Governance, Regulation and Performance of Non-listed Small Corporations in Australia: A Structural Equation Modelling Approach

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DEDICATION

For My Father and Mother

And to

Miaoli Du, Rui Li and Min Li

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ABSTRACT

Small corporations are the backbone of the Australian economy. Various studies have explored corporate governance as it applies to larger organisations. Few studies, however, have examined how corporate governance relates to small corporations. The "one size fits all model" adopted by most of the corporations' law frameworks and the "comply or explain" mentality places a significant amount of unnecessary and disproportionate compliance burden on small businesses. Worse still, non-listed small corporations are losers of the "corporate governance reform competition", given their resource constraints.

There is a dearth of evidence on the relationship between governance, regulation and performance of non-listed small corporations. Only in recent years have researchers in the field started to explore the governance issues facing small corporations in North America and Europe. Existing empirical studies have mainly focused on isolated governance mechanisms, while the interaction between different governance mechanisms has been ignored.

This project intends to address these gaps by applying systematic review, meta-analysis, Path Analysis (PA) and Structural Equation Modelling (SEM). The systematic review identifies relevant theories on the governance and regulation of small corporations. Grounded in these theories, meta-analyses have been applied to synthesize existing empirical evidence in view to developing a conceptual framework. A structured online questionnaire was employed to collect data, yielding 387 responses. Multiple indicators were adopted to measure five latent constructs such as governance, regulation, financial performance, social performance and sustainable performance. PA estimated the direct and indirect effects of governance mechanism on performance. SEM was introduced to confirm the hypothesized relationships, controlling variables such as firm age, size, and development stage.

The results revealed (1) the measurement models for four latent constructs including corporate governance, government regulation, financial performance and CSR; (2) the impact of individual governance mechanisms on performance; (3) governance as a bundle has negative impacts on both financial performance and CSR; (4) regulation has a positive impact on financial performance and CSR. Policy recommendations were developed based on the empirical evidence established from this study.

DECLARATION OF AUTHENTICITY

I, Yongqiang Li, declare that the PhD thesis entitled 'Governance, Regulation and Performance of Non-listed Small Corporations in Australia: A Structural Equation Modelling Approach' is no more than 100,000 words in length, including quotes and exclusive of tables, figures, reference, footnotes, appendices, and reference list.

To the best of my knowledge and belief this thesis contains no material previously published by any other person except where due acknowledgment has been made.

This thesis contains no material which has been accepted for the award of any other degree or diploma in any university.

Except where otherwise indicated, this thesis is my own work.

Yongqiang Li

[redacted]

March 25th, 2014

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Abbreviations

ABS	Australian Bureau of Statistics
ACCI	Australian Chamber of Commerce and Industry
Act	Corporations Act
ADB	Asian Development Bank
AG	Australian Government
ANZSIC	Australian and New Zealand Standard Industrial Classification
ASIC	Australian Securities and Investment Commission
ASX	Australian Securities Exchange
ATO	Australian Taxation Office
ACCC	Australian Competition and Consumer Commission
APRA	Australian Prudential Regulation Authority
BCA	Business Council of Australia
BERR	Department of Business Enterprise & Regulatory Reform
BRCWG	Business Regulation and Competition Working Group
CEO	Chief Executive Officer
CFA	Confirmative Factor Analysis
CFI	Comparative Fit Index
CI	confidence interval
COAG	Council of Australian Governments
COSBOA	Council of Small Businesses of Australia
CPA	Chartered Professional Accountants
CRC	COAG Reform Council
CSR	Corporate Social Responsibility
ecoDa	European Confederation of Directors' Associations, also called
EM	expectation maximization algorithm
EPS	Earnings per Share
FIML	full-information maximum likelihood methods

FTEs	Full time equivalent employees
GFI	Goodness-of-Fit Index
GST	Goods and Services Tax
HOMA	Hedges and Olkin
ICT	information and communication techniques
IISR	Department of Innovation, Industry, Science and Research
IPART	Independent Pricing and Regulatory Tribunal
IT	information technology
IV	Instrumental Variable
MAR	missing at random
MCAR	missing completely at random
MI	multiple imputation
MNAR	missing not at random
MNCs	Multinational corporations
NIA	National Institute of Accountants
OBPR	Office of Best Practice Regulation
OECD	Organisation for Economic Cooperation and Development
OMB	Office of Management and Budget
PC	Productivity Commission
RMSEA	Root Mean Square of Error Approximation
ROA	Return on Assets
ROE	Return on Equity
ROI	Return on Investment
RQ	Research Question
SBR	Standard Business Reporting
SBRC	Small Business Research Centre
SCSR	Strategic Corporate Social Responsibility
SEM	Structural Equation Models
SMEs	Small and medium enterprises

UCLA	University of California at Los Angeles
UK	United Kingdom
US	United States of America
VACC	Victorian Automobile Chamber of Commerce
VCEC	Victorian Competition and Efficiency Commission
VIF	variance inflation factor
VU	Victoria University

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CHAPTER ONE INTRODUCTION

> *The directors of such joint-stock companies, however, being the managers rather of other people's money than of their own, it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honour, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail more or less, in the management of the affairs of such a company* (Smith 1776, p.700).

1.1. Background to the Research

This study empirically examines the relationship between corporate governance, government regulation and business performance of small corporations in Australia. It specifically investigates three central questions. First, how to define and measure corporate governance, government regulation, and small corporations' performance? Second, to what extent is the corporate governance and government regulation of a small corporation related to its business performance? Third, can a small corporation improve its business performance may that better regulatory and governance mechanisms were introduced?

The research gap in corporate governance of small corporations in Australia

The first question involves a search for a robust conceptualization of corporate governance, government regulation, and small corporations' performance. Corporate governance might tentatively be associated with the 'health' of a business entity. However, is organizational health described in terms of flexibility, resilience, agility, or potential for success? Evidently a definition of corporate governance catering for the needs of small corporations requires considerable thought and reflection.

Extant literature is voluminous on the corporate governance issue and has been overly devoted to the large and publicly listed companies, while relatively few studies have been undertaken to explore the governance issues facing small corporations. An excellent review on corporate governance of small and medium sized enterprises has been provided by Audretsch and Lehmann (2011). However, as they admitted it, corporate governance in small corporations suffers from a shadowy existence and only marginal number of publications on this topic has been accepted to management and entrepreneurship journals, such as Journal of Business Venturing, Academy of Management Journal and Entrepreneurship Theory & Practice. There is an unmet need for the theoretical gap of corporate governance research into small corporations to be filled. In this regard, Australia is no exception.

The corporate governance issue not only warrants theoretical investigations, but also merits political endeavours. The Corporations Act 2001 Section 45A — master document guiding the regulation of corporate governance in small corporations, offers a definition for small corporations. However, the small corporation's definition from Corporations' Act 2001 (Cth) has never been used for regulatory purpose, neither had any data being collected based on this definition. Admittedly, small corporations are the backbone of the Australian economy.

Small corporations are regarded as the "engine room of the Australian economy" (Clarke 2007). Demographically speaking, of all the 2.7 million businesses operating in Australia, small businesses account for more than 95% of all businesses and employ more than 47% of the labour force in Australia. More than 40% of the small businesses employ one or more full-time equivalent Australian labour. More than 99% of the new businesses start-ups are small businesses and more than 98% of the business exits are made up by small businesses (ABS 2010). Given that the proportion of small corporations is substantial in Australia, proper design of corporate governance and its related regulatory issues will add great value to the improvement in allocation efficiencies, productivity and innovation of the small corporation cohort, which will further increase their economic contribution to the Australian economy as a whole (PC 2010).

The Stakeholder Theory is more relevant to the small corporations. As Du Plessis, Bagaric et al. (2010) suggested the ultimate goal for corporate governance should be toward the optimisation of efficiency and productivity, hence corproate governance can be defined as:

> *The system of regulating and overseeing corporate conduct and of balancing the interests of all internal stakeholders and other parties (external stakeholders, governments and local communities …) who can be affected by the corporation's conduct, in order to ensure responsible behaviour by corporations and to achieve the maximum level of efficiency and profitability for a corporation (Du Plessis, Bagaric et al. 2010, p. 10).*

The research gap in government regulation toward small corporations in Australia

Regulation is an important part of business life; and, if properly design, it maintains the market efficiency and offers a fair market place for all the small corporations. However, the "one size fits all" model imbedded in the Corporations' Act 2001 incurred extensive regulatory compliance burdens on small corporations, which borne disproportionately high regulatory costs due to their resource constraints and their difficulties in understanding and fulfilling the compliance requirements compare to the situation of their larger counterparts.

The regulations is an extra burden to the small corporations in particular, in that the regulatory system had been acknowledged as too complex, too many regulators and too difficult to capture the frequent changes in regulatory requirements (Armstrong et al. 2011). As mentioned earlier, the legal definition for small corporations was designed by the Corporations Act 2001 but had not been used in any practical forms by any agencies. To cater to the convenience of their regulatory needs, however, different government agents developed their own definitions for small businesses (Li 2010). 21,000 new legislations have been promulgated while the Labour party was in power. Though the Australian Federal Department of Treasury requires a regulatory impact assessment to be prepared once a new legislation is introduced, it had hardly been applied by the ministers in the recent decade (Abbott 2012).

The regulatory compliance requirements hold back the small corporations from performing to their optimal productivity, efficiency and innovation (Productivity Commission 2013). Small businesses are the backbone of the Australian economy. According to the ABS (2010), small and medium-sized enterprises (SMEs) contributes to 57.1% of the industry value added[1] to the national economy, they paid more than one third of the salary and service income, more than 40% of the operating profit before tax and generating 34% of the industry value-added to the national economy.

Worse still, small corporations have been a forgotten market player in the public policy decision making processes in Australia. Small corporations are under-represented in the political sphere. In the legal sense, the majority of the small corporations are companies as well as natural persons. One may wonder, what should be the proper treatment to small corporations when it comes to voting. Though small corporations behave more like individuals, they are legally bound by regulatory requirements promulgated in the Corporations Act 2001.

Yet the regulators have to reach a consensus on a consistent definition of a small corporation in Australia. The small corporations are marginally represented in the political system and only had a shadow existence in the parliament. The peak body of the industry associations — Council of Small Businesses of Australia (COSBOA) does not have any direct budgetary

[1] According to the ABS Cat. No. 8155.0, industry value added is derived as sales and service income plus funding from federal, state, and/or local government for operational costs, plus capital work done for own use, plus closing inventories, less opening inventories, less purchases of goods and materials, less other intermediate input expenses.

funding from the government, constraining it from performing its roles as an industry nexus and information hub of regulatory information updates.

Government regulation has been treated as exogenous to the economic system, or as a constant to be entered in economic calculations in classic economics theories. However, the capabilities of small corporations to comply with government regulation vary, incurring a heterogeneity issue. Moreover, there is a gap in the literature on empirically testing the impact of specific regulations on small corporations in Australian. Hence, this warrants study.

Government regulation can be defined as (1) a principle, rule or law designed to control or govern conduct of people and business; (2) the way a particular regulation is implemented in practice. This definition incorporates not only legislation and formal regulation, but also quasi-regulation, for example, a code of conduct or advisory instruments (Banks 2006).

Firm performance incorporates both financial performance measured in accounting terms (such as total assets, total sales, net profit, sales growth, net profit growth), and social performance measured by the extent to which firms consider the interests of relevant stakeholders such as suppliers, customers, employees, investors, community and environment (Stam et al. 2014).

Research gap in the impact of corporate governance and government regulation on performance

The second central issue analysed is whether the corporate governance or government regulation is related to the business performance of small corporations, defined here to include financial and social performance. An initial response from practitioners and academics might be that ‘well-governed’ small corporations are likely to achieve superior business performance. Conversely, a small corporation with a relatively low level of corporate governance might not be expected to survive and prosper. Owners and managers aim for their firms to be as ready and as prepared as possible for government regulatory compliance requirements, as well as any perceived threats or opportunities that may arise. A key question in this issue is to what extent is the governance structure of a small corporation associated with its superior business performance? And, to what extent, do government regulatory requirements facilitate or hinder small corporations from optimal performance?

In summary, corporate governance, government regulation and business performance of small corporations need to be examined in their own right. Thus, by providing specific evidence for small corporations, this study aims to address the aforementioned gaps in the literature by investigating the relationship between corporate governance, government regulation and business performance in an integrated framework.

1.2. Research Question (RQ)

RQ: What relationship, if any, is there between corporate governance, government regulation and performance of small corporations in Australia?

The purpose of the study was to examine the relationship between corporate governance, government regulation and performance of small corporations in Australia. The problem can be further examined through the following sub questions:

RQ 1a: What is the relationship, if any, between the corporate governance and financial performance of small corporations in Australia?

RQ1b: What is the relationship, if any, between corporate governance and Corporate Social Responsibility (CSR) of small corporations in Australia?

RQ2a: What is the relationship, if any, between government regulation and financial performance of small corporations in Australia?

RQ2b: What is the relationship, if any, between government regulation and CSR of small corporations in Australia?

RQ3: What is the relationship, if there is any, between government regulation and corporate governance of small corporations?

RQ4: How to develop a responsive regulatory system for small corporations in Australia?

Within this research framework, four objectives were identified:

i. Operationalize corporate governance, government regulation, financial performance and CSR in the small corporations context;

ii. Investigate the dimensionality and measurement of corporate governance, government regulation, financial performance and CSR in the small corporations;

iii. Analyse the extent to which corporate governance and government regulation is related to financial performance and CSR of small corporations; and

iv. Identify the unmet needs of small corporations in terms of corporate governance and government regulation and develop a regulatory reform system to address such needs.

