

NATIONAL CORPORATE GOVERNANCE CODES AND IT GOVERNANCE TRANSPARENCY

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Abstract

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The main purpose of this paper is to explore the influence of national corporate governance codes on IT governance transparency and was carried out by comparing the IT governance disclosure requirements across two jurisdictions Belgium and South Africa using the study by Huygh et al. (2017). The latter focused on these two countries since the South African corporate governance code King III (2009) contains detailed IT governance disclosures, while the Belgian corporate governance code Lippens (2009) does not. Huygh et al. (2017) found that listed South African financial services organizations were more concerned with disclosing their IT governance practices than their listed Belgian counterparts and that this observation held across the board for all four disclosure categories within the IT governance transparency framework. Further analysis at an individual item-level also found that many of the items for which the South African respondents reported frequently could be directly traced to the IT governance principles and recommended practices contained in the King III (2009) corporate governance code. Huygh et al. (2017) attributed the higher IT governance transparency of the South African respondents to the specific reporting requirements of their national corporate governance code King III (2009). Hence the recommendation that IT governance disclosures be proactively encouraged via national corporate governance codes to further enhance transparency.

Keywords: National Corporate Governance Codes, IT Governance Transparency, King III Code, Lippens Code, IT Governance Transparency Framework

1. INTRODUCTION

The potential benefits of IT governance have been well documented for over a decade now. Weill and Ross (2004) found that effective IT governance is the single most important predictor of the value an organization generates from IT. Juiz and Toomey (2015) note that to govern or not to govern IT is no longer a choice for any organization adding that effective governance of IT promotes achievement of business objectives, while poor governance of IT obstructs and limits such achievement. Many prior studies including Weill and Ross (2004), Huang, Zmud and Price (2010) and De Haes and Van Grembergen (2009) have identified mechanisms for strengthening IT governance. Due to the direct link between corporate governance and IT governance

identified by Weill and Ross (2004), many corporate governance mechanisms have been translated into the IT governance domain. An important aspect of corporate governance remains the issue of transparency or disclosure (Millar et al., 2005; Augustine, 2012). However, Joshi et al. (2013) observe that the issue of IT governance transparency/disclosure, which is about providing stakeholders with information about the way the organization is governing its IT assets, has received little attention in academic research. The purpose of this exploratory paper is to compare the influence that national corporate governance codes have on IT governance transparency. Indeed, there could potentially be differences in IT governance disclosures due to variations across national corporate governance codes. This is done by

comparing the IT governance disclosure requirements across two jurisdictions South Africa and Belgium using the study conducted by Huygh et al. (2017). Differences in IT governance transparency between these two jurisdictions can be expected, as the South African corporate governance code, King III (2009) contains a significant amount of IT governance related guidance, while the Belgian code Lippens(2009) does not. Hence it follows that annual reports prepared in jurisdictions where national corporate governance codes contain IT governance-related guidance ought to disclose more details about their IT governance practices and are therefore more transparent compared to annual reports prepared in jurisdictions where national corporate governance codes contain no such IT governance-related guidance. Hence the main research question being explored in this review paper is to inquire if the inclusion of specific and explicit IT governance disclosure requirements in National Corporate Governance Codes such as the King III Code in South Africa will help improve overall IT governance transparency. This paper is structured as follows: Section 2 is an overview of the theoretical background to IT governance, while Section 3 reviews the IT governance disclosure framework recommended by ITGI which is then followed by the conclusion in Section 4.

2. THEORETICAL BACKGROUND

2.1. IT governance

De Haes and Van Grembergen (2009) note that IT governance is an integral part of corporate governance, and addresses the definition and implementation of processes, structures and relational mechanisms in the organization that enable both business and IT people to execute their responsibilities in support of business/IT alignment and the creation of business value from IT-enabled business investments. Over time, IT governance has gained momentum as more and more companies become increasingly dependent on IT for their strategic and operational business activities (De Haes & Van Grembergen, 2015; Nolan & McFarlan, 2005). This definition by De Haes and Van Grembergen (2009) clearly indicates that IT governance is an integral part of corporate governance, requiring the involvement of the Board. Due to this direct link between both concepts, many of the issues that are discussed regarding corporate governance also apply to IT governance (De Haes & Van Grembergen, 2015; Nolan & McFarlan, 2005; Heart et al., 2010). Drawing on the ideas of corporate governance, IT governance can be implemented using structures, processes, and relational/communication mechanisms (De Haes & Van Grembergen, 2009; Mähring, 2006). In the IT governance literature, many different mechanisms are reported, such as strategy committees, steering committees, a portfolio management process, etc. (Weill & Ross, 2004; Huang, Zmud, & Price, 2010; De Haes & Van Grembergen, 2009). An important issue in corporate governance literature is transparency (Millar et al., 2005; Augustine, 2012). However, as noted by Joshi et al. (2013) the issue of IT governance transparency has received little attention to date in academic research.

