International Journal of Innovation, Creativity and Change. www.ijicc.net
Volume 12, Issue 11, 2020

Corporate Board Attributes and Accounting Conservatism: Evidence from Thai Firms

Surachai Am-ugsorn[a], Jintana Somsoda[b], Sukanya Wonglakorn[c], Laddawan Someran[d], [a,b,c,d]Rajamangala University of Technology Suvarnabhumi, Thailand, Email: [a]sudlo2000@hotmail.com, [b]jintana_nong@hotmail.com, [c]sukanya_su@hotmail.com, [d]noinoi5202@gmail.com

The objective of this research is to investigate the relationship between corporate board of directors' attributes and accounting conservatism of listed companies on the Stock Exchange of Thailand, using a pooled regression model over the period 2014-2018. The 1,855 samples of firm-year observations measuring accounting conservatism were taken using the Basu Model (1997). Our empirical results can be summarised as follows: first, there is a positive association between board duality and accounting conservatism; second, increasing the number of board meetings encourages more conservative reporting in financial statements; and lastly, a higher quantity of an audit committee's financial expertise increases accounting conservatism. Our findings suggest that boards of directors' attributes are an important factor in determining the financial reporting quality of Thai firms.

Key words: *Accounting conservatism, Board attributes, Corporate governance.*

Statement of the Problem

Accounting information, under the good corporate governance mechanism, is becoming increasingly important for current business operations amid inconsistent events, a prime example being the subprime mortgage crisis in the US during 2007-2008, when borrowing and lending for high risk investments in real estate occurred but the real estate prices were down (Donadelli, 2015). The preparation of a financial statement must be considered with conservatism, in accounting records or in the process of preparing financial information, so investors can make decisions based on the amount of risk. This increases the accounting

conservatism of a company, helping enhance or replace good corporate governance and making the firm value higher (Sirada, 2014).

The implementation of Thai accounting standards is sometimes contrary to the intention of the management of a company; if the management's return depends on the value of the stock, executives intend to show higher profits than are actual, in order to increase the stock value. They will conceal the true performance of the company to the stakeholder, manipulating earnings, obfuscating precise signals, and increasing the information asymmetric problems between executives and external financial statements users (McNichols & Stubben, 2008).

Many prior studies have found that accounting conservatism helps to reduce earning manipulation, especially in cases where the company's asymmetric information between managers and investors is high (Garcia Lara, Osma & Penalva, 2011; LaFond & Watts, 2008). Accounting conservatism is a mechanism to bridge the relationship between the effectiveness of corporate governance and firm performance. The main role of the Executive Committee is to use power instead of shareholders, and supervise management to operate according to policy and to plan effectively. Additionally, they resolve the problem of conflict of interest. Therefore, the board of directors plays an important role in directing a company towards accounting conservatism. This research aims to test the relationship between board attributes and accounting conservatism.

Corporate Governance

Corporate governance is the system of rules, practices, and processes by which a firm is directed and controlled. Corporate governance (CG) essentially involves balancing the interests of a company's many stakeholders, such as shareholders, senior management executives, customers, suppliers, financiers, the government and the community (Klinphanich, Puangyanee, Phoprachak & Jermsittiparsert, 2019; Puangyanee, Yaowapanee, Duangsawang & Jermsittiparsert, 2019). In 2017, the Stock Exchange of Thailand (SET) proposed the Strengthen Board Effectiveness, preliminary guidelines for Good Corporate Governance, supporting listed firms to achieve good CG. The guidelines suggest the following implementations: (1) board size: the board of directors should consist of at least five directors. Boonlert-U-Thai and Phakdee (2018) found that the size of the board helped increase accounting conservatism and reduce earnings manipulation; (2) board duality: the CEO and Chairman should be separate, since the board of directors is responsible for reviewing the executives and the CEO. Having a separate chairman from the CEO is an effective tool for board monitoring (Beasley, 1996), reducing the chance that the executive will use their power beyond normal business operations. However, Yunos, Smith and Ismail (2012) point out that the separation of the CEO's and Chairman's duties does not lead to a higher level of conservatism because the controlling shareholder has influence over the board

