

# The Effect of OECD Principles of Corporate Governance on Social Responsibility Accounting

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This study aims to examine the relationship between the OECD Principles of Corporate Governance on social responsibility accounting disclosure (SRAD) in Jordanian companies listed in the Amman Stock Exchange (ASE). The questionnaire and annual reports were both employed to collect the information from 104 companies in financial, services, and industrial sectors. SmartPLS3 was used to analyse the data. This study found that there is a relationship between the principle of the role of stakeholders, the principle of the rights of shareholders and key ownership functions and social responsibility accounting disclosure at p-value 0.029\* and 0.022\* (one tail) respectively. While there isn't a relationship between the other principles with social responsibility accounting disclosure. Therefore, it is recommended that Jordanian government should formulate a policy which will further encourage the listed companies toward social activities and their disclosure. The findings will no doubt be useful to the Jordanian policy makers, the board of directors, and other stakeholders in both ASE listed and unlisted companies.

**Key words:** *Corporate governance, OECD principles, Social responsibility accounting, Jordanian companies, Amman stock exchange.*

## Introduction

Initially, the existence of social responsibility accounting (SRA) resulted from the emergence of principles of social cost and social utility in economics as the pillars on which the concept of SRA relies on (Al-Sulaiti, 2009). Several researchers have defined SRA regarding its importance to the firm, the community and the environment. The most influential definition of SRA can be traced from the work of numerous researchers for instance Owen, Gray & Bebbington, (1997) and Gray, (2000). Therefore, in the modern capitalist economy, SRA is

regarded as the accounting information provided toward the investors besides shareholders through financial reports (Saunders & Tsumori, 2002; Ishikawa, 2000).

The main objective of SRA and reporting is to inspire both the firm's communication and social transparency with the stakeholders for responsible decision-making. Social reporting and presentation issues are the logical part of a social accounting approach which states the necessity to disclose the non-financial information to satisfy the stakeholder's goals (Leitoniene, Sapkauskiene & Dagiliene, 2015).

Accordingly, prior studies on SRA have concentrated on the developed countries for example the Japan, USA, UK and also the larger European region. For instance, see Echave, & Bhati, 2010; O'Dwyer, 2002; Hackston, & Milne, 1996; Hegde, Bloom, & Fuglister, 1997; and Gray, Kouhy, & Lavers, 1995. Literature gathers the wide debate on the application of SRA and its economic benefits. Where, Parker (2011); Thompson (2007) and Unerman, Bebbington & O'Dwyer (2007); mentioned that numerous methods and approaches have been built and developed to measure the effect of SRA on the company's performance and society in developed countries.

Comparatively, developing countries lack the resources to apply SRA and to measure its effect on community (Kisenyi & Gray 1998). Jamali & Mirshak, (2007) show that developing countries have various principles, societal norms, philosophies, and cultures compared to developed countries, but awareness and knowledge will lead to the successful and effective application of SRA. Besides, there is limited research that has focused on the impact of SRA besides other social responsibility disclosures in the developing countries (See, Alkababji, 2014; Hegde, et. al., 1997; Belal 2009; Deegan, 2008; De Villiers & Van Staden, 2006; Muhammad, & Teoh & Thong, 1984).

Furthermore, the studies conducted previously in Jordan indicate that, the level of SRA practice is relatively low (Abu Baker & Naser, 2000 and Barakat, Pérez and Ariza, 2014). For instance, Abu Baker & Naser (2000) discovered a low level of SRA compliance in most of the examined companies in Jordan. Consequently, the aim of this study to determine the effect of Organisation for Economic Cooperation and Development (OECD) principles of CG on SRA in the Jordanian listed firms.

### **Corporate Governance and Social Responsibility Accounting**

Karim and Zeina (2012) defined CG as the establishment of contractual internal control mechanisms, motives, and accountability to insure management and financial structure and

reports credibility. This interpretation defined the CG term as part of the operation of the firms and the central body for reaching the firm's aims.

