

CORPORATE GOVERNANCE MECHANISMS AND THE PERFORMANCE OF MALAYSIAN LISTED FIRMS

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Abstract

In the aftermath of the Asian Financial crisis in 1997/1998, the Malaysia Securities Commission (SC) issued the Malaysian Code on Corporate Governance in 2000 (MCCG 2000). It was subsequently revised in 2007 following the Enron and Transmile debacles. In 2012, the SC issued the latest MCCG 2012 which introduced several new recommendations that are in line with developments in other parts of the world. Hence, the purpose of this study is to investigate the influence of the structure of the board and its activities on firm performance post MCCG 2007. The study also aims to shed light on the effectiveness of the board of directors since the issuance of MCCG 2000 and of MCCG 2007. It also aims to reveal the preparedness of listed firms in Malaysia to embrace MCCG 2012. Using a population of non-finance listed firms for the 2009, 2010 and 2011 financial years, it was found that board independence, chief executive officer (CEO) duality, directors' busyness, nomination committee independence, the establishment of a risk management committee (RMC) and board meetings are not associated with firm performance, i.e. Tobin's q. However, the market appears to be in favour of a larger board size. As for return on assets (ROA), it is not associated with board independence, board size, directors' busyness and nomination committee independence. On the other hand CEO duality and the establishment of a RMC improve ROA, while board meetings are detrimental to ROA. It can therefore be concluded that board independence is not associated with either Tobin's q or ROA. Hence, any corporate governance reforms should not over-emphasize the representation of independent directors on the board, rather the focus might be shifted to board activities, such as board meetings and the establishment of a RMC. With regard to board size, since the market is in favour of a larger board size, firms should increase the board's size to enable the appointment of women directors to the board. Finally, combining the CEO and board chairman roles should not be disallowed as the market views this favourably. Hence, the 'one-hat approach' does not appear to be applicable in the case of CEO duality.

Keywords: Board Independence, CEO Duality, Directors' Business, Nomination Committee, Risk Management Committee

1. INTRODUCTION

The board of directors is a very important element of internal corporate governance in a company. A former British colony, Malaysia, has adopted a unitary board structure, where the board plays a dual-purpose role of leadership and control. Therefore, the board needs to be effective in both tasks (Finance Committee, 1999). The importance of the board of directors is founded on the premise that it is the highest body in a firm's overall internal governance mechanism. In fact, Jensen (1993, p. 40) argues: "The board, at the apex of the internal control system, has the final responsibility for the functioning of the firm." As stated by the Finance Committee on Corporate Governance in Malaysia (1999, p. 9), "The key to good governance lies in getting the right board in place." Hence, having the right corporate governance mechanism provides some reassurance to shareholders that the board can ensure that managers act in the shareholders' best interest (Shleifer & Vishny, 1997). In fact, it is argued that a variety of organizational outcomes could be influenced by board structure, i.e. board

composition and leadership structure, including a firm's financial performance (Dalton et al., 1998). Therefore, the concept of 'one-size-fits-all' corporate governance mechanisms may not be applicable to all companies because each has its own needs (Nicholson & Kiel, 2004; Society of Management Accountants of Canada, 2002). Demsetz (1983) and Hermalin and Weisbach (2003) argue that the corporate governance mechanisms of a firm are determined endogenously in the context of the firm's environmental variables. Therefore, the corporate governance mechanisms that a firm has adopted should match the firm's needs as their effectiveness depends on critical environmental variables (Aguilera et al., 2008) and the firm will change the configuration of their board members in response to the external environment (Hillman et al., 2000; Lynall et al., 2003). Thus, variation in the board structure among listed firms is expected to persist.

Despite the fact that several changes have been made to corporate governance codes around the world, the link between corporate governance mechanisms and firm performance remains unclear

(e.g. Anderson & Reeb, 2004; De Andres et al., 2005; Giovannini, 2010; Jackling & Johl, 2009; McKnight & Mira, 2003). In the Malaysian context, Abdullah (2004), whose study covers Malaysian listed firms for the period 1994–1996, i.e. before the 1997/1998 Asian financial crisis, reports that neither board independence nor chief executive officer (CEO) duality is associated with firm performance. Further, subsequent studies in the Malaysian context provide inconclusive evidence on the effectiveness of the board structure as measured by the firm's financial performance (e.g. Chan, 2004, 2005; Haniffa & Hudaib, 2006; Mohd Ghazali, 2010; Ponnu, 2008). Haniffa and Hudaib (2006) examined Malaysian listed firms for the period 1996–2000; Mohd Ghazali (2010) examined Malaysian listed firms for the 2001 financial year; while Ponnu (2008) re-examined the effect of board independence and CEO duality on firm performance in 100 Malaysian listed firms for the financial year 2005. Subsequently, Kamardin and Haron (2011) found that independent directors in Malaysia are not associated with management oversight roles. In addition, their evidence also shows that independent directors are negatively associated with performance evaluation roles. Hence, their evidence suggests that independent directors do not focus on the control roles, which implies that they perhaps focus more on the service or advisory roles.

The independence of the board of directors and directorial and managerial ownership are two important corporate governance tools that can be effective in maintaining managerial discipline and in aligning the interests of owners and managers, as argued in agency theory (e.g. Fama & Jensen, 1983; Jensen & Meckling, 1976). However, in Malaysian listed firms, ownership is almost always highly concentrated. It has been reported that Malaysia is second only to Indonesia in terms of the percentage of firms under family ownership in the Southeast Asian region (SCMP, 2002). Hence, the ownership pattern in listed firms in Malaysia is markedly different from that in the US or the UK, where agency theory originated. Thus, in Malaysia, the board's effectiveness could be affected negatively rather than positively by the concentration of ownership because the firm's controlling shareholders or their family members or their nominee directors usually sit on the board. In the case of family-owned firms, the family members are also in the firm's top managerial positions. Therefore, the board is often seen as performing a ceremonial role, i.e. providing a rubber stamp for the activities of managers, because management dominates the board (Mallette & Fowler, 1992). Hence, it is argued that in family-owned firms, independent directors are appointed not to monitor management, as posited by agency theory, but rather in the concentrated ownership environment, their presence is more likely due to their ability to provide expertise and advice on strategic direction (Anderson & Reeb, 2004; Johnson et al., 1996). Further, as the appointment and reappointment of independent directors is controlled by family members, the independent directors are unlikely to go against the wishes of the controlling shareholders (Jaggi et al., 2009). Therefore, in family-owned firms,

the priority is to maintain family relationships and unity in order to secure the family's survival (Bertrand & Schoar, 2006) rather than to control the firm's management, who might also be family members.

In light of the foregoing, the objective of this study is to examine the effect of board structure and board activities on the performance of Malaysian listed firms following the 2008 global financial crisis. It has been argued that corporate governance mechanisms change in response to external forces (e.g. Aguilera et al., 2008; Hillman et al., 2000; Lynall et al., 2003). Therefore, the 2008 global financial crisis must have influenced listed firms in Malaysia to react in some way and perhaps this included altering their corporate governance mechanisms to ensure their survival. Moreover, the crisis might have increased the motivation of the independent directors to perform their duties more effectively. In addition, the issuance of two new provisions, Sections 317A and 320A, which are contained in the revised Capital Market Services Act (CMSA), by the Securities Commission (SC) in Malaysia in 2010 is assumed to have enhanced the monitoring roles of the independent directors in Malaysian public listed firms. It is anticipated that the findings of this study will add to our knowledge on the effect of corporate governance mechanisms on firm performance in Malaysia, the evidence for which is currently inconclusive.

