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AN ANALYSE OF THE RELATIONSHIP BETWEEN STRENGTH OF AUDITING-ACCOUNTING STANDARDS AND CORPORATE GOVERNANCE

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ABSTRACT

Auditing/ accounting standards and corporate governance have important effects on not only the efficiency and productivity of the corporations but also economic, financial and social gains for the shareholders and stakeholders of the corporations. On the other hand, there is very important bidirectional relationship between auditing/ accounting standards and corporate governance.

In this study, we investigated the relationship between the strength of audit and accounting standards and corporate governance by using statistical techniques for 140 countries. In the study, considering the strength of auditing and accounting standards, the average of corporate governance level was tested among the country groups. As a result of the study, it is concluded that as the auditing / accounting standards strengthen, the power of corporate governance increased as the average.

Key Words: Auditing/ accounting standards, corporate governance, ANOVA

DENETİM-MUHASEBE STANDARTLARININ GÜCÜ VE KURUMSAL YÖNETİM ARASINDAKİ İLİŞKİNİN ANALİZİ

ÖZET

Denetim / muhasebe standartları ve kurumsal yönetim, sadece kurumların etkinliği ve verimliliği üzerinde değil aynı zamanda pay sahipleri ve kurum paydaşlarının ekonomik, finansal ve sosyal kazanımlar üzerinde önemli etkilere sahiptir. Öte yandan, denetim / muhasebe standartları ve kurumsal yönetim arasında çok önemli bir iki yönlü ilişki vardır.

Bu çalışmada, denetim ve muhasebe standartlarının gücü ile kurumsal yönetim arasındaki ilişkiyi 140 ülke için istatistik tekniklerini kullanarak araştırdık. Çalışmada, denetim ve muhasebe standartlarının gücü göz önüne alındığında, kurumsal yönetim düzeyi ortalamasının ülke grupları arasında eşit olup olmadığı test edilmiştir. Çalışmanın sonucunda, denetim / muhasebe standartları güçlendikçe, kurumsal yönetimin gücünün ortalama olarak arttığı sonucuna ulaşılmıştır.

Anahtar Kelimeler: Denetim / muhasebe standartları, kurumsal yönetim, ANOVA

1. Introduction

Auditing/ accounting standards and corporate governance have important effects on both the efficiency and productivity of the corporations and economic, financial and social outcomes for the shareholders and stakeholders of the corporations.

There is very important bidirectional relationship between auditing/ accounting standards and corporate governance. As auditing/ accounting standards are getting strong, the power of corporate governance increases, on the other hand, as the power of corporate governance increases, strength of auditing/ accounting standards also increases.

In this study, we investigated the relationship between strength of auditing and accounting standards and corporate governance by using statistical techniques, ANOVA test, for the 140 countries separated three (low, medium and high level) groups according to strength of auditing and accounting standards. The hypothesis testes is whether the means of corporate governance level by strength of auditing and accounting standards of these groups are equal or not.

2. Literature

There is an important literature on bidirectional relationship between auditing/ accounting standards and corporate governance, see Larcker et al (2007), Bushman and Smith (2001), Brown et al (2011), Bushman et al (2004), Bushman and Smith (2003), Bowen et al (2008), Lara et al (2009), Sloan (2001), DeAngelo (1988), Cohen et al (2002), Bhimani (2009), Carcello et al (2011), Francis et al (2003), Eng and Mak (2003), Niu (2006), Liguo and Ying (2003), Chi et al (2009), Seal (2006), Agoglia et al (2011).