Nowadays, many firms in both public and private sectors have recognised CG as an icon of success because of the benefits added from its implementation (Shahwan & Mohammad, 2016; Al Ramahi, et, al., 2014). The principles and the rules of CG have become an essential topic in the global economies. Recently, the Jordanian security exchange market have suggested non-mandatory principles of CG for firms based on the basis of universal criteria provided by OECD (Barakat, et al, 2014).

Thus, the OECD principles of CG contain: (i) Ensuring the basis for an effective corporate governance framework; (ii) The rights of shareholders and key ownership functions; (iii) The equitable treatment of shareholders; (iv) The role of stakeholders in corporate governance (v) Disclosure and transparency and (iv) The responsibility of the board of directors (OECD, 2004 & 2008).

### **Development of Hypotheses**

Several studies have found the significant influence of the OECD principles of CG towards the practice and disclosure of the non-financial and financial information related to the social responsibility (SR) activities in Jordan (See for example, Al-Sa'eed, 2013; Al-Ramahi, et.al, 2014). Accordingly, relationships may exist between the CG and the SRA which lead to profit maximisation (Davies & Okorite, 2007).

#### ***The practice of Principle of the Rights of Shareholders and Key Ownership Function and SRA disclosure***

Previously, various studies have revealed that, there is a positive relation between the shareholders right and the key ownership function and disclosure of SRA (See, Cormier, Magnan & Velthoven, 2005; Belal & Owen, 2007; Mangena & Tauringana, 2007). Hence, the majority of the Malaysian companies are attracting their foreign and local ownership through the practice and disclosure of the CSR (Amran & Devi, 2008). Whereas, firms whose ownership are dominated by the shareholders were expected to comply more with SRA (Teoh & Thong, 1984). It was argued that SRA is usually improved by the local and foreign ownerships of particular countries (Cormier et, al., 2005).

**H1:** There is a significant relationship between the principle of the rights of shareholders and key ownership functions and SRA disclosure.

### ***The Practice of Principle of Equitable Treatments of Shareholders and SRA***

Relatively, the shareholders of a company should have equal rights to express their feelings on the decisions made by the board of directors. For instance, all groups of shareholders have equal right to call the attention of the board towards appropriate CSR participation and its disclosure (Diffey, 2007). Based on the shareholder theory, the company should seek to achieve the highest level of benefit for the shareholders, and the main objective of the company is profit maximisation for the shareholders (Friedman, 1970). The equitable treatment must be rendered to all classes of the shareholders, regardless of their group size, which might lead to a sound SRA (Al-Sa'eed, 2013).

**H2:** There is a significant relationship between the principle of equitable treatments of shareholders and SRA disclosure.

### ***The Principle of the Role of Stakeholders and SRA***

The study of Dincer (2011) found a significant association between the stakeholders and SRA. It established that the practice and disclosure of the SRA of the firms is explained by the power of the stakeholders. The stakeholder theory of Freeman (1984), revealed a positive relationship between the organisational stakeholders and the activities of CSR, and its financial disclosure. According to the Business Impact Report (2000), it was argued that the interaction between the corporation and stakeholders could help a firm to understand its limitations and capacities towards accepting the rules and regulations concerning the organizational operations as well as societal needs and aspirations.

**H3:** There is a significant relationship between the principle of the role of stakeholders and SRA disclosure.

### ***The Principle of Disclosure and Transparency and SRA***

Among the key factors that hinder the flow of organisational CSR is the lack of accountability for corporate resources (Balanchandran & Chandrasekaran, 2011). Grant (2003) ascertained that the relationship between the disclosure and transparency of corporate resources, and SRA is likely to be positive. This assertion can be justified due to the fact that accountability, transparency, and disclosure on how the resources under custody were used, are part of the fundamental concepts of SRA. However, Kassinis & Vafeas (2002) mentioned that the reporting procedure of SRA is an integral part of CG; since, the disclosure of the environmental issues may add value to the welfare of the company's shareholders. The correlation between the disclosure and transparency and the SRA has raised the need to

install a framework for ensuring transparency and accountability in the management (e.g. separation of ownership) (Dincer, 2011).