Two measures for firm performance are used in this study. First, return on assets (ROA) was used as a measure of accounting-based firm performance. Second, Tobin's q was used as a measure of market-based firm performance. The evidence reveals that board independence, CEO duality, directors' busyness, nomination committee independence, the establishment of a risk management committee (RMC) and board diligence are not associated with firm performance, i.e. Tobin's q. Nevertheless, the market appears to be in favour of a larger board size. Perhaps, the market prefers a larger board to accommodate the appointment of more independent directors to strengthen board independence. As for ROA, it is not associated with board independence, board size, directors' busyness and nomination committee independence. On the other hand, CEO duality and the establishment of a RMC improve ROA, while board diligence is detrimental to ROA. It can therefore be concluded that board independence is not associated with either Tobin's q or ROA. Hence, any corporate governance reforms should not over-emphasize the representation of independent directors on the board, rather the focus could be shifted to board activities, such as board meetings and the establishment of a RMC. With regard to board size, since the market is in favour of a larger board size, firms should increase the board's size to enable the appointment of women directors to the board.

The remainder of the paper is structured as follows: First, the theoretical framework is developed and the hypotheses are formulated. Next, the research methods used in this study are discussed. Then, the findings are presented, followed by a discussion thereof. The paper ends with a summary and some conclusions.

2. THEORY AND HYPOTHESES

2.1. Development of corporate governance in Malaysia

In an attempt to strengthen the corporate governance mechanisms of listed firms following the Asian financial crisis in 1997/1998, the SC in Malaysia issued the first Malaysian Code on Corporate Governance (MCCG) in 2000. Bursa Malaysia adopted MCCG 2000 in 2001 and all listed firms were required to 'comply or explain'. Since the issuance of MCCG 2000, many changes to corporate governance in Malaysia have been made as a result of several issues starting with the Enron debacle in the US 2000, the exposure of accounting irregularities in Transmile in Malaysia in 2007, and not least the 2008 global financial crisis. In particular, the SC issued a revised version of the MCCG in 2007 in response to the Transmile scandal and to incorporate the developments in corporate governance principles and practices in the US and the UK. The main focus of MCCG 2007 was on strengthening the audit committee and specifying the criteria that the nomination committee should consider when nominating new directors. It also states that there is a need for the nomination committee to assess annually the performance of the board as a whole and of each individual director. Then, in 2010, the SC established the Audit Oversight Board whose function is to monitor auditors of public interest entities in Malaysia. Also in 2010, the CMSA 2007 was amended to include Sections 317A and 320A, which authorize the SC to act against directors of listed companies who cause wrongful loss to a company as well as against any person who misleads the public through falsely preparing or auditing the financial statements of a company. These new sections are intended to serve as a reminder to all directors, especially independent directors, to discharge their fiduciary duties effectively.

In 2011, the SC issued the Corporate Governance (CG) Blueprint 2011, the aim of which was to further strengthen the corporate governance mechanisms in Malaysia. The intention of the CG Blueprint 2011 was to instill a culture of good governance that would replace the old 'box-ticking' mindset of corporate gatekeepers. One of the deliverables of the CG Blueprint 2011 was MCCG 2012. Taking all the initiatives and changes together, the corporate governance in Malaysian listed companies is now expected to be sound and effective because directors and management have to be mindful of the consequences of committing any wrongdoing. As a case in point, in October 2011, two former independent directors of Transmile were sentenced to one year in jail and fined RM300,000 each for having authorized the furnishing of misleading quarterly financial reports to Bursa Malaysia. The most recent issuance of the MCCG in 2012 emphasizes the importance of board independence by requiring that the board chairman be non-executive and in the case of a non-independent chairman, that the board should be composed of a majority of independent directors. It also suggested limiting the tenure of an independent

director to nine years and the formalization of the board through the creation of a charter. These several recommendations indicate the commitment of the authorities in Malaysia to ensure that boards act independently and objectively.

2.2. The Board Of Directors

The board is the most important element in a firm's internal corporate governance system due to the separation of ownership and control, which is common in today's firms (Gevuretz, 2004; Hillman & Dalziel, 2003). Stressing the importance of the board, which is at the helm of a company, the Finance Committee on Corporate Governance in Malaysia (SC, 1999) states that "...good corporate governance rests firmly with the board of directors. Shareholders and auditors necessarily only play secondary roles" (p. 61). The dominant view is that the primary role of the board is one of oversight, i.e., it is the board's responsibility to monitor management to ensure that management always acts in the interest of the firm's shareholders and the wider stakeholders and to provide guidance and leadership to management as and when needed (Fleischer et al., 1998; Waldo, 1985). While agency theory dominates the research perspective on corporate governance, other theories are complementary to rather than substitute agency theory (Dalton et al., 2003). These other theories are needed to explain, for instance, the director's role in terms of resources, services and strategy (e.g. Johnson et al., 1996; Zahra & Pearce, 1989).

The structure of the board has been the focus of much empirical research because it is the most important internal corporate governance mechanism of a firm (Jensen, 1993). The focus of most studies falls largely on the firm's financial performance as it enhances the firm's value via stronger shareholder equity. Nevertheless, empirical studies on the relationship between the board and the firm's financial performance have provided mixed results. Researchers have examined the influence of the board from a number of perspectives, such as investigating the link between the proportion of independent directors (i.e. board independence) and the firm's financial performance (Abdullah, 2004; Bhagat & Black, 2002; Bhagat & Bolton, 2008; Fields & Keys, 2003; Haniffa & Hudaib, 2006; Hermalin & Weisbach, 2003). Also, research on board structure has examined the effect of board size (Mak & Kusnaldi, 2005; Yermack, 1999), CEO duality (Abdullah, 2004; Haniffa & Hudaib, 2006; Lam & Lee, 2008) and ownership structure (Mak & Li, 2001; Mohd Ghazali, 2010; Morck et al., 1988) on performance as well as the effect of the independence of the board nomination committee (Brown & Caylor, 2006). Researchers have also examined board activity, for instance, the frequency of board meetings (Brick & Chidambaram, 2010; Vafeas, 1999) on firm performance. The role of board diversity has also been investigated in terms of gender (Abdullah & Ku Ismail, 2013; Campbell & Minguez-Vera, 2007), racial diversity (Abdullah & Ku Ismail, 2013; Richard, 2000), cultural diversity (Haniffa & Hudaib, 2006) and age diversity (Abdullah & Ku Ismail, 2013).

2.3. Board independence

Board independence is the main focus of corporate governance because the generally held view is that the more independent the board is, the more able it is to carry out its role of oversight of management, which is seen as the primary role of the board of directors (Berle & Means, 1932; Jensen & Meckling, 1986; Williamson, 1985). Due to the importance of board independence, all corporate governance codes that are issued by countries around the world focus on this issue, i.e. how to make the board independent of management. In a survey by the Shareholder Watchdog Group (MSWG, 2010), it was found that only 23% of Malaysian listed firms had a majority of independent directors on their board. This indicates that most Malaysian listed firms maintain only the minimum number of independent directors on their board. In other jurisdictions, the required representation of independent directors is higher. For instance, the UK Corporate Governance (CG) Code (FRC, 2010) requires at least half of the board size to be made up of independent directors, while the Australian Corporate Governance Council requires that independent directors hold the majority of seats on the board. To be in line with best practices in corporate governance, MCGG 2012 requires that independent directors are in the majority if the board chairman is not independent (SC, 2012).