1.3. Overview of Research Findings

This study has found that one dimension of corporate governance has a negative impact on financial performance and CSR of small corporations respectively. In addition, the study has found that government regulation has a positive impact on financial performance and CSR of small corporations. Further, government regulation has a negative impact on the corporate governance of small corporations. Based on the empirical evidence, a responsive regulatory system was established for small corporations in Australia (Fig. 9.2).

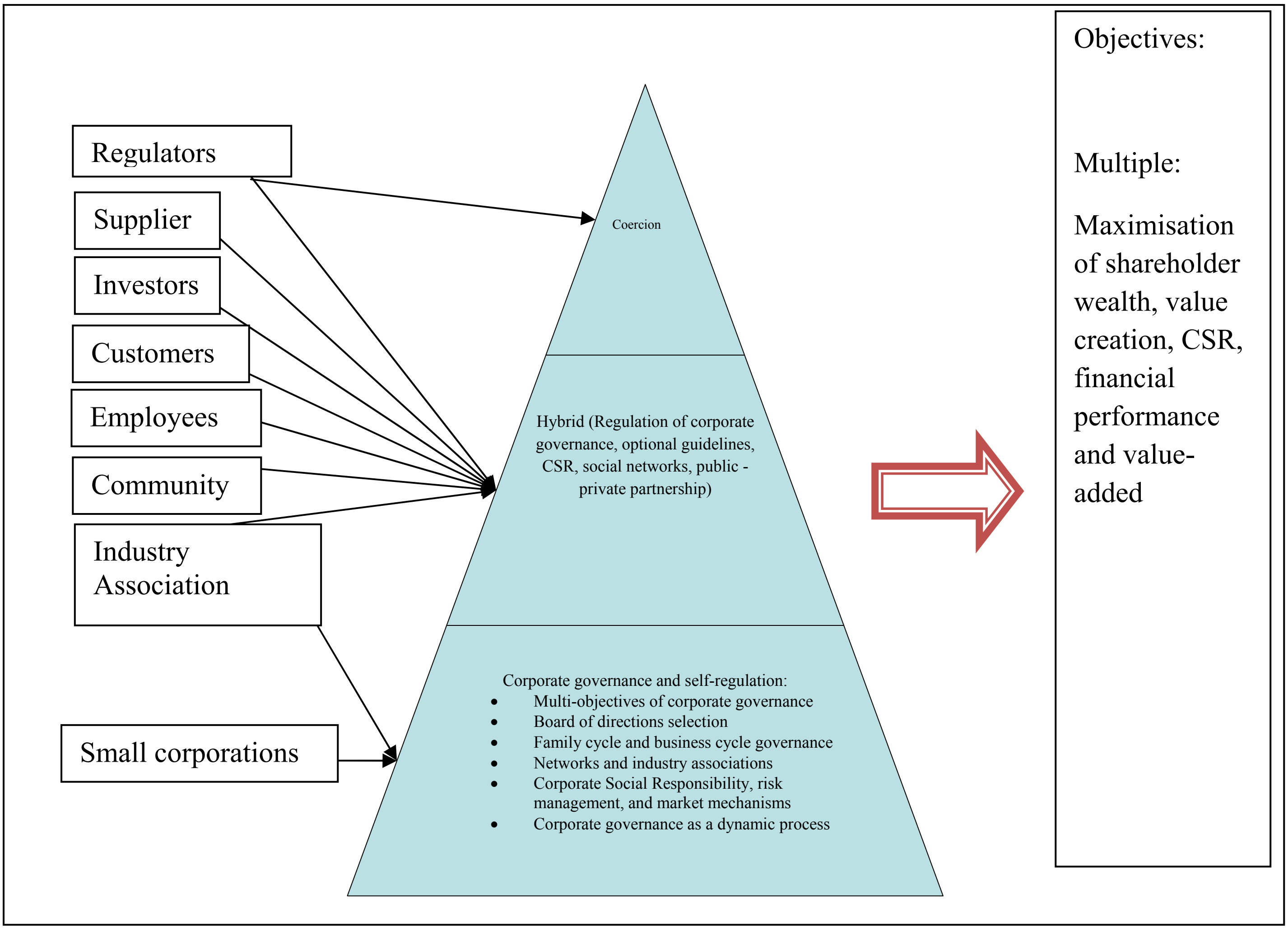


Fig 9.2 A responsive regulatory systems for small corporations in Australia

1.4. Recommendations

Recommendations on corporate governance of non-listed small corporations

Given the distinct features of both small corporations and the institutional context in Australia, corporate governance mechanisms tailored to the needs of the small corporations in Australia are proposed below. Such mechanisms include the role and selection of board of directions, family cycle and business cycle governance, networks and industry associations, corporate social responsibility, risk management and market mechanisms, and corporate governance as a dynamic process.

i. Corporate governance in small corporations serve multiple purposes

Corporate governance in small corporations serves multiple purposes. Such purposes include, but are not limited to, minority shareholder protection, value creation and value added, improvement in financial performance and CSR (Ingley and Karoui 2013; OECD 2012). Small corporations may have to develop a holistic view that incorporates financial performance, social performance, innovation and growth in the performance measurement system.

ii. Board of directors' role and structure

Boards of directors in small corporations serve in controlling and service roles. They fill in the gaps in resources and expertise and they expand business opportunities by making use of their personal and professional networks. Ideally, the board of directors should possess expertise and specialisation in areas of critical importance to the core business of the small corporation (Ingley and Karoui 2013).

Given the nature of blockholding and family ownership, small corporations may focus more on the diversity of the expertise and required industry experience of directions, while giving lesser weight to the independence of the board (Adams and Ferreira 2009).

iii. Family cycle governance and business cycle governance

The majority of small corporations are family owned (Armstrong, Li and Clarke et al. 2012). The corporate governance issue, therefore, is complicated with consideration to family life cycles and business life cycles. The literature has explored many aspects of corporate governance. Filatotchev and Wright (2005) has discussed the life cycle of corporate governance, while Bertoni et al. (2013) on corporate governance in high-tech firms, Uhlaner et al. (2012) on the effects of corporate governance on family businesses, Moore et al. (2012) on IPOs, Wu (2013) on multinational firms and international firms, Yiu et al. (2007) on business groups, and Ayotte et al. (2013) on financial distress and bankruptcy. Given the complexity of family cycles and business cycles, which may require benchmarking across the whole industry or sector, small corporations may have to resort to specialists for help in such matters.

Family governance concerns a number of issues, including succession planning, sustainability and social responsibility, and major events such as marriage and divorce of key family members.

iv. Network and industry associations

Recent developments in Network Theory have pinpointed the importance of networks in business development (Street and Cameron 2007; Perry 2013). Network and industry associations serve as a nexus for information exchange and sharing good practice for many small corporations.

v. CSR, risk management and market mechanisms

External corporate governance mechanisms have to be considered as an integrated part of the corporate governance framework. These mechanisms include corporate social responsibility, risk management and market mechanisms. CSR refers to the involvement and consideration of key stakeholders in major business decision-making. Such stakeholders include employees, customers, suppliers, investors, the environment, and philanthropy. Risk management may involve sound risk control systems, such as internal auditing, reporting and external auditing. Market mechanisms may include the competition in the labour market for qualified employees, directors and executives, the product market and the financial market.

vi. The corporate governance as a dynamic process

Contingency Theory argues that strategic management, in the form of corporate governance, is a dynamic process and should be contingent on the contextual factors such as industry environment and development stage. The majority of the businesses in the sample are at the established stage, where their governance needs would be more on the consolidation of the market position and product development; while those at the start up stage, may have to control and minimise risk. Thus, the owner and managers of small corporations should keep in mind that the corporate governance is a continuous process and demands updates given changes in the development stages.

1.4.2. Recommendations on government regulation

Government regulatory reform should include small corporations. Further recommendations include that they should be well-presented in the polity, de-regulating the 'red-tape', re-regulating the monopolies and factor industries, government taking a stakeholder approach to engage small corporations in regulatory reform, government should educate the small corporations and associated professionals who offer services to them.

i. Small corporations are under-presented in the polity

Most small corporations complained that their voices were never heard and their interests were also ignored by policy decision makers. They advocated that there should be one small business minister sitting in cabinet and speaking on behalf of small corporations. The small corporations are yet to catch the attention of the governments at various levels in Australia.

Small corporations responding to the survey also called for de-regulation to cut red-tape on superannuation management, Australian Securities and Investments Commission (ASIC) regulatory reporting requirements, environmental requirements, quality control, occupational health and safety, documenting Goods and Services Tax (GST), and other regulatory compliance requirements. In addition, small corporations requested that regulators review the maternity leave associated costs and taxation (Armstrong, Li and Clarke et al. 2012).

ii. Re-regulation

Small corporations indicated that they carried extra burdens due to the unfair market structure and market practice. Specifically, they pointed out that the monopolistic structures have to be broken so that small business can have a ‘fair go’. An example is the Supermarket industry. Supermarket giants such as Woolworth and Coles use their oligopolistic position to receive favourable prices by ‘block ordering’. In this regards, small corporations are unfairly disadvantaged (Armstrong, Li and Clarke et al. 2011).

In addition, small corporations request re-regulation of the factor market, in particular the utility sector. For example, a supermarket has to abide by the Occupational Health and Safety regulations to keep the fridge on for twenty four hours per day, seven days per week, which takes up a significant amount of their expenses.

Moreover, re-regulation should be applied to the professional service industries. Though there are price guides used by some professional services firms, such as lawyers and accountants, the price ranges are often so loosely set and poorly defined that they provide opportunities for professionals to over-charge small corporations due to information asymmetry.

iii. A stakeholder approach should be adopted in regulatory reforms

Stakeholders involved in the regulatory reforms include the governments/regulators, small corporations, industry associations, professional bodies, academics and the community. The regulatory impact analysis is a very useful tool; stakeholder views should be consulted at any stage of the regulatory reform development. In this regard, academics may play a crucial role by serving as an independent source to generate an evidence database for policy development.

In order to improve the governance and performance of small corporations, governments and regulators should reinforce the private-public partnership model in the forms of liaison, partnering, funding and delegating power to the private sector, such as industry associations,.

iv. Governments and regulators should engage with small corporations and educate them on corporate governance and government regulation compliance

Small corporations responding to the VU Small Corporations Regulation Survey 2012 (Armstrong, Li and Clarke et al. 2012) generally reported that the regulators and government agencies do not fail to communicate effectively with small corporations, nor had they provided sufficient and useful information for corporate governance and regulatory compliance. They complained that there is too much regulation and the changes in regulations are too frequent. In order to facilitate the compliance of regulatory compliance requirements and effective corporate governance requirements, the regulators should:

- Develop user-friendly tools, web service, smart phone and the other multi-media to communicate the regulatory requirements. They should also continuously evaluate the effectiveness of such tools and make sure that the tax-payers' money are well spent.

- Offer training to professionals who deal with regulatory or corporate governance related matters. Through training, accountants, lawyers and other relevant professionals can improve their efficiency and consequently reduce the cost of small corporations.

1.5. Justification for the Research

To the best of the author's knowledge, it is the first endeavour of any kind in small business research to systematically investigate corporate governance, government regulation, and the performance of small corporations and their intra-relationships.

This study merits theoretical and practical contributions, discussed as follows.

1.5.1 Theoretical implications

This study seeks to contribute incrementally to knowledge based on the following three parameters:

1) Empirical research for corporate governance, government regulation and the interactions between them has yet to be established (Crook et al. 2008; Foss and Klein 2012; Hodgson 2009; Williamson 2010). In addition, most of the existing work has been focused on analysing one of the three major constructs proposed by Williamson (2010), and studies using quantitative, systematic approaches are particularly lacking in the literature (Crook et al. 2008).

2) A systematic empirical examination of the impact of governance on the performance of small corporations addresses the criticism that such research in Australia is long overdue (Farrar 2008). Existing research on firm performance has focused on accounting and finance aspects. This study analyses performance factors such as strategic development (non-cost related growth) and corporate social responsibility.

3) Internationally, the state of research into the regulation of small corporations is underdeveloped. To date, there has there been no research that has as its central aim a review of regulation relevant to the 'whole sector' and focused on the "small corporation" definition (Clarke 2007). This research project, therefore, is also significant to the international context.

4) This is an original study in that it treats corporate governance as a "bundle" and has applied latent variable modelling techniques to demystify the relationships amongst latent variables.

1.5.2 Policy implications

This study is significant for policy decision-making in four aspects:

1) Small corporations play an important role in employing labour and boosting economic growth. A well-designed regulatory framework will help enhance the impact of small corporations on the Australia economy;

2) The in-depth evidence of small corporation performance and industry regulation can assist key policy decision makers to allocate scarce public resources to the most needed regulatory requirements of the sector. This study recognises that there are relevant pieces of literature on small business including: PC (2004, 2005, 2006, 2007a-b, 2008a-e, 2009a-b), ACCI (2005), AG (1997, 2006, 2007,2008, 2009a-b), ATO (2008), Blair (1998), Board of Taxation (2008), Bowen (2008), BRCWG (2009), BCA (2005), COAG (2006, 2007a-b, 2008a-b, 2009a-b), CRC (2008, 2009a-b), IPART (2006), Lattimore et al. (1998), Mason (2007), NSW Government (2007), OECD (1997, 2005, 2007), OBPR (2007, 2008), Regulation Taskforce (2006), SBR (2009), Swan and Tanner (2008), VCEC (2007), Victorian Government (2008) and World Bank (2009). However, to the best of the author's knowledge, this study is the first of its kind to devote all its focus into the research of issues of relevance to small corporations including governance, regulation and performance.

