Effect of Board Involvement on Corporate Sustainability Reporting: Evidence from Colombo Stock Exchange – Sri Lanka

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Abstract

Corporate sustainability is a wider concept with aspects of economic, society and environment. These aspects need to implement in a balanced manner to achieve the effectiveness of corporate sustainability. Purpose of this study is to investigate the effect of board involvement on corporate sustainability reporting. Board size, board independence, dual leadership, female directors of the board and ownership of the directors were identified as independent variables and level of GRI disclosures was identified as the dependent variable. Firm profitability and total assets were considered as control variables. Date was collected from 37 listed companies in the Colombo Stock Exchange over the period of 5 years from 2016-2020, representing all business sectors. Descriptive analysis and multiple regression analysis were done using the E-Views package. Findings revealed that board independence, female directors and board ownership have significant effect on level of corporate sustainability reporting. But, board size and CEO duality have no significant effect on corporate sustainability reporting.

Key Words: Board Involvement, Colombo Stock Exchange, Global Reporting Initiative, Sustainability Reporting

Introduction

Most of the big organizations in developed as well as developing countries like Sri Lanka are given their contribution to the expansion of the global economy and technology of the country. Such contributions have some negative impact on social, environment and economy, such as waste, pollution, rapid resource depletion and so on (Reverte, 2009). On the other hand, stakeholders are more concentrated on companies' impact on economic, environmental and social. Therefore, most of the organizations are interested to voluntarily publish their economic, environmental and social and governance impact raised their day-to-day business activities in their annual reports as well as websites (Arayssi et al., 2016). By using sustainability reporting companies are able to increase their transparency, enhance brand value, demonstrate the competitiveness of the company, benchmark against other companies, motivate employees and support corporate information and control processes (Hahn & Kuhnen, 2013).

As per the GRI (Global Reporting Initiative), "A sustainability report is a report published by a company or organization about the economic, environmental and social impacts caused by its everyday activities. A sustainability report also presents the organization's value and governance model, and demonstrates the link between its strategy and its commitment to a sustainable global economy." There are many words to describe sustainability and sustainability reporting. Those are corporate social responsibilities (CSR), corporate sustainability, corporate citizenship, corporate responsibility reporting, environmental and social reporting, integrated and sustainable entrepreneurship (Davis & Searcy, 2010). Sustainability reporting is not a mandatory requirement in many countries as well as in Sri Lanka. Even though sustainability reporting is, a voluntary practice the number of companies that issue sustainability reporting is increasing rapidly both in the global context as well as in the Sri Lankan context (Dissanayaka & Qian, 2019).

The board of directors of the company plays a vital role within the company. They are the main internal governing body of an organization and lead the company for success (Korechovska & Prochazkova, 2014). They have the power of the setting organization mission and policy, responsible for the stakeholder's interest and corporate strategic decision including sustainability disclosure (Wijethilake, 2018). As per Mudiyanselage (2018), the board of directors in listed companies in Sri Lanka highly influences the corporate strategic direction compared to listed companies operating in many other countries. Because listed companies in Sri Lanka are governed by one-tier boards. Therefore, attentions on board composition much more important in sustainability reporting and Sri Lankan companies are in the early stage of sustainability practices (Mudiyanselage, 2018). The relationship between the characteristics of the board of directors of the company and corporate sustainability reporting has been one of the most discussed and explored research problems in foreign countries (Barako et al., 2006; Villiers et al., 2011). There are not sufficient numbers of research conducted in Sri Lanka particular in this area. However, corporate sustainability reporting is more importance concept in present context. Therefore, this research focuses board involvement on corporate sustainability reporting in Sri Lanka.

Literature Review

According to Shamil et al. (2014), board size is positively associated with sustainability reporting. Board size will increase communication and coordination problems, leads to poor decision-making, decreased ability of the board to control management and the small board will minimize agency conflict between shareholders and managers. On the other hand, it will decrease communication and coordination and the CEO in the company will control the decision – making process in the company (Said et al., 2009). Furthermore, large board contains different expertise and found positive relationship between board size and voluntary corporate sustainability reporting (Shamil et al., 2014). Although, some other scholars (Amran et al., 2013; Said et al., 2009) verified no significant relationship between board size and sustainability disclosure. Better board monitoring quality and lower agency costs and there is a positive significant relationship between board independence and corporate sustainability reporting (Villiers et al., 2011). In addition, Chau and Gray (2010) found a positive relationship between voluntary disclosure and board independence in the company. Boesso and Kumar (2009) found an insignificant relationship between board independence and corporate sustainability reporting. On the independent directors company assign higher responsibilities, duties, and they always concern about the reputation of the company. Therefore, independent directors try to influence on sustainability disclosure of the company (Amran et al., 2013).