It is argued that the major benefit of having independent directors on the board is their impartiality, which is crucial for the effective monitoring of management, as argued by agency theory (Fama & Jensen, 1983; Jensen & Meckling, 1976; Williamson, 1985). In addition, their experience can give the board the benefit of other skills that are not held by the other non-executive and executive directors, as argued by resource dependency theory (Pfeffer, 1972). Further, these independent directors have more connections with external organizations and therefore can provide more external resources (Hillman & Daziel, 2003; Peng, 2004). Hence, not only do independent directors help strengthen the board oversight function, they also broaden the board perspective and consequently the quality of the decisions taken by the board. Nevertheless, the empirical evidence for the above arguments is not conclusive. Studies have shown either positive, zero or even negative effects of board independence on board effectiveness. Weisbach (1988), for instance, found that a high proportion of independent directors on the board leads to the dismissal of the CEO when the firm records poor financial performance. Some later studies have found a positive relationship between certain characteristics of the board and firm performance (Anderson & Reeb, 2004; Bhagat & Black, 1999; Bonn, 2004; Kiel & Nicholson, 2003; McKnight & Mira, 2003). In contrast, other studies (e.g. Dalton et al., 1998; Weir & Laing, 2000; Weir et al., 2002) find little evidence to suggest that board characteristics affect firm performance. Moreover, some have found a negative relationship between the proportion of outside directors and firm performance (e.g. Agrawal & Knoeber, 1996). In the case of Malaysia, Abdullah (2004) shows that board independence is not associated with the firm's financial performance. His sample of firms

comprised non-financial firms listed on the Main Board of Bursa Malaysia for the period 1994–1996, which was prior to the Asian financial crisis of 1997/1998. However, Ponnuru (2008), using a sample of 100 non-financial firms listed on Bursa Malaysia for the 2005 financial year, also found that there is no relation between board independence and the firm's financial performance.

In Malaysia, which is an emerging economy, the issue of board independence is even more crucial because the agency costs are not solely related to the separation of ownership and control, as in developed countries such as the US and the UK. Rather, in Malaysia, the conflict is between the controlling owners and managers on the one hand and the firm's minority shareholders on the other. However, the seriousness with which the SC has taken the issue of board structure, especially board independence, since the Asian financial crisis and the rigour of the Bursa Malaysia in enforcing the SC's initiatives would suggest that board independence affects firm performance positively. Therefore the following hypothesis is proposed:

H1: Board independence is positively associated with firm performance.

2.4. CEO duality

CEO duality is another important issue in corporate governance. Here, the issue is whether the positions of the CEO and board chairman should be separated. There are advantages and disadvantages to separating these top two roles. However, the overall tendency of the argument is more inclined towards their separation. One of the reasons for separating these roles is that while the CEO heads the firm's day-to-day operations the board chairman leads the firm's board of directors which oversees the firm's management on behalf of the firm's absent owners, i.e. the shareholders. The importance of the board chairman's independence is crucial because it is the chairman who sets the meeting agendas and determines the flow of information. It is argued that a non-executive chairman will promote a high level of openness in board meetings (Miller, 1997). Where there is a lack of separation, this has been found to lead to the board being aligned with management rather than with shareholders, notwithstanding the presence of independent directors (Greenspan, 2002, 2003). The chairman ensures that different views are heard and that an array of ideas is brought to the table for discussion to enable harmonious and effective decision making. Leighton and Thain (1993) argue that the effectiveness of the board is largely dependent on the efficacy of the chairman. Moreover, the Cadbury report (1992) states:

[the Chairman is] primarily responsible for the working of the board, for its balance of membership subject to board and shareholders' approval, for ensuring that all relevant issues are on the agenda, and for ensuring that all directors, executive and non-executive alike, are enabled and encouraged to play their full part in its activities (p. 21).

The MCGG (2000, 2007) recommends the separation of the CEO and board chairman positions. However, it also states that, if the two posts are combined, a strong independent element on the board should exist. Further, it requires that the decision to combine the two roles needs to be

publicly explained. The issue of CEO non-duality is also raised in the CG Blueprint (SC, 2011). The concern is that, given the concentrated ownership in Malaysian listed firms, the CEO and the board chairman tend to have familial relationships. Thus, even though there is some separation because the chairman is non-executive, the concentration of power remains, which makes it difficult for independent directors to exercise their monitoring role effectively. While the CG Blueprint 2011 recommends that the chairman be a non-executive director, it is of the view that the chairman should be an independent director. In MCCG 2012, it is recommended that the positions of chairman and CEO should be held by different individuals, and that the chairman should be a non-executive member of the board. It also states that the majority of the board should be independent directors if the chairman of the board is not independent. Although the argument for CEO duality outweighs that for combining the two posts, empirical studies reveal inconclusive results in this regard (e.g. Boyd, 1995; Coles & Hesterly, 2000; Rechner & Dalton, 1991). Rechner and Dalton (1991), for instance, report a positive relationship between CEO duality and firm performance, whereas Boyd (1995) found that CEO non-duality improves firm's performance. Others have found no significant difference in the performance of firms with CEO duality and in those without (Daily & Dalton, 1997; Dalton et al., 1998). Indeed, Daily and Dalton (1997) suggest that the separation of the CEO and board chairman positions would result in misdirected effort. In the case of Malaysia, Abdullah (2004) and Ponnuru (2008) found that CEO duality is not associated with a firm's financial performance. Nevertheless, the various versions of the MCCG (2000, 2007 and 2012) have continuously addressed the issue of the separation of the role of chairman and CEO and underscored the importance of the chairman's independence. Therefore, the following hypothesis is formulated:

H2: CEO duality is positively associated with firm performance.

2.5. Board size

The number of directors on a board has been a contentious issue for some time. Having an optimal board size is very important so that the chairman can effectively handle the discussion in a board meeting and every director is given a chance to give their view on the issue being discussed. Too small a board may limit the board perspective; too large a board may lengthen the discussion, which reduces the speed of the decision-making process and communication problems may arise. While it is important to have a board with members from diverse backgrounds, implying a large board size, it is also important to maintain group cohesion and participation. Due to the difficulty of determining the right board size, empirical research has provided mixed findings on the effect of board size on the firm's financial performance. Yermack (1996) and Eisenberg, Sundgren and Wells (1998) provide evidence that smaller boards are associated with higher firm performance. Large boards are thought to be associated with problems of communication and cohesiveness and the danger of not only developing factions and conflicts among board

members (O'Reilly et al., 1989), but also a lack of coordination (Huther, 1997) and limiting the board's ability to control management (Eisenberg et al., 1998, p. 37). On the other hand, the idea of a large board has been supported on the grounds that it would provide a greater capacity for monitoring (Boyd, 1990; Johnson et al., 1996; Mace, 1986; Pearce & Zahra, 1992), advice and networking (Adam & Mehran, 2003; Anderson et al., 2008; Klein, 1998; Mansi & Reeb, 2004; Pfeffer, 1972; Singh & Harianto, 1989).

Some researchers give a recommendation on the optimal board size. For instance, Lipton and Lorsch (1992) and Jensen (1993) observe that when board size goes beyond seven or eight directors, the effectiveness of the board control functions is reduced and it is easier for the CEO to dominate. However, the code on corporate governance in various countries requires companies to establish a number of committees such as an audit committee, nomination committee, remuneration committee and RMC to mitigate the likelihood of this occurring. In view of these requirements, Lipton and Lorsch (1992) suggest that the board size should consist of eight or nine and a maximum of 10 members as this size should lead to more effective discussion while allowing for the staffing of board committees.

