



The Study of the Relationship between the Corporate Governance and Conservatism in Financial Reporting in Cement Companies in Tehran Stock Exchange

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ABSTRACT: The purpose of this study is to evaluate the relationship between the corporate governance and the accounting conservatism criterions amongst active cement companies in Tehran stock exchange center. Accounting conservatism index is taken as the dependent variable and the corporate governance indexes are considered to be the independent variables in this study. The corporate governance indexes used in this study are ownership concentration, institutional shareholders ownership, independency of the board of directors, and the auditor's type which their relationship with the dependent variable is examined based on four different hypotheses. Basu adjusted model (1997) introduced by Khan and Watts (2007) has been used to measure the accounting conservatism. To examine the research hypotheses and the relationship of the variables, relevant data of 31 active cement companies in Tehran stock exchange center in course of 2006-2011 as the statistical population were used and analyzed as a mixed data analysis using a multi-variable regression. Chav and Hassman tests were used to estimate the appropriate models of the hypothesis for the mixed data. The results confirmed the first hypothesis and rejected the second, third and the fourth hypotheses. In other words, the results proved a meaningful positive relationship between the ownership concentration and the accounting conservatism and no meaningful relationship between the institutional ownership, the independency of the board of directors and the auditor's type and the accounting conservatism.

Keywords: Corporate governance, Accounting conservatism, Stock exchange center

ORIGINAL ARTICLE

INTRODUCTION

The final outcome of financial accounting is presentation of financial data to various internal and external users in form of accounting reports. The financial reports are the main part of the process of financial reporting. The performance of a commercial entity is the result of all its under-control resources. The appropriate association of all corporate governance mechanisms seems to be a crucial decision towards achieving optimum usage of resources, increasing accountability, clarity, fairness and profit of all corporate beneficiaries (Jalali, 2008).

The corporate governance was first introduced as a subject regarding the corporate strategies and shareholders' rights. Its role is to resolve the problems caused by the conflicts between shareholders' and managers' benefits. This conflict is often related to the problem of representation: first, corporate practitioners have different objectives and preferences and second, lack of complete knowledge of the performance, knowledge and preferences of each other. Theoretically, presence of independent and unrestricted managers who has the necessary expertise, independence and legal power to effectively

monitor the corporate performance could be a potentially powerful solution (Byrd et al., 1992).

Conservatism is one the fundamental concepts of accounting which has always been the subject of discussion by the statement of financial accounting concepts. This committee defines conservatism as: a conservative response towards assuring the presentation of sufficient and acceptable economic and financial information about the company (Biddle, et al., 2011).

Since the main goal of investors is to gain more profit rather than controlling the company, it is expected from the managers to be responsible for achieving the corporate goals and to manage and monitor the corporation towards achieving more profits for its investors. As there is no ways left for the financial markets but to rely on the managers to predict the companies' true future, an appropriate method of corporate governance could be a useful solution for efficient management and control of businesses.

Chi et al. (2009) in a study named "The Relationship between Corporate Governance and Conservatism"

used Khan's model to measure the accounting conservatism. After studying Taiwan stock exchange companies during years 1996-2004, they concluded that there is less need for accounting conservatism in companies which their shares are owned by institutional shareholders.

Lim (2009) in his research "Evaluation of Corporate Governance and Accounting Conservatism", three models were used to measure the accounting conservatism. He studied the Australian companies in period of 1998-2002. They concluded that there is a positive relationship between the independent managers in the board of directors and the accounting conservatism in one of the three models.

MATERIALS AND METHODS

The research methodology is a comparative-inductive one. Since the research methodology focuses on the existence of a relationship between the variables, its type is cohesion. Cohesion studies are those in which relationship of various variables with each other is proved using a cohesion coefficient. The statistical population of this study is the big cement companies in Tehran stock exchange center during 2006- 2011 for the period of six years. There are 31 companies on this list. The statistical sample and the statistical population are identical because the statistical population is only consisted of cement companies in Tehran stock exchange center. Data collection method is field study. For data collection, companies' financial reports available on Tehran stock exchange website (www.rdis.ir) and CDs published by Tehran stock exchange office as well as Tadbir Pardaz software program were used. The MS Excel was used for data analysis and sorting. Also, to codify the theoretical principals of the study, desk research methodology was adopted using popular relevant journals such as *Accounting Evaluations*, *Financial*

Research, *Accountant*, *Tadbir*, *Management*, and *etc.* After gathering sufficient information, multi-variable regression, Pierson Cohesion test, adjusted coefficient test (R2), and analysis of *t* and *f* statistics were used to examine the research hypotheses and prove a meaningful relationship between the independent and dependent variables. Watson test was used to measure the nonexistence of self-cohesion among the variables. JB test was used to evaluate the normality of variables and Chav and Hassman test was used for choosing the best methods for estimation of a model which is economically right for mixed data. The entire above mentioned tests were conducted in Eview 6 software environment.

RESULTS

In this study, the amount of independent variables is calculated using the raw data and research descriptive statistics including the mean, median, maximum, minimum, and the standard deviation were then calculated. These statistics are presented in table 1. The present numbers depict a general overview of the distribution of the research data. To estimate the strength of the relationship between the variables, Pierson cohesion coefficient test was utilized. Cohesion analysis is a statistical tool for evaluation of the strength of a linear relationship between multiple variables. The cohesion coefficient test estimates the mutual relationship between two variables without considering the direction of that relationship. The cohesion of the research variables is shown in 2. The cohesion coefficient of the variables must not be a significant number because the cohesion of the independent variable could corrupt the regression results. The meaningful acceptable level for any variable should be less than 5%, otherwise it is rejected.