OECD (2015) defined that *"Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined".*

Ball (2006) stated that *"Increased worldwide integration of both markets and politics makes increased integration of financial reporting standards and practice almost inevitable. But most market and political forces will remain local for the foreseeable future, so it is unclear how much convergence in actual financial reporting practice will (or should) occur. Furthermore, there is little settled theory or evidence on which to build an assessment of the advantages and disadvantages of uniform accounting rules within a country, let alone internationally".*

OECD (2015) stated that *"Corporate governance requirements and practices are typically influenced by an array of legal domains, such as company law, securities regulation, accounting and auditing standards, insolvency law, contract law, labour law and tax law".*

La Porta et al (2000) *"Financial markets need some protection of outside investors, whether by courts, government agencies, or market participants themselves. The existing corporate governance arrangements benefit both the politicians and the entrenched economic* *interests, including the families that manage the largest firms in most countries in the world. Corporate governance reform must circumvent the opposition by these interests."*

Table-1. shows the legal origin and investor rights, Panel C, Measures of enforcement, shows that accounting standards has important role of the protection of investor rights.

Table-1. Legal origin and Investor Rights

	Legal origin				
Variables	Common law (18 countries)	French civil law (21 countries)	German civil law (6 countries)	Scandinavian civil law (4 countries)	World average (49 countries)
Panel A: Measures of shareholder protection					
Antidirector rights index	4	2.33	2.33	3	3
Proxy by mail	39%	5%	0%	25%	18%
Shares not blocked before meeting	100%	57%	17%	100%	71%
Cumulative voting/proportional representing	28%	29%	33%	0%	27%
Oppressed minority	94%	29%	50%	0%	53%
Preemptive right to new issues	44%	62%	33%	75%	53%
% Share of capital to call and ESM ⩽10%	94%	52%	0%	0%	78%
Panel B: Measures of creditor protection					
Creditor rights index	3.11	1.58	2.33	2	2.3
No automatic stay on secured assets	72%	26%	67%	25%	49%
Secured creditors first paid	89%	65%	100%	100%	81%
Restrictions for going into reorganization	72%	42%	33%	75%	55%
Management does not stay in reorganization	78%	26%	33%	0%	45%
Panel C: Measures of enforcement					
Efficiency of the judicial system	8.15	6.56	8.54	10	7.67
Corruption	7.06	5.84	8.03	10	6.9
Accounting standards	***69.92***	***51.17***	***62.67***	***74***	***60.93***

Source: La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. (2000). Investor protection and corporate governance. Journal of financial economics, 58(1-2), 3-27.

Love and Klapper (2002) show that "*better corporate governance is highly correlated with better operating performance and market valuation. More important, firm-level corporate governance provisions matter more in countries with weak legal environments. Firms can partially compensate for ineffective laws and enforcement by establishing good corporate* *governance and providing credible investor protection. Love and Klapper (2002) stated that firm-level governance and performance is lower in countries with weak legal environments, suggesting that improving the legal system should remain a priority for policymakers".*

Agrawal and Chadha (2005) examined that *"Whether certain corporate governance mechanisms are related to the probability of a company restating its earnings. Agrawal and Chadha (2005 found that several key governance characteristics are unrelated to the probability of a company restating earnings, including the independence of boards and audit committees and the provision of nonaudit services by outside auditors. Agrawal and Chadha (2005 claimed that the probability of restatement is lower in companies whose boards or audit committees have an independent director with financial expertise; it is higher in companies in which the chief executive officer belongs to the founding family. They also stated that independent directors with financial expertise are valuable in providing oversight of a firm's financial reporting practices".*

Aysan (2007) stated that *"Implementation of corporate governance systems in organizations creates many changes in the traditional management systems.There is a direct relationship between the governance and financial information and reporting systems of business enterprises. Sound reporting systems are necessary ingredients of powerful governance systems."*

Pamukçu (2011) stated that *"The understanding of the corporate governance is the management of corporations in a manner that will provide the maximum benefit for all the related personalities and groups. The adoption of corporate governance in companies is directly related to the transparency of financial reporting and the increase in the level of public disclosure".*

It is clear that auditing/ accounting standards and corporate governance have important effects on not only each other but also social, economic and financial gains of corporations and the society.

3. Data and Method

The data used in the study is from World Economic Forum, The Global Competitivennes Index 4.0 2018 Dataset, version 13 October 2018.