3) The regulatory framework to be developed from this project may shed light on regulatory reform of small corporations in future;

4) Equally, the results on corporate governance practices in non-listed small corporations will help shed light on the development of guidelines for future small business research.

1.6. Scope of the Study

The focus of this study is to operationalise the measurement, analyse the dimensionality and relationship of corporate governance, government regulation, financial performance and social performance of non-listed small corporations in Australia. The study did not investigate family business in particular, nor did it discuss any non-private entities.

1.7. Organisation of the study

This thesis is organised into ten chapters, which are briefly described below.

Chapter 2 reviews the literature on corporate governance theories and the empirical literature on the impact of corporate governance and performance of non-listed small corporations. Theories relevant to the corporate governance of small corporations include Agency Theory, Stewardship Theory, Stakeholder Theory, Resource Dependence Theory, Institutional Theory and Network Governance Theory. There is no consensus on the impact of corporate governance on the financial performance and CSR of small corporations. Thus, meta-analyses were employed to develop the statistical hypotheses.

Chapter 3 reviews the theories of regulation and empirical studies that focuses on the relationship between regulation and small firm performance. Three major theories relevant to small corporations include Force of Ideas Theory, Interest Theory and Institutional Theory. Six types of regulatory strategies were reviewed including Coercion, Market-based approaches, Government compensation, Self-regulation, Responsive regulation and Network-based regulation. Empirical studies investigating the impact of regulation on small corporations’ performance are critically analysed. Due to the difficulties of coping with the broad scope of regulation and a lack of data on small corporations, the literature on the relationship between regulation and performance is yet to be established. Hence, meta-analyses were used in Chapter 5 to develop the hypotheses.

Chapter 4 provides the context of the study. Firstly, the status quo of small corporations in Australia and their contributions to the Australian economy is discussed, followed by an analysis of government regulation, corporate governance and difficulties facing small corporations in Australia.

Chapter 5 summarises the research literature on corporate governance mechanisms and performance using a meta-analysis approach. Research hypotheses on the relationship between corporate governance mechanisms and performance were developed. Due to a dearth of empirical studies between government regulation and the performance of small corporations, the research hypothesis on the relationship between government regulation and performance was based on a systematic review. Based on the causal propositions derived in Chapter 2 and Chapter 3 from the relevant theories and hypotheses developed from meta-analysis and systematic review, Chapter 5 establishes the conceptual framework.

Chapter 6 reports the research design and methodology. This chapter informs the whole research project, including research questions, the literature review, conceptual framework, data collection, data analysis and discussion of the results. An online survey tool called Surveymonkey was used for the data collection. The Structural Equation Modelling (SEM) was used as a major analytical approach for the examination of the relationships of interest.

Chapter 7 reports the results of the relationship between corporate governance and performance of small corporations based on the survey. SEM was used and found a negative impact of corporate governance as a bundle of mechanisms on the performance of small corporations in Australia.

Chapter 8 reports the results of the relationship between government regulation and performance of small corporations based on the survey. SEM analysis found a positive impact between government regulation and performance of small corporations in Australia.

Chapter 9 discusses the research findings from Chapter 7 and 8, in relation to theories and findings from previous empirical studies reviewed in Chapter 2 and Chapter 3.

The Chapter is structured around the sub-research questions of the research question 'What relationship, if any, is there between corporate governance, government regulation and performance of small corporations in Australia?'. As such,

- Section 2 to 4 addresses RQ 1a 'What is the relationship, if any, between corporate governance and performance of small corporations in Australia';
- Section 5 analysed RQ 1b 'How to develop a corporate governance framework for the small corporations in Australia in order to improve performance';
- Section 6 and 7 discussed RQ2a and RQ2b 'What is the relationship, if any, between government regulation and performance of small corporations in Australia';
- Section 8 discussed RQ3 'What relationship, if any, is there between corporate governance and government regulation?'; and,
- Section 9 discussed RQ4 'How to develop a responsive regulatory system for small corporations in Australia?'.

CHAPTER TWO LITERATURE REVIEW OF CORPORATE GOVERNANCE THEORIES AND PERFORMANCE OF NON-LISTED SMALL CORPORATIONS

2.1. Introduction

This chapter reviews the literature on corporate governance theories and performance of small firms. Section two first defines corporate governance; then assesses the relevance of corporate governance to non-listed small corporations, and discusses governance mechanisms followed by the good practice of corporate governance principles and guidelines pertinent to non-listed small corporations.

Section three examines theories relevant to the corporate governance of small firms, namely Agency Theory, Stewardship Theory, Stakeholder Theory, Resource Dependence Theory, Institutional Theory and Network Governance Theory.

Following a brief review of theories in section three, section four employs a meta-analysis approach to evaluate the empirical studies on the impact of corporate governance on performance of small corporations in Australia.

The last section identifies potential research gaps in empirical studies and summarises the theories introduced in this chapter.

2.2. Corporate governance of small firms

In this section, corporate governance is firstly defined; then its relevance to small firms is discussed. Two types of governance mechanisms, internal governance and external governance are introduced. Standards and guidelines for best practices of small firms are compared below in selected jurisdictions: Hong Kong, European Union (European Confederation of Directors' Associations, also called ecoDa), Belgium, Switzerland and the Netherlands. These jurisdictions were selected because best practices were developed by regulatory authorities and can be applied to all the small corporations alike in their respective jurisdictions (for an updated list of codes and guidelines of corporate governance, one may refer to the European Corporate Governance Institute 2013). The United States of America (US) was excluded in that, to the author's best knowledge of the author, the US has yet to codify corporate governance guidelines to cater to the need of small corporations.

2.2.1. Definition of corporate governance

Ever since the existence of corporations as a legal form, corporate governance has been an issue (Du Plessis et al. 2010). Only in recent decades has corporate governance attracted enormous attention from academics and practitioners. The worldwide adoption of corporate governance practice was mainly fuelled by an increasing number of scandals in large corporations and the global financial crisis (McCahery and Vermeulen 2010).

Academics and policy makers have yet to reach a consensus on a set definition for corporate governance. There have been many attempts to provide a working definition; however, definitions vary. Among these early efforts, including the United Kingdom Cadbury Report (1992, p.14) and the South African King Report (1994), corporate governance was defined as "the system by which companies are directed and controlled" (Cadbury 1992). That does not seem to be of particular help to clarifying the meaning of corporate governance (Du Plessis et al. 2010).

Sir Adrian Cadbury has called for a balance between the economic and social goals (Cadbury 2000, p. 9) in the updated definition of corporate governance as follows:

> *In its broadest sense, corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as*

nearly as possible the interests of individuals, of corporations, and of society. The incentive to corporations and to those who own and manage them to adopt internationally accepted governance standards is that these standards will assist them to achieve their aims and to attract investment. The incentive for their adoption by states is that these standards will strengthen their economies and encourage business probity (Cadbury 2000, p. v).

In Australia, the Australian Securities Exchange (ASX 2010, p.5) in its Principles of Good Corporate Governance and Best Practice Recommendations, defines corporate governance as:

the framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations. It encompasses the mechanisms by which companies, and those in control, are held to account. Corporate governance influences how the objectives of the company are set and achieved, how risk is monitored and assessed, and how performance is optimised.

The ASX adds more precision to the definition of corporate governance. However, stakeholders are not included in this definition. Such gaps have been addressed by the definitions proposed by Organisation for Economic Co-operation and Development (OECD 2004) and du Plesis et al (2010).

The OECD (2004) provides a broader definition, as follows

Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined (OECD 2004, p. 13).

The OECD definition acknowledges the existence and importance of the other stakeholders, though the focus is still on the relationship between managers and the disconnected shareholders. Incorporating recent advancement in theory and practice, du Plesis et al (2010, p. 10) defines corporate governance as:

> *The system of regulating and overseeing corporate conduct and of balancing the interests of all internal stakeholders and other parties (external stakeholders, governments and local communities …) who can be affected by the corporation's conduct, in order to ensure responsible behaviour by corporations and to achieve the maximum level of efficiency and profitability for a corporation (Du Plessis et al. 2010, p. 10).*

The de Plesis et al. (2010) definition above has the following four critical components:

i. Corporate governance is a system which regulates and oversees corporate conduct;

ii. All the related stakeholders' interests, be them internal or external, are considered;

iii. The main objective is to hold corporations responsible for their conduct;

iv. The ultimate goal is to achieve the optimal level of efficiency and profitability for the corporation.

2.2.2. Principles of corporate governance

The South African King II Report (King 2002) proposed seven principles for corporate governance of African companies, summarised as follows:

i. Discipline – To adopt internal audit as a disciplined approach for quality check in order to evaluate risk management, control and governance.

ii. Transparency – Transparency and full disclosure of committee matters.

iii. Independence – Sufficient amount of non-executive directors to be independent directors; the appointment of an independent deputy chairman who leads the evaluation of the performance of the chairman; independent directors should be part of the remuneration committee; the board of directors should have access to independent professional advice; majority of the audit committee should consist of independent directors; and any internal audit should be independent.

iv. Accountability – accountability of the board of directors, sub-committees, internal auditors and reports.

v. Responsibility – the board's responsibility in reporting, risk management and communication; the responsibility of directors, independent directors and sub-committees.

vi. Fairness – it is the directors' responsibility to report fairly.

vii. Social responsibility – policies, procedures, systems and commitments to social, ethical, safety, health and environment; should integrate stakeholder reporting in the sustainability reporting.

The revised King III report (King 2009) adds to the list three philosophical foundations for good governance practice, namely effective leadership, sustainability and corporate citizenship.

In conclusion, the King reports (King 2002, 2009) summarised the guidelines and principles, codes of corporate practice and conduct based on a stakeholder approach and extended the objectives of corporate governance from risk management and corporate control to corporate social responsibility.

The ASX (2010, p.13-14) Principles of Good Corporate Governance and Best Practice Recommendations recognised eight principles, as follows:

- Principle 1 – Companies should lay solid foundations and disclosure for management and oversight of the respective roles and responsibilities of board of directors and managers.
- Principle 2 – Companies should establish a board with an effective composition, size and commitment to adequately discharge its responsibilities and duties, with the ultimate goal of creating value to the companies.
- Principle 3 – Companies should actively promote ethical and responsible decision-making.
- Principle 4 – Companies should have a structure to independently verify and safeguard the integrity of their financial reporting.
- Principle 5 – Companies should promote timely and balanced disclosure of all material matters concerning the company.
- Principle 6 – Companies should respect the rights of shareholders and facilitate the effective exercise of those rights.
- Principle 7 – Companies should establish a sound system of risk oversight and management and internal control.
- Principle 8 – The remuneration of board of directors and top executives should be fair and responsible. Underlying this principle is the assumption that companies should ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to performance is clear.

The ASX takes an "if not, why not" approach to reporting, which is neither law based nor bounded by legal requirements. ASX acknowledges that the corporate governance practices will evolve in light of the changing circumstances of a company and must be tailored to meet those circumstances. Moreover, the evolution of corporate governance practices must fit the context of developments both in Australia and overseas.

In essence, the ASX principles (2010) are mainly designed for large listed corporations, and exclude small corporations from the scope of discussion. However, the ASX principles may shed light on corporate governance of small corporations in that they point out that good corporate governance should deal with matters such as oversight, management, value creation, ethical and responsible decision making, financial reporting and disclosure, risk management and appropriate remuneration. Comparing the widely cited corporate governance definitions discussed above, this study found that the definition of corporate governance provided by de Plesis et al. (2010) offers a good starting point because this definition not only deals with issues related to shareholders, but also stakeholders and risk management, which reflects the expectations of ASX principles.

2.2.3. Relevance of corporate governance to small firms

Corporate governance is an established and well-studied subject in Economics, Finance, Accounting, Management and Law (Audretsch and Lehmann 2011). Excellent surveys of the literature on corporate governance of large corporations can be found in Bebchuk and WeIsbach (2010) and Brown, Beekes et al. (2011). These reviews support the contention that, up to now, corporate governance research has mainly been dedicated to and concerned with the traditional American corporations that have thousands of employees and are publicly traded on stock exchanges with the free float of shares and shareholders holding a small fraction of equities in the firm. In contrast, evidence on corporate governance is scarce in non-listed small corporations.

The literature shows extensive research on the efficiency of a corporate board as a central institution of internal governance in large corporations (Audretsch and Lehmann 2011). The focus of interest on small firms is still emerging (Arosa, et al. 2012). However, the literature also identifies differences and similarities in corporate governance and boards in both large and small firms (Machold et al. 2011).

Agency Theory suggests that corporate governance mainly deals with three types of conflicts between: (1) shareholders and managers; (2) controlling shareholders and minority shareholders; and (3) shareholders and non-shareholding stakeholders (Davies 2000). The governance problems of large corporations mainly arise from the separation of ownership and control in different contractual arrangements. However, unlike their large counterparts, ownership and control are normally concentrated in small firms (Uhlaner et al. 2007). For example, the founding owner of a firm is also the manager. Therefore, the disparity between ownership and managerial self-interest may be relatively smaller in the small firms.

While Agency Theory may be relevant to small firms, the literature argues that the decision-making and control structure is less complex and less diffused in small firms. Thus, the monitoring role of boards is diminished (Arosa, et al. 2012). On the other hand, a firm's interests may change the board's role in small firms (Pugliese and Wenstøp 2007).

The content of board tasks may vary between small and large firms (Zahra and Pearce II 1989). Consequently, boards may also assume other roles, including supervisory, advisory and networking. In addition, small business owners are more concerned with firm survival, growth rate, family welfare, succession plan, personal status and long-term financial returns. Furthermore, the impact of founding managers/ entrepreneurs on boards of small firms may be greater than that of their larger counterparts (Arthurs et al. 2009).

