance at meetings and independent directors.

For board leadership (BLEAD), there is a positive correlation between board leadership and the proportion of non-independent non-executive directors (NINE) and the percentage of attendance at meetings (PMEET). A negative correlation is found between board leadership and managerial ownership (MOWN). This suggests that companies with independent leadership tend to have a higher proportion of

Table V.
Pearson correlations between internal corporate governance variables, control variable, and board performance

	BSIZE	BLEAD	INE	NINE	NED	PMEET	LGTEN	MMDIR	MOWN	LGTA	MONITOR1	MONITOR2
BSIZE	1.0											
BLEAD	0.15	1.0										
INE	−0.22**	−0.12	1.0									
NINE	0.20**	0.25***	−0.27***	1.0								
NED	0.07	0.18*	0.32***	0.82***	1.0							
PMEET	−0.31***	0.22**	0.09	−0.16*	0.16*	1.0						
LGTEN	−0.03	−0.07	−0.03	−0.21**	−0.22**	0.25***	1.0					
MMDIR	0.05	0.15	0.21**	0.10	0.22**	−0.04	−0.01	1.0				
MOWN	−0.08	−0.20**	−0.07	−0.59***	−0.63***	0.08	0.17*	−0.10	1.0			
LGTA	0.29***	0.09	0.10	0.14	0.20**	−0.05	0.05	0.35***	−0.23**	1.0		
MONITOR1	0.08	−0.08	−0.15	0.11	0.02	−0.06	−0.04	−0.09	0.05	0.23**	1.0	
MONITOR2	0.09	−0.09	−0.23**	0.10	−0.03	−0.05	−0.03	0.06	0.16*	0.09	0.59***	1.0

Note: $^{*}p < 0.10$; $^{**}p < 0.05$; $^{***}p < 0.01$

non-independent non-executive directors (NINE) and a higher percentage of meeting attendance (PMEET), but a lower percentage of managerial ownership (MOWN).

The proportion of non-independent non-executive directors (NINE) is found to be negatively correlated with managerial ownership (MOWN). Smaller companies tend to have higher managerial ownership (MOWN), while larger companies tend to have more management oversight roles (MONITOR1). Companies with lower proportion of independent directors (INE) and a higher percentage of managerial ownership (MOWN) tend to have greater involvement in performance evaluation roles (MONITOR2). Directors with multiple directorships are more attached to larger companies, and independent directors are more inclined to have higher multiple directorships.

5.5 Multiple regression between internal corporate governance and monitoring roles

Table VI shows the results of multiple regression analysis between internal corporate governance and management oversight roles (MONITOR1). In Model 1, using NED as the measure of board composition, the results indicate that multiple directorship is negatively related to management oversight roles ($p < 0.10$). In Model 2, using NINE as the measure of board composition, the results show that management oversight roles are positive and significantly related to the proportion of NINE ($p < 0.10$) and managerial ownership ($p < .10$). Similar to Model 1, multiple directorships are found to be negatively related to management oversight roles. Regression analysis using independent directors as the measure of board composition shows that none of the corporate governance mechanisms is significant ($R^2 = 13.01$ percent, $F = 2.56$, $p = 0.014$; results not shown in the text). For the control variable, it is found that larger companies are associated with higher management oversight roles in all models.

The results signify the importance of having non-independent non-executive directors (NINE) to undertake greater management oversight roles. Because they may have significant interests in the company, they need to make sure that management carries out their roles according to specific contracts. The insignificant relationship

	Model 1		Model 2	
	B	*t*-value	B	*t*-value
Constant	1.766	1.30	1.689	1.29
LGTA	0.142	3.06***	0.147	3.22***
BSIZE	0.001	−0.02	−0.010	−0.30
BLEAD	−0.116	−0.80	−0.150	−1.04
NED	0.282	0.79		
NINE			0.687	1.97*
PMEET	−0.444	−0.44	−0.402	−0.40
LGTEN	−0.120	−0.54	−0.110	−0.48
MMDIR	−0.078	−1.89*	−0.076	−1.88*
MOWN	0.371	1.29	0.540	1.97*
R^2	0.113		0.140	
F-statistics	1.64		2.09	
Significance of *F*-statistics	0.124		0.043	
n	112		112	