Table 1. Descriptive statistics of the independent variables

Variables	Symbol	Mean	Median	Max.	Min.	Skewness	SD
Ownership concentration	OWNCON	0.6836	0.7182	0.96	0.2546	0.6172	0.2168
Institutional ownership	INSOWN	0.6941	0.7257	1.0000	0.3783	-0.5381	0.3904
Independence of the board of directors	BRDIND	0.6243	0.6896	0.8977	0.2376	0.5674	0.3186
Auditor's type	AUDITK	0.4318	0.3671	1.0000	0.0000	0.7012	0.0042

Table 2. Pierson Cohesion Coefficients for variables

Parameters	CONCV	OWNCON	INSOWN	BRDIND	AUDITK	BM	LEVER	SIZE
CONCV	1							
OWNCON	0.32	1						
INSOWN	0.38	0.11	1					
BRDIND	0.09	0.15	0.44	1				
AUDITK	0.26	0.00	0.36	0.13	1			
BM	0.08	-0.31	0.04	0.49	0.26	1		
LEVER	0.00	0.14	0.23	0.08	0.02	0.00	1	
SIZE	0.39	-0.14	0.39	0.25	0.45	0.00	0.38	1

In the first hypothesis, accounting conservatism and the ownership concentration are respectively the dependent and the independent variables. To compute the coefficient level of meaningfulness, *t*-statistic is used. According to the results shown in table 3, *p*-value is equal to 0.013 for the first hypothesis.

Since the standard error is 0.05 for this study, it can be inferred that the ownership concentration has a meaningful effect on the accounting conservatism. The coefficient of this independent variable (first of corporate governance criterions) is positive. As a result, the type of the relationship between the ownership concentration and the accounting conservatism is direct. In other words, increase in ownership concentration amongst the target

population will result in increase in accounting conservatism. Accordingly, the first research hypothesis is confirmed with 95% of certainty. It can be concluded that increase in shares of the major shareholders (holding more than 5% of shares) will result in more control and management. As a result, a more conservative and real profit is achieved. In the second hypothesis, accounting conservatism and the percentage of the institutional ownership are respectively the dependent and the independent variables. According to the results shown in table 4, *p*-value is equal to 0.0896 for the second hypothesis.

Since the standard error of this study is 0.05, it can be inferred that the institutional ownership has no meaningful effect on the accounting conservatism. Therefore, the second hypothesis is rejected.

Table 3. Results of the first hypothesis: ownership concentration vs. accounting conservatism

Period of time	2011-2006
t-statistic	6.4763
(p-value)	0.0132
Coefficient of independent Variable	1.2056
No. Observations	186
Result	Confirmed
Type of relationship	Direct

Table 4. Results of the second hypothesis: the institutional ownership vs. the accounting conservatism

Period of time	2006-2011
t-statistic	-1.9961
(p-value)	0.0896
Coefficient of independent Variable	-0.0698
No. Observations	186
Result	Rejected
Type of relationship	-

In the third hypothesis, accounting conservatism and independency of the board of directors are respectively the dependent and the independent variables. According to the results shown in table 5, *p*-

value is equal to 0.4187 for the third hypothesis. Since the standard error of this study is 0.05, it can be inferred that independency of the board of directors has no meaningful effect on the accounting conservatism.

Therefore, the third hypothesis is rejected. In the fourth hypothesis, accounting conservatism and the auditor's type are respectively the dependent and the independent variables. According to the results shown in table 6, *p*-value is equal to 0.2421 for the fourth hypothesis.

Since the standard error of this study is 0.05, it can be inferred that the auditor's type has no meaningful effect on the accounting conservatism. Therefore, the fourth hypothesis is also rejected.

Table 5. Results of the third hypothesis: the independency of the board of directors vs. the accounting conservatism

Period of time	2006-2011
t-statistic	2.2183
(<i>p</i> -value)	0.4187
Coefficient of independent Variable	0.0027
No. Observations	186
Result	Rejected
Type of relationship	-

Table 6. Results of the fourth hypothesis

Period of time	2006-2011
t-statistic	-0.3648
(<i>p</i> -value)	0.2421
Coefficient of independent Variable	-1.4291
No. Observations	186
Result	Rejected
Type of relationship	-

DISCUSSION

Mixed data estimation method and multi-variable regression were used to evaluate the research hypothesis for 31 cement companies listed in Tehran stock exchange during years 2006-2011. In order to evaluate the relationship between the dependent variable and the independent variables, below steps were taken:

- 1- Statement of the research hypothesis according to the research literature and background;
- 2- Selection of sample companies and collection of required data using available software programs, websites, publications and other information resources;
- 3- Data transfer to excel sheets;
- 4- Data processing, classification and computation;
- 5- Conducting statistical examinations and data computation using Eview program;
- 6- Statistical output analysis and description of hypothesis test results.

The corporate governance has been evaluated by four different criterions: ownership concentration, institutional ownership, independency of the board of directors and auditor's type. The effect of each variable on the dependent variable (accounting conservatism) was tested separately based on four hypotheses. First, the Chav test was conducted for the

model and the obtained results showed that total data mixture model (money-data) is more appropriate and compatible for this study. Fischer statistic results (F) showed that our research model is generally meaningful. t-statistic was utilized for estimation of independent and dependent variables. The summary of all hypotheses results are shown in table 5-1. The results confirmed a meaningful relationship between the ownership concentration and the accounting conservatism (hypothesis 1). On the other hand, it was inferred that there is no meaningful relationship between the accounting conservatism and other independent variables. The results of this study are compatible with those conducted by Khan Beigi et al (2009), Azar et al. (2002), Rezaei (2009) and Ahmed Anvar et al. (2005).

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