Small firms' demand for corporate governance has been constrained by their resource constraints. Small firms do not have the luxury of hiring in-house experts. Large corporations, however, benefit from corporate governance in the forms of value creation, cost minimisation and efficiency improvement, while small firms are disadvantaged (Clarke 2006).

The number of shareholders in small firms is limited. Hence, the second type of conflict — the interest disparity between controlling shareholders and minority shareholders is not a main concern except for the existence of block-holdings. Thus, a main task for corporate governance in small firms is to address the third type of conflicts — the interest alignment between shareholders and shareholding stakeholders (McCahery and Vermeulen 2010).

Contingency Theory suggests that the proper design of corporate governance has to consider environmental factors, for example, institutional environment and ownership characteristics (Huse 2005). Though existing research and practice is highly concentrated on the corporate governance of listed companies, external stakeholders (such as customers, lenders, insurance companies and equity investors) increasingly require non-listed companied to adopt the corporate governance rules and principles of listed companies (McCahery and Vermeulen 2010). Thus, there is a growing practical need for corporate governance tailored to small firms.

In contrast to the large economies of scale and scope researched by Berle and Means (1932) or Chandler (1977), some researchers have predicted that small corporations are the future of all economies (Audretsch and Lehmann 2012). As Rajan and Zingales (2000) point out, small corporations are the backbone of any economy, the driving force in employment generation, the major contributor of exports, and the main innovators in research and development.

2.2.4. Internal and external governance

Based on the organization-environment relationships, corporate governance can be divided into internal governance and external governance (Filatotchev and Nakajima 2010). According to Gillan (2006), internal governance mechanisms include five categories: (1) the board of directors, for example, role, structure, incentives; (2) managerial incentives; (3) capital structure; (4) bylaw or provisions; and (5) internal control system. All the non-shareholding stakeholders are considered as external environments and hence their interaction is with the organisation through external governance mechanisms. The external governance mechanisms are also divided into five categories, namely (1) law and regulation, (2) capital market, labour markets, product markets and market for corporate control, (3) information providers of capital market; (4) accounting, financial and legal service providers; and (5) private sources of external oversight, for example, media and external lawsuits (Gillan 2006).

2.2.5. Corporate governance guidelines for small firms

Professor John Farrar, a pioneer of research into corporate governance of small and medium enterprises (SMEs), recommends three solutions for the governance problems of small firms: (1) the adoption of an optional code of self-regulation; (2) the development of supplementary private arrangements; and (3) the provision of a new legal model, for example, limited liability partnerships (Farrar 2008).

The first set of tools for the corporate governance of small firms is an optional code of self-regulation. To date, four economies have officially introduced new corporate governance guidelines tailored for small family businesses. They are Hong Kong (2003, 2009), Belgium (2005, 2009), Finland (2006) and Switzerland (2006). A comparison of the content of these four guidelines is shown in Table 2.1.

In Hong Kong, the *Guidelines on Corporate Governance for SMEs in Hong Kong (1st Edition)* was developed by Bosch and Farrar (2003). The revised version was published in 2009 (Charlton and Lau 2009). SMEs in Hong Kong are classified into one of the following five categories based on business principles:

1. Small entities owned by single individuals, i.e. a few family members:

2. Larger entities employing non-family people;
3. Medium sized companies with several shareholders, or unincorporated partnerships;
4. Large medium private or public companies with a substantial number of shareholders and with representative boards; and
5. Companies listed on the Stock Exchange of Hong Kong.

Corporate governance guidelines were developed according to each business category.

Unlike Hong Kong, Belgium took a different approach to developing their corporate governance code, with a particular focus on non-listed enterprises (Farrar 2008). *Code Buysse II (Corporate Governance Recommendations for Non-listed enterprises),* claimed to be the first corporate governance code for non-listed companies, was promulgated in 2005. The 2nd version of the code was developed in 2009. The Belgium *Code Buysse II* divided the non-listed businesses into four phases based on the business life cycle as follows:

Phase 1: Sound entrepreneurship

This is the phase in which entrepreneurs have not yet legally structured their business as a firm. Sound entrepreneurship corresponds to the state in which the founding owners/managers design their strategy so as to sustainably increase their attractiveness to all stakeholders, both internal and external, thereby safeguarding the continuity of the enterprise (Belgium 2008). For start-ups, as for all enterprises throughout their existence, sound entrepreneurship is important.

Phase 2: The advisory council

In this phase, an entrepreneur uses an advisory council for support, which gives the founder sound advice regarding his management style.

Phase 3: The active board of directors

In this phase, the board of directors is activated by frequent meetings and dealing with important and strategic matters. The functioning of the board of directors is optimised when non-executive, or outside, directors are added to it.

Phase 4: The continued expansion of the instruments of governance

Larger or faster-growing enterprises will need to continue to develop their corporate governance with special attention to committees.

Using the Phase-based categorisation, the Belgium corporate governance code provided recommendations to the following components of corporate governance (Belgium 2005; Belgium 2009): an active board of directors, high-performance (senior) management, involves shareholders, control and risk management, specific recommendations for family enterprises (family governance), and publication of the corporate governance rules.

The corporate governance code in Finland, *An agenda for improving corporate governance of unlisted companies*, was introduced in 2006 (Finland 2006). The Finnish corporate governance code was produced in a fashion similar to other codes that relate mainly to large corporations. It covers the following aspects of corporate governance: general Meeting of Shareholders, the board of directors, the managing director, compensation systems, internal control and risk management, audit, the articles of association, shareholders agreements, redemption and approval clauses, communication and information, and change-of-generation in family enterprises.

Innovations of the Switzerland *Corporate Governance Code for Family Firms*, compared with the other three codes, include the development of public governance as one of the major parts of the code, and the integration of family governance, corporate governance and public governance (Switzerland 2006). Firstly, family governance covers family charter, wealth strategy, family reunions and family council, information and communication, bridging successors into the business and the handover of business. Secondly, business management and corporate governance contains vision and strategic orientation, structures and bodies, management systems and instruments, corporate culture and motivation, requirements for the key people, change of generation. Finally, public governance includes customers, employees, investors, business partners, the public state, associations and professional organisations.

Table 2.1 Optional codes of corporate governance for small firms in different countries

Economy	Code	Year of introduction	Topics
Hong Kong	*Guidelines on Corporate Governance for SMEs in Hong Kong (2nd edition)*	2009	CATEGORY 1: Small entities owned by single individuals; operations may involve a few family members CATEGORY 2: Larger entities employing non-family people; owners may include a few family members or outsiders CATEGORY 3: Medium sized companies with several shareholders, or unincorporated partnerships CATEGORY 4: Large medium private or public companies with a substantial number of shareholders and with representative boards CATEGORY 5: Companies listed on the Stock Exchange of Hong Kong
Belgium	Code Buysse II (Corporate Governance Recommendations for Non-listed enterprises)	2009	Phase 1: Sound entrepreneurship This is the phase in which entrepreneurs have not yet legally structured their business as a firm. For start-ups, as for that matter for all enterprises throughout their existence, sound entrepreneurship, as described in part 2 of this Code, is important. Phase 2: The advisory council In this phase an entrepreneur uses an advisory council for support, which gives sound advice on management style. Phase 3: The active board of directors In this phase the board of directors is activated by frequent meetings and dealing with important and strategic matters. The functioning of the board of directors is optimised when non-executive, or outside, directors are added to it. Phase 4: The continued expansion of the instruments of governance Larger or faster-growing enterprises will need to continue to develop their corporate governance with special attention to committees. The Code also has the following sections: • An active board of directors • High-performance (senior) management • Involved shareholders • Control and risk management • Specific recommendations for family enterprises – Family governance • Publication of the corporate governance rules
Finland	*An agenda for improving corporate governance of*	2006	• General Meeting of Shareholders • The Board of Directors • The Managing Director • Compensation Systems

	unlisted companies		• Internal Control and Risk Management • Audit • The Articles of Association • Shareholders Agreements • Redemption and Approval Clauses • Communication and Information • Change-of-generation in Family Enterprises
Switzerland	*Governance Guide for Families and their Businesses*	2006	1. Family governance • Family charter • Wealth strategy • Family reunions and family council • Information and communication • Bridging successors into the business and the handover of the business 2. Business management and corporate governance • Vision and strategic orientation • Structures and bodies • Management systems and instruments • Corporate Culture and Motivation • Requirements for the key people • Change of generation 3. Public governance • Customers • Employees • Investors • Business partners • The public • State/associations/professional organisations

Source: Adapted from Farrar (2008, p. 219), and McCahery and Vermeulen (2010)

2.2.6. Association developed, principled-based guidelines

A principle-based approach has been adopted by the European Confederation of Directors' Associations to develop good practice corporate governance guidance for non-listed firms (ecODA 2011). The ecODA first provides guidelines for all non-listed companies in Europe, and then for large and complex non-listed companies.

The ecODA nine principles apply to all non-listed companies and are as follows:

Principle 1: It is the shareholders' responsibility to establish an appropriate constitutional and governance framework for the company, which may be required by the corporations' law or developed by the shareholders under the guidance of the corporations' law.

Principle 2: Every company should establish an effective board of directors. It is the board which is collectively responsible for the long-term success of the company, including the definition of corporate strategy. However, an advisory board may be created to steer short-term transitions into long-term strategies.

Principle 3: Board size and composition should be based on the scale and complexity of the company's activities.

Principle 4: The board should meet sufficiently regularly and be supplied with appropriate, updated information.

Principle 5: Remuneration should be decided to the extent that it is sufficient to attract, retain, and motivate executives and nonexecutives of the expected competency to run the company successfully.

Principle 6: The board should maintain internal control to safeguard shareholders' investment and the company's assets and oversee risk management.

Principle 7: The board should have dialogues with shareholders based on the mutual understanding of multiple objectives and should treat all shareholders equally.

Principle 8: Companies should provide induction and training to the directors in order to make sure that their professional and technical skills are up to date.

Principle 9: Family-controlled companies should establish family governance mechanisms to complement corporate governance.

The ecODA also developed the following five principles for large and complex non-listed companies (2011):

Principle 10: The board and the management should have separate roles, with the former monitoring management and the latter making business decisions. No party should be given unfettered power.

Principle 11: Board structures should maintain diversity in order to yield a sufficient mix of competencies and experiences.

Principle 12: The board should establish sub-committees to discharge specific duties.

Principle 13: The directors' performance should be evaluated both as a group and as individuals.

Principle 14: The board should engage external stakeholders with regards to their business prospects.

Both the Belgium Codes and the Hong Kong Codes emphasised that the diversified characteristics of each individual non-listed enterprise should be put at the centre of corporate governance regulation and practice. Particular attention should be paid to the nature, size, and growth phase of the enterprise (Belgium 2008).

2.3. Theoretical foundations of corporate governance

This section reviews the theoretical foundations of corporate governance. The economic foundations of corporate governance are firstly summarised then, a critical review is made of six theories pertinent to the corporate governance of small firms including Agency Theory, Stewardship Theory, Stakeholder Theory, Resource Dependence Theory, Institutional Theory and Network Governance Theory. Though other theories, for instance, Transaction Cost Economics and the Resource-based View, are also important to the understanding of the corporate governance; they are not discussed here due to their remote relevance to small firms.

2.3.1. Economic foundations of corporate governance

The economic theories of corporate governance have their origins mainly in inquiries into the division of labour and separation of ownership and control. Smith (1776) was perhaps the first to propose that the market force is like an invisible hand that creates value by organising production in a laissez faire way; while Chandler (1977), two hundred years later, stressed the importance of hierarchy rather than markets, stating that it is the specialisation of managers, internalisation of activities undertaking by different business units and the expansion of business size by utilising larger inputs of capital that creates the economies of scale. Berle and Means (1932) have also had an influence on contemporary thought on corporate governance, claiming that the growing concentration of economic power and increased dispersion of stock ownership has made public corporations central to the economic activities in the United States.

Acknowledging the central role of market forces as an invisible hand in creating the national wealth, Smith (1776, p.700) precisely captured the phenomena of division of ownership and management, as he succinctly argued:

> *The directors of such joint-stock companies, however, being the managers rather of other people's money than of their own, it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honour, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail more or less, in the management of the affairs of such a company* (Smith 1776, p.700).

For Smith, the advancement of industrial capitalism created new governance problems, which go beyond the scope of mere market forces. As a substitute to the belief of market forces, the managerial revolution fully acknowledged the role management plays as a visible hand in wealth creation (Chandler 1977). In his analysis of large-scale railroads companies in the US, Chandler claimed that (1) managers running larger enterprises serve as a fundamental drive to the size and concentration of the US industries; (2) creating hierarchical company structures by internalising multiunit business operations enhances coordination productivities, reducing costs and increases profits; and (3) professional management, separated from ownership, is critical to the long-term growth and sustainability of the enterprises (Clarke 2004).

Berle and Means' influential work *The Modern Corporation and Private Property* analysed the history of ownership, highlighting the change of control with the transition of two-thirds of the industrial wealth from individual ownership to the ownership of publicly financed corporations (Berle and Means 1932). They argued that the separation of control and finance involves a new form of economic organisation (Berle and Means 1967). Berle and Means (1967) also argued that, though the owners surrendered their control over to professional managers, the control group (managers) should place the community (and the whole society) in a position as important as owners and themselves.

Hung (1998) provides a typology of six theories of the role of governing boards, that includes Resource Dependency Theory, Stakeholder Theory, Agency Theory, Stewardship Theory, Institutional Theory, and Managerial Hegemony (Fig. 1). In the Australian context, however, more than 90% of the business entities are small firms (Armstrong et al. 2011), thus managerial hegemony may not be a main concern, while the network with the other business entities are of greater importance. Therefore, this study reviews Network Governance Theory instead of the Managerial Hegemony Theory.