of directors; (3) the board be independent: the audit committee must consist of at least three independent directors. Sultana (2015) found that having an independent director has a positive relationship with accounting conservatism. (4) board meeting frequency: the board should meet at least six times per financial year. Sultana (2015) found that the frequency of the meetings of the board enhanced accounting conservatism; (5) audit committee financial expertise: at least one audit committee has sufficient accounting or finance knowledge to verify the performance of a company. Sultana and Van der Zahn (2015) found a positive relationship between earnings conservatism and accounting financial expertise. (6) gender diversity: Francis, Hasan, Park and Wu (2015) found that female CEOs are more conservative in their financial reporting because they are more risk averse than male CEOs.

Accounting Conservatism

According to the Basu model (1997), developed from the theory of the relationship between earnings and stock return from a changed in the market price, accounting earnings and securities returns are related in such a way that both good news and bad news are reflected in the return of market securities immediately, according to Fama's (1970) Efficient Market Theory. The earnings value under accounting conservatism will reflect the bad news in a time and manner faster than the good news. Thai Accounting Standard Number 16 (TAS No. 16: Property, Plant and Equipment) says, "[if] a revaluation results in an increase in value, it should be credited to other comprehensive income and accumulated in equity under the heading "revaluation surplus" unless it represents the reversal of a revaluation decrease of the same asset previously recognized as an expense, in which case it should be recognised in profit or loss". This means that the bad news will be reflected immediately in both earnings and return, while the good news will only reflect immediately on returns and recognition will be delayed in accounting earnings. Resultingly, the relationship between earnings and negative returns will be at a higher level than the relationship between earnings and positive return. Therefore, the Basu (1997) concept measures accounting conservatism with the reversal regression of earnings on return, by giving earnings as a dependent variable and the return as an independent variable, as shown by the following regression model:

$$E_{it} / P_{it-1} = \beta_0 + \beta_l DR_{it} + \beta_2 R_{it} + \beta_3 R_{it} * DR_{it} + \varepsilon_{it}$$

Where:

E_{it} = Earnings per Share of business i at in fiscal year t

P_{it-1} = Price per Share of business i at end of fiscal year t – 1

R_{it} = Annual Return per Share of business i at end of fiscal year t – 1 to end of fiscal year

DR_{it} = Dummy variable is 1 if $Rit < 0$ and be 0 if $Rit \geq 0$

Annual Return per Share= $r_{it} = (P_{it} + D_{it} - P_{it-1})/P_{it-1}$

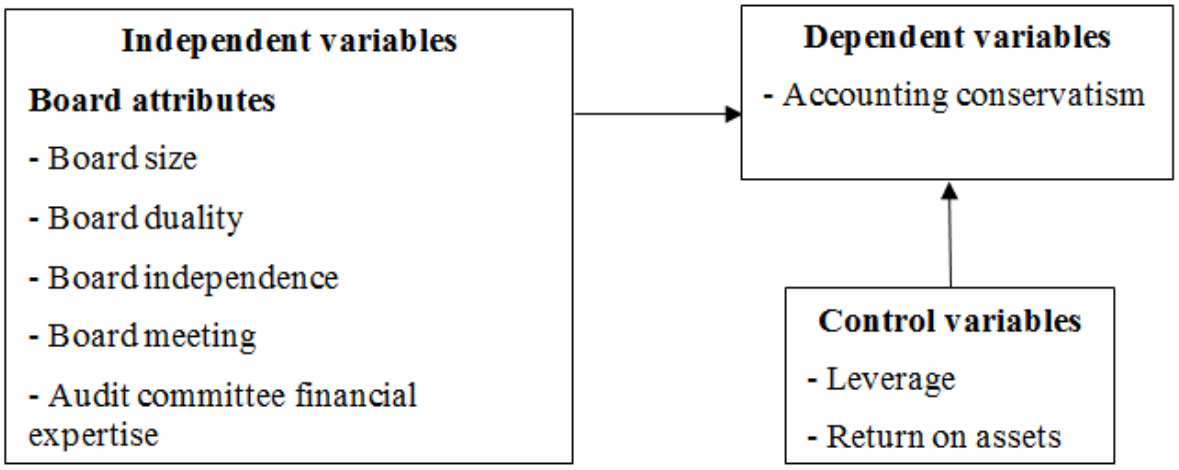
Where:

P_{it} = Price per Share of business i at end of time
P_{it-1} = Price per Share of business i at end of time t - 1
D_{it} = Dividend per Share of business i at end of time t

In the above regression, the coefficient on the interaction term β_3 is the measure of conservatism and is referred to as the asymmetric timeliness coefficient (Basu, 1997). β_3 is expected to be significantly positive, implying that more conservative firms have greater asymmetric verifiability between gains and losses (Basu, 1997; Beekes, Pope, & Young, 2004; García Lara, García Osma, & Penalva, 2007).

Research framework

Figure 1. Research Framework for the Study



Population and Sample

The population consists of 377 listed companies in the Stock Exchange of Thailand during the years 2014 – 2018. We eliminate the financial and banking firms from our sample, given that they have different accounting, financial and operating. In addition, some firm-year observations were excluded due to missing data. This process leaves 1,885 firm-year observations from the original sample.

The Model Used in Data Analysis

To investigate the association between accounting conservatism and board attributes, the standard Basu model was modified by introducing the variable of board attributes. Each independent and control variable including the model interacts with R, D, and R*D.

$$\frac{E_{it}}{P_{it-1}} = \beta_0 + \beta_l DR_{it} + \beta_2 R_{it} + \beta_3 R_{it} * DR_{it} + \beta_4 Board\ attribute_{it} + \beta_5 Board\ attribute_{it} * DR_{it} + \beta_6 Board\ attribute_{it} * R_{it} + \beta_7 Board\ attribute_{it} * DR_{it} * R_{it} + Other\ board\ attributes_{it} \& Control\ variables_{it} + \varepsilon_{it}$$

Our study tries to explain the relation between board of directors' attributes and accounting conservatism. In this section, we provide the definitions for the explanatory variables (see Table 1). Furthermore, to reduce the potential effect of the omitted variables, we also include in our model two control variables: (1) leverage and (2) return on assets.

Table 1: Independent Variables Definition

Variables	**Name**	**Measure**
Explanatory Variables		
Board Size	BS	The total number of directors serving on the board.
Board Duality	BD	The dummy variable equal to one if the CEO is chairman of the board, zero otherwise.
Board Independence	BI	The number of independent directors divided by board size (proportion of independent directors).
Board Meeting	BM	The total number of board meeting held per year.
Audit Committee Financial Expertise	AE	The ratio of an audit committee of financial expertise to total audit committee members
Gender Diversity	GD	The proportion of female directors on the board.
Control Variables		
Leverage	LE	The total long-term liabilities divided by total assets
Return on Assets	ROA	The return on assets ratio

The coefficient of the interaction term $R_{it} * DR_{it}$ with the explanatory and control variables represents the effect of the respective variable on asymmetric timeliness. For example, the

effect of a board attribute on asymmetric timeliness is observed on β_7, which is the coefficient of the interaction term $R_{it} * DR_{it}$ with the board attribute.

Descriptive Statistics and Correlations

Table 2 (Panel A, B) exposes descriptive statistics for the variables used in our model to investigate the relation between accounting conservatism and board attributes. In this table, we report only descriptive statistics for returns and earnings for the years 2014-2018 sample. We underline that the mean value of earnings items per share divided by the stock price is of (-61.6523), the minimum value is of (-77,365.91), and the maximum is of (46,806.25). Return varies from (-1%) to (26.5451%), and the mean value is (0.2065%).

On average, the boards of directors of the companies in our sample consist of ten members, with 22.13% of accounting expertise and with 18.72% of female. The mean number of board meeting is 7.49 times/year, with 40.83% outside directors. The mean value of leverage is (41.80%) and 4.18% of ROA. Panel B in Table 2 shows that in 27.90% of the firms sampled, the CEO is also the chair of the board.