In the statistical analysis, the sample consist of 140 countries and the countries are separated three (low, medium and high level) groups according to strength of auditing and accounting standards.

It is analysed that whether the means of corporate governance for the groups are equal or not. The main hypothesis is as follows:

- H_0: $\mu_1 = \mu_2 = \mu_3$
- H_1: $\mu_1 \neq \mu_2 \neq \mu_3$

The method used in the study is ANOVA (Analysis of Variance) test as holding relevant assumptions of the test.

4. Empirical Results

Table-2 shows the descriptive statistics for corporate governance by strength of auditing and accounting standards. According to the results, the mean of corporate governance by strength of auditing and accounting standards is 45.6 for low level countries, 58.2 for medium level countries and 67.6 for high level countries,

Table-2. Descriptive Statistics for Corporate Governance

	Strength of auditing and accounting standards		
Descriptive Statistics	Low	Medium	high
Mean	45.6	58.2	67.6
Median	43	59	68.5
Variance	101	75	92
Std. Deviation	10	8.7	9.6
Minimum	23	36	43
Maximum	68	74	83
Range	45	38	40
Interquartile Range	15	12	12
Skewness	0.3	-0.2	-0.7
Kurtosis	-0.2	-0.5	0.4

Table-3 shows the tests results of normality for corporate governance by strength of auditing and accounting standards. According to the test results, normality assumption is hold.

Table-3 Tests of Normality for Corporate governance

		Kolmogorov-Smirnov[a]			Shapiro-Wilk		
		Statistic	df	Sig.	Statistic	df	Sig.
Strength of auditing and accounting standards	Low	0.14	33.00	0.10	0.97	33.00	0.39
	Medium	0.07	69.00	,200*	0.98	69.00	0.35
	high	0.09	38.00	,200*	0.96	38.00	0.20

*. This is a lower bound of the true significance.

a. Lilliefors Significance Correction

Table-4 shows the test results of homogeneity of variances for corporate governance variable. According to the test results, assumption for homogeneity of variances is hold.

Table-4 Test of Homogeneity of Variances for Corporate Governance

Levene Statistic	df1	df2	Sig.
,705	2	137	,496

Table-5 shows the ANOVA test results, according to the test results, null hypothesis are rejected at 0.01 significance level, meaning that the means of corporate governance by strength of auditing and accounting standards among the groups are not equal.

Table-5 ANOVA Results

Corporate Governance	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	8,591.11	2.00	4,295.56	50.14	0.00
Within Groups	11,735.88	137.00	85.66		
Total	20,326.99	139.00			

Table-6 shows multiple comparisons for dependent variable that is corporate governance. Tukey HSD shows that the means of corporate governance by strength of auditing and accounting standards between the each pairwise groups are not equal at 0.01 significance level.

Table-6 Multiple Comparisons Dependent Variable: Corporate Governance

Strength auditing accounting standards			Mean Difference (I-J)	Std. Error	Sig.
Tukey HSD	Low	Medium	-12,59684*	1.96	0.00
		high	-22,02552*	2.20	0.00
	Medium	Low	12,59684*	1.96	0.00
		high	-9,42868*	1.87	0.00
	high	Low	22,02552*	2.20	0.00
		Medium	9,42868*	1.87	0.00

*. The mean difference is significant at the 0.05 level.

Table-7 shows homogeneous subsets for corporate governance. It is seen that the means of corporate governance by strength of auditing and accounting standards are not equal among the groups.

