The Relationship between Corporate governance and Conservatism in the Listed Companies in Tehran Stock Exchange

Ghasem Almasi, S. Ali Vaeez

Department of Accounting, Payam noor University, Izee, Iran
gh_almas@yahoo.com
Department of Accounting, Shahid Chamran University, Iran

Abstract: The aim of this study was to investigate the relationship between the components of corporate governance and accounting conservatism. Conservatism in this study is measured by Basu standard model. Corporate governance characteristics compared with non-duty members of the Board, CEO and Chairman of job separation and the ownership of institutional shareholders has been used as independent variables. Research data, using the population consists of 106 companies listed in Tehran Stock Exchange analyzes for the period 2001 to 2006 using a combination of data and ordinary least squares regression analyzes. The results of the regression estimates suggest that the timing of the financial reporting of listed companies in Tehran Stock Exchange will affect the index of profitability. The results reject the hypotheses of the study and showed that significant relationship does not exists between the proportion of non-duty members of the Board, CEO and Chairman of the Board and the task of separating ownership of institutional shareholders as a component of corporate governance and accounting conservatism .

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Introduction

Useful information to users of financial statements includes quality properties. The main qualitative characteristics associated with the content, relevance and reliability and prudence or conservatism is one of the main features of reliability. In theoretical concepts of financial reporting conservatism used for estimating the degree of care in the exercise of judgment is required in conditions of uncertainty. So that income or assets presented no greater than the fact and cost or liabilities no less than the fact. Cautious conservatism is a cautious response to ambiguity. If there is no ambiguity, Conservatism does not require and there is much more uncertainty and risk there is a greater need to Conservatism [2].

Basu (1997) argues that accounting conservatism at least a hundred years ago rose with the aim of preventing and reducing the risk of presenting an unrealistic situation in business bankruptcy raised by the various groups, especially the suppliers of capital. In addition, The Basu conservatism requiring high degrees of support for the recognition of good news, such as earnings, the recognition of such losses is bad news [3].

One of the most important functions of corporate governance is to ensure the quality of the financial reporting process. If there is good structure and good performance monitoring role of the board members and the quality of financial reporting of these violations can be reduced somewhat. The International Organization for Economic Co-operation and Development, corporate governance defined as "The complex relationship between the management (executive) board of directors, shareholders and other stakeholders in a company or the concerned parties." Corporate governance, a wide range of checks and balances on the performance and incentives affect firms' managers [7].

Research Theoretical principle

The information with qualitative characteristics that is useful to users of financial statements. The main qualitative characteristics associated with the content, relevance and reliability and prudence or conservatism is one of the main features of reliability.

Accounting conservatism is one of the basic concepts that consider the Financial Accounting Standards Board and in conceptual statement Number2. Financial Accounting Standards Board defines conservatism: Cautious to ensure that the economic and financial situation of the company is to provide sufficient [4].

Feltham and Ohlson (1995) in terms of balance sheet defuned conservatism: In case of doubt, there is a choice between two or more reporting methods, the

method must choice to be the least favorable effect on stockholders [5].

Another definition of conservatism that based on the profit and loss perspective, Basu (1997) have stated that such conservatism requiring high degrees of verification for recognizing good news such as profits, in the face of recognizing bad news such losses.

Third definition of conservatism by Givoly and Hayn (2000) based on the combined balance sheet and profit and loss perspective. In this view, conservatism is an accounting concept leading to a reduction of retained earnings reported by later identify and recognize revenue faster than expenses, evaluation low assessment and over liabilities [6] .

The International Organization for Economic Cooperation Development (OECD), corporate governance defined as "The complex relationship between the management (executive) board of directors, shareholders and other stakeholders or the concerned parties in a company." Corporate governance affect a wide range of checks and balances on the performance and incentives affect firms' managers. If poor corporate governance, where the owner not the manager, the manager may not attempt to maximize shareholder profits and reduce costs not and will not perform their duties to the fullest. In such circumstances, even theft and fraud may also arise in the interests of managers. The difference between investment purposes (the owners) and their representatives (managers) is called "agency problem". Align managers' incentives, so that instead of looking to their own interests to act in the interests of owners, corporate governance is a major challenge. Corporate governance mechanisms can divide into two groups: 1 - internal governance (eg, board structure and independence) and 2 - external authority (such as institutional ownership concentration) [9].

Other institutional investors in corporate governance mechanisms that can monitor the management of the company, they can also have a significant influence on the management to provide the interests of shareholders. Although the concentration of ownership of corporate governance can notice as an important mechanism to control agency problems and improves the protection of investors, however, such a focus can also be negative. For example, access to confidential information of major shareholders and shareholder information asymmetry between them is smaller conflict of interest between managers and shareholders altered to the majority shareholder and minority interests' conflict [7].

