WHERE INSTITUTIONAL LOGICS OF CORPORATE GOVERNANCE COLLIDE: OVERSTATEMENT OF COMPLIANCE IN A DEVELOPING COUNTRY, BANGLADESH

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Where Institutional Logics of Corporate Governance Collide: Overstatement of Compliance in a Developing Country, Bangladesh.

ABSTRACT

**Manuscript Type:** Empirical

**Research Question/Issue:** How do conflicting institutional logics predict and explain the overstatement of corporate governance compliance in a developing country?

**Research Findings/Insights:** A unique opportunity to study overstatement of compliance is available through checklists published in annual reports by companies in Bangladesh. A data set contrasting with that available from the checklists is collected by a confidential survey of company secretaries. Overstatement of compliance with the country’s Corporate Governance Guideline issued in 2006 is measured by comparing the published compliance with that revealed by the survey. There is significant overstatement of compliance in annual reports, particularly with respect to the less directly observable provisions of the Guideline. The overstatement is positively associated with control by a sponsor family and is negatively associated with the presence of an institutional investor on the board of directors.

**Theoretical/Academic Implications:** The logic associated with the regulative framework of an Anglo-American-based corporate governance model conflicts with the logic of a cultural-cognitive institutional framework in a developing country. The resulting contest of legitimacy motivates firms to overstate compliance with the Corporate Governance Guideline 2006 in annual reports.

**Practitioner/Policy Implications:** This study highlights the challenges of introducing an Anglo-American model of corporate governance in a developing country. National and international investors should seek to understand the reality of the corporate governance structure of firms in developing countries, rather than relying solely on compliance reported
in annual reports. For researchers, there may be limitations in using the compliance reported in annual reports as a measure of corporate governance.

**Key words:** Corporate Governance, Competing Institutional Logics, Overstatement of Compliance, Family Control, Institutional Investor Director, Bangladesh.
INTRODUCTION

In Bangladesh, as in other developing countries, a corporate governance (CG) guideline has been introduced based on an Anglo-American approach (Siddiqui, 2010). This brings a regulative institutional context to the implementation of CG. In contrast, the country’s traditional governance of family-controlled firms is based within a cultural-cognitive context (Uddin & Choudhury, 2008). In this paper, the regulative and the cultural-cognitive contexts and their respective logics, which Scott (2014:60) describes as instrumentality and orthodoxy, are contrasted in order to predict and explain observed overstated reporting of CG compliance in Bangladesh.

Prior firm-level studies on CG codes mostly investigate the level of compliance with national codes and on the association between the level of compliance with codes and firm performance (see recent review by Cuomo, Mallin and Zattoni, 2015:10). In the works on compliance with CG codes, scepticism is evident around congruity between compliance as stated in compliance statements and actual governance arrangements. For example, Akkermans et al. (2007:1109) cautioned that compliance rates based on public information may overstate actual compliance. The level of overstatement could be significant in developing countries because institutional characteristics of developing countries (e.g., cultural characteristics and the existence of institutional voids) are not supportive of effective implementation of an Anglo-American model of CG (Wanyama et al., 2009). Theoretical development also suggests that organizations choose ‘window-dressing’ to conceal non-conformity with a formal compliance program while they face competing institutional logics (Greenwood, Raynard, Kodeih, Micelotta and Lounsbury, 2011:349; Pache & Santos, 2010; Oliver, 1991). However, investigation of overstatement of compliance with a national code has not featured to any meaningful degree in the empirical work. The suspicion around the congruity between compliances as stated in compliance statements and actual governance
arrangements, together with the above-mentioned theoretical development, provide the motivation for the investigation of overstatement of compliance in a developing country.

The context of Bangladesh, as an example of a developing country, is chosen due to an interesting data source available. Although the CG guideline is based upon the principle of ‘comply or explain’, the regulator requires a checklist to be published in annual reports, specifying ‘compliance’ or ‘non-compliance with an explanation’ with each provision of the Bangladesh Corporate Governance Guidelines-2006 (BSEC, 2006). Having observed in a preliminary review of corporate annual reports that compliance reported in the checklists appeared to be uniformly high, a questionnaire survey is used to establish whether such high compliance existed in reality. In prior research on Bangladesh, Uddin and Choudhury (2008) used interviews to show that a traditionalist culture mediates the rationalist/legalist framework of CG. The respondents indicated that it was not unusual, in family-controlled businesses, to find family members were instructing their accountants to prepare favorable reports for important stakeholders such as creditors, the Bangladesh Securities and Exchange Commission (BSEC) and stock exchange officials. However, the World Bank (2009) reported a significant improvement in CG practices, finding an average level of 82 percent compliance based upon information reported in the annual report. Comparing these two sources indicates a high probability of overstatement of compliance in annual reports. Overstatement behavior is hypothesized in this paper, in terms of competing institutional logics, as the orthodoxy logic of a cultural-cognitive pillar, competing with the instrumentality logic of a regulative pillar.

Overstatement is investigated by matching the responses to survey questions put to 91 companies in 2012 with the published accounts of their CG compliance. Results show a statistically significant overstatement of CG compliance in the annual reports. Control by the sponsor family is directly associated with overstatement. The presence of an institutional
investor representative on the board of directors is inversely associated with overstatement. In both cases the overstatement is more pronounced in respect of those CG requirements that are not directly observable externally.

The contribution of the paper is to demonstrate that observed overstatement behavior can be an outcome of conflict at the organizational field level, organizational level and actor level. On the one hand the regulative logic of instrumentality causes firms to report high compliance in order to achieve legally sanctioned legitimacy in the eyes of the domestic regulatory agencies and the International Financial Institutions (IFIs) such as the World Bank, the Asian Development Bank and the International Monetary Fund. On the other hand the cultural-cognitive logic of orthodoxy causes businesses to avoid implementing CG procedures in reality. Family-controlled businesses overstate compliance more due to the 'cognitive consistency' of organizational structures of family-controlled firms and in order to protect private benefits of control afforded by controlling shareholder family due to the existence of 'institutional voids'. The maintenance of 'cognitive consistency' is explained by Scott (2014:74) as the legitimation of the ‘structural template.’ The presence of an institutional investor representative on the board of directors modifies the power structure and encourages more compliance with the Anglo-American model. However, even here overstatement remains, albeit reduced. The instrumental logic of institutional investors is an incomplete challenge to the orthodoxy of family-controlled firms. The findings of this paper suggest that due to coercive pressures from the IFIs and BSEC, companies attempt to maintain regulative legitimacy by overstating compliance in annual reports as they cannot implement the recommended CG practices due to the orthodoxy logic of cultural-cognitive institutions. Thus, two apparently contradictory findings reported by Uddin and Choudhury (2008) and the World Bank (2009) are reconciled by this paper.
CORPORATE GOVERNANCE IN BANGLADESH

This section describes the process of adoption of an Anglo-American-based CG guideline in Bangladesh highlighting aspects of the cultural-cognitive framework of Bangladesh that were in conflict with an Anglo-American style of CG guideline.

Following the Bangladesh stock market crash of 1996, the Asian Development Bank (ADB) funded an $80 million project to transform the country’s capital markets (ADB, 1997). One objective was to produce a comprehensive manual of CG for public limited companies and issuers of securities. That project was assisted by a US consultant, The Aries Group Ltd, who formulated a CG guideline consistent with the Principles of Corporate Governance 1999 (OECD, 1999) of the Organization for Economic Cooperation and Development (ADB, 2005). The BSEC adopted the guideline in 2006 (BSEC, 2006). It is described hereafter as the BCGG-2006 (Bangladesh Corporate Governance Guideline 2006). The BCGG-2006 is recognized in the listing rules of both the Dhaka and Chittagong Stock Exchanges, in a manner typical of an Anglo-American governance code (Uddin & Choudhury, 2008). Siddiqui (2010:269) noted that the BCGG-2006 was ‘remarkably similar’ to the voluntary Bangladesh Corporate Governance Code-2004 (BCGC-2004) previously issued (BEI, 2004) by the Bangladesh Enterprise Institute (BEI). The BEI is a private-sector think-tank organization which, funded by the IFIs, first studied the CG practices in Bangladesh (BEI, 2003) and subsequently issued the BCGC-2004 (BEI, 2004) as an initiative to improve CG practices. Siddiqui (2010) argued that by adopting the BCGG-2006 resembling the BCGC-2004, the BSEC demonstrated its legitimacy to the IFIs.

However, wider cultural, social, regulatory and political factors in Bangladesh may lead to tensions with such Anglo-American-based CG practices. Bangladesh is characterised as a country with high levels of collectivism and power distance (Hofstede, Hofstede & Minkov, 2010). The promotion of incompetent family members and associates at the
expense of talented individuals (Ahsan, 2010), and the concentration of authority and power at the top is evident in every sphere of life, from political parties to business organizations (Kochanek, 2000). As in other countries with a similar cultural profile (Chakrabarty, 2009), family ownership dominated in Bangladesh long before Independence in 1971 (Kochanek, 1996). The large corporations, nationalized as a result of independence, were returned to families after 1975 when Bangladesh adopted market-based capitalism (Belal & Cooper, 2011). The families were selected based upon their relationship with, and the amount of illicit payment that they could offer to, the contemporary ruling parties (Uddin & Choudhury, 2008). The movement to market-based capitalism, however, was not supported by formal legal and regulatory institutions as they were dysfunctional (Uddin, 2009) but was implemented due to the intervention of the IFIs in development policies (Uddin & Hopper, 2003).

Since then, Bangladesh has achieved limited improvement in its formal legal and regulatory institutions. At present, Bangladesh suffers from a high level of corruption (TIB, 2012), poor implementation and enforcement of regulations (World Justice Project, 2015), significant difficulties in enforcement of contracts (World Bank, 2014), a small and volatile stock market (The Aries Group Ltd, 2012), unavailability of credit rating information (IMF, 2013), and a passive managerial labor market (Siddiqui, 2010). Several researchers regarded such a lack of formal legal and regulatory institutions as institutional voids (e.g., Khanna, Palepu, & Sinha, 2005; Peng & Jiang, 2010). According to Chakrabarty (2009), institutional voids reinforce family ownership and control. Consequently, the ownership and management of Bangladeshi companies is concentrated in sponsor families and groups (Haque, Arun, & Kirkpatrick, 2011).