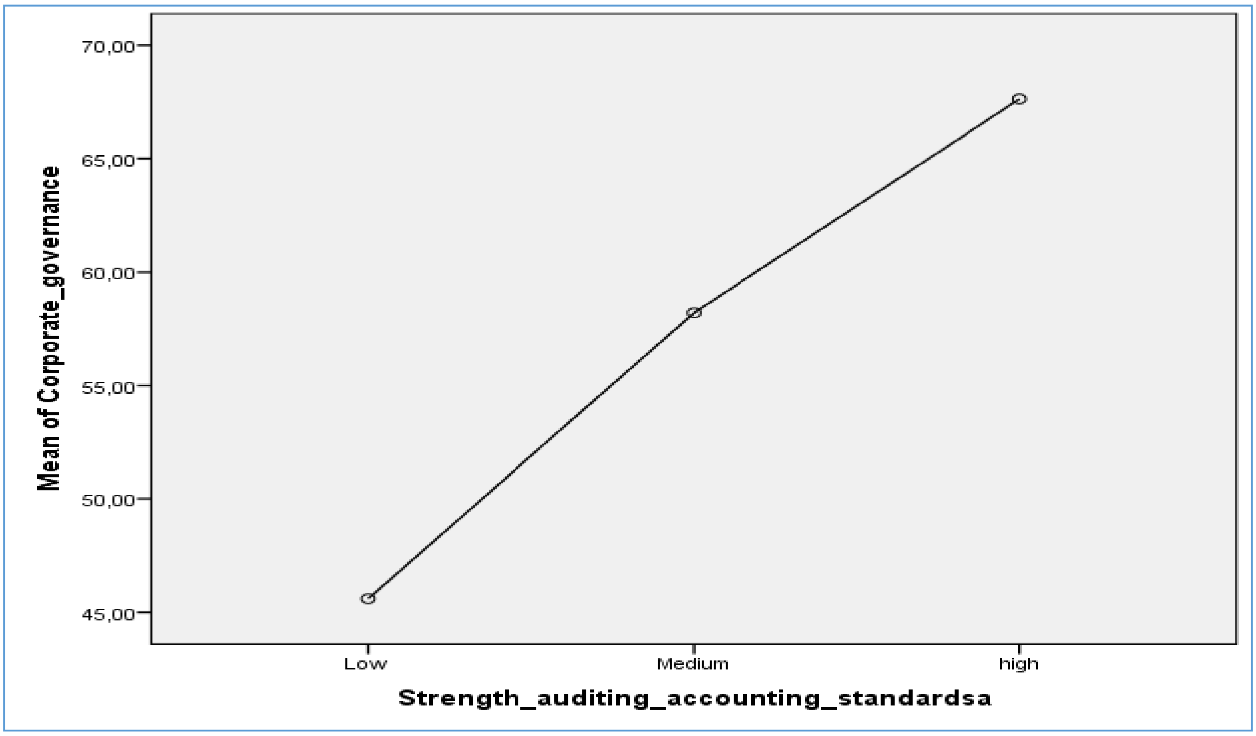
Table-7 Homogeneous Subsets for Corporate Governance

Strength auditing accounting standards		N	Subset for alpha = 0.05		
			1	**2**	**3**
Tukey HSDa,b	Low	33	45.61		
	Medium	69		58.20	
	high	38			67.63
	Sig.		1.00	1.00	1.00

Means for groups in homogeneous subsets are displayed.
a. Uses Harmonic Mean Sample Size = 42,187.
b. The group sizes are unequal. The harmonic mean of the group sizes is used.
Type I error levels are not guaranteed.

Figure-1. shows the corporate governance level by the strength auditing accounting standards. As strength auditing accounting standards increases, corporate governance level also increases, meaning that it is very important strength auditing accounting standards for improving of corporate governance level.

Figure-1. Corporate Governance Level by The Strength Auditing Accounting Standards



5. Conclusion

In this study, we investigated the relationship between the level of strength of audit and accounting standards and corporate governance by using statistical techniques for 140 countries.

In the study, considering the level of implementation of auditing and accounting standards, the average of corporate governance level was tested among the country groups.

As a result of the study, as the auditing / accounting standards strengthened, we concluded that the power of corporate governance increased as the average. Hence, it is vital to increase the strength of audit and accounting standards to strengthen corporate governance leading to not only to improve the efficiency and productivity of the corporations but also to increase economic, financial and social gains for the shareholders and stakeholders of the corporations.

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