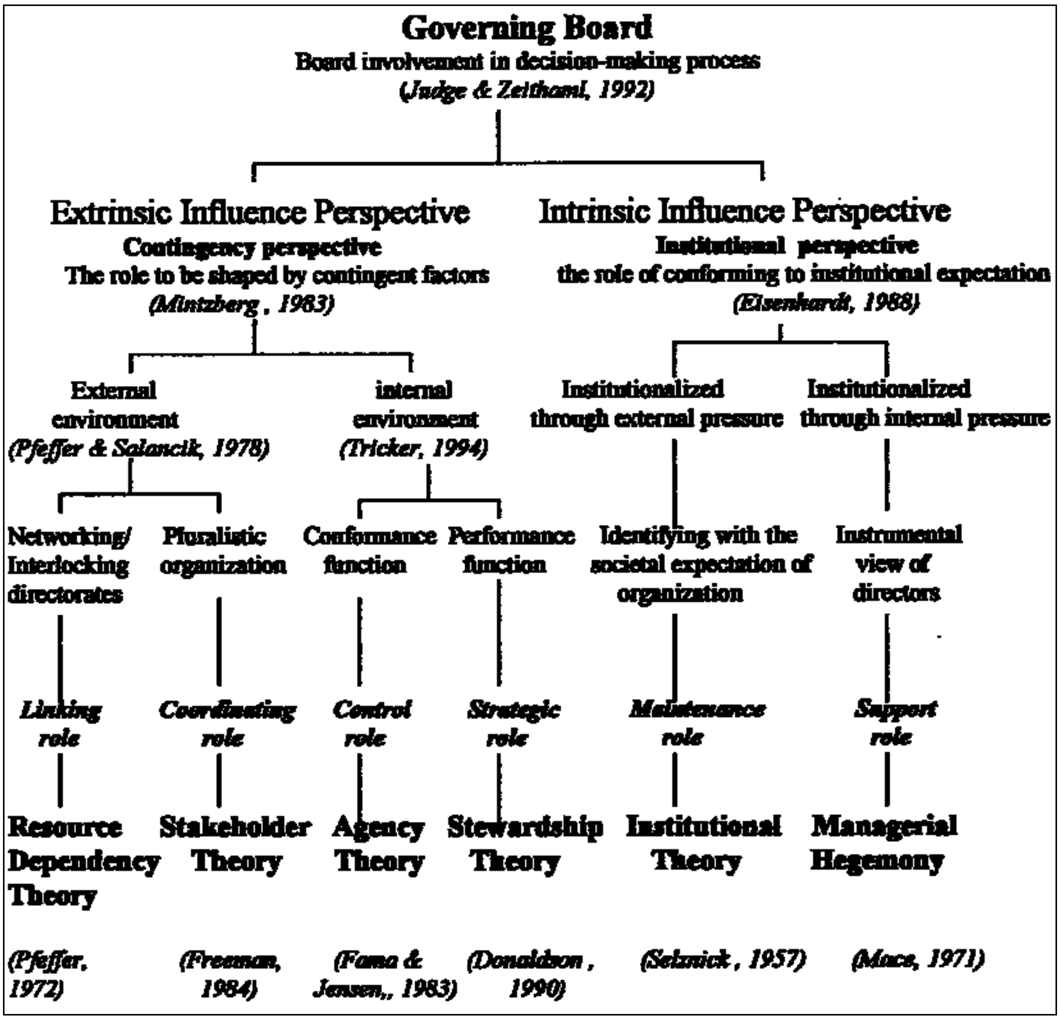


Figure 1.1 A typology of the theories relating to roles of governing boards
Source: Hung (1998: 105)

2.3.2. Agency Theory

Agency theory is highly relevant to understanding corporate governance. Ross (1973) first formulated the Agency Theory Paradigm in the 1970s, identifying it as a principal problem. The term was first associated with agency costs by Jensen and Meckling in 1976 (Ross 1973; Jensen and Meckling 1976; Shapiro 2005). Agency Theory spread to the other disciplines such as banking and finance (Adams, Hermalin et al. 2008), accounting (Brown, Beekes et al. 2011), marketing and organisational behaviour (Bammens, Voordeckers et al. 2010), and has became a dominant concept in the field of corporate governance research (Zajac and Westphal 2004).

Rooted in Information Economics (Turnbull 1997), Agency Theory complements the risk sharing literature by including the agency problem that occurs when goals of cooperating parties differ (Ross 1973; Jensen and Meckling 1976). Using contracts as a metaphor, Agency Theory attempts to resolve two problems that may occur when one party (the principal) delegates work to another (agent). The first is the conflict of goals between the principal and agent and the costs associated with the minimisation of such discrepancy; the second is the problem of sharing risk when the risk preference of the principal and agent differs (Eisenhardt 1989).

Ross (1973) suggested that the principal-agency problem is universal and ubiquitous. In developing this idea, Jensen and Meckling (1976) argue that agency costs include monitoring costs, bonding costs and residual loss. The monitoring costs are the expenditure paid by the principals to observe, to measure and to align the agents' interest and behaviour. The bonding costs are the expenditure (in monetary or non-monetary forms) that agents incur to establish systems which prove that they are acting in the principal's best interests.

The rest of the costs are incurred by misalignment, not counted for by monitoring and bonding costs, and are called residual costs (Table 2.2 provides a summary of the theoretical literature).

Table 2.2 Theoretical literature on Agency Theory

Author(s)	Analytic unit	Targeted firms	Problem of governance	Research stream	Proposition
Berle and Means (1932)	Principal-agent	Large public corporations	Separation of ownership and control	Positivism	Corporations are political constructs. Passive property increasingly loses its capital function and becomes a method for distribution of liquid wealth. Corporations may retain earnings for the maintenance and enlargement of its capital plant and operations..Sstockholders use the liquid value of his shares under his command.
Alchian and Demsetz (1972)		All types of organizations, eg. nonprofit, proprietary for profit, unions, cooperatives, partnerships	Team production and contractual form		Firm is a contractual form for team production with multiple inputs and it reduces monitoring costs.
Jensen and Meckling (1976)		Firms	Agency costs		Firms are the nexus of the contracts. The essence of the agency problem is the separation of management and finance. Due to the incompleteness of contracts, managers withhold control over the residual control rights, which are not foreseeable ex ante. Thus, corporate governance concerns with managers putting constraints on themselves, or investors putting constraints on managers, so that the misallocation problem can be reduced and investors will be induced to provide more funds.
Fama (1980)		Large corporations	Agency costs		The ownership of the firm is meaningless. What matters is the deviation of management from owners of the security. The firm is disciplined by competition with other firms, so are the individual participants, including managers. Managers face discipline and opportunities within and outside the firm.
Fama and Jensen (1983)		Large organizations	Agency costs		The separation of decision-making and risk-bearing functions exists in large organizations. As 'residual claimants' shareholders bear the risk of the corporation making a profit or loss. The maximisation of the shareholder value results on superior economic performance for the economy and the other stakeholders.
Ross (1973)		Firms	Principal problem	Principal-agent	Mathematical deduction of utility functions shows that the payoff structures and the motivation of agents do not conflict with Pareto efficiency.
Eisenhardt (1989)		Large firms	Principal-agent		Mathematical and logical deductions are used to produce general theory of the principal-agent relationship, eg. employer-employee, lawyer-client, buyer-supplier.

Key assumptions of Agency Theory

The key idea of Agency Theory is that, as a solution to the "principal-agent" problem, contracts between principals and agents should reflect efficient organisation of information and risk-bearing costs. Agency Theory rests on a number of assumptions, including human assumptions on self-interest, bounded rationality and risk aversion; organisational assumptions on partial goal conflict among participants, efficiency as the effectiveness criterion and information asymmetry between principal and agent; and information assumptions on information as a valuable commodity. The information asymmetry problem embedded in the principal-agency relationship may result in moral hazard and adverse selection and precludes cooperative parties from the benefits of sharing risks. Consequently, the ex-ante contracts between the principal and agent are incomplete. Agency Theory may be applied to any contractual relationships in which the principal and agent have partly differing goals and risk preferences, for example, compensation, regulation, leadership, impression management, whistle-blowing, vertical integration, merge & acquisition, and transfer pricing (Eisenhardt 1989).

Ramifications of Agency Theory

Agency Theory has developed along two lines: positivist and principal-agent problem. Both lines share a contract between principal and agent as the common unit of analysis. The positivist approach to Agency Theory focuses on large, public corporations (Berle and Means 1932). Positivist research intends to identify situations in which conflicts occur and governance mechanisms limit the agents' behaviour (Jensen and Meckling 1976; Fama 1980; Fama and Jensen 1983). Principal-Agent research is concerned with a general theory of the principal-agent relationship (Eisenhardt 1989).

The positivist approach proposes that (1) when the contract of principal-agent relationship is outcome-based, the agency cost will be minimised; and (2) when the principal has information to verify agent behaviour, the agent is more likely to act in the interest of the principals (Eisenhardt 1989).

In the principal-agent paradigm, researchers suggest that (1) information systems, outcome uncertainty, risk aversion of the agent, task programmability and length of the agency relationship are positively related to behaviour-based contracts and negatively related to outcome-based contracts; and (2) risk aversion of the principal, goal conflict between principal and agent, outcome and measurability are negatively related to behaviour-based contracts and are positively related to outcome-based contracts (Eisenhardt 1989).

The relevance of Agency Theory to small firms

Agency Theory serves as the underlying rationale for corporate law as well as principles and regulations of corporate governance. These address three sets of principal-agency conflicts: (1) the shareholders and the management; (2) majority shareholders and minority shareholders; and (3) the controller of the company and non-shareholding stakeholders (Davies 2000).

For small firms, particularly for micro- businesses and family businesses, ownership and control are concentrated in the owner/manager's hands. Thus, the board's role of monitoring may not be as strong as it is expected in large companies, rather the board of directors should be used for resource purposes. Moreover, the board should be expected to protect minority shareholders and non-shareholding stakeholders (Corbetta and Salvato 2004).

The critics of Agency Theory

Agency Theory has been widely criticised by the advocates of alternative theories such as Stewardship Theory (Donaldson and Davis 1991) and Stakeholder Theory (Donaldson and

Preston 1995; Freeman, Harrison et al. 2010). The major criticisms include: (1) the over-simplification by economists in their assumptions of the nature of contracts (e.g. self-interested and opportunistic individuals are utility maximisers) for the purposes of convenient mathematical computation, while ignoring more substantive considerations (Shapiro 2005); (2) the classic agency theory "is an organizational theory without organizations" (p.150) (Kiser 1999). Scholars from other disciplines have borrowed Agency Theory to help understand all sorts of organizations by relaxing their unrealistic assumptions of the economics paradigm (Shapiro 2005); (3) the solitary principal and agent assumption does not hold in practice as there are always multiple principals and agents in a single firm. The collective behaviour of multiple agents may dramatically change the economic models; (4) agency theory assumes that the principals dominate the specification of preferences, the creation of incentives and the making of contracts that agents must follow; (5) scholars abandon the assumption that the principal-agent relationship is enacted in the social context and constrained by outside forces, that is, other agency relationships, competitors, regulators (Shapiro 2005).

2.3.3. Stewardship Theory

Stewardship theory holds that managers seek other ends besides financial ones and, thus, there is no conflict of interest between stakeholders and managers. These include a sense of worth, altruism, a good reputation, a job well done, a feeling of satisfaction and a sense of purpose (Donaldson and Davis 1991). Stewardship theorists believe that managers have the good will to seek to do a good job in the forms of maximizing company profits and bringing high returns to stockholders and other stakeholders. They do not necessarily achieve these goals for their own sake, but because they have a strong duty to the firm.

Assumptions of Stewardship Theory

Agency Theory and Stewardship Theory begin from two very different assumptions. As Clarke (2004) pointed out, the former derives from the classical economic assumption that each individual is an economic being who is a self-interest oriented and is a self-optimizer. However, stewardship theory holds that individuals in management positions consider themselves as part of the firm and attach their career and fame to the firms. Hence, Stewardship Theory submits that managers merge their ego and sense of worth with the reputation of the firm and are neutral rather than self-interested (Clarke 2004). The Stewardship is solidly founded on Psychological and Sociological grounds in regards to their assumption on human behavior (Shapiro 2005).

Propositions of the Stewardship Theory

Donaldson and colleagues adopted a contingency approach to analyzing the agency-principal problem (Donaldson and Davis 1991; Davis, Schoorman et al. 1997; Muth and Donaldson 1998). Using the firm as the basic analytic unit, Donaldson et al. (1997) argued that the objective function for managers is to maximize shareholders' wealth. Consequently, managers will achieve personal satisfaction at the firm's optimal performance.

The alignment of the managers' motivation and principals' expectation is affected by role selection. Managers often choose to behave as stewards or agents, contingent on their motivations and perceptions of situations. Consequently, principals choose to create an agency or stewardship relationship (Donaldson and Davis 1991).

Governance applications of the Stewardship Theory

If a firm adopts a stewardship mode of governance, certain policies naturally follow. Firms will spell out in detail the roles and expectations of managers. These expectations will be highly goal-oriented and designed to evoke the manager's sense of ability and worth. Stewardship theory advocates the appointment of managers who are free to pursue their own goals. It follows from this that managers are "company men" who will put the firm ahead of their own ends. The managers' behavior will be influenced by both internal and external mechanisms. Freedom will be used for the good of the firm (Davis, Schoorman et al. 1997).