A single sponsor family often controls a number of firms in the manufacturing, financial and service sectors (Nuruzzaman, 2004) indicating the family’s custody of a
formidable amount of economic resources. The controlling sponsor families can also easily ensure access to bank finance using their reputation, relationship and ability to provide collateral (Masum & Parker, 2013). Most of the controlling sponsor families are either directly or indirectly politically connected with one of the two major political parties (Uddin, 2009). Consequently, several prior studies have depicted Bangladesh as an example of crony capitalism (Haque et al., 2011; Uddin & Hopper, 2003). The capital market is populated mostly by poorly-literate ill-informed retail ‘momentum’ investors (The Aries Group Ltd, 2012). Consequently, a few business elites can manipulate the stock price, legally or illegally (Khaled, Chowdhury, Baree, & Kabir, 2011) and combat regulatory enforcement using ‘political influence’ (Uddin, 2009:789). The controlling sponsor families take advantage of institutional voids to constrain accountability to general shareholders (BEI, 2003). On the other hand, general shareholders do not challenge the controlling sponsor families in the annual general meeting (Uddin & Choudhury, 2008).

The BCGG-2006 requires listed companies to include a checklist in their annual report specifying ‘compliance’ or ‘non-compliance with an explanation’ with each provision of the BCGG-2006. In 2009, the World Bank, in a study of compliance with the BCGG-2006 as reported in annual reports, found compliance, on average, with 82 per cent of the BCGG-2006 provisions (World Bank, 2009:41). The World Bank claimed this indicated a significant improvement in CG practices of firms. An analysis of annual reports of the BSEC from 2007-8 to 2011-12 by the researcher revealed that around 75 percent of companies complied fully with the BCGG-2006 and the remaining (approximate) 25 per cent complied partly. In contrast, Uddin and Choudhury (2008:1045), applying an interview method, found that companies in Bangladesh fail to comply with basic corporate rules and regulations, with the dominance of sponsor families weakening the state’s power in the enforcement of rules
and regulations. From survey evidence Haque et al. (2011) found that sponsor family control and political affiliation of directors hinder improvement in CG practices.

The section on development of hypotheses discusses how conflicting logics predict that the circumstances prevailing in Bangladesh will lead to ‘window-dressing’ of reported compliance that exceeds the reality.

THEORETICAL FRAMEWORK

Corporate governance codes based upon the Anglo-American model have been adopted by nations worldwide for reasons of efficiency and legitimacy (Zattoni & Cuomo, 2008). Legitimacy-based reasons have been particularly pronounced in developing countries (Reed, 2002; Siddiqui, 2010). Aguilera and Cuervo-Cazurra (2004) posited that, depending on the nature of the issuing authority, the adoption of a CG code creates different types of legitimacy pressures for compliance. Non-compliance can result in a loss of external legitimacy.

However, scholars have argued that an Anglo-American model is ‘unsuitable for developing country economies’ (Singh & Zammit, 2006:221) due to cultural characteristics (Lau & Young, 2013) and the existence of institutional voids (Young, Peng, Ahlstrom, Bruton et al., 2008). Developing countries rank high with regard to collectivism and power distance relative to Anglo-American countries (Hofstede, 1980). Institutional voids also exist due to factors such as poor enforcement of regulations, difficulties in enforcement of contracts, high levels of corruption, and inefficiency of product, labor and capital markets (Khanna et al., 2005). Family-controlled businesses dominate due to cultural profile (Chakrabarty, 2009) and the existence of institutional voids (Peng & Jiang, 2010). At the same time, the existence of institutional voids creates an opportunity for the controlling
shareholder families to afford significant private benefits of control (Young, Peng, Ahlstrom, Bruton et al., 2008).

The implementation of a CG code which is based upon an Anglo-American model can be hindered by the distinct cultural and institutional characteristics of developing countries (Wanyama, Burton, & Helliar, 2009) and powerful interest groups who fear a reduction in the private benefits of control afforded to them by existing corporate governance practices (Bebchuk & Roe, 1999; DiMaggio, 1988). Thus, firms’ responses toward compliance with a CG code based upon an Anglo-American model, in the context of developing countries, are subject to conflicting institutional demands. CG mechanisms based upon an Anglo-American model are also perceived as institutionally contested practices in developed countries where cultural and institutional characteristics are contrasting with those of Anglo-American countries (e.g., stock-based executive pay in Germany by Sanders and Tüschke, 2007; disclosure of individual executive pay in Germany by Chizema, 2008; shareholder value orientation in the Netherlands by Bezemer, Zajak, Naumovska, Van Den Bosch et al., 2015).

The structure of the organizational field fundamentally shapes the nature and extent of competing institutional logics which organizations face (Greenwood, Raynard, Kodeih, Micelotta et al., 2011:334). Organizations more likely face competing institutional demands when the organizational field is fragmented (Pache & Santos, 2010). A fragmented organizational field refers to a number of uncoordinated constituents motivated by competing institutional logics to exert competing demands (Scott & Meyer, 1991). Organizations facing competing institutional logics are often subject to contradictory regulative, normative and cultural-cognitive logics (Kraatz & Block, 2008:243). According to Scott (2014:74), a prescription that conflicts with the cultural-cognitive element lacks a taken-for-granted status. Legitimacy gains from implementation of such prescription remain unclear to organizations
(DiMaggio & Powell, 1983), as organizational responses to a prescription which may be perceived legitimate by one constituent may be perceived illegitimate by another (Scott, 2014:73). Under such conditions, organizations must maintain ‘pluralistic legitimacy’ (Kraatz & Block, 2008:249). In order to gain and maintain ‘pluralistic legitimacy’, organizations exercise some level of strategic choice when selecting their responses (Oliver, 1991; Pache & Santos, 2010).

Organizations facing competing institutional logics strategically select one or more of the following strategies; compromise, avoidance, manipulation and defiance, in order to gain and maintain legitimacy, as proposed by Oliver (1991) and developed more explicitly by Pache and Santos (2010). Compromise involves balancing, pacifying and bargaining with institutional referents (Oliver, 1991; Scott, 2014:211) which is less likely to be achievable in the case of a formal compliance program (Jamali, 2010). Pache and Santos (2010:464) emphasize that manipulation and defiance requires ‘overt contestation of institutional demands’ leading to loss of organizational legitimacy to the constituents who recommend new practice. This suggests that an avoidance strategy, more particularly ‘window-dressing’ to conceal non-conformity with institutional demands, can be a feasible strategic choice with respect to a formal compliance program. Oliver (1991) cites Meyer and Rowan (1977) who indicate that concealment tactics such as ‘window-dressing’ involve disguising nonconformity behind a facade of acquiescence. ‘Window-dressing’ is synonymous with the concept of ‘decoupling’ as pioneered by Westphal and Zajak (1994), which indicates a situation whereby organizations declare the adoption of CEO long-term incentive plans without their actual implementation. Jamali (2010), using the framework of Oliver (1991), investigated managerial perceptions of institutional antecedents of compliance with the International Accountability Standards. She demonstrated that managerial perceptions of institutional antecedents correspond most closely to a strategic response of avoidance.
This study argues that the reporting of compliance in annual reports differs from actual implementation at the organizational level with respect to adoption of an Anglo-American model in developing countries, as the policy is recommended by a regulative institutional profile but less favored by a cultural-cognitive institutional profile.

Organizational-level dynamics further create variation in strategic responses to an institutionally contested new practice (Fiss, Kennedy and Davis, 2012). Shipilov, Greve and Rowley (2010) demonstrated that organizations with internal authority structures sharing the contrasting logic underlying a new practice will more likely resist the implementation of the new practice. Organizational-level dynamics such as organizational goals, culture and authority relations are difficult and costly to change (Rao, Morrill & Zald, 2000:240). Hence, organizations with goals, culture and authority relations based upon institutional logic competing with that of the new practice are under more pressure to ‘window-dress’ compliance with the practice to gain and maintain legitimacy (Oliver, 1991).

Individual-level experiences and identities of internal actors influence their cognitive processes as to their understanding of what is a legitimate organizational response under conflicting institutional pressures (George, Chattopadhyay, Sitkin, & Barden, 2006). The relative power and influence of internal actors will create variation in organizational responses since those which protect the interests of external audiences may hinder the interests of internal actors. Both theory (Pache & Santos, 2010:465; Oliver, 1991) and empirics (Fiss & Zajak, 2004; Westphal & Zajak, 2001) suggest that when the personal interests of managers are potentially threatened by the adoption of a new practice, the selection of an avoidance strategy is more likely to maintain legitimacy to external constituents.

Internal actors can be heterogeneous in terms of their goals and interests (Greenwood & Hinings, 1996). Each group may attempt to influence organizational responses for its own
benefit. In such a case, the relative bargaining strength of internal actors affects the strategic responses of organizations (Greenwood, Raynard, Kodeih, Micelotta et al., 2011). More specifically, Pache and Santos (2010) posited that when internal groups representing two sides of conflicting institutional pressures have the power to influence decisions, the likelihood of using an avoidance strategy is reduced.

However, the practicality of gaining and maintaining legitimacy by using an avoidance strategy depends on the level of information asymmetry that firms can maintain with respect to the practice (Crilly, Zollo & Hansen, 2012). The external constituents recommending change cannot easily observe firms’ internal practices (Christmann & Taylor, 2001). Consequently, firms are more successful in using an avoidance strategy with respect to internal practices rather than externally observable practices (Crilly et al., 2012). Hence, this study argues that the difference between compliance reported in annual reports and actual implementation which prevails at the organizational level will be higher with respect to CG provisions that are less observable externally.

This section has discussed the role of the organizational field, the organization and the individuals within organizations and information asymmetry in selecting an avoidance strategy as an organizational response to competing institutional logics. Using this literature, the next section develops the hypotheses.

**HYPOTHESES**

Non-conformance with coercive pressures created by regulatory agencies threatens a firm’s regulative legitimacy (Ruef & Scott, 1998). Prior research around compliance with CG codes indicates that apparent over-compliance is triggered by regulative legitimacy (Arcot, Bruno, & Faure-Grimaud, 2010). In Bangladesh, Siddiqui (2010:270) explains that coercive and mimetic forces allowed the BEI and BSEC to demonstrate their legitimacy to the IFIs and
respond to perceived legitimacy threats by adopting an Anglo-American CG model. Coercive pressures on firms may have been created by the BEI in drawing on a wide range of key players to write the BCGC-2004 (BEI, 2004). These pressures increased further when the BSEC adopted the BCGG-2006 drawn from the BCGC-2004 and the stock exchanges included the BCGG-2006 in their listing rules. The Corporate Finance Department (CFD) of the BSEC ensures that the statement of compliance with the BCGG-2006 is included in the annual reports of listed companies as part of its supervisory process (BSEC, 2012:34-35). A number of prior studies suggest that stock markets react positively to announcements of levels of compliance with CG codes (e.g., Goncharov, Werner, & Zimmermann, 2006; Alves & Mendes, 2004). Hence disclosure of ‘non-compliance without an explanation’ could be regarded by managers as a threat to regulative legitimacy.