Notes: $^{*}p < .10$; $^{**}p < 0.05$; $^{***}p < 0.01$

Table VI. Multiple regression between internal corporate governance and management oversight roles (MONITOR1) between independent directors and management oversight roles is not in line with the corporate governance literature on the positive effect of independent directors on enhancing the monitoring roles. This result is consistent with previous studies, which found that independent directors are not significantly or negatively related to firm performance (Yermack, 1996; Agrawal and Knoeber, 1996; Bhagat and Black, 1999).

The significant relationship with managerial ownership (MOWN) suggests that when managers hold a higher percentage of ownership in a company, greater management oversight roles are conducted to protect managers' interests, as a higher percentage of ownership would align managers' interests with the shareholders' interests. The results are consistent with the results of Bhagat and Black (1999) and Wiwattanakantang (2001). The negative relationship of multiple directorships with management oversight roles suggests that non-executive directors with multiple directorships lead to less activities being conducted to monitor management. This result is consistent with the "busyness hypotheses".

For the relationship between internal corporate governance and the evaluation of managers' performance (MONITOR2), the result in Table VII shows that the proportion of non-independent non-executive directors (NINE) is positively related to MONITOR2 ($p < 0.01$) in Model 2. However, independent directors are found to be negatively related to MONITOR2 ($p < 0.05$) in Model 1. The result may be due to less involvement of independent directors in evaluating the performance of managers. Managerial ownership (MOWN) is found to be significant and positively associated with MONITOR2 in both models. Other variables are not significantly related to MONITOR2.

6. Conclusion

The results of the study indicate the different impact of internal corporate governance mechanisms on each dimension of monitoring roles. For the management oversight

	Model 1		Model 2	
	B	t-value	B	t-value
Constant	2.586	1.61	1.450	0.92
LGTA	0.111	1.57	0.107	1.47
BSIZE	0.003	0.06	0.010	0.17
BLEAD	−0.142	−0.78	−0.149	−0.83
INE	−1.663	−2.31**		
NINE			1.321	2.85***
PMEET	−0.297	−0.22	−0.264	−0.20
LGTEN	−0.021	−1.04	−0.013	−0.66
MMDIR	−0.193	−0.25	−0.055	−0.74
MOWN	0.599	2.07**	1.245	4.05***
R^2	0.111		0.120	
F-statistics	2.11		3.35	
Significance of F-statistics	0.041		0.002	
n	112		112	

Notes: $^{*}p < 0.10$; $^{**}p < .05$; $^{***}p < 0.01$

Table VII. Multiple regression between internal corporate governance and performance evaluation roles (MONITOR2) roles, *H3*, *H4* and *H7* are supported. For the performance evaluation roles, *H3* and *H7* are supported. The study highlights some internal corporate governance mechanisms (non-independent non-executive directors and managerial ownership), which are found to be significantly related to the extent of the roles conducted in both dimensions of monitoring functions. The results support the importance of having non-independent non-executive directors as effective monitoring mechanisms. This finding suggests that non-independent non-executive directors have relevant incentives (represent blockholders and/or have significant shareholdings in the company) to monitor management decisions and evaluate management performance. The positive relationship of non-independent non-executive directors supports the argument by Klein (1998) and Roberts *et al.* (2005) in terms of the possibility of the increased involvement of non-independent non-executive directors in monitoring management. The negative and significant relationship between independent directors and performance evaluation roles has some implications for the policy makers and regulators to improve corporate governance. Attention should be given to the roles of independent directors to increase their involvement in performance evaluation roles.