Corporate governance as an engine of economic enterprises play a major role in determining corporate policy in terms of both operational and reporting. However, the corporate governance is stronger lead to better quality of financial reporting. Level of conservatism applied in the financial statements of one of the parties will determine the quality of accounting earnings (Dechow, Ge and Schrand, 2010). Conditional conservatism (or conservatism depends News) refers to the idea that profits reflect bad news faster than good news. According to the above discussion, it expected that corporate governance might have meaningful relationship with the degree of conservatism practices on businesses [11].

Research hypotheses

According to the theoretical assumptions of the study and the previous study and answer to the research questions, research hypotheses formulated as follows:

Main hypothesis:

There is a significant relationship between corporate governance and accounting conservatism.

Sub-hypotheses:

First hypothesis: there is a meaningful relationship between the number of board members and the applied non-mandated conservatism.

Second hypothesis: there is a significant relationship between the separation of CEO and corporate board of directors of applied conservatism.

Third hypothesis: there is a significant relationship between the proportion of institutional investors and the level of applied conservatism.

Literature reviewe

Some researches has done within and outside the country in the field of corporate governance and conservatism to be expressed in countinue.

In these researches, there was a positive relationship between Corporate Governance and Conservatism. From them cited to Lara et al (2005) and Lim (2006) that conducted using Australian examples [12].

The research by Lafond and Richvdary (2007) carried out in total and the results were consistent with previous studies itself. Moreover, they expect to see a negative relationship between the survivals of the company's managers is conservative and the percentage of ownership.

One of the wide fields that in recent year researchers have studied about conservatism, the problem of transfer agency and wealth management incentives and the company pays for their own benefit; hence, in this case something has done whether conservatism can serve as an effective mechanism for strengthening corporate governance

and use information asymmetry as well as the balance. Lara et al (2006) study a research and concludes that conservatism in financial reporting as collateral reactions to represent problems that the information asymmetry between informed and uninformed investors [11].

The result of Klein and Marquardt (2006) research in the United States on the subject of the relationship between accounting conservatism and the loss of 846 firms during the period 1997 to 2005 shows that there was a direct relationship between accounting losses and accounting conservatism. In other words, the results showed that the more conservative, the reported losses of tested company is more [10].

Lara, Osma, and Penalva (2006) in their study examined the relationship between conservatism and quality financial information on 420 Japanese companies over a period from 1989 to 2002. The results indicate that the conservatism in addition to increasing the quality of financial information cause to reduces the of risk liquidity and securities transactions costs. They ultimately concluded that conservatism reduces the cost of capital to companies.

Balachandran and Mohanram (2008) in their study examined the relationship between unconditional conservatism and income information content of the 438 Canadian firms over the period 1996 to 2005. They presented evidence that showed a significant positive association between accounting non-conditional conservatism and net benefit content information [1].

Variables and model research

In this study, measures of corporate governance, including the non-duty members of the Board, CEO and Chairman of job separation and ownership of institutional shareholders as independent variables and the dependent variable were used as accounting conservatism.Variables mentioned above based on the breakdown of the assumptions are shown in Table 1.

Table 1: independent and dependent variables of the study

Dapendent Variables	Indapendent Variables	Hyphotises
Accounting Conservatism	Other members of the board shall	Hypothesis 1
Accounting Conservatism	The task of separating the CEO and Chairman of the Board	Hypothesis 2
Accounting Conservatism	Ownership of institutional shareholders	Hypothesis 3

To test three sub- hypotheses and and main hypotheses of research, the three following model is estimated respectively using combined data:

Sub-model 1

$$X_{it} = \alpha + \beta_1 Dum + \beta_2 outdir_{it} + \beta_3 Dum \times outdir_{it} + \beta_4 R_{it} + \beta_5 Dum \times R_{it} + \beta_6 outdir_{it} \times R_{it} + \beta_7 Dum \times outdir_{it} \times R_{it} + + \varepsilon_{it}$$

Sub-model 2

$$X_{it} = \alpha + \beta_1 Dum + \beta_2 Duality_{it} + \beta_3 Dum \times Dualityit + \beta_4 R_{it} + \beta_5 Dum \times R_{it} + \beta_6 Duality_{it} \times R_{it} + \beta_7 Dum \times Dualityit \times R_{it} + \varepsilon_{it}$$

Sub-model 3

$$X_{it} = \alpha + \beta_1 Dum + \beta_2 Ins_{it} + \beta_3 Dum \times Ins_{it} + \beta_4 R_{it} + \beta_5 Dum \times R_{it} + \beta_6 Ins_{it} \times R_{it} + \beta_7 Dum \times Ins_{it} \times R_{it} + + \varepsilon_{it}$$

Main model

$$X_{it} = \alpha + \beta_1 Dum + \beta_2 Totgov_{it} + \beta_3 Dum \times Totgov_{it} + \beta_4 R_{it} + \beta_5 Dum \times R_{it} + \beta_6 Totgov_{it} \times R_{it} + \beta_7 Dum \times Totgov_{it} \times R_{it} + + \varepsilon_{it}$$

Where in :

X: Net profit after tax is equal to the stock price at the beginning of the period.