However, cultural and institutional profiles of Bangladesh, as in many other developing countries, act as deterrents not only for managers’ motivation to present themselves as accountable but also for shareholders’ motivation and ability to monitor managers. Bangladesh is characterized as a country with high levels of collectivism and power distance. Cultures of strong collectivism, underestimating the value of personal competence and talent in career advancement, reduce the accountability of managers (Hooghiemstra, Hermes & Emanuels, 2015). Conversely, cultures of high collectivism, deemphasizing the importance of personal judgement in investment decision making, reduce the monitoring ability of shareholders (Chan & Cheung, 2008). Cultures with high levels of power distance, invoking power and wealth differentials between managers and shareholders (Fidrmuc & Jacob, 2010), stimulate managerial entrenchment and shareholders powerlessness (Chan & Cheung, 2008). This, in turn, reduces the need for managers to present them as accountable to shareholders.
In Bangladesh, the projected careers of managers depend upon their kinship and relationship with powerful families rather than their personal competence and talent (Uddin and Choudhury, 2008). The consecutive crashes of stock markets and constant high volatility of stock prices in Bangladesh (Hossain, 2013) suggest limited application of independent personal judgement by the general shareholders. The AGM is stage-managed by managers to limit shareholders’ participation in decision making process and to limit dividend payments (Uddin & Choudhury, 2008). General shareholders are found to be reluctant to speak out in AGMs (BEI, 2003) possibly indicating their acceptance of their powerlessness. This behavior suggests that the concepts of accountability advocated by an Anglo-American model are not well ‘recognizable and located within the set of the widely held cognitive structures’ (Sanders & Tüschke, 2007:33) of managers and shareholders in Bangladesh.

Institutional voids are the result of institutional characteristics such as high levels of corruption, high inefficiencies in the judicial systems. Such institutional voids induce managers to resort to the unofficial economy (Friedman, Johnson, Kaufmann, & Zoido-Lobaton, 2000) and reduce managerial transparency in accounting and governance (Bushman, Piotroski, & Smith, 2004). They also constrain the monitoring ability of shareholders (Klapper & Love, 2004). Under high levels of corruption, firms are required to make illicit payments to government officials and crime organizations in order to obtain scarce resources and protect their interests (Uddin & Hopper, 2003:749, Li, 2013). Furthermore, significant difficulty in enforcement of contracts threatens confidentiality of proprietary information (Morck, 2007) and creates uncertainty towards the protection of rights on general and intellectual properties (Bushman et al., 2004).

Because of illicit payments, firms maintain strong secrecy and control over the preparation of accounting reports (Uddin, 2009:789), comply poorly with International Accounting Standards (Mir & Rahaman, 2005) and make limited disclosure (Akhtaruddin,
Effective implementation of the BCGG-2006 could create uncertainty by revealing proprietary information and unethical practices of firms. This suggests that larger belief systems and the reality of daily life experienced by managers are not consistent with an Anglo-American model that asks for rule-based formal practices, openness and transparency (Judge, 2012). On the other hand, shareholders cannot enforce their legal rights as the judicial systems of Bangladesh are inefficient and corrupt (The Aries Group Ltd., 2012).

Finally, from the annual report of the BSEC it would appear that the CFD does not investigate compliance in depth, whilst the Enforcement Department (ED) has not taken any identifiable action in relation to compliance with the BCGG-2006. Historically the CFD has been small in number and limited in relevant qualifications (The Aries Group Ltd., 2012).

The consequence of strong cultural-cognitive logics and the lack of effectiveness of regulative logics means that firms may engage in ‘window-dressing’ to conceal their non-conformity with the BCGG-2006 and appear to prove their regulative legitimacy to the BSEC and stock exchanges. Hence, the first hypothesis is as follows:

**H1:** There is a significant level of overstatement of compliance with the BCGG-2006 as reported in annual reports.

Legitimacy is determined by mutual observations between managers and external constituents who recommend institutional change and observe managers’ actions (Seidl, 2007). Hence, the level of information asymmetry plays an important role in determining organizational responses (Crilly et al., 2012). With respect to CG codes, Seidl (2007:713) hypothesized that conformance between compliance with CG codes declared by managers and what is actually put into action depends considerably on the extent to which external
constituents are able to assess the conformance. The BCGG-2006 contains provisions that can be divided into more observable and less observable categories as explained later. Hence, it is hypothesized:

H1a: The extent of overstatement of compliance with the BCGG-2006 is higher with respect to the provisions of the BCGG-2006 which are less observable by outsiders.

One of the major characteristics of companies in Bangladesh is family ownership and control, an important feature of many developing countries (e.g., Peng & Jiang, 2010; Young et al., 2008). The IFIs and their supporters (e.g., Morck, Wolfenzon & Yeung, 2005) argue that family ownership and control are the root causes of CG problems in developing countries (Singh & Zammit, 2006) and advocate CG policies targeting reduction in family control (World Bank, 2002). In Bangladesh, the IFIs first act through their funded research organization, the BEI. In its study of CG practices the BEI argues that ‘closely-held family ownership leads to limited transparency and accountability’ (BEI, 2003:109). Subsequently, cognisant of this view, the domestic regulators attempted to dilute family control. This may suggest that threats to regulative legitimacy resulting from non-compliance with the BCGG-2006 without explanation are more pronounced for family-owned and controlled firms. By disclosing compliance with the BCGG-2006 in annual reports, family-controlled firms can alleviate pressures from the IFIs and domestic regulators.

However, family ownership and control are embedded in a nexus of cultural profile and institutional voids of Bangladesh. High levels of collectivism supplemented by difficulties in enforcement of contracts encourage family owners to retain ownership and control of their business activities within their extended families (Chakrabarty, 2009). High levels of collectivism promote centralized authority (Li & Harrison, 2008). High levels of
power distance favor hierarchical organizational structures (Hofstede, 1980). In Bangladesh, family owners are reluctant to appoint, and relinquish authority to, outside professional managers (Uddin & Choudhury, 2008). They maintain extremely centralized and hierarchical organizational structures. It could be argued that the organizational structure of family-controlled firms in Bangladesh achieves ‘cognitive consistency’ (Scott, 2014:74) as it is based on a cultural-cognitive element. However, this organizational and management structure is inconsistent with the type of formal and decentralized CG structure advocated by an Anglo-American model (Judge, 2012). Change in corporate culture is difficult and costly, more especially when a change in an organizational culture will conflict with the social cultural and institutional profile (Rao et al., 2000). Furthermore, potential extra benefits from the effective implementation of the BCGG-2006 are inadequate, as stock markets in Bangladesh are small and family-controlled firms can easily gain access to finance from banks (Masum & Parker, 2013).

The case study evidence provided by Uddin (2009) shows that control by family members and their few trusted managers helps the firm gather updated market data on its own sales positions and those of its competitors on a day-to-day basis, use managerial expertise across group companies and use surplus cash to finance associated companies. This evidence is consistent with prior evidence in developing countries that family-controlled group firms fill the voids created by the absence of institutions that support efficient functioning of markets for product, labor and capital (Khanna & Rivkin, 2001, Khanna et al., 2005). The effective implementation of the BCGG-2006 may constrain the ability of controlling families to use resources across group firms.

The existence of institutional voids, at the same time, creates an opportunity for the controlling shareholder families to afford significant private benefits of control (Young, Peng, Ahlstrom, Bruton et al., 2008; Peng & Jiang, 2010). In Bangladesh, the controlling
shareholder family are found to expropriate company resources by paying salaries and other benefits to family cronies who make no contribution to the company (Uddin, 2009). The effective implementation of the BCGG-2006 would reduce the opportunities for such private benefits of control. Hence, the following testable hypothesis:

H2: Overstatement of compliance with the BCGG-2006, as reported in annual reports, is positively associated with family control.

Meyer and Rowan (1977) argued that firms resisting change try to keep internal structures unaltered in order to maintain efficiency. It is more difficult for regulatory authorities to reveal overstatement with respect to less observable provisions as these provisions are subject to level of information asymmetry. Hence, to assess the roles of more observable and less observable provisions of the BCGG-2006, this study tests each of the following hypotheses.

H2a: Overstatement of compliance with respect to observable provisions of the BCGG-2006, as reported in annual reports, is not associated with family control.

H2b: Overstatement of compliance with respect to less observable provisions of the BCGG-2006, as reported in annual reports, is positively associated with family control.

The relative power of heterogeneous internal constituents actively influences organizational actions (Greenwood, Raynard, Kodeih, Micelotta et al., 2011) as each group may attempt to influence organizational responses for its own benefit (Pache & Santos 2010). DiMaggio (1988:14) argued that ‘new institutions arise when organized actors with sufficient resources see in them an opportunity to realize interests that they value highly’. Ownership
of the constituents often determines their relative power in a firm (Fiss & Zajak, 2004). Amongst different ownership groups, independent institutional investors are more powerful in terms of uniformity of demand as they provide significant amount of resources and can act independently of the insider’s agenda (Almazan, Hartzell, & Starks, 2005). Prior research has demonstrated that independent institutional investors prefer an Anglo-American model as it emphasizes maximization of shareholder value (Bezemer, Zajac, Naumovska, Van Den Bosch et al., 2015; Chizema, 2008) and take actions in line with an Anglo-American model to protect their legitimacy in a contested environment (Bates & Hennessy, 2010).

The institutional investors, who are independent of sponsor families, could provide a force to discourage overstatement. In Bangladesh, the institutional investors are represented on the board of directors (World Bank, 2009) when they own a significant percentage of shares. Thus, representation of an institutional investor on board indicates a firm’s relatively high resource dependence on institutional investors. The presence of a powerful external representative on the board with a divergent interest is likely to create pressure on insiders for at least symbolic compliance with the BCGG-2006 and thus could reduce the overstatement of compliance. Due to the high social position of institutional investors in Bangladesh and pressure from the IFIs, who continuously criticise them for their inactivity (see, e.g., The Aries Group Ltd, 2012), institutional investors may also have an interest in protecting their own legitimacy. The CEO of the first private sector mutual fund company was included in the working group of the BEI in the formulation of the voluntary BCGC-2004 (BEI, 2004). The participation by this CEO indicates support from institutional investors for an Anglo-American model of CG to be developed in Bangladesh.³ Prior interview evidence provided by Uddin and Choudhury (2008) has also indicated that the presence of a representative of an institutional investor on a board of directors improves CG practices. Hence, this study hypothesizes:
H3: Overstatement of compliance with the BCGG-2006, as reported in annual reports, is negatively associated with the presence of an institutional investor representative on the board.