The board size in Malaysia ranges from four to 15 and the average is nine (8.82) (Abdullah, 2010). However, MSWG (2010) states that the average board size for main market companies is seven (7.74). The MCCG (2000, 2007, 2012) does not state an optimal board size. Nevertheless, all the versions of the MCCG state that the number of directors affects board effectiveness. Consequently, in view of the various board committees that need to be maintained by a company's board, the size of many boards of directors in Malaysia needs to be increased as well, especially in terms of the number of independent directors. Currently, boards are required to maintain an audit committee, nomination committee and remuneration committee, all of which require the presence of independent directors. In addition, some boards also establish a RMC, which also requires the presence of independent directors. Further, in view of the current business environment, the size of the board is expected to increase to accommodate the appointment of more directors with specific areas of expertise that are relevant to the nature of the business. This will result in a more balanced board that is able to supply information and expertise to the firm in order to secure critical resources (Hillman & Daziel, 2003; Klein, 1998; Pfeffer, 1972; Pfeffer & Salancik, 1978). In response to resource dependencies and regulatory pressures, organizations create large boards to acquire directors from different backgrounds (Pearce & Zahra, 1992; Pfeffer, 1972). Hence, the following hypothesis is postulated:

H3: Board size is positively associated with firm performance.

2.6. Directors' Busyness

Most non-executive directors and independent directors also hold full-time positions in other organizations, but some are also retirees. They also tend to be CEOs of other listed firms, professionals

in their own field or politicians. Given the demands of their full-time job and the demands placed upon them as directors of listed companies, the Bursa Malaysia Listing Requirements limit a director of a listed firm to holding not more than 25 directorships in other companies, i.e. not more than 10 directorships in listed firms and not more than 15 directorships in unlisted firms. However, the CG Blueprint 2011 states that an individual should hold no more than five directorships in listed firms. In a survey by Bursa Malaysia (2010, cited in SC, 2011), it was found that the average number of directorships held by a director is five and that the majority of directors hold either one or two directorships. In the case of the UK, the CG Code (FRC, 2010) does not specify a particular number of directorships; rather it requires that the board does not give consent to a full-time executive director taking more than one non-executive directorship or the chairmanship in a FTSE 100 company. In the US, the National Association of Corporate Directors guidelines recommend that senior corporate executives including CEOs hold no more than three outside directorships. Mace (1986) argues that outside directorships are valuable to executives as they provide prestige, visibility and commercial contacts. While Fama (1980) and Fama and Jensen (1983) contend that the number of outside directorships held by a director serves as an important means to develop a reputation as a monitoring specialist. However, holding numerous outside directorships leads to overcommitment (Ferris et al., 2003; Fich & Shivdasani, 2006).

Empirical evidence on the link between outside directorships and firm performance is mixed. While the findings of some studies (Coles & Hoi, 2003; Gilson, 1990; Kaplan & Reishuh, 1990) support the reputation hypothesis, others (Core et al., 1999; Fich & Shivdasani, 2006; Shivdasani & Yermack, 1999) show that the number of outside directors hurts firm performance due to overcommitment. Jiraporn, Singh and Lee (2009) document a U-shaped relationship, where in the case of smaller boards there is a negative association between outside directorships and board committee memberships, which supports the busyness hypothesis, while in the case of larger boards the reputation hypothesis is supported.

Based on a survey, Bursa Malaysia (2010) found that the majority of directors of listed firms (77.1%) hold only one directorship while only a small proportion (i.e. 15.6%) hold two directorships. Given the difficult workload and the high commitment that is expected from Malaysian directors, it appears that directors in Malaysia prefer to hold a small number of directorships. This may be due to the high regulation of the market for public listed companies and the concomitant commitment that is required, which deters them from holding more than one directorship. Thus, the busyness hypothesis that seems to hold in Malaysia is as follows:

H4: Outside directorships held by independent and non-executive directors are negatively associated with firm performance.

2.7. Nomination Committee

A nomination committee is tasked with identifying candidates who can be appointed as directors and

with reviewing the performance of the board. The committee also recommends to the board those directors whom it believes should fill the seats on the board's committees. The MCCG (SC, 2000) recommends that each firm appoints a nomination committee composed solely of non-executive directors, the majority of whom should be independent. The CG Blueprint (SC, 2011), realizing the importance of the nomination committee in the recruitment of directors and the assessment of the quality and performance of members of the board, suggests that the establishment of a nomination committee should be made mandatory. Indeed, it goes further by proposing that the chairman should be an independent director as required in the UK CG Code (FRC, 2010). The CG Blueprint (SC, 2011) also suggests that the role of the nomination committee be expanded to include the annual assessment of independent directors including their time commitment and their ability to fulfil their responsibilities.

Evidence on the effect of nomination committee independence on firm performance is limited. Brown and Caylor (2006) found a positive relation between nomination committee independence and firm performance. However, in the case of Malaysia, Abdullah et al. (2010) did not find any association between nomination committee independence and the incidence of financial restatement. The insignificant role of nomination committee independence reported in Abdullah et al. (2010) is due to the fact that the study investigated financial restatements during 2002-2005. The recommendation that firms set up a nomination committee was only introduced in MCCG 2000 (SC, 2000), so the problems that led to financial restatement might have occurred before the formation of the nomination committees studied. After a few years of establishment, it is likely that a nomination committee would become more effective in carrying out its duties and would be an integral part of the corporate governance mechanism. In addition, an appointment to the board starts with a nomination by this committee. Therefore, the more independent and established the nomination committee, the more qualified the directors appointed to the board because the committee is no longer as heavily influenced by the firm's management. Hence, the following hypothesis is proposed:

H5: Nomination committee independence is positively associated with firm performance.

2.8. Risk Management Committee

Effective risk management is vital in today's volatile economic environment. A RMC is established to assist the board in managing risk so that the company is not exposed to any risk that would affect its ability to achieve its objectives. If management is not monitored closely by the RMC, it may choose high-risk projects because of the predicted high returns, as argued in agency theory. The presence of a RMC deters management from taking on high-risk projects or engaging in high-risk activities. In addition, a RMC ensures that the firm has a system in place that continuously identifies, measures and manages risk so that it is always at an acceptable level. Even though the establishment of a

RMC is clearly vital, none of the versions of MCCG specifically state that a stand-alone RMC should be established. Rather, the risk management function is subsumed in the internal audit function, which MCCG 2007 requires firms to form (SC, 2007). However, following the 1997/1998 Asian financial crisis, banks in Malaysia usually maintain a RMC as a matter of good practice and a proactive measure.

The lack of risk management among Malaysian listed firms was evident during the 1997/1998 Asian financial crisis. During the economic boom in 1993–1995, listed companies expanded their operations through debt financing, e.g. bank loans and loan stocks. When the economy contracted in 1997/1998, these companies were not able to service these loans and many companies went bankrupt or became financially distressed. The financially distressed companies were put into the PN4 category, which was subsequently changed to PN17.

An effective RMC will ensure that the risk level is always acceptable so that the firm is not subjected to excessive operational and financial risks. In fact, Yatim (2010) found that the establishment of a RMC by Malaysian listed firms is associated with a strong board structure, i.e. a high proportion of non-executive board members and CEO non-duality. Hence, this evidence indicates that independent boards place an emphasis on implementing an effective risk management system in their firms to ensure that the interests of shareholders are protected, in contrast to the approach taken by less-independent boards. Thus, the hypothesis is that:

H6: The establishment of a risk management committee is positively associated with firm performance.