Rit: is on common return equity that obtained of the difference between the beginning and the end of the financial year and their prices and cash dividends to shareholders.

Dum: is a dummy variable equal to 1 when the outcome is negative or zero, and is zero otherwise.

Outdirit: is the percentage of the Board of Directors shall that the percentage of non-executive board members is obtained by divid the total number of board members in the end.

Dualityit: Duality Managing Director and Chairman: The Chairman or Vice-Chairman and Managing Director of the company, not a single person (the two side posts, one is not provided). If the Chairman or Vice-Chairman and Managing Director of the company's board of directors is one, number one, and zero otherwise be attributed to this variable.

Insit: percentage of institutional ownership. This value is the percentage of shares that preserved by institutional investors - in particular investment.
Totgovit: overall corporate governance index that is derived from a combination of the above. If the coefficient is significant in these models, the hypothesis was not rejected.

Conducting personal or institutional investors pay such a huge amount of public and private banks, pension funds, insurance companies and social security funds and companies, and foundations investing and institutions.

Methodology

The study is application based on aim and the nature and methods is descriptive - correlational. This study is based on a quasi-experimental research design and performed using to casual approach (from the past).

Statistical population and samplesize

Statictics population in this study included all companies that admit between the years 2001-2006 in Tehran Stock Exchange and preserved his membership in this period. The reason for selecting and surveying of stock companies, allowing easier access to the financial information of the company and having a more homogeneous due to the provisions of the Stock Exchange of Tehran. The sampling method in this study is a systematic deleting method. Thus, among all the listed companies that it meets any of the following conditions have been removed and finally the remaining companies were selected for testing:

• Companies must have complete information for all financial statements including balance sheet, income statement and cash flow statements. • The fiscal year end is 19th March.

• Research companies must be active on the Stock Exchange during the period when they are active. • During the research period not change the financial year. • The types of companies are not investment companies or financial intermediation and insurance.

Due to the constraints mentioned in the study, 106 selected companies have studied as statistical sample.

Research findings

Descriptive statistics

In order to better understand the community and learn more about the research variables, before analyzing the data, it is necessary to describe the data. Describe the data, a step in the direction of the pattern recognition and basis for explaining the relationship between the variables used in the study. Thus, before testing the research hypotheses sometimes in recognizing descriptive statistics of the variables used for calculating in the study presented in Table 2. Descriptive statistics presented overview of the research data.

Table 2: Descriptive statistics results of research variables

Totgov	Ins	X	R	
1.261	0.470	0.192	0.374	Average
1.243	0.511	0.166	0.160	Middle
2.800	1.000	1.001	5.666	Maximum
0.200	0.000	-0.228	-0.984	Minimum
0.520	0.324	0.134	0.788	Standard deviation

Source: Research finding

The results of testing the first hypothesis

In this study, the type of data and methods of statistical analysis, data econometric methods combined (total study period) to the estimated model is used to investigate the hypothesis testing. In this research, a quantitative value of independent and dependent variables on the one hand, about 106 different companies and on the other hand, covers the period 2001-2007. Thus, the total number of observations in regression analyzes 636 company-years. The results of the first study in are presented in Table 3.

According to the model to test the research hypotheses, the model parameters or the model coefficients represent the independent variables related to the severity and type of relationship between the independent variable and the dependent variable. Thus, if the coefficient of the independent variables βn is positive, the independent variables accounting conservatism (the dependent variable) and the direct relationship between the coefficients is negative, it will have an inverse relationship.

Table 3: Results of testing the research first sub-hypothesis

D-W	F-Prob	F-static	Adjusted R^2	R^2	t- static p-value	Cofeince	Description
1.58	0.00	52.87	0.38	0.39	8.047 0.000	0.213	Intercept
					-1.252 0.211	-0.048	**Dum**
					-1.648 0.163	-0.065	**Outdir**
					0.741 0.459	0.044	**Dum× Outdir**
					3.161 0.002	0.068	**R**
					0.513 0.609	0.065	**Dum× R**
					0.777 0.437	0.025	**Outdir× R**
					-0.004 0.997	-0.001	**Dum× Outdir× R**

Source: Research findings

Adjusted coefficient of determination of the model test research indicates that some of the dependent variable is explained by the independent variables. Much more dependent variable will be correlated with the independent variables. The adjusted R2 of the model test is equal to 0.38. In other words, 38% of the change in accounting conservatism (the dependent variable) is due to changes in the independent variables (indicators of corporate governance, respectively). According to the estimation results of the research model to the data model, the F statistic is significant at 1% error. Thus, research model was overally significant. To examine the significant relationship between each independent variable with the dependent variable use the resulted values for the t-statistic and the p-value.