However, family-controlled firms that overstate compliance run the risk of undermining their regulative legitimacy if the overstatement is subsequently revealed by the regulatory agencies. This indicates that externally observable provisions are more likely to be implemented due to fear of revelation by regulatory authorities. Institutional investor directors’ ability to reduce overstatement with respect to observable provisions will be less pronounced. Consequently, to assess the roles of more observable and less observable provisions of the BCGG-2006, this study tests each of the following hypotheses.

H3a: Overstatement of compliance with respect to observable provisions of the BCGG-2006, as reported in annual reports, is not associated with the presence of an institutional investor representative on the board.

H3b: Overstatement of compliance with respect to less observable provisions of the BCGG-2006, as reported in annual reports, is negatively associated with the presence of an institutional investor representative on the board.

RESEARCH DESIGN

Sample and Data Collection

The sample consists of 91 non-financial companies that responded to a questionnaire survey. The survey was conducted between January and March 2012 and addressed to company secretaries or chief financial officers (CFOs). The survey collected detailed data on compliance with the provisions of the BCGG-2006, family relationships among directors, the
composition of the board of directors and the ownership structure of the company. The detailed questionnaire\textsuperscript{4} probed beyond simple compliance with the items to be reported in annual reports as part of the compliance statement and consequently could not be answered purely by referring to the annual reports. I deliberately avoided direct questioning on overstatement and its motivation; as such questions could raise respondents’ awareness of overstatement. For the purpose of this study, compliance with 20 provisions of the BCGG-2006 (see Table 1) as stated in the survey is selected as these provisions could be compared directly with compliance reported in annual reports.

\begin{center}
Insert Table 1 about here
\end{center}

The questionnaire included both open and closed questions. The introductory letter accompanying the survey explained its purpose as to understand the underlying level of compliance with the provisions of the BCGG-2006. It assured anonymity of the respondents and their organizations (Van der Stede, Young, & Chen, 2005). The questionnaire was pre-tested with two company secretaries.

The survey instrument was mailed to all 136 non-financial companies listed on the Dhaka Stock Exchange (DSE), Bangladesh as at 31 December, 2011. The names of company secretaries or CFOs and the addresses of companies’ headquarters were retrieved from Central Depository Bangladesh Limited.\textsuperscript{5} Banks and financial institutions were excluded as they are subject to other CG rules issued by different regulatory authorities. I personally visited companies whose registered offices are situated in Dhaka and persuaded the company secretaries or CFOs to participate in the survey in the form of a structured interview. During the visits, I assured anonymity frequently. Alumni connections assisted in reaching the respondents. Loyalty might also have featured in the willingness to participate where the alumni connection generated some trust between the respondents and the researcher. The
total of 91 usable responses represented a response rate of 66.91 percent was obtained. In order to test for response bias, respondents were compared with the population on the basis of industry sectors, family control, market capitalization and total assets (Wallace & Mellor, 1988). As shown in Table 2, no significant difference was indicated by a chi-square test in the distribution of companies across any of these categories.

In order to have available the most recent accounting information at the date of the survey, annual reports were collected for all 136 non-financial companies, for the financial year 2011. Reports were obtained in printed format, from the BSEC and DSE Libraries.

Data Analysis

For each company two measures of compliance with the BCGG-2006 were constructed. One was compliance as reported in the annual reports and the other was compliance as stated in the survey. These two variables were each accumulated as totals with a maximum of 20, using a binary indicator [1 for compliance and 0 for non-compliance] for each governance provision. ‘Non-compliance with an explanation’ is an ambiguous item creating coding difficulty as nominally it constitutes compliance according to the ‘comply or explain principle’ but is in reality it is non-compliance. In the sample, there were 13 companies who used the ‘non-compliance with an explanation’ facility for a total of 42 provisions ranging from one to 12 provisions. However, scrutiny of the reasons given indicated poor quality excuses rather than explanations, which made any coding of those items potentially ambiguous. One common example of such an explanation is ‘under process’, [i.e. not yet implemented] as used by 10 companies for a total of 39 provisions. Two companies provided size-related justification and one company claimed the scarcity of CEOs with relevant
industry-related expertise for not separating the position of chairman and CEO. Hence, those particular characteristics were excluded from both the compliance as reported in annual reports and compliance as stated in the survey. Where a company uses explanation for non-compliance, it has a lower overstatement value\(^6\) than the company which gives no explanation and hence any bias is against the predicted direction. The omission of the ‘explained’ items as used in this study means the analysis only focuses on the deliberate concealment of non-compliance with the BCGG-2006. This binary coding method of measuring CG is based on Gompers, Ishii, and Metrick (2003) and is extensively used by subsequent researchers (see, e.g., Ammann, Oesch, & Schmid, 2011; Bebchuk, Cohen, & Ferrell, 2009).

Overstated compliance is defined as the extent to which compliance as reported in annual reports exceeds compliance as stated in the survey. This study measured it by calculating the difference between compliance as reported in annual reports and compliance as stated in the survey, scaling the difference by compliance as reported in annual reports.

Overstated compliance =

\[
\frac{(\text{Compliance as reported in the annual reports} - \text{Compliance as stated in the survey})}{\text{Compliance as reported in the annual reports}}
\]

Subsequently, the 20 items as shown in Table 1 were classified into observable and less observable provisions. The nine observable provisions are those that are easily verifiable or subject to strong monitoring by regulatory authorities such as the BSEC and the stock exchanges. Board meeting is categorized as an observable as companies are under a legal obligation to announce, through the stock exchange website, the time, date and venue of the meeting in advance, and the subsequent decisions taken. The 11 less observable provisions are related to the internal practices of the company and therefore, are relatively less visible to
an outside individual or organization. For instance, the existence of a written charter for the audit committee is classified as less observable as there is no regulatory requirement to submit the written charter of the audit committee to the BSEC, unlike the case in the USA. Based on this classification of provisions, four sub-indices were calculated as:

- compliance with observable provisions as reported in the annual reports;
- compliance with observable provisions as stated in the survey;
- compliance with less observable provisions as reported in the annual reports; and
- compliance with less observable provisions as stated in the survey.

Based on these four sub-indices, this study then calculated overstatement of observable and less observable provisions using formulae similar to that applied to overstated compliance.

Family control is coded as 1, if an individual member or members of the founding family either directly or indirectly owns at least 20 per cent of the equity and occupies the positions of chairman and CEO; otherwise as 0. In the case of Bangladesh, ownership is concentrated and the sponsor family frequently holds the key governance and management positions. Hence, family ownership and family presence in key governance and management positions are combined. This definition of control by family is more aligned with Villalonga and Amit (2006) who argue that the familial nature of firms depends on three aspects: ownership, governance and management. This definition also signifies the power of the sponsor family (Klein, Astrachan, & Smyrnios, 2005:324).

This study follows Pucheta-Martínez and García-Meca (2014) in defining institutional investor representatives on the board. Institutional investor director is coded as 1, if at least one institutional investor representative sits on the board; otherwise the code is 0.

To test H1, the mean of overstated compliance is compared with zero using a one sample t-test and the median with 0 using a Wilcoxon signed-rank test. This study also
compared compliance as reported in annual reports and compliance as stated in the survey using a paired t-test of the means and a Wilcoxon matched-pairs signed-rank test of the medians. H1a is tested by comparing overstated compliance of observable provisions and overstated compliance of less observable provisions, using a paired t-test of the means and a Wilcoxon matched-pairs signed-rank test of the medians.

To test H2 and H3, this study used a Tobit regression, similar to Sakawa, Moriyama and Watanabel (2012) as the distribution of the overstated compliance has no negative values and so is truncated at the lower bound of 0. A Tobit regression is more appropriate than ordinary least square (OLS) to predict a truncated dependent variable as the use of OLS provides inconsistent estimates of the parameters (Wooldridge, 2002:668). In order to use a Tobit regression model, a logarithmic transformation is used to linearize the distribution of the overstated compliance.\(^7\) One is added to the value of overstated compliance before taking the log, as this variable is a ratio.

The regression model is:

\[
\text{Linearized overstated compliance} = f(\text{Family control, Institutional investor director, Controls})
\]

Linearized overstated compliance is replaced by linearized overstated compliance of observable provisions for testing H2a and H3a, and linearized overstated compliance of less observable provisions for testing H2b and H3b. The variables are defined in Table 3.

\[\text{---------------------------}\]
\[\text{Insert Table 3 about here}\]
\[\text{---------------------------}\]

This study selected control variables by assuming that overstatement of CG compliance with the BCGG-2006 is a function of external and internal legitimacy of CG. The
control variables are firm size, audit quality, prior year ROA, need to access external capital markets, market-to-book ratio and export-oriented industry, explained as follows.

First, larger firms have a greater need (Dedman, 2000) and better capacity (Akkermans, Van Ees, Hermes, Hooghiemstra et al., 2007:1109) to maintain a strong CG structure. Larger firms, attracting more attention, are also more likely try to maintain their reputation by providing credible and trustworthy accounting reports (Cao, Myers & Omer, 2012). Consequently, this study included a control for firm size using log of total assets.

Second, prior research has shown that international auditors play an important role in the diffusion of western practices in emerging markets (Mennicken, 2008). On the other hand, firms with higher quality auditors encounter less external pressure for internal CG in emerging countries (Fan & Wong, 2005). The auditing profession in Bangladesh is underdeveloped and the Big 4 audit firms operate through local representatives. Kabir, Sharma, Islam, & Salat (2011) argue that these representatives maintain better audit quality due to monitoring by Big 4 audit firms. Following Kabir et al. (2011), this study uses a categorical variable where 1 represents the representatives of the Big 4 audit firms as a proxy for audit quality.

Third, poor firm performance reduces external legitimacy and therefore, increases external pressure for better CG (Bates & Hennessy, 2010; Sanders & Tüschke, 2007). Firm performance is found to be negatively associated with decoupling with respect to CEO long-term incentive plans (Westphal & Zajak, 1994). In respect of Bangladesh, Haque et al., (2011) find a positive association between profitability and the value of their survey-based CG index. Hence, better-performing firms may be less inclined to overstate compliance with BCGG-2006 in their annual reports. In line with Westphal and Zajak (1994) and Sanders and Tüschke (2007), this study included a control for prior year return on assets (ROA_1).
Fourth, prior research has demonstrated that firms can ensure better valuation of their initial public offerings by legitimizing their governance structure (Bell, Filatotchev, & Aguilera, 2014). Although stock markets in Bangladesh are nascent, firms need the approval of the BSEC to raise finance by issuing equity, preference stock and a significant amount of long-term loans which may trigger overstatement of compliance with the BCGG-2006. Following Aier, Comprix, Gunlock and Lee (2005), this study measures the need to access external capital markets (Finance raised) by the ratio of additional cash raised from issuance of equity, preferred stock and long-term debt to average total assets in the accounting year ended in 2011.