**H4:** There is a relationship between the principle of disclosure and transparency, and SRA disclosure.

#### ***The Principle of Responsibility of the Boards and SRA***

According to Hansen and Hill (1991), the organisational concern that relates to the long-term investment may serve as a motivation to the board of directors to invest in quality products and services in order to prevent the firm from obtaining adverse reputations from the environmental policy. In some cases, directors and/or the managers were found to think that the only way to improve the financial position of the firm is to engage the irresponsible social conducts (Campbell, 2007). Consequently, the responsibilities of managers and the directors of the company are likely to be positive with the SRA, when the firm is operating under a favourable economic condition than otherwise (Campbell, 2007).

**H5:** There is a relationship between the principle of the responsibilities of the board and SRA disclosure.

#### **Research Methodology**

##### ***Survey and Sampling Technique***

This study was designed using quantitative approaches to determine the effect of OECD principles of CG toward SRA in the Jordanian listed firms. The listed firms in the ASE as at the 2015 financial year were considered as the population of this study. The use of both primary and secondary data was employed. A structured questionnaire with a five Likert scale was used as primary source data towards measuring the exogenous and moderator variables. While, the secondary data was sourced from the published audited financial reports of the selected samples for the measurement of endogenous variables.

The sample size was selected based on the following criteria:

- i. That the cCompanies have published their audited financial reports for the year 2015.
- ii. That the companies have never been unlisted in the ASE throughout the research period.

Accordingly, 104 firms out of 236 firms were selected in concurrence with above criteria. A total of 104 questionnaires were distributed to the top management offices of the sampled firms due to their vast experience and their role in the organisational decisions.

### ***Research Variables and Measurement***

The study consists of six exogenous variables and one endogenous variable as OECD principles of CG and SRA respectively. The exogenous variables were reflective indicators presented as: the right of shareholders (ROSH), equitable treatment of shareholders (ETOS), the role of stakeholders in CG (ROS), disclosure and transparency (DT), and responsibility of the board (ROB). Whereas, the endogenous variable is measure through reflective indicators as: employee dimension (EMD), environment dimension (END), community dimension (COD), and the quality of product (QPD). The SRA is measured using the adapted check list in the work of Barakat (2014) and Sharif & Rashid (2014) in line with the Global Reporting Initiatives (GRI G4). Thus, dummy variable was measured as 1 indicates compliance and 0 indicates non-compliance.

### ***Analysis Method***

In this study, SmartPLS3 was used to analyse the data. As suggested by Ringle et al. (2005), confirmatory factor analysis (CFA) was used across the reflective constructs to validate the instruments. Hence, the used of the selected tool was followed by the recommendation of Birkinshaw, Morrison, & Hulland, (1995) where they revealed that PLS is the efficient tool for analysing small sampled data with expectations of multivariate normality and aimed to predict the dependent variable.

### **Data Presentation and Analysis**

#### ***Convergent Validity***

Convergent validity is the extent to which measures correlate positively with alternative measures of the same construct. Therefore, the convergent validity of the instruments used were simultaneously tested based on the following criteria: composite reliability (CR), average variance extracted (AVE), Cronbach's Alpha as suggested by Hair et al. (2010).

**Table 1:** Average variance extracted, composite reliability, and Cronbach's alpha

<b>Construct</b>	<b>CR</b>	<b>AVE</b>	<b>Cronbachs Alpha</b>
ROSH	0.909	0.668	0.931
ETOS	0.879	0.594	0.829
ROS	0.865	0.616	0.793

DT	0.950	0.703	0.939
ROB	0.929	0.650	0.910
EMD	0.891	0.621	0.847
END	0.890	0.619	0.844
COD	0.943	0.646	0.931
QPD	0.942	0.670	0.928

**Source:** Data analysis, SmartPLS3.

The above table 1 shows that the factor loading of the measurements exceeded the minimum value of 0.70 as suggested by Hair et al (2013), thus its ranged between 0.694 to 0.898. Moreover, as indicated above, the recommended minimum values of CR, AVE and Cronbach's Alpha as 0.70, 0.50 and 0.60 respectively were achieved (see, Hair et al., 2013; Valerie, 2012;).