Table 2 (Panel C) presents the Pearson correlation coefficient between the dependent variable (E/P), the independent variables (BS, AE, GD, BM, BI, BD) and control variables (LE, ROA). The validating of the independence of the errors, the correlation among the independent variables is between 0.003-0.265 (r is less than 0.80). It is found that all the pairs have no correlation exceeding 0.80, and the variance inflation factor (VIF) test was between 1.010-1.162, which is lower than 10 and indicates the absence of multicollinearity among the independent variables. Therefore, these variables can be included together in a regression model without estimation bias.

Table 2: Descriptive statistics for variables

Panel A. Continuous variables					
Variables	Obs.	Min	Max	Mean	Std. Dev.
E/P	1,885	-77,365.9100	46,806.2500	-61.6523	2,856.7958
R	1,855	-1	26.5451	0.2065	1.0244
BS	1,885	5	22	10.13	2.538
AE	1,885	0.0111	0.8333	0.2213	0.1273
GD	1,885	0	0.6300	0.1872	0.1444
BM	1,885	6	24	7.49	3.365
BI	1,885	0.0833	0.8750	0.4083	0.0968
LE	1,885	0.0025	1	0.4180	0.2077
ROA	1,885	-1.4993	3.2155	0.0418	0.1279

Panel B. Dichotomous variable					
Variables		Value 0		Value 1	
		Frequency	Percent	Frequency	Percent
BD		1,360	72.10	525	27.90

Panel C. The Pearson Correlations										
	E/P	BS	AE	GD	BM	BI	BD	LE	ROA	VIF
E/P	1	-.011	-.036	-.019	-.042	.010	-.021	-.061**	.147**	
BS	-.011	1	-.146**	-.073**	.120**	-.265**	-.004	.065**	.032	1.162
AE	-.036	-.146**	1	.162**	-.036	.025	-.004	.021	-.014	1.052
GD	-.019	-.073**	.162**	1	.073**	-.072**	-.023	-.088**	.000	1.060
BM	-.042	.120**	-.036	.073**	1	.140**	-.072**	.095**	-.132**	1.103
BI	.010	-.265**	.025	-.072**	.140**	1	-.018	.057*	-.018	1.132
BD	-.021	-.004	-.004	-.023	-.072**	-.018	1	.003	-.053*	1.010
LE	-.061**	.065**	.021	-.088**	.095**	.057*	.003	1	-.097**	1.039
ROA	.147**	.032	-.014	.000	-.132**	-.018	-.053*	-.097**	1	1.075

The Relation between Board Attributes and Accounting Conservatism

Table 3 reports the results of pooled regressions with backward 5 years. Model (1) presents the multivariate regression results based on asymmetric timeliness to measure accounting conservatism. In models 2, 3 and 4, we allow the asymmetric timeliness coefficient to vary with board attributes and control variables. Because we generally find heteroscedasticity problems, we report corrected t-values for each coefficient (White, 1980). The significant coefficient (0.156) on the conservatism variable ($R_{it} * DR_{it}$) in model (1) indicates that Thai companies use conservative financial reporting. The test results of the relationship between the board attributes and accounting conservatism are shown below.

Accounting conservatism and board composition: Model (2) examines the relation between board composition and accounting conservatism, the coefficient on board size ($BS * R_{it} * DR_{it}$) is positive but insignificant (0.122). The regression coefficient on board duality ($BD * R_{it} * DR_{it}$) is significantly positive (0.290), and the coefficient on board independence ($BI * R_{it} * DR_{it}$) is negative but insignificant (-0.051). **Accounting conservatism and board meetings**: Model (3) examines the relation between board meetings and accounting conservatism. The coefficient on board meetings ($BM * R_{it} * DR_{it}$) is positive and significant (0.268). **Accounting conservatism and personal characteristics**: Model (4) examines the relation between personal characteristics and accounting conservatism. The regression coefficient on audit committee financial expertise ($AE * R_{it} * DR_{it}$) is significantly positive (0.156), and the regression coefficient on female participation on boards ($GD * R_{it} * DR_{it}$) is positive but insignificant (0.089). Turning to the control variables, the coefficient on leverage indicates a positive significance and ROA indicates a negatively significant relation with accounting conservatism against all board attributes.