Fifth, as this study questions the reliability of disclosures in annual reports, it may not be sufficient to control only for accounting report-based variables. Therefore, this study also controls for market-to-book ratio defined as the ratio of market value of equity to book value of equity at the end of accounting period.

Sixth, a number of prior studies provide evidence that the accountability of Bangladeshi manufacturers who make products for western retailers is influenced by the retailers (Islam & Deegan, 2010; Khan, Muttakin & Siddiqui, 2013). Following Khan et al. (2013), this study considers any firm in the textile and pharmaceutical industries as an export-oriented industry and uses a dummy variable where 1 indicates firms in the textile and pharmaceutical industries.

RESULTS

Table 4 presents descriptive statistics of the sample firms. The mean of compliance as reported in annual reports is 16.25 and the mean of compliance as stated in the survey is 11.04. The minimum and maximum values of both compliance as reported in annual reports and compliance as stated in the survey are 3 and 20 respectively. With respect to compliance
as reported in annual reports and compliance as stated in the survey, eight and five firms respectively have the maximum score of 20. The values of compliance as reported in annual reports and compliance as stated in the survey of the other companies are within the range 3 - 20. No company has a value of compliance as stated in the survey greater than that of compliance as reported in annual reports. The mean (median) of overstated compliance in annual reports is 32 (31) percent and standard deviation is 25 percent. The maximum value of overstated compliance in annual reports is 82 percent. The mean of overstated compliance of observable provisions is 16 percent while the mean of overstated compliance of less observable provisions is 48 percent.

The sponsor family owns at least 20 percent of shares and members of the sponsor family occupy the positions of both chairman and CEO in the case of 51.64 percent of sample firms. Institutional investors occupy board positions in the case of 23.08 percent of sample firms. Other independent variables show sufficient variations, suggesting that it is meaningful to use these variables as controls in estimation of the association of family control and presence of institutional investor directors on the board with overstated compliance.

**Total Overstatement of Compliance**

The results of a one-sample t-test and a Wilcoxon signed-rank test suggest that the mean and median of overstated compliance in annual reports is significantly greater than 0 at the 1 percent level (Table 5).
(see Table 6). The results, thus, support H1, indicating that, on average, the level of compliance as reported in the annual reports is not a reliable reflection of actual compliance with the BCGG-2006.

Overstated Observable and Less Observable Corporate Governance

Table 7 shows that the mean and median of overstated compliance of less observable provisions are significantly higher than the respective values of overstated compliance of observable provisions at the 1 percent level. This evidence provides support for H1a that overstatement of compliance in annual reports is higher for less observable provisions of the BCGG-2006.

Association with Family Control and Institutional Investor Directors

In Table 8, the mean differences of independent variables for total overstated compliance, overstated compliance of observable provisions, and overstated compliance of less observable provisions without and with overstatement of compliance in annual reports are presented, respectively, in Panels A and B.

Panel A shows that the average of family control is higher for firms that overstate compliance in annual reports, implying that firms controlled by sponsor families tend to overstate compliance. The presence of institutional investor directors is higher for firms with no overstatement of compliance. The difference implies that when institutional investors
occupy positions on the board, they can play a part in reducing overstatement of compliance in annual reports. Firms that do not overstate compliance with the BCGG-2006 in their annual reports are relatively larger in size, were more profitable in last accounting period, and are more proportionately audited by audit firms affiliated with an international Big 4 audit firm. However, there is no significant difference between firms without and those with overstatement of compliance in annual reports with respect to the percentage of finance raised from external markets, market-to-book ratio and firms belonging to export-oriented industries.

Panel B presents the mean differences of independent variables without and with overstated compliance of observable provisions and overstated compliance of less observable provisions in annual reports. The results of mean difference tests are almost identical to those of the total overstatement of compliance, with the exception that firms which overstate observable provisions raise more finance relative to total assets from external markets and have a higher market-to-book ratio. These results seem counter-intuitive. One possibility is that the differences in finance raised and market to book ratio, between firms that do not overstate and those that overstate observable provisions, are driven by differences in other firm-level characteristics. Indeed, in the multivariate estimation, both finance raised and market-to-book ratio do not maintain any significant association with overstated compliance of observable provisions.

**Results for Association with Family Control and Institutional Investor Directors**

In Table 9, the estimated results of the association of family control and presence of institutional investor directors on the board with total overstated compliance, overstated compliance of observable provisions, and overstated compliance of less observable provisions are presented, respectively, in Models 1, 2, and 3.
Model 1 (Table 9) shows that the coefficient of family control is positive and significant ($\beta = 0.135$, $p < .001$), indicating that control by the sponsor family is positively associated with the total overstatement of compliance with the BCGG-2006 in annual reports. This result supports H2. The results in Model 1 (Table 9) also reveal that the coefficient of institutional investor director is negative and significant ($\beta = -0.092$, $p < .05$). This result supports H3. The coefficients of control variables indicate that firms that overstate compliance with the BCGG-2006 in annual reports raise a higher percentage of finance from external markets; are relatively smaller in size; were less profitable in the last accounting period and are less likely to be audited by audit firms affiliated with an international Big 4 audit firm.

Model 2 (Table 9) presents results of the association of control by sponsor family and institutional investor directors with overstatement with respect to observable provisions. The coefficients of family control and institutional investor director are insignificant, indicating that overstatement of compliance of observable provisions are apparently unaffected by control by the sponsor family and the presence of institutional investor directors on the board. This evidence supports H2a and H3a respectively. The coefficients of control variables suggest that larger firms and firms audited by audit firms affiliated with an international Big 4 audit firms tend to overstate compliance less with respect to observable provisions.

Model 3 (Table 9) presents results of the association of control by sponsor family and institutional investor directors with overstatement of compliance with respect to less observable provisions. The coefficient of family control is positive and significant ($\beta = 0.155$, $p < .01$), indicating that control by the sponsor family is positively associated with the overstatement of compliance of less observable provisions in annual reports. This result
supports H2b. The results in Model 3 (Table 9) also reveal that the coefficient of institutional investor directors is negative and significant (β = -0.098, p < .05). This result supports H3b. Regarding the control variables, the results are identical to those of the total overstatement of compliance in annual reports, with the exception that percentage of finance raised from external markets is no longer significant at conventional level.

**Sensitivity Analysis for Association with Family Control and Institutional Investor Directors**

A series of tests is conducted to check the robustness of the results presented in Table 9. (The detailed results of these tests are not reported due to limitations of space but are available from the author upon request.) First, the untransformed values of overstated compliance, overstated compliance of observable provisions and overstated compliance of less observable provisions are regressed on the independent variables of Table 9. The estimated results are qualitatively identical to those in Table 9. Second, control by sponsor family is measured by using four alternative variables: (1) a dichotomous variable where 1 indicates that an individual member or members of the sponsor family either directly or indirectly own at least 15 percent of ownership and occupy the positions of both chairman and CEO; 0 otherwise;11 (2) a dichotomous variable where 1 indicates that an individual member or members of the sponsor family either directly or indirectly own at least 30 percent of ownership and occupy the positions of both chairman and CEO; 0 otherwise; (3) both the chairman of the board and the CEO are members of the sponsor family following Yeh and Woidtke (2005); (4) either the chairman of the board or the CEO is a member of the sponsor family based on Ho and Wong (2001). All coefficients for variants of family control retain the level of significance and signs found in Table 9 with the following exception. The coefficient of family control is significantly positively associated with overstated compliance.
of observable provisions at the 5 percent level when family control is measured as a dummy variable indicating (a) the sponsor family owns at least 15 percent of ownership and sponsor family members hold the positions of both chairman and CEO; 0 otherwise and (b) both the chairman of the board and the CEO are members of the sponsor family; 0 otherwise. Third, the power of the institutional investor directors is measured by the percentage of institutional investor directors on the board as in Pucheta-Martínez and García-Meca (2014). The coefficient of percentage of institutional investor directors retains the level of significance and signs found in Table 9. Finally, in order to test whether institutional investor directors mitigate overstatement in family controlled companies; the linearized value of overstated compliance, overstated compliance of observable provisions and overstated compliance of less observable provisions are regressed on the institutional investor directors and the control variables of Table 9 for a reduced sample consisting of family-controlled firms only. The coefficients of institutional investor directors on linearized overstated compliance (β = -0.099, p < .05) and linearized overstated compliance of less observable provisions (β = -0.118, p < .05) are negative and significant. The coefficient of institutional investor directors on linearized overstated compliance of observable provisions is not statistically significant at the 10 percent level. These results provide further support for H3, H3a and H3b.

To summarize, the results of the sensitivity checks provide support that the results in Table 9 are not apparently affected by linearization of the dependent variables and definitions of family control and institutional investor directors.

**DISCUSSION AND CONCLUDING REMARKS**

This paper has examined the antecedents of overstatement of compliance with the BCGG-2006. It has discussed how the introduction of an Anglo-American-based CG guideline to an organizational field characterised by contending cultural and institutional profile created
competing institutional logics and therefore, legitimacy contention. Following competing institutional logics, this paper has developed three main hypotheses to evaluate the organizational field-level, the organizational level and the individual level antecedents of overstatement of compliance with the BCGG-2006. These main hypotheses are extended by incorporating the role of information asymmetry in selection of organizational strategic responses to an institutional pressure subject to competing logics. This study finds support for all eight proposed hypotheses.