Shamil et al. (2014) found that there is a positive relationship between dual leadership and corporate sustainability reporting. As per Gul and Leung (2004), there is a negative association between CEO Duality and voluntary disclosure, and also Haniffa and Cooke (2002) found that there is no any association between dual leadership and sustainability reporting. If the ownership of the directors is high it gives more power to the directors of the company on decision-making (Subramaniam & Muttakin, 2014). When managers hold the small number of shares in company leads to engage in opportunistic behavior and higher director's ownership will decrease agency problems (Said et al., 2009). On the other hand, the conflict between principal and agent is reduced due to the director's concentration on more disclosure (Subramaniam & Muttakin, 2014). Brammer and Pavelin (2008) found negative relationship between ownership and sustainability reporting. Villiers et al. (2011) found that corporate sustainability reporting statistically significant with ownership of the board. Gender diversity is most important in the board diversity and gender diversity mainly focus on female directors in the board (Shamil et al., 2014). Arayssi et al. (2016) found that women on board positively affect sustainability reporting and firm performance by effective social engagement to promoting a firm's investment. Amran et al. (2013) explained a positive relationship between female directors and corporate sustainability reporting. In addition to that, Shamil et al. (2014) mentioned no relationship between gender diversity and corporate sustainability reporting and three or more women in the board did not relate to social and environment disclosures. On the other hand, Williams (2003) explained that companies with a higher proportion of women as directors on the board they highly engaged with charitable activities and therefore there is a greater sustainability disclosure within the organization.

Conceptualization

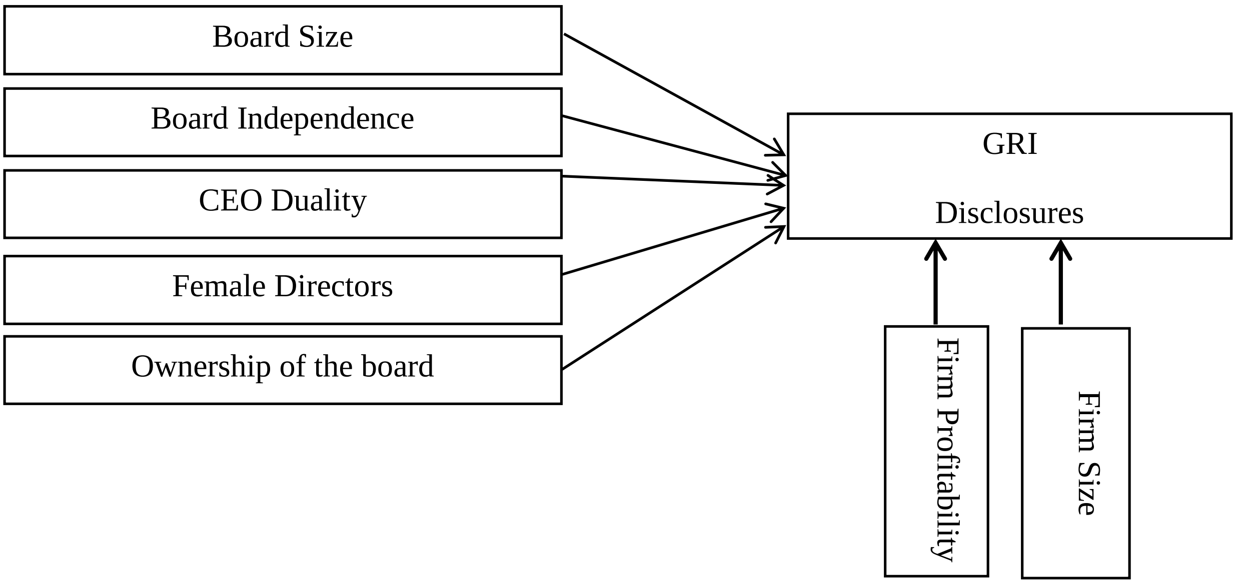

Figure 1. Conceptual Framework
Source: Developed by Researcher (2021)

According to Figure 1, there is one dependent variable (GRI disclosure) and five independence variables (Board size, Board independence, CEO Duality, Female directors and Ownership of the board) and there are two control variables (Firm profitability and Firm size). This conceptual framework shows that GRI disclosure is depend on Board size, Board independence, CEO Duality, Female directors and Ownership of the board. And also shows that Firm profitability and Firm size are used to control the relationship between board involvement and corporate sustainability reporting.

Hypotheses

H1: There is a significant effect of board size on level of corporate sustainability reporting.

H2: There is a significant effect of board independence on level of corporate sustainability reporting.

H3: There is a significant effect of Dual leadership on level of corporate sustainability reporting.

H4: There is a significant effect of Female directors of the board on level of corporate sustainability reporting.

H5: There is a significant effect of Board ownership on level of corporate sustainability reporting.

Operationalization

Table 1. Operationalization of variables

Variables		**Measurement**	**Acronyms**	**Source**
Dependent Variable	Sustainability Reporting (GRI)	*No. of GRI Indexes Disclosed* Total No. of GRI Indexes	GRI	(Shamil et al., 2014)
Independent Variables	Board Size	Number of board of directors	BS	(Mudiyanselage, 2018)
	Board Independence	*Independence Directors* Total number of directors	BI	(Shamil et al., 2014)
	CEO Duality	0 = Chairman and CEO roles are combined 1 = Chairman and CEO roles are separated	CEOD	(Shamil et al., 2014)
	Female Directors	*Number of female directors* Total number of directors	FD	(Feijoo et al., 2012)
	Ownership of the board	*No. of directors shareholding* Total number Of shares	BO	(Said et al., 2009)
Control Variables	Firm profitability (Return On Assets)	*EBIT* Total Assets	FP	(Mudiyanselage, 2018)
	Firm Size (Total Assets)	Natural logarithm of Total Assets	FS	(Dissanayaka et al., 2019)

Source: Developed by Researcher (2021)

Population and Sample

The study is based on companies listed in Colombo Stock Exchange have been consecutively disclosed their sustainability information from the year 2016 to 2020 representing various business industries including manufacturing, Engineering, construction and food & beverages, health care, etc. Sample of 37 listed companies are selected from a population of 220 companies representing 19 business sectors except the bank & finance sector.