The Stewardship Theory concluded that the individualistic agency theory is overdrawn. Trust, *ceteris paribus*, exists between managers and board members. Whenever the CEO is not the chairman of the board, the CEO is able to perform well given that his or her major objective is not to maximize personal wealth at the cost of the company but to maximize the company wealth. Putting it differently, Stewardship Theory holds that managers do want to be richly rewarded for their efforts, but they will not do so if it were at the expense of the firm.

Criticisms toward Stewardship Theory

Given that the Stewardship Theory was developed largely as a critique of Agency Theory, it has also attracted criticism from proponents of Agency Theory:

(1) An example is in the debate between Albanese, Dacin and Harris (Albanese et al. 1997) and Davis, Schoorman and Donaldson (Davis et al. 1997). Albanese et al. (1997) argued that Davis et al. (1997) had misrepresented Agency Theory; in particular, the divergence of interest between an owner and managers. While Davis et al. (1997) countered that their arguments are mainly focused on the major school of Agency Theory (Jensen and Meckling, 1976);

(2) As Davis et al. (1997) acknowledged in the section of future research directions, their analysis rests on over-simplified assumptions and focuses only on the debate between Agency Theory and Stewardship Theory;

(3) Davis et al. (1997) admits the broadness of the psychological and situational constructs underpinning stewardship theory and calls for a finer grained analysis; and

(4) Stewardship Theory fails to articulate what determines the alignment of interests and is of no practical use when the interests of stewards and principal are aligned, e.g. venture capitalists and entrepreneurs (Arthurs and Busenitz, 2003).

2.3.4. Stakeholder Theory

Freeman was the first scholar to provide details of Stakeholder Theory in his book *Strategic Management: A Stakeholder Approach* (Freeman 1984). Recognised as the "father of stakeholder theory", Freeman (1984) identifies and models the groups who are stakeholders of a corporation. He also both describes and recommends methods by which management can give due regard to the interests of these groups. Freeman's initial objective was to develop a pragmatic approach to strategy which urges organizations to recognise the significance of stakeholders to achieve superior performance. Freeman drew on various pieces of literature to develop Stakeholder Theory including strategic management, corporate planning, systems theory and corporate social responsibility (Laplume, Sonpar et al. 2008). In short, it attempts to address whose stake counts in business decisions.

There have been numerous articles and books written on Stakeholder Theory. Recent scholarly works on the topic of stakeholder theory that exemplifies research and theorizing in this area include Donaldson and Preston (1995), Mitchell, Agle, and Wood (1997), Friedman and Miles (2002), Phillips (2003) and Freeman, Harrison et al. (2010).

Assumptions of Stakeholder Theory

The theoretical foundation of the Stakeholder Theory is private ownership (Donaldson and Preston 1995). Freeman (2010) challenged the long-standing assumption in economics and management literature of the past two centuries that the objective of firms is to maximize shareholders' wealth. Rather, Freeman suggested that the firm's objective is to optimize stakeholders' wellbeing in order to create strategic advantage (Laplume, Sonpar et al. 2008). In Stakeholder Theory, a firm is assumed to be a business opportunity (Freeman, Harrison et al. 2010), which is fundamentally different from Friedman's treatment of business as markets and maximizing tools (Friedman 1970), Jensen and Meckling's move toward business as an agency (Jensen and Meckling 1976), Porter's perspective of business as a competitive strategy (Porter 1979), and Williamson's treatment of business as a nexus of transaction costs (Williamson 1981).

Propositions of Stakeholder Theory

Freeman's Stakeholder Theory intends to address three problems: (1) the problem of value creation and trade; (2) the problem of the ethics of capitalism; and (3) the problem of a managerial mindset (Freeman et al. 2010, p. 29). Freeman et al. (2010) holds that: (1) the basic objective of a firm is to create value for stakeholders; (2) business is a set of relationships among groups which have a stake in the business activities; (3) business is about how customers, suppliers, employees, financiers (such as stockholders, bondholders, banks, or investors), communities, and managers interact and create value. To understand a business is to know how these relationships work. In this context, the executive's or entrepreneur's job is to manage and shape these relationships. Hence, stakeholders are defined as customers, suppliers, employees, investors, communities, and managers who interact and create value for firms (Freeman, Harrison et al. 2010, p. 24).

Stakeholder theory stresses the dependency of many different groups on the firm's management. It strongly suggests that corporations are run by loosely defined groups of people, each seeking something different from the organization. This theory identifies who benefits from a firm, as well as locates who, in fact, controls its corporate policy. The stakeholder view of strategy is an instrumental theory of the corporation, integrating both the resource-based view as well as the market-based view, and adding a socio-political level. This view of the firm is used to define the specific stakeholders of a corporation (the normative theory of stakeholder identification (Donaldson and Preston, 1995)) as well as examine the conditions under which these parties should be treated as stakeholders (. The normative aspect and the descriptive aspect combined forms the modern treatment of Stakeholder Theory.

Donaldson and Preston (1995) argue that the normative base of the theory, including the "identification of moral or philosophical guidelines for the operation and management of the corporation", is the core of the theory. Mitchell et al. (2012) derive a typology of stakeholders based on the attributes of power (the extent a party has means to impose its will in a relationship), legitimacy (socially accepted and expected structures or behaviors), and urgency (time sensitivity or criticality of the stakeholder's claims). By examining the combination of these attributes in a binary manner, eight types of stakeholders are identified and described along with their implications for the organization. Friedman and Miles (2002) explore the implications of contentious relationships between stakeholders and organizations by introducing compatible/incompatible interests and necessary/contingent connections as additional attributes with which to examine the substance of these relationships.

Criticisms against Stakeholder Theory

Stakeholder Theory has been criticized in the following aspects:

i. Stakeholder Theory is limited to human participants and their behavior, while it fails to provide managers with credible ethical principles (Orts and Strudler, 2002);

ii. The complexity of multiple stakeholder involvement and little constraint on the managerial obligations toward employees may make it convenient for managers with special interests to use the resources of firms for their own needs, thus exacerbating agency problems (Jensen 2002);

iii. Stakeholder Theory creates a domain so broad that some of its assumptions on firms and stakeholders may be invalid for SMEs (Perrini 2006; Perrini, Pogutz et al. 2006); and

iv. The streams of Stakeholder Theory are so divergent that it is untenable to aggregate them as an integrated theory (Donaldson 1999).

2.3.5. Resource Dependence Theory

Jeff Pfeffer's 1972 dissertation and prolific proceeding publications marked the birth of resource dependence theory. In 1978 Pfeffer and Salancik published *The External Control of Organization*, which pinpointed the "power-dependence relations" and led to the popularity of the resource dependent theory.

Assumptions of Resource Dependence Theory

The Resource Dependence Theory assumes that a firm's power over its external environment is critical to earning a competitive advantage for a firm. The external environment such as suppliers, customers and board of directors, are contingencies of the organisation's power. By applying multiple strategies, the firm is able to combat the contingencies and minimise uncertainty and interdependence on the environment (Hillman et al. 2009).

Propositions of Resource Dependence Theory

The Resource Dependence Theory has three major ideas: (1) external environment matters. The social context in which a business operates may have direct impact on resource allocation; (2) organisations should develop strategies to enhance their autonomy of acquiring and allocating resources with a view to improving their organisations' performance. The process of seeking autonomy reduces the organisation's dependency on resources; and (3) market power is important for understanding internal and external actions of the organisation (Pfeffer 1972). In particular, the emphasis on market power distinguishes resource dependence theory with other competing theories in explaining the firm's behaviour.

The resource dependence theory considers internal and external resources as major contingencies for organisational performance. The underlying assumption is that, though resource allocation can be planned there are uncertainties in the availability and cost of obtaining the resource related information. Hence, resources are critical to organisations. Resources may come from environments internal or external to the organisations. Internal resources may include input such as capital, labour and technology, management knowledge, production and marking capabilities, board of directors, employees' morale and satisfaction, the owners' family networks and managers' networks; external resources may include customers, investors, suppliers, competitors, regulators, community, and environment. The resources one organization needs are thus often in the hands of other organizations (Williams and McWilliams, 2014). Such resources serve as a basis for market power, which enables one organisation to be dependent on each other, even though they are legally independent. Pfeffer (1972) also contends that the market power of an organisation and its dependence on resources are intertwined. Such powers are constrained by environmental contingencies and are potentially mutual to the two organisations which have the relationship.

Hillman et al. (2000) further argued that though resource contraints of an organisation may come from numerous sources such as labour, capital, raw material, board of directors, personal networks, and entrepreneurship, each resource does not have an equal weight on organisational performance. In addition, given that organisations face limited resources and tight budgets for accessing resource related information, they may not be able to use each resource contingent fairly. Hence, organizations should make scarcity at the core of business when dealing with the resource dependency issue. Critical resources required to add value to tan organization’s core business must have to function. Thus organisations should identify critical resources and attend to them in order to achieve optimal performance.

The Resource Dependence Theory complements the Agency Theory by arguing that the board of directors can be used as a mechanism to curb the managerial self-service behaviour, but also, in the meantime serve as valuable resource for the organisation. Directors are selected based on a range of technical,, interpersonal and conceptual skills, their motivation to manage and their strong connections with the market, in particular, with the resources external to the organisation such as customers, suppliers and financers. Hence, the board of directors may serve as a nexus between the internal environment and external environment, which may further synergize internal and external resources. Furthermore, having more external directors sitting on the board may benefit the organisation in more ways than one. Though they may have less impact on key business decision making, their view as an independent voice, their role as an extra source to understand the customer's needs, and their capability of offering a balanced understanding of the potential social and economic impact of a business decision will add significant value to the organisations performance (Hillman and Dalziel 2003).

The Resource Dependence Theory is a well-established framework to understand the relationships between firms, their external environments and the strategies they take to reduce these dependencies. In the past three decades, Resource Dependence Theory has been widely used in explaining at least five areas of business: (1) mergers/vertical integration, (2) joint ventures and other inter-organizational relationships, (3) board of directors, (4) political action, and (5) executive succession (Hillman et al. 2009).

Criticisms of Resource Dependence Theory

As with Agency Theory and Stakeholder Theory, Resource Dependence Theory has also been scrutinized. Criticisms against it (especially Hillman et al. (2009)) are summarised as follows:

i. The theoretical development or refinement of Resource Dependence Theory has been bogged down since its introduction in the 1970s. For instance, recognizing multiple environmental contingencies and their relationships is not sufficient. The theory needs to provide a better understanding of the web and dynamics of interdependences amongst the contingencies;

ii. Empirical and theoretical work is yet to be done with regards to the strategies of political action and executive succession, incorporating the heterogeneity nature of dependence in government decision-making;

iii. The boundary conditions of Resource Dependence Theory have yet to be articulated.

2.3.6. Institutional Theory

Institutional Theory has its roots dating back to the nineteenth century. The essence of institutional theory is that it analyses the role institutions play in maintaining social stability and in determining social reproduction (Scott 2008). Institutional theory focuses on deeper and more resilient aspects of social structure. It considers the processes by which structures, including schemes, rules, norms, and routines, become established as authoritative guidelines for social behaviour (Scott 2004). Different components of institutional theory explain how these elements are created, diffused, adopted, and adapted over space and time; and how they fall into decline and disuse.

Assumptions of the Institutional Theory

Institutional Theory is grounded in assumptions about the behaviour of human beings, including opportunism and bounded rationality. Opportunism means that human beings are self-interest seekers. While bounded rationality means that human beings acts rationality with intention but that rationality is limited by access to information (Williamson 1981). The consequences of opportunism and bounded rationality are incomplete contracts and moral hazard problems.

Propositions of the Institutional Theory

Institutional Theory goes beyond technological advancements, as do traditional economists or the resource dependencies suggested by the Resource Dependence Theory, to argue that formal organisational structure reflects institutional forces (Scott 2008).

Powell and DiMaggio (1991) define an emerging perspective in organization theory and sociology, which they term the 'new institutionalism', as rejecting the rational-actor models of classical economics. Instead, it seeks cognitive and cultural explanations of social and organizational phenomena by considering the properties of supra-individual units of analysis that cannot be reduced to aggregations or direct consequences of an individual's attributes or motives (Powell and DiMaggio 1991).

Scott (2004) takes this idea further arguing that, in order to survive, organisations must conform to the rules and belief systems prevailing in the environment (DiMaggio and Powell 1991), because institutional isomorphism, both structural and procedural, will earn the organisation legitimacy (Suchman 1995). Multinational corporations (MNCs) operating in different countries with varying institutional environments will face diverse pressures. Some of those pressures in host and home institutional environments are proven to exert fundamental influences on competitive strategy (Porter 1979).

There is substantial evidence that firms react differently to different contextual factors, such as social, economic, and political factors. This constitutes an institutional structure of a particular environment which provides firms with advantages to engage in specific types of activities there. Businesses tend to perform more efficiently if they receive institutional support (Knetter 1989).

Criticisms of the Institutional Theory

Institutional Theory has been critiqued (Lawrence et al. 2011) on three major points:

i. More work has to be done to the relationship between institutions and the actors who populate them;

ii. More why and how questions should be asked to combine the theory of institutional work with practice;

iii. The construct of institutional work has to be refocused to the relationship between institutional change and entrepreneurial behavior.

2.3.7. Network Theory

Unlike previous theories, the basic analytic unit of Network Theory is network, defined as groups of three or more legally autonomous organizations that work together to achieve the same goals which benefit themselves and the collective interests (Provan and Kenis 2008).

Sorensen and Torfing (2005, p.3) define network governance as a network structure, formed by components as follows:

- actors who are relatively stable horizontal interdependent but operationally autonomous
- actors who interact through negotiations that involve bargaining, deliberation and intense power struggles
- negotiations occur within a relatively institutionalized framework
- self-regulating governed by rules set by external agencies and

- contribute to the shared vision, mission, strategies and business decisions beneficial to the those in the network.