2.9. Board Diligence

Boards that actively advise, give input and lead and monitor management are arguably better than boards that are less active. This activeness is also referred to as board diligence, which is always measured by the number of board meetings held annually; the more frequent the meetings, the more diligent the board. Board meetings serve as an effective way to monitor the performance of the firm (and thus the performance of management), get feedback from management, identify any problems or issues, identify solutions and provide advice or guidance to move forward. Therefore, the more frequently the meetings are held, the more and better the interaction and communication between the board and management. The MCCG (SC, 2000, 2007) does not specifically mention the frequency of board meetings; it only states that the board should meet regularly. However, Brick and Chidambaran (2010) argue that board activity can increase firm performance; in fact, they show that board activity, measured by board meetings, improves Tobin's q. However, their evidence shows that board activity is not associated with ROA.

The frequency of board meetings can enable the board to detect any major problems the company is facing early on, which enables the board to identify the solution quickly. When there is a high frequency of meetings, many matters can be discussed, including risk management issues. It is therefore not surprising that Yatim (2010) found that board diligence is associated with the

establishment of a stand-alone RMC. Therefore, it is hypothesized that:

H7: Board diligence is positively associated with firm performance.

3. METHODS

Data were collected from companies listed on the Bursa Malaysia Main Market (2009–2011), resulting in a total of 2,510 firm years (2009: 844; 2010: 844; 2011: 822) before excluding firms falling under the categories of finance, real estate investment trusts (REITs), closed-end funds, infrastructure project companies (IPCs), PN4 and PN17. Financially distressed firms are categorized by Bursa Malaysia under PN17 (or PN4 prior to 2005). To continue having listed status, these distressed companies need to regularize their financial situation within a specified time frame. The year 2009 was chosen as the start year as it falls two years after the first revision of the MCCG was issued in 2007 (SC, 2007). It was also one year after the global financial crisis of 2008. Even though the subprime fiasco emerged in 2008, the effect on the Malaysian economy was not as severe as it was on the US economy. Thus, the subprime crisis is not expected to confound the findings of this study.

Firm performance is measured by using (1) Tobin's q, which is the sum of the market value of equity and book value of total debts divided by the book value of total assets and (2) ROA, which is computed by dividing profit before interest and taxes by the firm's total assets. Tobin's q measures the market perception of the firm's performance (Weir et al., 2002). The ROA, on the other hand, indicates the effective use of the firm's assets in achieving shareholders' economic goals (Haniffa & Hudaib, 2006). To test the hypotheses, a pooled regression is developed as follows:

$$FP_{i,t} = \alpha_0 + \beta_1 BDIND_{i,t} + \beta_2 CEODLTY_{i,t} + \beta_3 BSIZE_{i,t} + \beta_4 BUSY_{i,t} + \beta_5 NCIND_{i,t} + \beta_6 RMC_{i,t} + \beta_7 MEET_{i,t} + \beta_8 FSIZE_{i,t} + \beta_9 GRG_{i,t} + \beta_{10} FAMFIRM_{i,t} + \beta_{11} GRWTH_{i,t} + \beta_{12} INDS_{i,t} + \beta_{13} FP_{i,t-1} + \epsilon \quad (1)$$

where:

FP: firm performance, measured by Tobin's q or ROA;

BDIND: board independence, measured by the percentage of independent directors;

CEODLTY: CEO duality, dummy variable; 1 if the posts of chairman and CEO are separated (duality), 0 otherwise;

BFSIZE: board size, measured by the number of directors on the board;

BUSY: directors' busyness; measured by the number of outside directorships held by independent and non-executive directors;

NCIND: nomination committee independence, dummy variable; 1 if the chairman is independent, 0 otherwise;

RMC: risk management committee, dummy variable; 1 if the RMC is established, 0 otherwise;

MEET: number of board meetings in the year;

FSIZE: firm size, measured by total assets;

GRG firm leverage or gearing, measured by total debts to total assets;

FAMFIRM: family ownership, a dummy variable; 1 if two or more directors are family members, 0 otherwise;

GRWTH: firm's growth opportunities, measured by $\text{Sales}_{i,t} / \text{Sales}_{i,t-1}$;

INDS: industry type; consumer, industrial, trading and services, construction, property and plantation sectors;

e: error term;

i: firm 1, 2, 3,..... j; and

t: year 2009,..... 2011.

The lagged performance variable (Tobin's q and ROA) is included because, consistent with prior studies (e.g. Haniffa & Hudaib, 2006; Klein, 1998; Weir et al., 2002), the performance in the current year is dependent on the performance in the previous year. Several control variables are included in the analyses to ensure the robustness of the findings. First, family ownership is included because firms in Malaysia are predominantly owned by families. Claessen et al. (2000) found that more than two-thirds of Malaysian listed firms are owned by families. Indeed, Claessen et al. (1999) found that one-fourth of the Malaysian corporate sector is controlled by 10 families. Moreover, Anderson and Reeb (2003) show that family-owned firms are associated with a higher Tobin's q and ROA. This variable is measured by using a 20% cut-off line; if a family owns 20% or more of the firm's shares, the firm is considered to be a family-owned firm, as in Jaggi et al. (2009). The second control variable is the firm's leverage or gearing. This variable measures the closeness to breaching the debt covenant, thus it is a measure of a firm's risk. Third, the firm's size is included as a measure of the political cost (Watts & Zimmerman, 1980). That is to say, due to political scrutiny, large firms tend to show lower profits and thus lower value. Further, large firms are expected to be at the mature stage of their life cycle (Maury & Pajuste, 2005), suggesting a negative association between firm size and firm value. The fourth control variable is the firm's growth potential. High-growth firms tend to have a higher valuation and therefore this variable is associated with the firm's value (Maury & Pajuste, 2005). Finally, industry type is included as a control variable because it affects accounting profit (Schmalensee, 1985) and both Tobin's q and ROA (Haniffa & Hudaib, 2006). The industrial classification follows the method used by Haniffa and Hudaib (2006).

4. FINDINGS

Out of 2,510 firm years, a total of 2,329 firm years with complete data were included in the study after excluding firms under the categories of finance/REITs/close-end funds/PN4/PN17 and also firms which changed their financial year end (2009: 795; 2010: 782; 2011: 752). Table 1 shows that distribution of firm years according to Bursa Malaysia's sectorial classification.

As shown in Table 1, firms that belong to the industry category dominate the sample. Table 2 presents the descriptive statistics of all the variables in the study. Panel A shows the continuous variables, while Panel B provides the frequency of the dummy variables.

Table 1. Firm years by sector

Sector	Number of firm years	Percentage
Consumer	406	17.4%
Industrial	754	32.4%
Construction	141	6.1%
Trading/services	523	22.5%
Property	250	10.7%
Plantation	129	5.5%
Technology	89	3.8%
Infrastructure	21	0.9%
Hotels	13	0.6%
Mining	16	0.1%
Total	2,329	100%

The results in Panel A of Table 2 show that both of the dependent variables (Tobin's q and ROA) as well as board meetings, firm gearing and firm growth potential are not normally distributed, as evidenced by the skewness being greater than +/- 1.96 or the kurtosis being greater than +/- 3 (Haniffa & Hudaib, 2006). Hence, these variables are either normalized using the Van de Waerden procedure or log transformation in the subsequent regression analyses (see Cooke, 1998). The results in Panel B indicate that about 21% of firms still combine the chairman and CEO roles (2009: 21%; 2010: 21%; 2011: 20%), which is consistent with Abdullah (2004), who reports a proportion of 22%, and with a more recent study by Mohd Salleh and Omar (2014), who also found that 22% firms combine these two roles. Therefore, even after the issuance of the MCGG (2000 and 2007), the practice of combining the two roles does not seem have decreased, let alone disappeared.