The significant relationship between managerial ownership and monitoring roles supports the role of managerial ownership as an effective mechanism to align managers' decisions with shareholders' interests. The negative relationship between multiple directorships and monitoring roles has some implications for the current practices of allowing directors to hold up to ten directorships in public listed companies. Multiple directorships are found to have a negative impact on the management oversight roles; however, they have no influence on the performance evaluation roles of BOD. The study also shows that board size, board knowledge (based on board tenure), and frequency of board meetings do not influence the execution of monitoring roles by the BOD. The insignificance of board size is not consistent with agency theory that a small board is considered to be an effective board. The insignificant findings for board knowledge as measured by board tenure and board process as measured by the frequency of board meetings may indicate that neither variable matters in the execution of monitoring roles by the BOD. However, the findings may also indicate that the measurement used may not really represent the variables. Thus, future studies should consider other proxies to further research the impact of these variables on the monitoring roles of the BOD.

The main limitation of the study is that the sample of the study only focuses on the main boards of companies. Thus, the findings of the study may not be generalized to other boards. Further research should be conducted on other boards to determine whether the survey instruments for monitoring roles hold for other boards. The other limitation is the low R^2 in both models. However, the fact that the models are significant at 5 percent when NINE is used in the models indeed indicates that the findings from this study are still relevant.

Further research should be conducted on multiple directorships, as limited knowledge is available concerning the status of multiple directorships in Malaysia, such as determining the optimum multiple directorships for each type of directors. Another area of concern that requires further attention is the performance evaluation roles of the board of directors. This is in line with the revised code of the corporate governance (Securities Commission Malaysia, 2007) to be more transparent in the board evaluation process.

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Appendix 1

Please **circle** a number from 1 to 5 to indicate to what extent board of directors performs various board tasks in the company in the financial year 2006.

1	**Very little**
2	**A little**
3	**To an average extent**
4	**Much**
5	**Very much**

Board of directors…

	Very little		……………		Very much
1. ensures corporate survival (protect shareholders’ interests)	**1**	**2**	**3**	**4**	**5**
2. specifies lines of authority of management and board	**1**	**2**	**3**	**4**	**5**
3. monitors top management in decision making	**1**	**2**	**3**	**4**	**5**
4. formally evaluates performance of top company executives	**1**	**2**	**3**	**4**	**5**
5. evaluates the skill mix on the board	**1**	**2**	**3**	**4**	**5**
6. has internal mechanisms to evaluate board members’ performance yearly	**1**	**2**	**3**	**4**	**5**
7. involves in succession planning for top management	**1**	**2**	**3**	**4**	**5**
8. requires information of company performance showing progress	**1**	**2**	**3**	**4**	**5**
9. reviews company performance against strategic plan	**1**	**2**	**3**	**4**	**5**
10. ensures compliance with statutory and other regulations	**1**	**2**	**3**	**4**	**5**
11. reviews social responsibilities of the company	**1**	**2**	**3**	**4**	**5**

Figure A1.
Questionnaire items on monitoring roles of BOD

Appendix 2

Dimensions	Factors 1	2
MONITOR1 (six items)		
Ensure compliance with statutory and other regulations	*0.784*	−0.054
Review company performance against strategic plan	*0.784*	0.235
Require information of company performance showing progress	*0.734*	0.266
Specify lines of authority of management and board	*0.671*	0.405
Ensure corporate survival	*0.660*	0.383
Monitor top management in decision making	*0.636*	0.404
MONITOR2 (four items)		
Have internal mechanisms to evaluate board members' performance yearly	0.110	*0.824*
Evaluate the skill mix on the board	0.222	*0.805*
Evaluate performance of top company executives	0.252	*0.787*
Involve in succession planning for top management	0.332	*0.771*
Eigenvalue	5.06	1.38
Percentage variance explained	50.63	13.75
Cronbach's α	0.86	0.85

Notes: The KMO is 0.855, with Bartlett's test of sphericity being significant at 0.000. The actual questionnaire had 11 items. However, factor analysis and reliability analysis identified only ten items fitting into the two factors. Italicised loadings indicate the inclusion of that item in the factor

Table AI. Results of the factor analysis and reliability analysis of board performance in monitoring roles

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