As Table 3 it can be seen, the t-statistic to test the model variables Dum × Outdir × R based on the relationship between the number of directors shall not be rejected and conservatism. Therefore, the results were not confirmed the first sub-hypothesis. Result findings related to this hypothesis is similarto the results of Garcia et al (2007) Qi et al (2007) researches.

The results of testing the second hypothesis

The results of the second model are presented in Table 4.

Table 4: Results of testing the research second sub-hypothesis

D-W	F-Prob	F-static	Adjusted R^2	R^2	t- static p-value	Coeifence	Description
1.84	0.00	53.96	0.38	0.39	19.637 0.000	0.166	Intercept
					-1.027 0.310	-0.013	**Dum**
					1.687 0.092	0.034	**Duality**
					-1.399 0.163	0.048	**Dum× Duality**
					13.276 0.000	0.094	**R**
					1.249 0.212	0.045	**Dum× R**
					-4.423 0.713	-0.073	**Duality × R**
					0.718 0.476	0.071	**Dum×Duality×R**

Source: Research findings

Adjusted coefficient of determination test the research model is equal to 0.38. In other words, 38% of the change in accounting conservatism (the dependent variable) was due to changes in the explanatory variables. The estimation results of the research model to the data model, the F statistic is significant at 1% error. Because of its significance level is less than the error level. As in Table 4 show, the t-statistic to test denied the model variables Dum × Duality × R based on the relationship between the roles of CEO and chairman of the board and conservatism. Therefore, the results represent not cofirm the second sub-hypothesis. Research findings related to this hypothesis, the results of Garcia et al (2007) is similar. Research findings related to this hypothesis is similar to the results of Garcia et al (2007).

The results of testing the third hypothesis

The results the third hypothesis is presented in Table 5.

Adjusted coefficient of determination test the research model is equal to 0.38. In other words, 38% of the change in accounting conservatism (the dependent variable) was due to changes in the explanatory variables. The estimation results of the research model to the data model, the F statistic is significant at 1% error. Because of its significance level is less than the error level. Thus, the research model was significant overally. The t-statistic to test denied the model variables Dum × Duality × R based on the relationship between the roles of CEO and chairman of the board and conservatism. Therefore, the results represent not cofirm the second sub-hypothesis. Research findings related to this hypothesis, the results of Garcia et al (2007) is similar. Research findings related to this hypothesis is not similar to the results of Garcia et al (2007) but the results are consistent Bix and colleagues (2004).

Table 5: Results of testing the third sub-hypothesis research

D-W	F-Prob	F-static	Adjusted R^2	R^2	t- static p-value	Cofeince	Description
1.86	0.00	52.25	0.38	0.38	13.199 0.000	0.177	Intercept
					-1.644 0.101	-0.033	**Dum**
					-0.369 0.712	-0.009	**Ins**
					0.731 0.436	0.027	**Dum× Ins**
					8.738 0.000	0.088	**R**
					0.723 0.470	0.034	**Dum× R**
					-0.486 0.628	-0.019	**Ins × R**
					0.368 0.720	0.040	**Dum× Ins × R**

Sources: Researcher,s Findings

Results of testing basic hypothesis of the research

The estimation results of the research model are presented in Table 6.

Adjusted determination coefficient results of testing the research model is equivalent to 0.39. In other words, 39% of the change in accounting conservatism (the dependent variable) was due to changes in the explanatory variables. According to The estimation results of the research model to the data model, the F statistic is significant at 1% error level. To examine the relationship between each independent variable with the dependent variable, the values for the t-statistic and the p-value use associated with it. As in Table 6 show, deny the t-statistic to test the model variables Dum × Totgov × R based on the relationship between corporate governance and conservatism. Thus, the results indicate the main research hypothesis not confirmed. Findings related to this hypothesis are inconsistent with the results of Garcia et al (2007) and Qi et al (2007) respectively.

Table 6: Results of testing basic hypothesis of the research

D-W	F-Prob	F-static	Adjusted R^2	R^2	t- static p-value	Coefficient	Description
1.86	0.00	54.59	0.39	0.39	8.439 0.000	0.160	**Intercept**
					-0.259 0.796	-0.007	**Dum**
					0.741 0.459	0.010	**Totgov**
					-0.552 0.581	-0.023	**Dum× Totgov**
					8.029 0.000	0.141	**R**
					-0.248 0.746	-0.025	**Dum× R**
					-3.682 0.000	-0.0483	**Totgov × R**
					0.866 0.387	0.064	**Dum× Totgov × R**

Source: Research findings

Resources

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