Table 2. Descriptive statistics (N=2,329)

Panel A: Continuous variables					
Variable	Mean	Standard deviation	Min	Max	Skewness
Tobin's q	0.8153	0.7650	0.0001	14.2560	6.1880
Return on assets (ROA)	0.0448	0.4699	-21.166	4.250	-39.359
Board independence (BDIND)	0.4556	0.1289	0.1429	1.000	0.733
Board size (BDSZ)	7.34	1.875	3	17	0.909
Outside directors' busyness (BUSY)	4.66	4.566	0	27	1.417
Board meetings (BDMTG)	5.41	2.043	0	27	2.846
Firm size (SIZE) (log natural)	19.7416	1.4209	14.835	25.035	0.748
Firm leverage (GRG)	0.2061	0.2103	0	3.1954	4.022
Firm growth (GRW)	1.1398	0.8536	0	23.546	14.352
Lagged ROA	0.0652	0.5283	-2.9610	24.7002	43.420
Lagged q	0.7623	0.0000	14.2566	0.7204	6.871
Panel B: Dummy variables (N=2,329)					
Variable	1		0		
CEO duality (1: duality; 0: combined)	1,850 (79.4%)		479 (20.6%)		
Risk management committee (1: RMC established; 0: otherwise)	399 (17.1%)		1,930 (82.9%)		
Nomination committee independence (1: independent chairman; 0: otherwise)	374 (16.1%)		1,802 (77.4%)		
Family firm (FAMILY) (1: family owned; 0: otherwise)	1,107 (47.5%)		1,222 (52.5%)		
Industry (IND) (1: firm in industrial sector; 0: otherwise)	754 (32.4%)		1,575 (67.6%)		

With regard to risk management, only around 17% firms have established a RMC (2009: 17.2%; 2010: 16.5%; 2011: 17.7%). Even after the Enron debacle in the US and Malaysia's own Transmile case, firms in Malaysia do not appear to place importance on having a committee that focuses on managing the firm's risk. Similarly, as shown in Panel B of Table 2, the majority of firms do not have a nomination committee headed by an independent chairman. The presence of an independent

nomination committee chairman is very important as it is this committee that nominates and evaluates the performance of the directors on the firm's board. This evidence indicates that the practice of having an independent nomination committee chairman in Malaysia is still far from that found in the UK as prescribed by the UK CG Code (FRC, 2010). To understand the association between the variables, a correlation analysis was carried out. Table 3 presents the results.

Table 3. Pearson's correlation analysis (N=2,329)

Variable	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
Tobin's q (1)	1.00												
ROA (2)	0.03 0.09	1.00											
BDIND (3)	0.00 0.22	-0.04** 0.03	1.000										
CEODLTY (4)	-0.03 0.15	-0.03 0.15	0.03*** 0.060	1.00									
BDSZ (5)	-0.06 0.00	0.06 0.00	-0.13** 0.00	-0.07 0.00	1.00								
BUSY (6)	0.12* 0.00	0.03 0.10	0.10** 0.00	-0.08* 0.00	0.23** 0.00	1.00							
RMC (7)	0.02 0.28	0.02 0.28	0.01 0.41	-0.02 0.33	0.09** 0.00	0.07** 0.00	1.00						
NCIND (8)	-0.03 0.15	-0.03 0.15	0.15** 0.00	0.03 0.12	-0.10** 0.00	-0.08** 0.00	0.00 0.66	1.00					
BDMTG (9)	-0.02 0.22	-0.06** 0.00	0.12** 0.00	-0.06** 0.00	0.05** 0.00	0.08** 0.00	0.12* 0.00	0.00 0.76	1.00				
SIZE (10)	0.09* 0.00	0.09* 0.00	0.00 0.67	-0.08* 0.00	0.35** 0.00	0.41** 0.00	0.13* 0.00	-0.09* 0.00	0.06* 0.00	1.00			
GRG (11)	0.06* 0.00	-0.06** 0.02	0.04** 0.03	0.03 0.87	-0.01 0.52	0.02 0.33	0.04** 0.02	0.04** 0.06	0.13* 0.00	0.10* 0.00	1.00		
FAMFIRM (12)	-0.09* 0.00	0.03*** 0.09	-0.25** 0.00	0.05** 0.01	0.10** 0.00	-0.18*** 0.00	-0.11*** 0.00	0.04** 0.02	-0.19* 0.00	-0.14* 0.00	-0.01 .59	1.00	
GRWTH (13)	-0.00 0.94	0.05** 0.03	-0.06* 0.00	-0.00 0.15	0.02 0.18	0.00 0.33	0.00 0.99	-0.05** 0.01	-0.03 0.10	0.06* 0.00	-0.07** 0.03	-0.09* 0.00	-0.03 0.18

Note: *p* values are shown below the respective correlation coefficients; *1% significance level (2-tailed); **5% significance level (2-tailed); ***10% significance level (2-tailed).

The results in Table 3 indicate that the multicollinearity problem is not serious as all correlation coefficients are low, i.e. none of the coefficients exceeds 0.80, which is the cut-off for multicollinearity suggested by Gujarati (1995). Subsequently, multivariate analyses were carried out to test the hypotheses, the results of which are presented in Table 4. Panel A of Table 4 shows the results when Tobin's *q* is the dependent variable, while Panel B shows the results when the dependent variable is ROA.

For both of the dependent variables (Tobin's *q* and ROA), fixed effect models are used instead of random effect models because the results of the Hausman test indicated that fixed effect models are better than random effect models (*p* values < 0.05). Based on the findings in Table 4, the influence of the tested variables on Tobin's *q* and ROA is mixed. When Tobin's *q* is used as the dependent variable, only board size is significant, which supports H_3 . However, the other hypotheses, i.e. H_1 , H_2 , H_4 , H_5 , H_6 and H_7 , are not supported. With regard to the significant association between board size and Tobin's *q*, the findings support the argument put forward by resource dependency theory as opposed to that for smaller board size as proposed in agency theory. The other tested variables (i.e. board independence, CEO duality, directors' busyness, nomination committee independence, establishment of a RMC and board diligence) are not significant.

With regard to the control variables, firm size is negatively associated with market-based firm performance while gearing, on the other hand, is perceived positively by the market. As for sectorial classification, firms in the trading and services sector outperform firms in all the other sectors. However, most of the underperforming firms are in the property sector. Hence, industry type has a significant effect on firm performance, which supports the argument by Schmalensee (1985).

When ROA is used as the dependent variable, only three tested variables are significant (i.e. CEO duality, establishment of a RMC and board diligence). However, only two of these variables (i.e. CEO duality and establishment of a RMC) support hypotheses H_2 and H_6 ; they do not support the other hypotheses, i.e. H_1 , H_3 , H_4 and H_5 . As for hypothesis H_7 , board diligence, although significant, is not consistent with the prediction that more board meetings would be detrimental to a firm's accounting performance.

Three control variables, namely firm size, gearing and firm growth potential, are significant in determining accounting-based firm performance and their direction is as expected. Finally, the evidence suggests that industry type either has no effect or a negative effect on ROA. Firms in the plantation sector perform the worst compared to firms in the other sectors.