### ***Discriminant Validity***

**Table 2:** Discriminant Validity- Square Root of AVE

Constructs	CMP	DT	EMP	ENP	EToS	QPP	RoB	RoS	RoSH
CMP	0.804								
DT	0.332	0.838							
EMP	0.617	0.471	0.788						
ENP	0.553	0.410	0.495	0.788					
EToS	0.337	0.650	0.417	0.408	0.770				
QPP	0.556	0.406	0.577	0.682	0.404	0.818			
RoB	0.325	0.699	0.365	0.391	0.567	0.400	0.807		
RoS	0.431	0.612	0.544	0.557	0.513	0.475	0.499	0.785	
RoSH	0.355	0.693	0.504	0.408	0.535	0.500	0.640	0.502	0.817

**Source:** Data analysis, SmartPLS3.

Table 2 above revealed the result of discriminant validity test following the recommendation of Hair et al., (2013) and Fornell & Bookstein (1982) where they opined that discriminant validity occurs when the calculation of square root of AVE is greater than the correlation between the factors making each pair. Consequently, it is indicated that in this study, the AVE values are more than the squared correlations of the latent variables.

### ***Testing the Structural Model (Inner Model)***

#### ***R-Square ( $R^2$ ) and the Effect Size ( $f^2$ )***

The table 3 bellow shows the results of  $f^2$  for the first order of every latent variable which was obtained from the division of  $R^2$  Included by the  $R^2$  Excluded by 100. It predicts the

extent at which the independent variables contributed in the prediction of the dependent variables.

**Table 3:** The Effect Size for Social Responsibility Accounting Disclosure

Constructs	R <sup>2</sup> Include	R <sup>2</sup> Exclude	f <sup>2</sup>
ROSH → SRAD	0.049	0.037	0.013
ETOSH → SRAD	0.049	0.040	0.010
ROS → SRAD	0.049	0.037	0.013
DT → SRAD	0.049	0.048	0.001
ROB → SRAD	0.049	0.047	0.003

Source: Data analysis, SmartPLS3.

### *Predictive Relevance of the Model (Q<sup>2</sup> Q<sup>2</sup>)*

In this study, the minimum value of Q<sup>2</sup> is greater than zero at 0.268 which proved the quality of Inner model and its relevance in the prediction of latent variables involved as suggested that value of Q<sup>2</sup> lower than zero indicates inefficacy of the model towards predictive relevance (Hair et al, 2013 and Chin, 1998).

### **Findings and Discussion of the Hypotheses Testing**

The hypothesised relationships were tested by implementing bootstrapping as shown in the table 4 below:

**Table 4:** Result of hypotheses test

Hypotheses	Relationship	Std. Beta	Std. Error	T-Value	P-Value	Decision
H1	ROSH → SRAD	0.163	0.085	1.914	0.029*	Supported
H2	ETOSH → SRAD	-0.133	0.099	1.352	0.090	Not Supported
H3	ROS → SRAD	0.142	0.070	2.034	0.022*	Supported
H4	DT → SRAD	-0.065	0.093	0.697	0.244	Not Supported
H5	ROB → SRAD	0.078	0.073	1.069	0.144	Not Supported

t > 1.64, and P < or = 0.05, (one tail)

**The Hypothesis 1** indicates the influence of ROSH on SRAD. It shows that, there is a positive and significant relationship between the principle of the rights of shareholders and social responsibility accounting disclosure. Hence, the hypothesis is supported by the assertion of Amran & Devi (2008) that majority of the Malaysian firms are attracting their foreign and local ownership through the disclosure of CSR. Organisational disclosure of its social engagements has an effect on the users of the information including community and other stakeholders (Ball, Owen & Gray 2000). Protecting the shareholders' right is one of

the key factors that proof the quality of CG in an organisation which improves its performance and engagements in CSR to the society (Belal, et.al., 2009) and SRA practice and disclosure (Handajani, Subroto, Sutrisno & Saraswati, 2014; Cheung et, al., 2010).