In Bangladesh, the most closely relevant prior study is by Uddin and Choudhury (2008) in which interviews were used to show that a traditionalist culture mediates the rationalist/legalist framework of CG in Bangladesh. Their findings suggest that CG practices recommended by the BCGG-2006 are not practised by companies in Bangladesh. Uddin and Choudhury (2008) make an implicit assumption that either the IFIs and the BSEC turn a completely blind eye to the state of compliance or the companies do not concern themselves with regulative legitimacy. However, some efforts by the IFIs (e.g. World Bank, 2009 finds that an average level of compliance is 82%) and the BSEC (e.g., the CFD ensures that the statement of compliance with CG guidelines is included in the annual report) are exercised to augment compliance and thus, create regulatory pressures. By providing evidence of overstatement, this study shows that companies maintain regulative legitimacy by reporting compliance with the BCGG-2006 in their annual reports, because the IFIs and the BSEC use the CG compliance statement to examine the state of compliance, whilst companies do not actually implement the practices recommended by the BCGG-2006 due to the contradiction with the cognitive-cultural framework. In so doing, this paper also reconciles the two contradictory prior findings as reported by Uddin and Choudhury (2008) and World Bank (2009).
In other developing countries, research on CG codes cautions that “the mere emergence of detailed governance codes in developing countries does not necessarily mean that de facto practices will improve” (Wanyama et al., 2009:159). This indicates a possible gap between compliances as stated in compliance statements and actual governance arrangements. This study, using an appropriate theoretical framework, demonstrates that the stated compliance with a national code as reported in annual reports is significantly higher than the reality of the underlying compliance. This study thus provides systematic empirical evidence to support the caution expressed by prior researchers.

The contribution of this study to the literature of competing institutional logics is a multilevel explanation of decoupling as a form of ‘window-dressing’ of compliance with a regulative institution, the BCGG-2006 that is challenged by the cultural-cognitive profile in the context of a developing country. Most studies of regulative legitimation focus on either diffusion of institutionally contested CG practices (Chizema, 2008; Sanders & Tüschke, 2007; Fiss & Zajak, 2004) or policy-practice decoupling (Fiss & Zajak, 2006; Bezemer, Zajak, Naumovska, Van Den Bosch et al., 2015). This study, however, conceptualizes decoupling as a form ‘window-dressing’ of compliance as pioneered by Westphal & Zajak (1994; 2001) with a regulative institution, the BCGG-2006. The studies of Westphal & Zazaj (1994; 2001) are based on the USA and investigate the managers’ conflicting interests around decoupling. This study, however, investigates and finds supports for the organizational field-level, the organizational level and the individual level antecedents of ‘window-dressing’ of compliance with a regulative institution in a developing country. This study, thus, demonstrates that firms that ‘window-dress’ compliance are to some extent achieving regulative legitimation.

This study identifies the Bangladesh CG arena as an organizational field subject to competing institutional logics. In this field, a regulative institution, such as adoption of the
BCGG-2006 and general capital market-oriented reforms, conflict with cultural-cognitive institutions creating a case for legitimacy contention for firms with respect to compliance with the BCGG-2006. Whilst this identification is not new in CG literature (Bezemer, Zajak, Naumovska, Van Den Bosch, 2015; Chizema, 2008; Sanders & Tüschke, 2007), most of these studies focused upon developed non-Anglo-American countries which do not suffer from ‘formal institutional voids’ which prevail in developing countries. In contrast, this study focused on a developing country where pre-existing CG practices embodied in a cultural-cognitive framework contradict with rule-based CG practices emanating from regulatory change. Under such legitimacy contention, firms maintain regulative legitimacy by reporting compliance in annual reports whilst maintaining cultural-cognitive legitimacy by not implementing the BCGG-2006 in reality. While attempting to maintain both kinds of legitimacy, firms take a calculated approach in respect to selection of provisions of the BCGG-2006, as demonstrated by systematic overstatement of compliance with respect to less observable provisions. Higher levels of information asymmetry associated with less observable provisions may constrain the BSEC and stock exchanges to reveal non-conformity between reported compliance and actual implementation with these provisions.

Within this field, sponsor families are powerful actors due to their control over firms and close association with corrupted political leaders. By demonstrating a positive relationship between overstatement of compliance and family control, this study shows that the interplay between organizational culture and governance structures of family-controlled firms which are cognitively consistent with cultural-cognitive element of the country and the private benefits of control afforded to controlling sponsor families by existing formal institutional voids results in reluctance to change to a rule-based Anglo-American model. However, the positive association between overstatement of compliance in annual reports and family control is mainly driven by overstatement with less observable provisions.
Another important actor with a conflicting interest in sponsor families in this field is the independent institutional investors. This research demonstrates that the presence of a representative of an independent institutional investor on the board is negatively associated with overstatement of compliance with the BCGG-2006. Again the negative association between the presence of independent institutional investor directors on the board and overstatement of compliance is driven by the negative association between the presence of independent institutional investor directors on the board and overstatement of compliance with respect to less observable CG provisions. These results also remain valid when an analysis is carried out for family controlled firms only. These results may suggest that regulatory agencies such as the BSEC should promote more institutional investor representation on board of directors to augment congruence between compliance reported in annual reports and underlying compliance.\textsuperscript{13}

The findings of this study are also relevant to academics and practitioners. Based upon the results, it appears that contradiction between a regulative institution and the prevailing cultural and institutional characteristics of developing countries aid in a decoupling of stated intent and actual practice. This research thus questions prior research, based upon public disclosures, that tends to suggest that IFIs play an important role in developing accountability in developing countries (World Bank, 2009). Insights revealed by this study are also relevant to practitioners, particularly international investors who need to assess the CG constructs of developing markets in order to make informed investment decisions. They must seek validation of reported CG structures of companies from alternative sources before committing investments.

The results of this study should be interpreted with caution outside the scope of developing countries, where the cultural profile is different and institutional voids do not exist and where external shareholder associations, financial analysts and regulatory agencies
are active enough to reveal underlying non-conformity with a CG code. Moreover, the results provide evidence of association of overstatement of compliance with the BCGG-2006 with family control and the presence of institutional investor presentative on the board. It is not possible to provide evidence of causality due to the dependence on survey data. Survey data are intrinsically cross-sectional (Van der Stede et al., 2005). Hence, several econometric tests of causality (e.g., the effect of change in control by sponsor families on change in overstatement of compliance with the BCGG-2006 in annual reports (Woodward, 2003:35-36) cannot be performed.

Finally, although the survey sample represents the distribution of the underlying population with respect to industry, family control, market capitalisation and total assets (Table 1), indicating that there is minimal concern around response bias, the respondents firms may still be those that better implement the BCGG-2006 in reality. In that case, actual overstatement will be greater than the overstatement which this study reports and will not invalidate the main results of this study.

Further research is needed to understand whether firms that overstate compliance with the BCGG-2006 in order to gain and maintain regulative legitimation are also able to gain CG legitimacy from other stakeholders such as shareholders. Following Zajak and Westphal (2004), this future study could investigate whether market participants discount share of firms that ‘window dress’ compliance in annual reports and thus, provide evidence on costs of ‘window dressing’ of compliance. Moreover, following Fiss & Zajak (2004), a closer examination of the history of sponsor family control in Bangladesh is needed, in order to improve the understanding of whether the presence of first or second (and subsequent) generations of sponsor family produces different outcomes with respect to overstatement of compliance with the BCGG-2006. Finally, the finding of this study with respect to the role of the institutional investors does not explicitly demonstrate how the presence of institutional
investors on the board incurs change towards an Anglo-American model of CG. A future study can investigate the process taken by institutional investor directors to ensure compliance with an Anglo-American model of CG and whether that process encourage firms to substantively adopt an Anglo-American model.
END NOTES

1. I am indebted to an anonymous reviewer for suggesting this line of thought.
2. Bangladesh Bank, the central bank of Bangladesh, has long been stipulating that not more than one member of a family can sit in the same board (BRPD Circular No12 April 26, 2003). A recent directive of Bangladesh Bank stipulates that any individual family directly or indirectly willing to hold 5 percent shares or more in any commercial bank needs to take prior permission from the Bangladesh Bank (BRPD Circular No15 November 3, 2014).
3. The website of the mutual fund (http://www.aims-bangladesh.com/index.php), in the section ‘About us’, gives specific indications of adherence to Anglo-American features of governance, such as separation of ownership and management, and adherence to principles of the Chartered Financial Analysts Institute (CFA). In a presentation on corporate governance the CEO of the mutual fund specifically references the UK guidance on independent directors.
4. The main questionnaire is available from the corresponding author.
6. Here is an example of two companies. Company A reported compliance with all 20 provisions and does not use explanation for non-compliance, but in survey it stated that it comply with 18 provisions. Company B reported compliance with 19 provisions and used explanation for non-compliance with one provision but in the survey, it stated that it comply with 18 provisions. The overstatement measure for A is = (20-18)/20 = 0.10 while the overstatement measure for Company B is = (19-18)/19 = 0.0526. As company B used explanation for non-compliance, it has a lower overstatement value than company A which gives no explanation.
8. I am indebted to an anonymous reviewer for suggesting this analysis.
9. I am indebted to an anonymous reviewer for suggesting this analysis.
10. I am indebted to an anonymous reviewer for suggesting this point.
11. I am indebted to an anonymous reviewer for suggesting this point.
12. I am indebted to an anonymous reviewer for suggesting this analysis.
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<table>
<thead>
<tr>
<th>Corporate Governance Provision</th>
<th>Nature of provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board size (min 5, max 20)</td>
<td>Observable</td>
</tr>
<tr>
<td>Independent directors (10% with a minimum of one)</td>
<td>Observable</td>
</tr>
<tr>
<td>Separation of chairman and CEO</td>
<td>Observable</td>
</tr>
<tr>
<td>Define the respective roles and responsibilities of the chairman and CEO</td>
<td>Less observable</td>
</tr>
<tr>
<td>Board meetings (at least four per year)</td>
<td>Observable</td>
</tr>
<tr>
<td>An audit committee is constituted</td>
<td>Observable</td>
</tr>
<tr>
<td>Written charter for audit committee</td>
<td>Less observable</td>
</tr>
<tr>
<td>Audit committee size (at least three directors)</td>
<td>Observable</td>
</tr>
<tr>
<td>Presence of an independent director on audit committee</td>
<td>Observable</td>
</tr>
<tr>
<td>Appointment of the chairman of audit committee</td>
<td>Observable</td>
</tr>
<tr>
<td>Professional qualification of the chairman of audit committee</td>
<td>Less observable</td>
</tr>
<tr>
<td>Audit committee meetings (at least four per year)</td>
<td>Less observable</td>
</tr>
<tr>
<td>Audit committee reports its activities to the board of directors</td>
<td>Less observable</td>
</tr>
<tr>
<td>Audit Committee evaluates the effectiveness of internal control systems</td>
<td>Less observable</td>
</tr>
<tr>
<td>Appointment of CFO</td>
<td>Observable</td>
</tr>
<tr>
<td>The CFO attends board meetings</td>
<td>Less observable</td>
</tr>
<tr>
<td>A written charter specifying roles, responsibilities and duties of the CFO</td>
<td>Less observable</td>
</tr>
<tr>
<td>Appointment of Head of Internal Auditor</td>
<td>Less observable</td>
</tr>
<tr>
<td>A written charter specifying roles, responsibilities and duties of the Head of Internal Auditor</td>
<td>Less observable</td>
</tr>
<tr>
<td>External auditor has not been engaged in non-audit services</td>
<td>Less observable</td>
</tr>
</tbody>
</table>