Table 4. Regression analyses (N=2,329)

Panel A: Tobin's q as the dependent variable employing fixed effects							
Variable	Expected sign	Model 1		Model 2		Model 3	
		Coeff.	t-stat.	Coeff.	t-stat.	Coeff.	t-stat.
Constant	?	-0.024	-0.0117	8.765	8.527***	8.927	8.638***
BDIND (H.)	+	-0.386	-1.704**	-0.443	-2.07**	-0.461	-2.169**
CEODLTY (H.)	+	-0.007	-0.067	0.012	0.116	0.035	0.333
BDSZ (H.)	+	0.017	1.015	0.033	2.106*	0.030	1.909**
BUSY (H.)	-	0.000	0.003	0.000	0.096	0.002	0.217
NCIND (H.)	+	0.051	0.510	0.052	0.548	0.021	0.223
RMC (H.)	+	-0.121	-0.960	-0.113	-0.951	-0.053	-0.449
BDMTG (H.)	+	0.082	0.568	0.079	0.580	0.086	0.641
Lagged Tobin's q	?	-0.063	-3.203*	-0.017	-0.923	-0.021	-1.099
SIZE	-			-0.449	-8.712***	-0.475	-9.237***
GRG	+			0.334	11.401***	0.335	11.538***
FAMILY	+			-0.042	-0.430	-0.043	-0.443
GRWTH	+			0.004	0.392	0.007	0.652
Consumer	?					0.457	2.334**
Industry	?					0.364	2.417**
Trading and Services	?					1.004	5.301***
Construction	?					-0.369	0.267
Property	?					-0.358	-1.752*
Plantation	?					0.236	0.538
Adjusted R ²		0.805		0.827		0.830	
F statistics		12.51***		14.24***		14.45***	
Panel B: ROA as the dependent variable employing fixed effects							
Constant	?	0.038	0.151	-2.971	-2.301**	-2.814	-2.150*
BDIND (H.)	+	0.248	0.868	0.184	0.278	0.154	0.553
CEODLTY (H.)	+	0.561	4.001***	0.493	3.584***	0.465	3.381***
BDSZ (H.)	+	0.035	1.661**	0.022	1.073	0.026	1.265
BUSY (H.)	-	-0.000	-0.078	0.003	0.261	0.002	0.233
NCIND (H.)	+	0.038	0.300	0.025	0.206	0.040	0.330
RMC (H.)	+	0.238	1.504*	0.255	1.652**	0.217	1.399**
BDMTG (H.)	+	-0.833	-4.604***	-0.861	-4.883***	-0.834	-4.735***
Lagged ROA	?	-0.142	-6.268***	-0.151	-6.818***	-0.151	-6.784***
SIZE	+			0.160	2.470***	0.166	2.552***
GRG	-			-0.100	-2.644**	-0.095	-2.524**
FAMILY	+			-0.010	-0.083	-0.004	0.127
GRWTH	+			0.116	8.051***	0.116	8.048***
Consumer	?					-0.527	-2.063*
Industry	?					-0.177	-0.903
Trading and Services	?					-0.423	-1.717**
Construction	?					-0.457	-1.308
Property	?					0.422	1.585
Plantation	?					-1.578	-2.753***
Adjusted R ²		0.694		0.711		0.711	
F statistics		7.318***		7.779***		7.779***	

Note: Fixed effects models were used based on the Hausman tests which indicated that $p < 5\%$. Standard errors are in parentheses. ***1% significance level (1-tailed); **5% significance level (1-tailed); *10% significance level (1-tailed).

5. DISCUSSION

Our evidence reveals mixed findings on the influence of corporate governance mechanisms on Tobin's q and ROA. First, while board independence adversely affects Tobin's q, the firm's accounting-based performance is not influenced by board independence. Thus, in terms of ROA, our findings are consistent with prior studies (Dalton et al., 1998; Weir & Laing, 1999; Weir et al., 2002). Our findings are also supportive of earlier findings for Malaysia (Abdullah, 2004; Haniffa & Hudaib, 2006; Ponnun, 2008). Therefore, as far as ROA is concerned, board independence is not important. However, the market perceives that board independence is negatively associated with Tobin's q. In other words, board independence is detrimental to a firm's Tobin's q. This evidence is inconsistent with Haniffa and Hudaib (2006), who found that board independence and Tobin's q are not related. Nevertheless, the findings are consistent with Agrawal and Knoeber (1996), who found a negative association between the proportion of outside directors and firm

performance. The negative and significant influence of board independence on Tobin's q could also be due to board independence not really reflecting real independence (Demb & Neubauer, 1991) or because independent directors lack the business knowledge to be effective in discharging their duties (Patton & Baker, 1987). Given that Malaysian firms are typically controlled by families, it is more likely that independent directors lack independence as the appointment and reappointment of independent directors is controlled by family members, so they are unlikely to go against the wishes of the controlling shareholders (Jaggi et al., 2009).

As for CEO duality, the findings are mixed. While the market, proxied by Tobin's q, generally views CEO duality as not important, the evidence on the association between CEO duality and ROA is positive and significant. The insignificant influence of CEO duality on Tobin's q is consistent with the findings of Haniffa and Hudaib (2006). Hence, based on this evidence, CEO duality is not an important issue to the market. However, our evidence shows that CEO duality is good for ROA. Thus, this

evidence is not consistent with earlier evidence for Malaysia, which shows that CEO duality is not associated with accounting-based firm performance for family-owned firms (Abdullah, 2004; Ponnur, 2008; Shukeri, Ong & Shaari, 2013). Nevertheless, our evidence contradicts the findings of Haniffa and Hudaib (2006), who show that CEO duality is negatively associated with ROA. While Haniffa and Hudaib (2006) argue that the concentration of power in one individual is not good, our evidence suggests otherwise. Therefore, while the market is indifferent to CEO duality, CEO duality improves the firm's ROA, perhaps because it allows a sharper focus on company objectives and rapid implementation of operational decisions (Stewart, 1991), minimal board interference (Dahya et al., 1996) and unfettered leadership of the board (Rechner & Dalton, 1991), when a person holds both the chairman and CEO posts.

The fact that board size is seen favourably by the market indicates that a larger board size means that the firm is attempting to utilize expertise from outside to help the firm, which is consistent with resource dependency theory that posits that outside members provide useful advice to the board (Adam & Mehran, 2003; Anderson et al., 2004; Coles et al., 2008; Klein, 1998; Pfeffer, 1972; Singh & Harianto, 1989). Further, the market may perceive that a larger board size could improve board diversity and thus enable the firm to secure critical resources and bring a wealth of experience and expertise to the board (Goodstein, Gautum & Boeker, 1994; Pearce & Zahra, 1992). As for ROA, our evidence indicates that board size does not have any significant impact on this variable, although the direction of the influence is consistently positive. Thus, taking all the evidence together, in the Malaysian context, a larger board size is preferred to a smaller board size, which contradicts the arguments and evidence in some prior studies (e.g. Eisenberg et al., 1998; Yermack, 1996). Given that firms in Malaysia are typically highly concentrated and owned by families, appointments of outside directors may primarily be for the purpose of tapping their external experience and advice (Anderson & Reeb, 2004).

The busyness of both independent directors and non-executive directors seems to be unimportant to both the market and to the accounting returns. This evidence is consistent with an earlier study in the Malaysian context by Abdul Latif et al. (2013). However, in all the regression results, although not significant, the direction of the influence of busyness on Tobin's q and ROA is consistently positive. In fact, in the correlation analysis, busyness is positively and significantly associated with Tobin's q, thus the reputation hypothesis, consistent with Fama (1980) and Fama and Jensen (1983), rather than the busyness hypothesis as argued by other scholars (e.g. Ferris et al., 2003; Fich & Shivdasani, 2006), is partially supported. Therefore, while our evidence for Malaysia shows that the holding of additional directorships by independent directors and non-executive directors is neither good nor bad for a firm, it is more inclined to support the viewpoint that additional directorships are beneficial to the firm's value. Perhaps the fact that Malaysian firms are closely held means that having outside directors with additional directorships enables the board to

gain insights on other companies and to facilitate comparison (Dahya et al., 1996; Lorsch & MacIver, 1989; Turnbull, 1997).