Table 3: Regression results of effects of boards of directors' attributes on accounting conservatism

		Model (1)	**Model (2)**	**Model (3)**	**Model (4)**
	Expected	Coeff	Coeff	Coeff	Coeff
	Signs	(t-stat)	(t-stat)	(t-stat)	(t-stat)
Intercept		36.368	-138.253	-138.891	59.735
		(0.372)	(-0.251)	(-0.446)	(0.189)
R		0.016	0.174	0.012	-0.072
		(0.654)	(0.876)	(0.138)	(-0.851)
DR		0.066*	0.049	-0.306**	-0.283**
		(2.052)	(0.313)	(-3.646)	(-3.527)
R * DR		0.156**	-0.150	-0.648**	-0.548**
		(4.972)	(-0.939)	(-7.691)	(-6.955)
BS * R *DR	+		0.122		
			(1.009)		
BD * R *DR	+		0.290**		
			7.215		
BI * R *DR	+		-0.051		
			(-0.575)		
BM * R *DR	+			0.268**	
				(3.785)	
AE * R *DR	+				0.156**
					(2.612)
GD * R *DR	+				0.089
					(0.809)
LE * R *DR			0.611**	0.614**	0.581**
			(9.516)	(9.540)	(8.929)
ROA * R *DR			-0.359**	-0.322**	-0.348**
			(-11.739)	(-10.113)	(-10.686)
Durbin-Watson		1.986	1.949	1.962	1.959
Adjusted R Square		0.014	0.167	0.143	0.139

* Significant at the 5% level, ** Significant at the 1% level.

Discussions and Conclusion

The main purpose of this paper is to examine the relationship between board attributes and accounting conservatism among 377 listed companies on the Stock Exchange of Thailand during the years 2014 – 2018. Six board attributes are investigated, namely: board size; board

duality; board independence; board meeting frequency, gender diversity and the quantity of audit committee's financial expertise. The hypothesis testing results showed no relationship between board size and accounting conservatism. This result is not supportive of our first hypothesis. Rather, our finding is consistent with previous studies such as those by Bushman, Chen, Engel and Smith (2004) and A. S. Ahmed and Duellman (2007). The result is supportive of our second hypothesis, which is a positive relationship between accounting conservatism and board duality. Our finding is similar to Krishnan and Visvanathan (2008) and Lim (2011). The study found no relationship between board independence and accounting conservatism, this result is not supportive of our third hypothesis. Empirical evidence by Bushman et al. (2004) and K. Ahmed and Henry (2012) supports our finding. The result confirms the fourth hypothesis, which presents a positive association between board meetings and accounting conservatism. In conjunction with other studies such as Vafeas (1999) and Sultana (2015), our result suggests that more active boards, as measured by the number of board meetings, require managers to practice better accounting choices, causing increases in the level of reporting quality. The result is supportive of our fifth hypothesis, which posits that there is a positive relation between accounting conservatism and the quantity of audit committee's financial expertise. Our finding is similar to Krishnan and Visvanathan (2008) and Sultana and Van der Zahn (2015), finding that the degree of accounting expertise on audit committees is positively related to accounting conservatism. The study result is not supportive of our sixth hypothesis. Our finding is consistent with Shrader, Blackburn and Iles (1997) who report no significant association between gender diversity on boards and firm performance.

Overall, our results show that board duality is positively associated with accounting conservatism. This is consistent with the incentive alignment effect. Secondly, board meetings positively affect accounting conservatism. Board activities improve board governance, which in turn are likely to improve the financial reporting quality in the Thai context. In addition, we find a positive association between the quantity of audit committee financial expertise and accounting conservatism. This positive influence suggests that an audit committee with financial expertise improves board monitoring, which in turn is likely to require a higher degree of verification for recognising good news than bad news in financial statements. Lastly, in contrast to what is expected, board size, independence and gender diversity do not appear to have a significant relation with accounting conservatism.

REFERENCES

Ahmed, A. S., & Duellman, S. (2007). Accounting conservatism and board of director characteristics: an empirical analysis. Journal of Accounting and Economics, 43, 411-437.

Ahmed, K., & Henry, D. (2012). Accounting conservatism and voluntary corporate governance mechanisms by Australian firms. Accounting and Finance, 52(3), 631-662.