With this definition in mind, Sorenson and Torfing (2005) identify four democratic principles for use in assessing the democratic performance of a governance network. These points are the extent to which the network:

- is controlled by democratically elected politicians;
- represents the membership basis of the participating groups and organizations;
- is accountable to the territorially defined citizenry; and
- follows the democratic rules specified by a particular grammar of conduct.

Assumptions of the Network Governance Theory

Network Governance Theory assumes that organisations are autonomous entities. The major assumption of this theory is that organisations are governed by neither the market nor the hierarchy (organisational form) but by collective behaviour, either initiated by individual organisations or mandated by the public sector. In other words, the properties of the networks and network evolution determine the performance of organisations and the society as a whole (Provan and Kenis 2008).

Propositions of the Network Governance Theory

Network governance constitutes a “distinct form of coordinating economic activity” (Powell 1990, p. 301) which contrasts and competes with markets and hierarchies. As such, governance networks distinguish themselves from the hierarchical control of the state and the competitive regulation of the market in at least three ways (Powell 1990; Kersbergen and Waarden 2004):

- In terms of the relationship between actors, governance networks can be described as a "pluricentric governance system" as opposed to the "unicentric system of state rule and the multicentric system of market competition". In contrast to state rule and competitive market regulation, governance networks involve a large number of interdependent actors who interact in order to produce public purpose.
- In terms of decision-making, governance networks are based on negotiation rationality as opposed to substantial rationality that governs state rule and the procedural rationality that governs market competition.
- Compliance is ensured through trust and political obligation which, over time, becomes sustained by self-constituted rules and norms.

As a concept, network governance explains increased efficiency and reduced agency problems for organizations existing in highly turbulent environments. On the one hand, efficiency is enhanced through distributed knowledge acquisition and decentralised problem solving; on the other, effectiveness is improved through the emergence of collective solutions to global problems in different self-regulated sectors of activity. Due to the rapid pace of modern society and competitive pressures from globalization, network governance has gained prominence and development among sociological theorists (Sørensen and Torfing 2005).

Provan and Kenis (2008) reviewed a range of literature on network governance and proposed the following assumptions: (1) network governance efficiency is contingent on consistency between contingency factors and a particular governance form, trusts, and tension; and (2) the evolution of a network is more likely from concentrated form to a more dispersed form.

Criticisms of the Network Governance Theory

Network Governance Theory is not without its critics (Jones et al. 1997; Provan and Kenis 2008) Several major criticisms of this theory have been articulated in the literature and these include that:

i. Empirical work has yet to be done to test theory related to network-level activities, structures and outcomes.

ii. Interaction between governance interaction and operational interaction should also be researched.

iii. Evolution of governance forms and its impact on network effectiveness has yet to be researched in detailed studies.

2.3.8. Summary

Adapting the paradigm adopted by Letza et al. (2004), the six theories reviewed are summarized in Table 2.3. The theories are compared using a range of criteria including: main contributors, analytic unit, theoretical perspective on purpose of corporation, problem of governance, causes of governance problems, assumptions about causation, rejection, and criticisms.

Main contributors

The main contributors of these six theories come from the disciplines of economics, management, organizational behavior and finance. Main contributors identified and reviewed for each of the theories are (but not limited to) the following:

i. Agency Theory: Alchian and Demsetz (1972); Berle and Means (1932); Eisenhardt (1989); Fama (1980); Fama and Jensen (1983); Jensen and Meckling (1976); and Ross (1973).

ii. Stewardship Theory: Davis, Schoorman and Donaldson (1997); Donaldson and Davis (1991); and Muth and Donaldson (1998).

iii. Stakeholder Theory: Blair (1995); Donaldson and Preston (1995); Freeman (1984); Freeman et al. (2010); Friedman and Miles (2002); Mitchell, Agle and Wood (1997); and Phillips (2003).

iv. Resource Dependence Theory: Hillman, Cannella and Paetzold (2000); Pfeffer (1972); Pfeffer and Salancik (1978).

v. Institutional Theory: Judge and Zeithaml (1992); Powell and DiMaggio (1991); Scott (1995; 2004) Suchman (1995); Willamson (1981).

vi. Network Governance Theory: Jones, Hesterly and Borgatti (1997); Provan and Kenis (2008); Sorensen and Torfing (2005).

Analytic unit

Of all the six theories, the Institutional Theory uses transaction and contracts as the basic analytic unit, and Network Governance Theory uses the network. The rest of the theories all use the firm as the analytical unit.

Purpose of corporation

The purpose of corporations using these theoretical frameworks range from the maximization of shareholder wealth in the Agency Theory, to the maximization of shareholder wealth and stewards' personal satisfaction in Stewardship Theory, and then to the maximization of stakeholders' wealth in Stakeholder Theory. Resource Dependence Theory intends to remove corporations from the contingencies of the external environment. Institutional Theory focuses on transaction costs, opportunism and uncertainty in the corporations' contracts. The Network Governance Theory focuses on enhancing the efficiency and reducing the agency costs for corporations.

Problem of governance

The main governance problems addressed by the theories include the separation of ownership and control (the agency problem), the absence of stakeholder involvement, the alignment of environmental contingencies and firm's power and the impact of social structure on organization performance.

Assumptions about causation

The six theories reviewed all originate from assumptions about human behavior, which includes self-interest, self-actualization, private ownership, autonomy and bounded rationality.

Table 2.3 Summary of theories on corporate governance

	Agency Theory	Stewardship Theory	Stakeholder Theory	Resource Dependence Theory	Institutional Theory	Network Governance Theory
Main contributors	Alchian and Demsetz (1972); Berle and Means (1932); Eisenhardt (1989); Fama (1980); Fama and Jensen (1983); Jensen and Meckling (1976); and Ross (1973)	Davis, Schoorman and Donaldson (1997); Donaldson and Davis (1991); and Muth and Donaldson (1998);	Blair (1995); Donaldson and Preston (1995); Freeman (1984); Freeman et al. (2010); Friedman and Miles (2002); Mitchell, Agle and Wood (1997); and Phillips (2003)	Hillman, Cannella and Paetzold (2000); Pfeffer (1972); Pfeffer and Salancik (1978)	Judge and Zeithaml (1992); Powell and DiMaggio (1991); Scott (1995; 2004) Suchman (1995); Willamson (1981)	Jones, Hesterly and Borgatti (1997); Provan and Kenis (2008); Sorensen and Torfing (2005)
Analytic unit	Firm	Firm	Firm	Firm	Transaction and contract	network
Purpose of corporation	Maximization of shareholder wealth	Maximization of shareholder wealth and stewards' personal satisfaction	Maximization of stakeholder wealth	Reduce environmental interdependency and uncertainty	Reduce transaction costs, opportunism, and uncertainty	Enhance efficiency and reduce agency costs
Problem of governance	Agency problem	Steward and principal motivation alignment	Absence of stakeholders' involvement	Environmental interdependency and uncertainty	Organizations are influenced by social structure.	Agency problem
Cause	Separation of management and finance	Social and psychological causes	Stakeholders' interests are forgotten	Corporations as an open system is constrained by external environment	Incomplete contract	Distributed knowledge acquisition and decentralized problem solving
Assumptions about causation	Self-interest human behavior, economic man	Self-actualizing man, collective serving	Private ownership	Organizations attempts to reduce others' power over them and increase their own power over others.	Bounded rationality, opportunism, and uncertainty	Autonomous organizations
Rejection	Any external intervention	Agency Theory	Agency Theory, Institutional Theory, Corporate Social Performance,			Agency Theory

			Corporate Citizenship, and Integrated Social Contract Theory			
Proposition	Market efficiency	Managers choose to behave as stewards or agents, contingent on their psychological motivations and perceptions of situations. Consequently, principals choose to create an agency or stewardship relationship.	Social efficiency of the economy; stakeholder participation	A complement to the Agency Theory and focuses on the external environment. Organization is the basic unit for interrelation analysis; organization has interdependency and uncertainty, which can be influenced by organization actions.	Institutions have significant impact on firm performance. Board of directors as an institutional form may restrain the agency problem and increase firm profitability.	Network governance efficiency is contingent on consistency between contingency factors and a particular governance form, trusts, and tension. The evolution of network is more likely from shared form to a more broken form.
Criticisms	Over-simplified, no organizations, solitary principal and agent problem, principals dominates, relevance of social context and outside forces violate assumptions	Only contested one version of the Agency Theory; over-simplified assumptions; variables and constructs are broad and general; and not useful for venture capitalists – entrepreneur relationship	Not well grounded, too broad, based on false assumptions, does not recognize the effects of incentives, difficult to implement, may not be applicable to SMEs	Other mechanism may also reduce environmental dependency. Dependencies exist in multiple contingencies. Resource provision role of directors may affect executive selection and the role of succession in managing environmental uncertainties.	Static view of institutionalization; Measure of institutions	Empirical work is yet to be done to test theory related to network-level activities, structures and outcomes. The interaction between governance interaction and operational interaction should also be researched. Evolution of governance form and its impact on network effectiveness has yet to be researched in finer levels.

2.4. Empirical studies on corporate governance and performance of small firms

Empirical studies reviewed here are mainly focused on the relationship between corporate governance and the performance of small firms. Prior research has identified five corporate governance mechanisms, namely (1) board of directors ; (2) managerial incentives; (3) capital structure; (4) internal control systems; and (5) ownership structure (Audretsch and Lehmann 2012; Bebchuk and Wesbach 2010; Bhagat and Bolton 2008; Brown, Beekes et al. 2011; Gillan 2006).

Performance is measured by accounting performance, marketing performance and social performance. Accounting performance is defined as the extent to which businesses generate accounting based profits. Measures for accounting performance include Return on Equity (ROE), Return on Assets (ROA), Return on Investment (ROI), Earnings per Share (EPS), and profit margin. Marketing performance is defined as the extent to which businesses generate market-based performance. Measures for marketing performance include book-to-market ratio, Tobin's Q, and stock returns (Bhagat and Bolton 2008; Brown, Beekes et al. 2011; Filatotchev, Lien et al. 2005; van Essen, Oosterhout et al. 2012).

Due to the heterogeneity of definitions of small firms used in different studies, this section only reviews literature whose authors identify their sample as small business or SMEs.

Empirical research in Management, Economics and Finance relates to Agency Theory and can be divided into four streams (Shapiro 2005):

i. The trade-offs between behaviour-oriented (salary) and outcome-oriented (commission, bonus, equity ownership and compensation linked to the shareholder wealth) (Eisenhardt 1989). Agency Theory assumes that incentive mechanisms may reduce the opportunism of managers. However, meta-analyses found no statistical support for the relationship between incentives to monitor and firm performance (Dalton, Daily et al. 1998; Dalton, Daily et al. 2003).

ii. The relationship between corporate governance and control, for example, the monitoring role of the board of directors, the duality of board chair and CEO (as the same person), the succession of CEO (Corbetta and Salvato 2004), the recruiting of external directors, the bonding mechanisms and the implications of different forms of capitalisation (in the forms of debt or equity, or dividends payout and activating the monitoring role of the financial market when managers must solicit for additional funding). Agency Theory assumes that the firm's performance will improve in the following scenarios: (1) when the roles of board chairman and CEO are separated; or (2) a higher proportion of outside directors are appointed to the board; or (3) increasing the board size; or (4) a higher proportion of independent or non-executive directors on board; or (5) board with higher average age; or (6) board members with lower average tenure. However, Muth and Donaldson (1998) found that none of the above mentioned assumptions are valid using Australian data.

iii. The agency costs, efficacy and trade-offs of different control mechanisms, for example. the length of principal-agent relationship, organisational structure and form, characteristics of industries, organisations and employees, programmability of the task or how well the required behaviour can be defined, and organisational environment. The hypotheses propose low agency costs which leads to better firm performance (Jensen and Meckling 1976). However, empirical evidence has found no statistical significance of the relationship between control and performance (Dalton, Daily et al. 2003). Further research is required into the substitution and supplementation that impacts governance bundles (Ward 1991; Rediker and Seth 1995; Hoskisson, Castleton et al. 2009).

iv. The costs and process of searching for boards of directors, in particularly in the light of the potential impact of adverse selection. Thus, Agency Theory assumes that the firm's performance will improve if there is a closer alignment between the interests of board members and shareholders. However, this assumption has been refuted (Muth and Donaldson 1998).

Counter-arguments from other theories are discussed specifically within each component of the internal corporate governance below.

2.4.1. Board of directors

Research into the board of directors can be divided into three categories, (1) board roles such as, advising, monitoring, supervising, networking; (2) board structure such as CEO duality, board size, board independence, board expertise, board sub-committees, board meetings; and (3) board incentives such as board ownership, board compensation (Gillan 2006).

2.4.1.1. Board roles

Boards of directors are created to serve certain functions, rather than to substitute the operational management of the firms. However, a common misconception in the literature is that a board of directors is explicitly assuming omnipotent power in nearly all aspects of the business activities, henceforth influencing the business performance (Aaboen, Lindelof et al. 2006; Bhagat and Bolton 2008; Arosa, Iturralde et al. 2012). Some research assumes that only corporate governance mechanisms related to small and medium sized firms can be classified as boards of directors (Abor and Adjasi 2007; Bennedsen, Kongsted et al. 2008). Literature related to the roles of boards is first discussed.

Assumptions suggested by each theory

Given the interest and risk-bearing disparities, Agency Theory posits that a board of directors is created to control and to monitor management on behalf of shareholders and to provide resources (Fama and Jensen 1983). Boards are expected to complement incomplete contracts between shareholders and managers.