This table presents CG provisions which are the subject of this study. Observable provisions are easily verifiable or subject to strong monitoring by regulatory authorities such as the BSEC and stock exchanges. Less-observable provisions are related to internal practices of a company and thus are relatively less visible to an outside individual or organization. An audit committee chairman holds a qualification in accounting or finance if he has either a professional qualification in accounting such as FCA, FCMA and PhD in Accounting or has held a senior management position (e.g. Chairman or CEO) with another public limited company or financial institution but has not held that position due to his/her shareholding.
### TABLE 2
Response Bias Tests

<table>
<thead>
<tr>
<th></th>
<th>Population(^b)</th>
<th></th>
<th>Sample(^c)</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>n</td>
<td>Percentage</td>
<td>n</td>
<td>Percentage</td>
</tr>
<tr>
<td><strong>(a) Industry Sector</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cement</td>
<td>6</td>
<td>4.41</td>
<td>4</td>
<td>4.4</td>
</tr>
<tr>
<td>Ceramics</td>
<td>5</td>
<td>3.68</td>
<td>5</td>
<td>5.49</td>
</tr>
<tr>
<td>Engineering</td>
<td>22</td>
<td>16.18</td>
<td>13</td>
<td>14.29</td>
</tr>
<tr>
<td>Food</td>
<td>16</td>
<td>11.76</td>
<td>9</td>
<td>9.89</td>
</tr>
<tr>
<td>Fuel and Power</td>
<td>13</td>
<td>9.56</td>
<td>9</td>
<td>9.89</td>
</tr>
<tr>
<td>IT</td>
<td>5</td>
<td>3.68</td>
<td>3</td>
<td>3.3</td>
</tr>
<tr>
<td>Jute</td>
<td>3</td>
<td>2.21</td>
<td>2</td>
<td>2.2</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>9</td>
<td>6.62</td>
<td>5</td>
<td>5.49</td>
</tr>
<tr>
<td>Paper and Printing</td>
<td>1</td>
<td>0.73</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Pharmaceuticals</td>
<td>20</td>
<td>14.71</td>
<td>16</td>
<td>17.57</td>
</tr>
<tr>
<td>Services and Real Estate</td>
<td>4</td>
<td>2.94</td>
<td>3</td>
<td>3.3</td>
</tr>
<tr>
<td>Tannery</td>
<td>5</td>
<td>3.68</td>
<td>4</td>
<td>4.4</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>1</td>
<td>0.73</td>
<td>1</td>
<td>1.1</td>
</tr>
<tr>
<td>Textile</td>
<td>25</td>
<td>18.38</td>
<td>17</td>
<td>18.68</td>
</tr>
<tr>
<td>Travel and Leisure</td>
<td>1</td>
<td>0.73</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>136</strong></td>
<td><strong>100</strong></td>
<td><strong>91</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>(b) Family Control</strong>(^a)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Family control</td>
<td>76</td>
<td>55.88</td>
<td>47</td>
<td>51.64</td>
</tr>
<tr>
<td>No family control</td>
<td>60</td>
<td>44.12</td>
<td>44</td>
<td>48.36</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>136</strong></td>
<td><strong>100</strong></td>
<td><strong>91</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>(c) Market Capitalization</strong>(^a)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>First quartile</td>
<td>38</td>
<td>27.94</td>
<td>18</td>
<td>19.78</td>
</tr>
<tr>
<td>Second quartile</td>
<td>35</td>
<td>25.74</td>
<td>21</td>
<td>23.08</td>
</tr>
<tr>
<td>Third quartile</td>
<td>33</td>
<td>24.26</td>
<td>27</td>
<td>29.67</td>
</tr>
<tr>
<td>Fourth quartile</td>
<td>30</td>
<td>22.06</td>
<td>25</td>
<td>27.47</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>136</strong></td>
<td><strong>100</strong></td>
<td><strong>91</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>(d) Total Assets</strong>(^a)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>First quartile</td>
<td>38</td>
<td>27.94</td>
<td>17</td>
<td>18.68</td>
</tr>
<tr>
<td>Second quartile</td>
<td>35</td>
<td>25.74</td>
<td>23</td>
<td>25.28</td>
</tr>
<tr>
<td>Third quartile</td>
<td>32</td>
<td>23.53</td>
<td>25</td>
<td>27.47</td>
</tr>
<tr>
<td>Fourth quartile</td>
<td>31</td>
<td>22.79</td>
<td>26</td>
<td>28.57</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>136</strong></td>
<td><strong>100</strong></td>
<td><strong>91</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Notes: \(^a\) Chi-square tests of significant difference between population and sample based on family control ($\chi^2=1.99; p=0.157$) market capitalization group ($\chi^2=2.89; p=0.409$) and total assets group ($\chi^2=2.99; p=0.392$) are not rejected.

\(^b\) Population consists of 136 non-financial companies listed on Dhaka Stock Exchange, Bangladesh on 31 December, 2011.

\(^c\) Sample consists of 91 companies that respond to the survey conducted in January – March, 2012.
<table>
<thead>
<tr>
<th>Variables</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Linearized overstated compliance</td>
<td>Log (1 + Overstated CG).</td>
</tr>
<tr>
<td>Linearized overstated compliance of observable provisions</td>
<td>Log (1 + Overstated observable CG).</td>
</tr>
<tr>
<td>Linearized overstated compliance of less observable provisions</td>
<td>Log (1 + Overstated less observable CG).</td>
</tr>
<tr>
<td>Finance raised</td>
<td>The ratio of additional cash raised from issuance of equity, preferred stock and long-term debt to average total assets at the end of the company’s accounting period in 2011.</td>
</tr>
<tr>
<td>Firm size</td>
<td>The natural logarithm of book value of total assets at the end of the company’s accounting period in 2011.</td>
</tr>
<tr>
<td>ROA_1</td>
<td>Proxy for prior year profitability, is the ratio between net profit before extraordinary items and average total assets at the end of the last accounting period.</td>
</tr>
<tr>
<td>Market-to-book</td>
<td>Proxy for growth opportunity, is the ratio of the firm’s market value of common equity to book value of common equity at the end of the company’s accounting period in 2011.</td>
</tr>
<tr>
<td>Family control</td>
<td>A dummy variable indicating the sponsor family owns at least 20 percent of ownership and sponsor family members hold the positions of both chairman and CEO; 0 otherwise.</td>
</tr>
<tr>
<td>Institutional investor director</td>
<td>A dummy variable indicating the presence of at least one institutional investor director on the board; 0 otherwise.</td>
</tr>
<tr>
<td>Audit quality</td>
<td>A dummy variable equals 1 if the audit firm of the company is affiliated with international big-four audit firms, 0 otherwise.</td>
</tr>
<tr>
<td>Export-oriented industry</td>
<td>Proxy for the firm’s dependence on western buyers, is a dummy variable equals 1 if the firm belongs to textile or pharmaceutical industry and otherwise 0.</td>
</tr>
</tbody>
</table>

This table presents definitions of variables used for testing the association of overstatement of compliance with family control and the presence of institutional investor directors on the board of directors.
**TABLE 4**

Descriptive Statistics

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>Median</th>
<th>Standard Deviation</th>
<th>Min</th>
<th>Max</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Panel B: Continuous variables</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compliance as reported in AR</td>
<td>16.25</td>
<td>17.00</td>
<td>3.47</td>
<td>3.00</td>
<td>20.00</td>
</tr>
<tr>
<td>Compliance as stated in survey</td>
<td>11.04</td>
<td>11.00</td>
<td>4.98</td>
<td>3.00</td>
<td>20.00</td>
</tr>
<tr>
<td>Overstated compliance</td>
<td>0.32</td>
<td>0.31</td>
<td>0.25</td>
<td>0.00</td>
<td>0.82</td>
</tr>
<tr>
<td>Compliance with observable provisions as reported in AR</td>
<td>7.98</td>
<td>9.00</td>
<td>1.73</td>
<td>3.00</td>
<td>9.00</td>
</tr>
<tr>
<td>Compliance with observable provisions as stated in survey</td>
<td>6.66</td>
<td>8.00</td>
<td>2.37</td>
<td>2.00</td>
<td>9.00</td>
</tr>
<tr>
<td>Overstated compliance of observable provisions</td>
<td>0.16</td>
<td>0.00</td>
<td>0.23</td>
<td>0.00</td>
<td>0.67</td>
</tr>
<tr>
<td>Compliance with less observable provisions as reported in AR</td>
<td>8.31</td>
<td>9.00</td>
<td>2.09</td>
<td>0.00</td>
<td>11.00</td>
</tr>
<tr>
<td>Compliance with less observable provisions as stated in survey</td>
<td>4.38</td>
<td>4.00</td>
<td>3.22</td>
<td>0.00</td>
<td>11.00</td>
</tr>
<tr>
<td>Overstated compliance of less observable provisions</td>
<td>0.48</td>
<td>0.50</td>
<td>0.33</td>
<td>0.00</td>
<td>1.00</td>
</tr>
<tr>
<td>Linearized overstated compliance</td>
<td>0.26</td>
<td>0.27</td>
<td>0.19</td>
<td>0.00</td>
<td>0.60</td>
</tr>
<tr>
<td>Linearized overstated compliance of observable provisions</td>
<td>0.13</td>
<td>0.00</td>
<td>0.18</td>
<td>0.00</td>
<td>0.51</td>
</tr>
<tr>
<td>Linearized overstated compliance of less observable provisions</td>
<td>0.37</td>
<td>0.41</td>
<td>0.23</td>
<td>0.00</td>
<td>0.69</td>
</tr>
<tr>
<td>Finance raised</td>
<td>0.08</td>
<td>0.00</td>
<td>0.18</td>
<td>0.00</td>
<td>0.80</td>
</tr>
<tr>
<td>Firm size</td>
<td>21.44</td>
<td>21.45</td>
<td>1.62</td>
<td>17.32</td>
<td>25.41</td>
</tr>
<tr>
<td>ROA_1</td>
<td>10.93</td>
<td>8.89</td>
<td>8.82</td>
<td>-10.29</td>
<td>36.88</td>
</tr>
<tr>
<td>Market-to-book</td>
<td>4.45</td>
<td>3.04</td>
<td>6.25</td>
<td>0.22</td>
<td>55.46</td>
</tr>
<tr>
<td><strong>Panel B: Dichotomous variables</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>0</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Family control</td>
<td>47 (51.64%)</td>
<td>44 (48.36%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Institutional investor director</td>
<td>21 (20.08%)</td>
<td>70 (76.92%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Audit quality</td>
<td>24 (26.37%)</td>
<td>67 (73.63%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Export-oriented industry</td>
<td>33 (36.26%)</td>
<td>58 (63.74%)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Sample size = 91 firms. Compliance as reported in AR and Compliance as stated in survey are CG compliance indices of 20 provisions of the BCGG-2006. Overstated compliance is the difference between Compliance as reported in AR and Compliance as stated in survey scaled by Compliance as reported in AR. Compliance with observable provisions as reported in AR and Compliance with observable provisions as stated in survey are CG compliance indices of nine observable provisions of the BCGG-2006. Overstated compliance of observable provisions is the difference between Compliance with observable provisions as reported in AR and Compliance with observable provisions as stated in survey scaled by Compliance with observable provisions as reported in AR. Compliance with less observable provisions as reported in AR and Compliance with less observable provisions as stated in the survey are CG compliance indices of 11 relatively less observable provisions of the BCGG-2006. Overstated compliance of less observable provisions is the difference between Compliance with less observable provisions as reported in AR and Compliance with less observable provisions as stated in the survey scaled by Compliance less observable provisions as reported in AR. The definitions of the remaining variables are detailed in Table 3.
### TABLE 5
Univariate Tests Comparing Overstated compliance and Hypothesized Values \( \mu = 0 \) and \( \text{Median} = 0 \).