Basu, S. (1997). The conservatism principle and the asymmetric timeliness of earnings Journal of Accounting and Economics, 24, 3-37

Beasley, M. S. (1996). An empirical analysis of the relation between the board of director composition and financial statement fraud. Accounting Review, 71 (4), 443-465.

Beekes, W., Pope, P., & Young, S. (2004). The link between earnings timeliness, earnings conservatism and board composition: evidence from the UK. Corporate Governance, 12(1), 47-59.

Boonlert-U-Thai, K., & Phakdee, A. (2018). Board Characteristics, Accounting Conservatism, and Firm Performance of Thai Listed Companies. Journal of Accounting Profession, 14(43), 27-47.

Bushman, R., Chen, Q., Engel, E., & Smith, A. (2004). Financial accounting information, organizational complexity and corporate governance systems. Journal of Accounting and Economics, 37(2), 167-201.

Donadelli, M. (2015). Uncertainty shocks and policymakers' behavior: evidence from the subprime crisis era. Journal of Economic Studies, Emerald Group Publishing, 42(4), 578-607.

Fama, E. (1970). Efficient Capital Markets: A Review of Theory and Empirical Work. The Journal of Finance, 25(2383-417).

Francis, B., Hasan, I., Park, J. C., & Wu, Q. (2015). Gender Differences in Financial Reporting Decision-Making: Evidence from Conservatism. Contemporary Accounting Research, 32(3), 1285-1318.

Garcia Lara, J., Osma, B. G., & Penalva, F. (2011). Conditional conservatism and cost of capital. Review of Accounting Studies, 16, 247-271.

García Lara, J. M., García Osma, B., & Penalva, F. (2007). Board of directors' characteristics and conditional accounting conservatism: Spanish evidence. European Accounting Review, 16(4), 727-755.

Klinphanich, W., Puangyanee, S., Phoprachak, D., & Jermsittiparsert, K. (2019). Influence of Representative Factors on Tax Planning through Corporate Governance of Listed Companies in the Stock Exchange of Thailand. *International Journal of Innovation, Creativity and Change, 7*(1), 300-316.

Krishnan, G. V., & Visvanathan, G. (2008). Does the SOX Definition of an Accounting Expert Matter? The Association between Audit Committee Directors' Accounting Expertise and Accounting Conservatism. Contemporary Accounting Research, 25(3), 827-858.

LaFond, R., & Watts, R. L. (2008). "The information role of conservatism". The Accounting Review, 83(2), 447-478.

Lim, R. (2011). Are corporate governance attributes associated with accounting conservatism? Accounting & Finance, 51(4), 1007-1030.

McNichols, M. F., & Stubben, S. R. (2008). Does Earnings Management Affect Firms' Investment Decisions? The Accounting Review, 83(6), 1571-1603.

Puangyanee, S., Yaowapanee, P., Duangsawang, K., & Jermsittiparsert, K. (2019). The Influence of the Shareholding Structure on Economic Performance through Good Corporate Governance of Listed Companies in the Stock Exchange of Thailand. *International Journal of Innovation, Creativity and Change, 7*(8), 116-133.

Shrader, C. B., Blackburn, V. B., & Iles, P. (1997). Women in management and firm financial performance: An exploratory study. Journal of Managerial Issues, 355-372.

Sirada, N. (2014). Accounting conservatism and future investment opportunities. Ph.D. Dissertation, Department of Accountancy, Chulalongkorn University

Sultana, N. (2015). Audit Committee Characteristics and Accounting Conservatism. International Journal of Auditing, 19, 88-102.

Sultana, N., & Van der Zahn, J. (2015). Earnings conservatism and audit committee financial expertise. Accounting & Finance, 55, 279-310.

Vafeas, N. (1999). Board meeting frequency and firm performace. Journal of Financial Economics, 53, 113-142.

White, H. (1980). A Heteroskedasticity-Consistent Covariance Matrix Estimator and a Direct Test for Heteroskedasticity. Econometrica, 48(4), 817-838.

Yunos, R. M., Smith, M., & Ismail, Z. (2012). Ethnicity and accounting conservatism: Malaysian evidence. Asian Review of Accounting, 20(1), 34-57.