2.2. IT governance transparency

The disclosure of non-financial information improves the value of a firm's stock due to the reduction of information asymmetry (Healy & Palepu, 2001). Therefore, such disclosure is essential for organizations that are actively seeking investors. As IT governance-related information is a subset of non-financial information, IT governance disclosure can also be considered by organizations as a means to enhance firm value. The importance of transparency about IT governance is mentioned in the literature (Raghupathi, 2007) but is currently under-researched compared to overall corporate governance disclosures as observed by Joshi et al. (2013). IT governance transparency can be defined as "the ability of firms to provide adequate and relevant IT governance information in a timely and effective manner to their stakeholders, such as investors, policy makers, and regulatory bodies, so that they can assess management's behaviour in using IT" (Joshi et al., 2013, p. 118). It should be noted that IT governance transparency can be both about internal transparency such as making IT governance practices known on the firm's intranet, as well as external transparency. However, this paper only looks at the aspect of public voluntary disclosure about IT governance with the goal of informing external stakeholders. COBIT 5 (ISACA, 2012) the international best-practice framework for enterprise governance and management of IT, also refers to the importance of ensuring stakeholder transparency in the context of IT governance. COBIT 5 describes this process, as the requirement to "ensure that enterprise IT performance, conformance measurement and reporting are transparent, with stakeholders approving both the goals and metrics as well as the necessary remedial actions" (ISACA, 2012, p. 47).

3. IT GOVERNANCE DISCLOSURE FRAMEWORK

Joshi et al. (2013) present an IT governance disclosure framework based on the IT governance focus areas as defined by the IT Governance Institute (ITGI, 2003) and is built around the following four domains: IT strategic alignment, IT value delivery, IT risk management, and IT performance measurement.

- IT strategic alignment deals with the fact that IT investments need to support the strategic goals and objectives of an organization in order to enable the creation of current and future business value. (ITGI, 2003, p. 22)

- IT value delivery is concerned with the optimization of IT-enabled value creation, where the value is broader than strictly monetary such as competitive advantage, higher employee productivity, etc. (ITGI, 2003, p. 24)

- IT risk management is concerned with the protection of IT assets and recovery from IT-related disasters. (ITGI, 2003, p. 26)

- IT performance measurement is related to the IT budget and IT investments. It is specifically concerned with the expenditure on IT resources and its association to business value. (ITGI, 2003, p. 29)

This paper focuses on public corporate disclosure of IT governance with the goal of informing external stakeholders. In this regards,

firms that are publicly listed can be expected to disclose more information about their IT governance practices, as part of non-financial disclosures in general, compared to firms that are not publicly listed, as they have more incentive to do so. The disclosure of non-financial information improves the value of a firm's stock, due to the reduction of information asymmetry (Healy & Palepum, 2001).

The corporate governance code of South Africa, King III (2009), is rather unique as it contains specific directives related to IT governance. King III (2009) came into effect for South African entities starting from the 1st of March 2010 and is applicable to all entities, regardless of their size and listing status. Specifically, Chapter 5 King III (2009) called 'The governance of information technology (IT)' contains 7 broad IT governance principles (Appendix 1). At the present time, most corporate governance codes around the world do not contain any specific IT governance-related guidance. However, King III (2009) and most national corporate governance codes start from the "comply-or-explain" principle, meaning that ultimately the guidance contained in these codes is at best non-binding. Hence the title of this paper 'National Corporate Governance Codes and IT Governance Transparency'. A study was carried out by Huygh et al. (2017) using a sample of listed financial services organizations across two jurisdictions Belgium and South Africa to obtain the first global overview of IT governance transparency. Their study found that listed South African financial services organizations were more concerned with disclosing their IT governance practices than their Belgian counterparts and that this observation held for all disclosure domains of the IT governance framework. This result is not surprising given that the South African code King III (2009) contains IT governance-related guidance albeit non-binding while the Belgian code Lippens (2009) does not contain any IT governance-related guidance. Huygh et al. (2017) study based on empirical data provides some evidence that firms submitting their annual reports based on corporate governance codes containing non-binding IT governance-related guidance like the South African code King III (2009) disclose more information about their IT governance practices compared to firms that are submitting their annual reports based on corporate governance codes that contains no IT governance-related guidance like the Belgian code Lippens (2009).