<table>
<thead>
<tr>
<th>Overstated compliance</th>
<th>Hypothesized value</th>
<th>t/z value</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean(^a)</td>
<td>0.319</td>
<td>0.000</td>
<td>12.24</td>
</tr>
<tr>
<td>Median(^b)</td>
<td>0.310</td>
<td>0.000</td>
<td>8.039</td>
</tr>
</tbody>
</table>

Sample is 91 firms. Overstated compliance is the difference between compliance as reported in annual reports and Compliance as stated in the survey scaled by Compliance as reported in annual reports.

\(^a\)Difference in means is tested by using one-sample t-tests.

\(^b\)Difference in medians is tested by using Wilcoxon signed-rank tests.

*** Significant at 0.001 level (one-tail).

### TABLE 6
Univariate Tests Comparing Compliance as reported in annual reports and Compliance as stated in the survey.

<table>
<thead>
<tr>
<th>Compliance as reported in AR</th>
<th>Compliance as stated in survey</th>
<th>t/z value</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean(^a)</td>
<td>16.25</td>
<td>11.04</td>
<td>11.58</td>
</tr>
<tr>
<td>Median(^b)</td>
<td>17.00</td>
<td>11.00</td>
<td>8.043</td>
</tr>
</tbody>
</table>

Sample is 91 firms. Compliance as reported in AR and Compliance as stated in survey are CG compliance indices of 20 provisions of the BCGG-2006.

\(^a\)Difference in means is tested by using pair t-tests.

\(^b\)Difference in medians is tested by using Wilcoxon matched-pair signed-rank tests.

*** Significant at 0.01 level (one-tail).

### TABLE 7
Univariate Tests Comparing Overstated compliance of less observable provisions and Overstated compliance of observable provisions.

<table>
<thead>
<tr>
<th>Overstated compliance of less observable provisions</th>
<th>Overstated compliance of observable provisions</th>
<th>t/z value</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean(^a)</td>
<td>0.479</td>
<td>0.156</td>
<td>10.71</td>
</tr>
<tr>
<td>Median(^b)</td>
<td>0.500</td>
<td>0.000</td>
<td>7.263</td>
</tr>
</tbody>
</table>

Sample is 89 firms. Overstated compliance of less observable provisions is the difference between Compliance with less observable provisions as reported in the annual reports and Compliance with less observable provisions as stated in the survey scaled by Compliance with less observable provisions as reported in the annual reports. Overstated compliance of observable provisions is the difference between Compliance with observable provisions as reported in the annual reports, and Compliance with observable provisions as stated in the survey scaled by Compliance with observable provisions as reported in the annual reports.

\(^a\)Difference in means is tested by using pair t-tests.

\(^b\)Difference in medians is tested by using Wilcoxon matched-pair signed-rank tests.

*** Significant at the 0.001 level (one-tail).
TABLE 8
Test of Differences in Means of Independent and Control Variables

<table>
<thead>
<tr>
<th>Panel A</th>
<th>Overstated compliance</th>
<th>Group</th>
<th>Mean</th>
<th>NO</th>
<th>YES</th>
<th>t-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Family control</td>
<td></td>
<td></td>
<td>0.52</td>
<td>0.25</td>
<td>0.57</td>
<td>(-2.40)***</td>
</tr>
<tr>
<td>Institutional investor director</td>
<td></td>
<td></td>
<td>0.23</td>
<td>0.38</td>
<td>0.20</td>
<td>(1.51)*</td>
</tr>
<tr>
<td>Financed raised</td>
<td></td>
<td></td>
<td>0.08</td>
<td>0.04</td>
<td>0.09</td>
<td>(-1.04)</td>
</tr>
<tr>
<td>Firm size</td>
<td></td>
<td></td>
<td>21.44</td>
<td>22.53</td>
<td>21.21</td>
<td>(3.08)***</td>
</tr>
<tr>
<td>ROA_1</td>
<td></td>
<td></td>
<td>10.93</td>
<td>21.47</td>
<td>8.67</td>
<td>(6.29)***</td>
</tr>
<tr>
<td>Market-to-book</td>
<td></td>
<td></td>
<td>4.45</td>
<td>5.07</td>
<td>4.33</td>
<td>-0.43</td>
</tr>
<tr>
<td>Audit quality</td>
<td></td>
<td></td>
<td>0.26</td>
<td>0.75</td>
<td>0.16</td>
<td>(5.56)***</td>
</tr>
<tr>
<td>Export-oriented industry</td>
<td></td>
<td></td>
<td>0.36</td>
<td>0.43</td>
<td>0.35</td>
<td>-0.68</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Panel B</th>
<th>Overstated compliance of observable provisions</th>
<th>Overstated compliance of less observable provisions</th>
<th>Group</th>
<th>t-value</th>
<th>Group</th>
<th>t-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Family control</td>
<td></td>
<td></td>
<td>NO</td>
<td>0.42</td>
<td>0.67</td>
<td>(-2.36)**</td>
</tr>
<tr>
<td>Institutional investor director</td>
<td></td>
<td></td>
<td>YES</td>
<td>0.27</td>
<td>0.58</td>
<td>(-2.26)**</td>
</tr>
<tr>
<td>Finance raised</td>
<td></td>
<td></td>
<td>NO</td>
<td>0.05</td>
<td>0.12</td>
<td>(-1.67)*</td>
</tr>
<tr>
<td>Firm size</td>
<td></td>
<td></td>
<td>YES</td>
<td>0.40</td>
<td>0.05</td>
<td>(3.90)***</td>
</tr>
<tr>
<td>ROA_1</td>
<td></td>
<td></td>
<td>YES</td>
<td>0.80</td>
<td>0.16</td>
<td>(5.95)***</td>
</tr>
<tr>
<td>Market-to-book</td>
<td></td>
<td></td>
<td>YES</td>
<td>5.17</td>
<td>4.36</td>
<td>(-0.45)</td>
</tr>
<tr>
<td>Audit quality</td>
<td></td>
<td></td>
<td>YES</td>
<td>0.33</td>
<td>0.42</td>
<td>(-0.86)</td>
</tr>
<tr>
<td>Export-oriented industry</td>
<td></td>
<td></td>
<td>YES</td>
<td>0.47</td>
<td>0.35</td>
<td>-0.84</td>
</tr>
</tbody>
</table>

This table presents the mean difference of independent variables for Overstated CG in Panel A and the same for overstated observable CG and overstated less observable CG in Panel B. The definitions of variables are detailed in Table 3. Difference in means is tested by using t-tests. T-values are in parentheses. ***, * Significant at the 0.001 and 0.10 level respectively (one-tail).
<table>
<thead>
<tr>
<th>Dependent variables</th>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Linearized overstated compliance</td>
<td>1.097*** (0.211)</td>
<td>0.968 (0.591)</td>
<td>1.582*** (0.257)</td>
</tr>
<tr>
<td>Linearized overstated compliance of observable</td>
<td>0.135*** (0.033)</td>
<td>0.134 (0.099)</td>
<td>0.155*** (0.039)</td>
</tr>
<tr>
<td>Linearized overstated compliance of less observable</td>
<td>-0.092*** (0.034)</td>
<td>-0.162 (0.112)</td>
<td>-0.098** (0.04)</td>
</tr>
<tr>
<td>Explanatory variables</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Intercept</td>
<td>0.136*** (0.073)</td>
<td>0.249 (0.203)</td>
<td>0.129 (0.085)</td>
</tr>
<tr>
<td>Family control</td>
<td>-0.038*** (0.009)</td>
<td>-0.046* (0.027)</td>
<td>-0.053*** (0.012)</td>
</tr>
<tr>
<td>Institutional investor director</td>
<td>-0.004** (0.002)</td>
<td>-0.002 (0.006)</td>
<td>-0.005** (0.002)</td>
</tr>
<tr>
<td>Finance raised</td>
<td>-0.184*** (0.036)</td>
<td>-0.363*** (0.135)</td>
<td>-0.23*** (0.042)</td>
</tr>
<tr>
<td>Firm size</td>
<td>-0.002 (0.002)</td>
<td>-0.002 (0.006)</td>
<td>-0.004 (0.003)</td>
</tr>
<tr>
<td>ROA_1</td>
<td>-0.030 (0.032)</td>
<td>-0.018 (0.091)</td>
<td>-0.049 (0.036)</td>
</tr>
<tr>
<td>Audit quality</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Market-to-book</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Export-oriented industry</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of observations</td>
<td>91</td>
<td>91</td>
<td>89</td>
</tr>
<tr>
<td>Pseudo R²</td>
<td>4.9939</td>
<td>0.3368</td>
<td>2.1112</td>
</tr>
<tr>
<td>LR chi-square statistics</td>
<td>103.96***</td>
<td>34.00***</td>
<td>111.53***</td>
</tr>
</tbody>
</table>

This table presents the results based on Tobit regression. The definitions of variables are detailed in Table 3. ***, **, * coefficients are statistically significant at 0.01, 0.05, 0.10 level respectively.