**The Hypothesis 2** tests the relationship between the equitable treatment of shareholders and the social responsibility accounting disclosure. The results indicate that, there is no relationship between the ETOSH and SRAD. Hence, this shows that, the hypothesis is not supported which attuned with the study conducted by Qi & Cao (2013). Accordingly, the findings conformed with declaration that the interest of minority shareholders is not taken into consideration especially in the execution of CSR although they are considered as part of the stakeholders (Qi & Cao, 2013). In some instances, minority shareholders, invovedinvolved only in company's long-term strategies (Bondy et al., 2012; Money & Schepers, 2007).

**The Hypothesis 3** indicated that, there is a significant relationship with positive influence between the principle of the role of stakeholders and social responsibility accounting disclosure at significant value of  $\beta= 0.142$ ,  $t= 2.034$ , and  $P= 0.022$ . Consequently, the hypothesis is supported. This result is consistent with the work of Prado-Lorenzo, Gallego-Alvarez & Garcia-Sanchez, (2009) and Dincer (2011), who in their individual studies found that, the stakeholders are the reason that forces the companies to disclose the social responsibility in their annual report.

**The Hypothesis H4** shows that there is no relationship between the principle of disclosure and transparency, and social responsibility accounting disclosure. The significance value, the standard beta and t-value are ( $\beta= -0.065$ ,  $t=0.697$  and  $P=0.244$ ). Hence the hypothesis is not supported. This finding contradicts the results of previous works although there is limitation to quantity rather than quality, because Jordan has fully adopted the IFRS and ISA (Shanikat & Abbadi, 2012). Relatively, it was discovered that, the level of disclosure in the Jordanian companies is low, despite the similarities between the Jordanian and the United States Securities laws (Malkawi, & Haloush, 2007). They further narrated that the disclosure requirements mandated the disclosure of material information to the stakeholders only annually or semi-annually, despite that some companies do not want to increase the level of information disclosure due to political impact.

As shown in the table 4 above, **hypothesis 5** indicated that there is no relationship between the principle of responsibilities of the board and social responsibility accounting disclosure based on the significance values;  $\beta= 0.078$ ,  $t=1.069$ , and  $P=0.144$ . Hence the hypothesis is not supported. The findings concurred with work of Al Ramahi, et,al, (2014) where they related that unethical act of the board members affects the reputation of the companies even if they are disclosing their social activities. Conversely, the findings of Corporate Social Responsibility Watch (CSRWATCH, 2014) proved that over 70% of the CSR decisions related to its directions and priorities are solely taken by the Jordanian company's management. Therefore, the study of Awad (2014), stated the inability to perform the social responsibility and its disclosure among the industrial and corporate platforms in the ASE was

resulted from the social and cultural weaknesses in the environmental responsibility and higher costs of its practice and disclosure.

## **Conclusion**

The engagement of the private sector in the social responsibility activities is differed from country to country, which could be an underlying impulse that lead the sector towards engaging in the social activities of the community. Accordingly, the current study became one of its kind amongst the studies conducted in Jordan, in which the study has primarily determined the effect of OECD principles of CG on SRA in the shareholding companies listed in Amman stock exchange. Accordingly, findings of this study were summarised and presented in the table 4 above, where the results of the tested hypotheses shown that hypothesis 1 and 3 were positively supported at p-value 0.029\* and 0.022\* (one tail) each. Therefore, the remaining hypothesis 2, 4 and 5 were not supported at p-value 0.090, 0.0244 and 0.0144 respectively.

Additionally, this study indicated that, there is low SRAD in the published annual reports of ASE listed firms. Consequently, it is recommended that Jordanian government should encourage companies to fully participate in the practice of SRAD. It is also suggested that Jordanian government may consider making social responsibility practice and disclosure as one of the common conditions for tenders and bidding in Jordan. The Board of Directors of companies should encourage CEOs to contribute to the society and expand the methods of disclosure of the SR. Moreover, the responsibility of the Board of Directors should not only be limited to monitoring the performance of the CEOs or the financial performance, because they are the head of the bodies of the companies.

This study focuses on the SRAD, although the level of disclosure is still weak. It is recommended that further study needs to be conducted to investigate the level of government efforts and encouragements towards social responsibility and its disclosure in the other Jordanian private sectors.

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