3.1. IT strategic alignment

Huygh et al. (2017) found IT strategic alignment to be the least reported upon amongst the four disclosure domains of the IT governance framework. This is a surprising result, given that IT governance is the responsibility of the Board (De Haes & Van Grembergen, 2015) and the majority of the items in the IT strategic alignment domain are specifically situated at the Board level for instance, 'IT expert on the Board', 'IT expert with experience on the Board', 'CIO or equivalent is on the Board', 'IT committee' etc. Academic literature indicates that a high degree of Board involvement in IT governance, and IT experience on the Board, has a positive effect on organizational performance (Nolan & McFarlan 2005; Bart & Turel, 2010; Turel & Bart, 2014). Despite acknowledging the importance of Board involvement

in IT governance, Nolan and McFarlan (2005) state that Boards are often not aware of the importance of IT when it comes to supporting corporate objectives and the need for alignment between the overall corporate strategy and the IT strategy. Additionally, the Board is often incapable of asking IT management "the right questions" due to a lack of expertise, leading to an inability to effectively monitor the management of IT (Bart & Turel, 2010). It should also be noted that putting the CIO (or equivalent) on the Board, putting an IT expert on the board, or putting an IT committee in place at Board level, can help resolve some of these issues (De Haes & Van Grembergen, 2009). This discussion is wholly in line with principle 5.1 of King III (2009) (Appendix 1) that the board should be responsible for IT governance, clearly pointing to the need for Board involvement in IT governance. The issue of strategic alignment is clearly articulated in principle 5.2 of King III (2009) (Appendix 1) which states that IT should be aligned with the performance and sustainability objectives of the company.

3.2. IT value delivery

Meanwhile, Huygh et al. (2017) found that in respect of the IT value delivery domain, the difference between the average reporting rates of Belgian and South African firms was the largest. For the Belgian firms, this was the domain which was least reported upon, while for the South African firms it was the domain which was most frequently reported upon. When it comes to IT value delivery in general, King III (2009) makes it clear that the board should oversee the value delivery of IT and monitor the return on investment from significant IT projects. Academic research has already identified the importance of disclosing details about IT investments. Investors tend to reward disclosure about IT investments when they expect these investments to have a positive effect on current and future business value (Im, Dow, & Grover, 2001).

As King III (2009) Chapter 5 is dedicated wholly to IT governance, containing 7 principles (Appendix 1), it makes sense for firms to cluster these issues in their annual reports. As noted earlier, the Belgian code Lippens (2009) does not make any explicit reference to IT governance principles or practices. Huygh et al. (2017) observed that including a specific section on IT related matters in the annual report enables firms to think about ways to disclose information about their IT governance and IT management arrangements, thereby increasing their overall IT governance transparency. Huygh et al. (2017) concluded that South African firms appeared to be guided in this direction because of the specific reporting requirements of King III (2009).

3.3. IT risk management

King III (2009) also contains specific principles and recommended practices in the area of IT risk management and IT security. King III (2009). Principle 5.5 (Appendix 1) notes that IT should form an integral part of the company's risk management stating that the risk committee should obtain appropriate assurance that controls in place are effective in addressing IT risks. Huygh et al. (2017) found that in respect of the IT risk management

domain, Belgian firms trailed behind their South African counterparts in average disclosure rates. King III (2009) states that the Board should ensure that the company complies with IT laws and that all IT related rules, codes and standards are observed. Huygh et al. (2017) found that South African firms report considerably more information than their Belgian counterparts regarding the use of IT for regulation and compliance. South African firms also appeared to be more concerned with reporting on IT security compared to Belgian firms. King III (2009) states that the Board should ensure that there are systems in place for the management of information which should include information security, information management and information privacy. Meanwhile, King III (2009) states that the Board should ensure that all personal information is treated by the company as an important business asset and is identified. Further, it is the responsibility of the Board to ensure that an information security management system is developed and implemented. Besides that, the Board should approve the information security strategy, then delegate and empower management to implement the strategy. However, in spite of all of these IT security-related recommendations in King III (2009), Huygh et al. (2017) found that only half of the South African respondents were reporting on this IT security related issue. This finding is especially noteworthy since their study was dealing specifically with financial services organizations, a sector which is known for dealing with large amounts of confidential data, making the issue of IT security imperative. Academic research also indicates the need for IT security, for instance, Campbell et al. (2003) found that a security breach, leading to unauthorized access to confidential data has a significant negative impact on the value of a firm's stock. Meanwhile, Gordon et al. (2010) found a positive correlation between the voluntary disclosure of information security and the market value of a company.

3.4. IT performance measurement

Finally, in the last category of IT performance measurement, Huygh et al. (2017) found that explicit information in this area was more readily forthcoming from South African firms than Belgian firms. This should not be surprising when viewed within the overall context of greater IT governance transparency for the South African respondents since most annual reports in that country contain a specific section devoted to IT-related matters as a result of the disclosure requirements of King III (2009).