Research Model

$$Y = \beta0 + \beta1\ (BS) + \beta2\ (BI) + \beta3\ (CEOD) + \beta4\ (FD) + \beta5\ (BO) + \acute{\varepsilon}$$

Where,

Y=Sustainability Reporting (GRI)
β0 = the intercept of the regression
β1, β2, β3, β4, β5, β6 = Coefficient of Variables
BS = Board size
BI = Board Independence
CEOD = CEO Duality
FD = Female directors
BO = Board ownership
έ = the error term

Data Analysis and Discussion of Results

Descriptive Analysis

Table 2. Results of Descriptive statistics

	GRI	BS	BI	BO	CEOD	FD	FP	FS
Mean	0.499	0.935	0.388	0.142	0.758	0.074	2.094	0.989
Median	0.470	0.954	0.375	0.008	1.000	0.083	0.084	0.989
Maximum	0.845	1.113	0.888	0.960	1.000	0.333	139.4	1.388
Minimum	0.242	0.898	0.000	0.000	0.000	0.000	-0.073	0.824
Std. Dev.	0.143	0.097	0.125	0.217	0.430	0.085	13.185	0.088

Source: E Views output (2021)

As per the output of the descriptive statistics, mean or average level of sustainability disclosure (GRI) of listed companies is 0.499. That explains the average ratio of the companies sustainability reporting is around 0.499 (50%). Standard deviation is 0.143 and it represents that mean value can be deviate by 14.3 percent.

Multiple Regression Analysis

Table 3. Results of Multiple Regression Analysis

Variable	Coefficient	Std. Error	t-Statistic	Prob.
BS	-0.0696	0.0522	-1.3330	0.1842
BI	0.0687	0.0360	1.9084	0.0480
CEOD	-0.0672	0.0557	-1.2075	0.2288
FD	0.1691	0.0848	1.9937	0.0477
BO	-0.0411	0.0168	-2.4471	0.0154
FP	-0.2470	0.0001	0.0427	0.9660
FS	-0.0160	0.0451	0.0008	0.9993
C	0.6053	0.0906	6.6813	0.0000
R-squared	0.1011	F-statistic		2.4757
Adjusted R-squared	0.0602	Prob(F-statistic)		0.0144

Source: E Views output (2021)

According to Table 3, R-Square value is 0.1011 which indicates, 10.11% of variability of the level of GRI Disclosures is explained by the selected variables of the Board of directors (Board Size, Board Independence, CEO Duality, Female Directors and Ownership of the Directors). Furthermore, F-Static is 0.0144 and probability value is 0.0144 at 0.05 level of significant. It represents that model is fit to the data.

According to regression results, there is a positive significant effect of board independence on sustainability reporting. This finding is compatible with findings of Subramaniam and Muttakin (2014), Villiers et al. (2011) and Chau and Gray (2002). Female directors of the company have a significant positive effect with sustainability reporting. Further, the results of this research confirmed by the prior research by mentioning the positive effect between female directors and sustainability reporting (Shamil, 2014; Zhang, 2012; Amran, 2013). And also, the higher amount of women on the board increases the quality of the sustainability report (Feijoo et al., 2012). Some scholars found a negative effect between board ownership and sustainability reporting (Chau, 2002; Brammer, 2008; Said, 2009) and it is further verified the findings of this research. According to the results of this research, there is a significant negative effect between Ownership of the directors and level of sustainability reporting.

Conclusion and Recommendations

The main objective of this research is to identify the effect of board characteristics on sustainability reporting of the listed companies in CSE during the year 2016-2020. According to regression results identified that, board independence and female directors of the companies have a positive effect with sustainability reporting. Other than that, sustainability reporting has significant negative effect with board ownership. Moreover, board size and CEO Duality have insignificant negative effect. Lastly, this research concludes that there is an effect between characteristics of the Board of Directors and Sustainability Reporting of the listed companies in Sri Lanka. As per the findings of this research, there is a positive relationship between the Independent directors and the level of sustainability reporting of the listed companies in Sri Lanka. This means, if the company with a large independence directors, they have a wide range of knowledge and expertise. Therefore, companies should expand their independence directors with expertise in order to the sustainability of the company. According to research findings, the company with the higher number of female directors with indicates the level of the sustainability of the company also high. Because, female directors are highly interested in charity activities and therefore, the impact on social, environmental and economic also high. Therefore, researcher recommends that company should expand their female directors for awareness of the sustainability reporting.

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