The issue of the nomination committee was among the key issues addressed in the CG Blueprint 2011, which proposed that the establishment of the nomination committee should be mandatory and its chairman should be an independent director (SC, 2011). However, neither MCCG 2012 nor Bursa Malaysia took up this recommendation. Instead, MGCC 2012 states that the establishment of this committee is voluntary and that if it is set up then all the members should be non-executive directors, with the majority being independent. These recommendations in MCCG 2012 reaffirm those in MCCG 2000. In the absence of a mandatory requirement, only about 46% of listed firms in our sample have established a stand-alone nomination committee. Hence, establishing a stand-alone nomination committee seems not to be a widespread practice among listed firms in Malaysia. Perhaps this could be the reason why our evidence shows that nomination committee independence is not associated with either Tobin's q or ROA, which is consistent with the earlier evidence offered by Abdullah et al. (2010), who reveal that nomination committee independence is not related to financial restatements.

On the issue of the RMC, its establishment as a stand-alone committee is not yet widely practised among Malaysian listed firms. Our evidence shows that only 17% of listed firms have established a separate RMC. We found that most of the listed companies incorporate the RMC functions into their internal audit function, whose formation is required by MCCG 2007. Our multivariate analyses nevertheless indicate that while the market is not bothered about firms having a separate RMC, ROA seems to improve with the establishment of a separate RMC. In fact, in the correlation analysis, gearing and firm size are associated positively with a RMC. Hence, having a RMC is important for a firm with high gearing (a measure of risk) and for a large firm (a measure of the scale of the firm). Thus, even though the establishment of a RMC is not important to the market, firms should establish it as it is good practice to do so and it leads to a higher ROA.

As for the impact of the frequency of board meetings, our findings are also mixed. While having more board meetings is detrimental to ROA, its effects on Tobin's q are not significant. Hence, our evidence is not consistent with Brick and Chidambaran (2010). However, it is consistent with evidence for the US, as presented by Vafeas (1999). The correlation analyses in our study reveal that the number of board meetings is positively and significantly related to board size and the holding of additional directorships by outside directors. In fact, our correlation analysis also reveals that there are more board meetings held in highly-g geared firms. Taking all the evidence together, while both market-based and accounting-based firm performance are generally not in favour of more board meetings, it does appear that more board meetings seem to be important for firms with a large board size, for those with high gearing and for large firms. Perhaps having more board meetings is detrimental because the majority of Malaysian listed firms are closely held and it is most likely that in family-owned firms

the board members and management are family members, so information could be obtained outside board meetings.

Our evidence on the firm's gearing and the firm's size is consistent with Haniffa and Hudaib (2006), where gearing is positively associated with Tobin's *q* and firm size is negatively associated with Tobin's *q*. Thus, the market views gearing as being helpful in terms of maintaining discipline among management and improving performance (e.g. Jensen, 1986; Stulz, 1990). As for the positive association between firm size and Tobin's *q*, this suggests that the market sees the performance of smaller firms as better than that of larger firms (Hannan & Freeman, 1989; Weir et al., 2002). When ROA is used as the dependent variable, the influence of firm gearing and firm size remains significant, but the direction of the influence is opposite to that found when Tobin's *q* is used as the dependent variable. This evidence is consistent with Haniffa and Hudaib (2006), McConnell and Servaes (1995) and Weir et al. (2002). One explanation for the negative influence of gearing on ROA is that the interest expenses might have depressed the reported profits, and hence adversely affected the ROA.

6. SUMMARY AND CONCLUSIONS

This study examined the impact of the characteristics and the activities of the board of directors on firm performance. The evidence gathered is useful in determining the benefits of board characteristics and board activity on firm performance post MCGG 2007 and pre MCGG 2012. From an analysis of the data on non-financial listed firms for the 2009–2011 financial years, the evidence is mixed in that the effect of board characteristics and board activity differs depends on whether firm performance is market-based (i.e. Tobin's *q*) or accounting-based (i.e. ROA). However, there is no difference with respect to board independence, where firm performance (based on both ROA and Tobin's *q*) is not affected by board independence. Hence, board independence is not an issue as far as firm performance is concerned. The implication is that firms should focus more on the quality of the independent directors. Second, while the market is indifferent to CEO duality, it is generally beneficial to ROA. The implication is that it is a good idea to separate the roles of the board chairman and CEO because, even though CEO duality is not associated with Tobin's *q*, it improves ROA. Third, board size has a favourable effect on Tobin's *q*, but it does not have any effect on ROA. Therefore, firms that can afford to increase their board size should do so in order to bring in more capable independent directors and female directors. Since our evidence indicates that the average board size (median) in our sample is 7.34 (7.00), there is still room for expansion. While Jensen (1993) suggests a limit of eight directors, Lipton and Lorsch (1997) propose a maximum board size of 10 directors for effective discussion and staffing of board committees. In addition, in light of the Malaysian Government's policy on female directors which is to increase the representation of female directors on the board of listed firms to 30% by 2016, firms should take the opportunity to expand their board

size to accommodate women. The move to appoint female directors could be seen as an effort to diversify the composition of the board and thus its perspectives, which is consistent with resource dependency theory (Anderson et al., 2004; Coles et al., 2008; Pfeffer, 1972; Pfeffer & Salancik, 1978). Moreover, it might be beneficial if listed firms appointed other stakeholders to sit on their board so that the board's perspectives could be further broadened.

The busyness of independent directors and non-executive directors does not appear to be important to firm performance. Therefore, while limiting each director to holding a maximum of 10 directorships in listed firms, as stated in the Bursa Malaysia Listing Requirements, is good practice, it does not have any impact on firm performance. However, the SC of Malaysia incorporated another recommendation in MCGG 2012, where the board is required to set out its expectations on the time commitment of its members and the procedure for accepting new directorships. These requirements mirror those in the UK CG Code (FRC, 2010, 2014). Therefore, taking the evidence together with the content of MCGG 2012, the requirements in MCGG 2012 are very relevant as they can ensure that each director is able to give an appropriate level of commitment to the firm when serving as an independent or non-executive director.

The independence of the nomination committee was also found not to have a significant effect on Tobin's *q* and ROA. This result could be explained in two ways. First, the recommendation to establish of a nomination committee is not heavily emphasized in the MCGG (2000, 2007) compared to the issues of the representation of independent directors on the board and CEO duality, so not all firms have yet done so, so there is a lack of data. Second, where the committee is in place, it probably still needs more time to become embedded and effective. However, the presence a stand-alone RMC was found to be good for ROA enhancement. Thus, even though the market is indifferent about the establishment of a RMC, firms should establish one to ensure that risks are identified and managed appropriately. Finally, the number of board meetings has a negative effect on ROA, while its effect on Tobin's *q* is not significant. Therefore, firms still need to find the right number of board meetings as beyond a certain number, the evidence suggests that a higher number of board meetings is detrimental to ROA.

To conclude, firm performance, as measured by Tobin's *q*, is generally not affected by the board's structure and its activities, except for board size where the market prefers a larger board size. Hence, the market does not seem to have reacted positively to the initiatives that have been taken by the SC and Bursa Malaysia to strengthen the corporate governance mechanisms through the recommendations in MCGG 2007 and 2012. Perhaps this is because the market places more emphasis on the substance rather than on the form of the board. With regard to ROA, more encouraging results were observed as making efforts to have the right board structure and activities in place is good for ROA enhancement, but not for Tobin's *q*.

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