4. CONCLUSION

This paper provides an exploratory insight into the contemporary state of IT governance transparency across two jurisdictions Belgium and South Africa starting off from the premise that the issue of IT governance transparency has thus far received little attention in academic research as reported by Joshi et al. (2013). The main purpose of this paper is to explore the influence of national corporate governance codes on IT governance transparency. This objective was approached by comparing the IT governance disclosure requirements, across two

jurisdictions Belgium and South Africa. These two countries were deliberately chosen, as the South African corporate governance code, King III (2009) contains specific IT governance related guidance, while the Belgian code Lippens (2009) does not. Prior research carried out by Huygh et al. (2017) across two jurisdictions Belgium and South Africa found that listed South African financial services organizations were more concerned with disclosing their IT governance practices than their listed Belgian counterparts. This observation held across the board for all four disclosure domains of the IT governance transparency framework. Further analysis at an individual item-level also indicated that many of the items for which South African firms tended to report frequently could be directly traced to the IT governance principles and recommended practices contained in the King III (2009) corporate governance code. Huygh et al. (2017) therefore attributed the higher IT governance transparency of the South African respondents to the specific reporting requirements of their national corporate governance code King III (2009). Hence, the case for including more IT governance-related guidance in any future updates of existing national corporate governance codes.

From an academic point of view, this paper adds to the literature of IT governance transparency. Moreover, this paper adds to the theoretical framework of IT governance transparency as a research topic in general and the IT governance disclosure framework more specifically by investigating the influence of national corporate governance codes on IT governance transparency. From a practitioners' standpoint, this exploratory paper highlights the need to incorporate IT governance-related initiatives in national corporate governance codes. As IT becomes more pervasive in firms worldwide, it makes sense for firms to be transparent about these often very important IT-related matters; and for national corporate governance codes to guide firms in such a direction. This paper also helps to explore the fundamental role of corporate governance principles in shaping IT governance practices at firm level by providing evidence that the presence of IT-related principles in corporate governance codes can encourage firms to disseminate IT governance information in their Annual Reports. The importance of IT governance transparency is also stressed outside of national corporate governance codes. For instance, COBIT 5 (ISACA, 2012) which is the current edition of the international best-practice framework for IT governance also makes reference to the importance of ensuring transparency for stakeholders. The existing South African corporate governance code King III (2009), already contains specific IT governance-related guidance.

Many new digital era companies like Uber, for instance, are very much dependent on their IT platforms. Yet they offer very limited transparency about their IT-based business models and investors have a very little basis for confidence about the underlying engine of the business. Despite all the secrecy, Uber was still hacked. Investors not only had no basis for confidence, but any confidence they had earlier would have been undermined not just because Uber got hacked, but because, lacking transparency, Uber took a long time to confess and even undertook inappropriate actions to try and

cover up the breach. Another illustration might be the recent theft of bitcoin through a hack on a bitcoin exchange. How much transparency was there for investors and customers? Furthermore in many jurisdictions now for e.g. the UK, one aspect of IT governance is mandated that of breach disclosure for which there are frequently also substantial fines. Europe's GDPR also mandates some transparency. However, none of these governance codes prompts the need for greater overall transparency. Hence, the urgency of including more IT governance-related guidance in any future updates of national corporate governance codes using the existing King III (2009) report from South Africa as our template.

5. LIMITATIONS AND OPPORTUNITIES FOR FUTURE RESEARCH

In this final section, we discuss the limitations of our research and identify related opportunities for future work. First, this research only deals with disclosed information. There could very well be

discrepancies between what is reported and what is implemented regarding IT governance. For instance, an organization may have a dedicated CIO function, but it is possible that this is not explicitly mentioned in their annual report. It would, therefore, be very interesting to link this study with IT governance maturity to detect discrepancies between the IT governance implementation in organizations and their disclosure. Another opportunity for future research is data triangulation. This study only used annual reports as a data source. This was motivated by the fact that annual reports seem to be the preferred medium for IT governance-related disclosure. Nevertheless, data triangulation using additional data sources (e.g. press releases, company website, etc.) would enable a richer understanding of a firm's IT governance disclosure. Finally, this research only deals with the quantity of publicly available IT (governance)-related information. It would be interesting to also investigate the quality of such information, as is sometimes analyzed in the area of corporate governance disclosure.

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Appendix 1

Table 1. King III (2009) Information Technology (IT) governance principles

<i>Number</i>	<i>Description</i>
5.1	The Board should be responsible for Information Technology (IT) governance
5.2	IT should be aligned with the performance and sustainability objectives of the entity
5.3	The Board should delegate the responsibility for the implementation of an IT governance framework to management
5.4	The Board should monitor and evaluate significant IT investments and expenditure
5.5	IT should form an integral part of the entity's risk management process
5.6	The Board should ensure that information assets are managed effectively
5.7	A risk committee and audit committee should assist the Board in carrying out its IT responsibilities