Stewardship Theory, in contrast, claims that there are no essential conflicts of interest between the owner and managers. Rather, the board should endeavour to empower managers, who are stewards of the owners; and the board should maintain the relationship between the owners and stewards. In other words, according to the Stewardship Theory, the role of the board is not to control or monitor the managers; rather, the board should hand over the control function to the managers (Davis et al. 1997).

Resource Dependence Theory maintains that the board of directors is a unique strategic resource to small firms, in which the board is able to minimise the intra-organisation dependency and secure critical resources for the firm (Pfeffer and Salancik 1978). Small firms generally lack knowledge and in-house experts. The introduction of external experts can facilitate the knowledge transfer and sustain a long-term competitive advantage. Thus, the board serves as advisers (Huse 2000). Moreover, boards of directors are able to provide contact with the external environment and establish business connections based on their own network. Hence, they assume a networking function as well (Gabrielsson and Huse 2005; Voordeckers et al. 2007).

Network Governance Theory emphasises the importance of external networks to the performance of small firms. Networks expand the business opportunities in the form of larger markets or easier access to funds, facilitate strategic growth and innovation and improve the market access of small firms (Wincent et al. 2009; Wincent et al. 2010).

Empirical studies

Empirical evidence has shown support for a boards' supervisory, advisory and networking roles (Minichilli and Hansen 2007; Huse 2009; Minichilli, et al. 2009; Arosa, et al. 2010; Wincent et al. 2010; Basco and Pérez Rodríguez 2011; García-Ramos and García-Olalla 2011; Arosa et al. 2012).

Arosa et al (2012) empirically tested the relationship between board structure and firm performance in 307 unlisted SMEs in Spain. They found weak support for the monitoring role, while strong support for the alternative roles. They also found that the involvement of external directors has a positive impact on the strategic planning of the Spanish SMEs. Minichilli and Hansen (2007; 2009) surveyed 881 small Norwegian firms and found that the advisory role has a positive impact on the firm performance, contingent on the situation the firm is experiencing.

Basco and Pérez Rodríguez (2011) used 732 privately held family firms and discovered that the external groups' participation in the management and on boards has a positive impact on strategic planning, family competency, and firm competency resulting in a better fit between family and the firm.

Bennet and Robson (2004) argued that in SMEs, the board, external consultants and management are substitutes for each other, meeting different demands.

Boards' roles in practice

The board of directors in SMEs may assume a control and monitoring role, as proposed in Agency and Stewardship Theory. However, given the lower level of resources available to SMEs, may also enable the boards of directors to be valuable resources, providing service to the firm as proposed by Stewardship Theory, Resource Dependence Theory and Network Governance

Theory (Stevens 2011). Apart from the resource provider's role, the board of directors may be created only to meet the regulatory compliance requirements for legitimacy purpose, for example, as a figurehead of the firm (Fiegener et al. 2000; Fiegener 2005).

The boards' role may vary contingent on both the stage of business development and environmental factors. As Stevens (2011) has proposed, boards play control and monitoring roles when the firms have external ownership, significant debt, are highly complex or family involvement is less cohesive. The service role is played when the resource level is lower but the requirement for resources is higher, and the networks are shallow. The legitimacy role is mainly for newer small companies with extended sales to external parties and external resource requirements. Specifically, the Belgium code for non-listed companies (Belgium 2005; Belgium 2009) suggests the following tasks for a board of directors:

- Strategic management role: the boards should make decisions which are significant and critical to strategic matters in the long term;
- To supervise and monitor the management and shareholders who can take initiatives that fall within their competency;
- The appointment of the managing director, the executive committee and the management;
- The financial and operational controls, including the introduction of an internal control system;
- Dividend policy;
- Succession planning for the managing director, the executive committee and the management; and
- Safeguarding the interests of the firm in the event of crisis and conflicts.

Tasks Beyond the Boards' Responsibilities

Given the limitations and time constraints of the boards, they are not expected to undertake the following tasks (Belgium 2009):

- Organize general meetings, which is required to change the capital structure, to appoint or reject directors, to approve annual accounts, to decide the dividends suggested by the board;
- Substitute for management, which undertakes the operational management of the firm and implementation of the strategies;
- Serve as the executive committee and tradeoff between monitoring and controlling powers.

2.4.1.2. CEO Duality

Agency Theory advocates that the CEO and chairman of the board should be separate. However, Stewardship argues that the CEO and chairman should be the same person (Muth and Donaldson 1998). Empirical evidence on the impact of CEO Duality on firm performance shows mixed results (Baliga et al. 1996; Judge, et al. 2003; Bennett and Robson 2004; Abor and Biekpe 2007; Amedeo and Pingying 2007; Voordeckers et al. 2007; Bennedsen et al. 2008; Bhagat and Bolton 2008; Chen and Hsu 2009; Gnyawali and Park 2009; Hoskisson et al. 2009; Huang 2010; Kota and Tomar 2010; Lily Julienti Abu and Ahmad 2010; Bergenholtz 2011; Brown, Beekes et al. 2011; de Clercq and Voronov 2011; Fooladi 2011; García-Ramos and García-Olalla 2011; Hotho and Champion 2011; Valenti et al. 2011; Lin and Liu 2012).

Abor and Biekpe (2007) found a positive impact of CEO duality on the financial performance of Ghanaian SMEs., Bennedsen et al. (2008) also found that the CEO as owner/manager has a positive impact on the Return on Asset (RoA) using the instrumental variable modelling approach based on 7000 close-held firms in Denmark. However, Voordeckers et al. (2007) identified a negative relationship between CEO duality and firm performance using a Belgian sample.

Pugliese and Wenstop (2007) found that the separation of CEOs and chairman of the board positively contributes to the formation of social strategies, a measure of social performance in SMEs. Rashid and Lodh (2011) analysed 769 firm-year observations of 87 firms listed on the stock market in Bangladesh. They obtained a negative relationship between CEO duality and firm financial performance (measured by ROA), but a positive relationship between CEO duality and firm's market performance (measured by Tobin'q) and social performance (measured by firm growth opportunities and risk). Thus, the relationship between CEO duality and firm financial performance is conclusive. Though the research into CEO duality and market/social performance is, at best, sparse, existing literature does shows a positive relationship.

2.4.1.3. Board size

Empirical tests on the impact of board size on firm performance shows a prevailing negative impact in the literature for large corporations; however, there are researchers who challenges this view (Hermalin and Weisbach 2003; Van Den Heuvel, Van Gils et al. 2006; Bennedsen, Kongsted et al. 2008; Adams, Licht et al. 2011). Hermalin and Weisbach (2003) suggest that the rationale is that the agency problem increases within a board when the board becomes too big, in which case the board turns into a symbol rather than a part of the management process. However, Adams, Lichet et al. (2011) reviewed the existing theoretical and empirical literature and found no evidence to support this contention.

Empirical evidence on the impact of board size and firm performance is also mixed in the small business literature (Abor and Biekpe 2007; Bennedsen, Kongsted et al. 2008; Cowling 2008). Using the instrumental variable modelling approach to analyse 7000 close-held firms in Denmark, Bennedsen et al. (2008) found a slightly negative impact of board size on firm performance. However, Abor and Biekpe (2007) and Cowling (2008) found a positive relationship between board size and firm's accounting performance.

2.4.1.4. Board independence

Agency Theory suggests that a majority of independent directors sitting on a board has a positive impact on the firm performance, while Stewardship Theory argues that boards with a low level of board independence, measured by multiple variables leads to higher company performance (Muth and Donaldson 1998). The functions of boards are also different in both theories. In Agency Theory, boards monitor and control the behaviour of the managers. While in Stewardship Theory, boards provide advice and counselling to firms (Arosa, Iturralde et al. 2010).

Kula (2005) found a negative relationship between independent boards and financial performance in their study of a sample of 386 small and non-listed companies in Turkey. Their conclusion was that independent directors bring in extra resources to the firm, which improves their effectiveness and information access as well as the financial performance (Kula 2005). In contrast, Kyereboah-Coleman and Amidu (2008) based on an analysis of Ghanaian SMEs identified board independence and the presence of outsiders on the board. This enhanced the firm's financial performance. In particular, they found that SMEs in the exporting industry benefit more from board independence (Kyereboah-Coleman and Amidu 2008).

Arose et al. (2010) broke down independent directors into two categories, namely unaffiliated independent directors and affiliated directors. They found a negative relationship between board independence and firm performance for Spanish SMEs, though the relationship was not statistically significant. In the correlation analysis, they did find a negative relationship between board independence and financial performance (ROA) as well as social performance (growth). For the affiliated directors, they reported a positive correlation with ROA and negative correlation with growth.

Thus, the empirical evidence on the impact of board independence on the firm's financial performance was conflicting. Few pieces of research were found that analyzes the relationship between board independence and either marketing or social performance.

2.4.1.5. Characteristics of board of directors

A board of directors, as an institutional mechanism, is endogenously determined by the firm's performance (Hermalin and Weisbach 2003). The characteristics of a board of directors, via the board actions, have a causal impact on the firm's performance. Here, the author discussed four characteristics of the board of directors, namely their expertise and experience, the director's gender, tenure, and age.

Expertise and experience

Expertise and experience can impact a board's performance. Abor and Biekpe (2007) found a negative relationship between the board's skills and ROA . However, their analysis shows a positive relationship between management skills and ROA in Ghanaian SMEs (Abor and Biekpe

2007). Ben Hamad and Karoui (2011) analysed the relationship between governance mechanism practices and financial performance of Tunisian industrial SMEs. They found that the expertise of a board of directors has a positive impact on the financial performance of Tunisian SMEs, measured by ROA (Ben Hamad and Karoui 2011). Wincent et al. (2010) analysed the relationship between board network activities and the innovative performance of SMEs. They found that both board diversity and board education can have a positive impact on the innovative performance of SMEs (Wincent, Anokhin et al. 2010).

Hsu, Chen et al. (2012) applied the panel data model to 187 SMEs in Taiwan. Controlling for firm level factors, they found that the higher the CEO's education level, the higher the ROA, though the relationship was not statistically significant (Hsu, Chen et al. 2012). However, their analysis indicates that CEOs with international experience tended to also enhance the financial performance of SMEs.

Gender

Gender is another variable that has been studied. Since male executives tend to dominate board composition in most companies, having female directors on a board can help increase the diversity of the board. According to Agency Theory, the firm's performance should improve as a result. However, a study on Spanish SMEs shows a negative impact of the presence of women on the board for financial performance (Mínguez-Vera and Martin 2011). The authors argue that women tend to propose less risky strategies, which inhibits the firm performance. Moreover, they found that firms with a financial institution as the main stakeholder tend to have female directors on board. They also show that firms with less debt, more assets and larger boards are inclined to have female directors.

Tenure and Age

Hsu et al. (2012) has found a positive relationship between the CEO's tenure and the financial performance of the SMEs in Taiwan. However, Arosa et al. (2012) have concluded that the average of tenure of board of directors has a negative impact on the ROA of Spanish firms. Hsu, Chen et al. (2012) shows that the younger the CEO, the higher the SME's ROA in Taiwan.

2.4.1.6. Board sub-committees

Based on a sample of 386 small and non-listed Turkish companies, Kula (2005) has found a positive impact of board sub-committees on a firm's financial performance. Kyereboah-Coleman and Amidu (2008) have analysed the link between governance and performance of the Ghanaian SMEs. They found that the presence of the audit committee positively contributes to the ROA, but the size and composition of the audit committee has a negative influence on the ROA (Kyereboah-Coleman and Amidu 2008).

2.4.1.7. Board meetings

Arosa and colleagues (2010; 2012) have found that the frequency of board meetings has a positive impact on the ROA of Spanish firms. Wincent, Anokhin et al. (2010) has similar findings that the meeting frequency of the board has a positive impact on innovative performance.

2.4.1.8. Board ownership and compensation

Agency Theory has argued that the board ownership is negatively influenced by the firm's performance (Guthrie et al. 2012). While Stewardship Theory claims that board ownership enables directors to become good stewards (Barontini and Bozzi 2011; Muth and Donaldson 1997).

2.4.2. Managerial ownership and incentives

Managerial incentives include three components, namely managerial ownership, managerial compensation and employment arrangements. Calabrò and Mussolino (2011) analyse the board of director's contributions to the family SMEs' export intensity. They found that board ownership structure has a positive impact on export intensity (Calabrò and Mussolino 2011).

2.4.3. Capital structure

Weill (2008) has analysed the impact of leverage on the performance of small firms in Europe, mediated by the institutional factors. Weill found that leverage negatively affects the efficiency of firms in Belgium, France, Germany, Italy, Norway, Portugal, with Spain as the only exception. However, debt has positively contributed to the efficiency of firms in Germany, Portugal and Spain, but has had a negative impact on firms in Belgium, France, Italy and Norway (Weill 2008).

Li and Armstrong et al. (2012) have found that Australian SMEs use more debt than equity, though it is not cost effective.

2.4.4. Ownership structure

Ownership structure is a further consideration. Calabrò and Mussolino (2011) have found that a concentrated ownership structure positively contributes to the export intensity of family SMEs. This finding is confirmed by Wellalage and Locke (2011) who studied SMEs in New Zealand. They concluded that the ownership concentration is the most important contributor to the financial performance of SMEs and concentrated ownership helps to reduce agency costs (Wellalage and Locke 2011).

2.4.5. Network

Network, a governance mechanism in addition to market and hierarchy, influences the firm performance by its size, age, and mediating effect with board characteristics (Hsu, Chen et al. 2012; Wincent, Anokhin et al. 2010). Below discussed major properties identified in prior literature on business network, including network size, network age, network and board characteristics.

Network size

Wincent et al. (2010) studied the impact of network size on innovative performance of SMEs. They found that the network size alone has a positive and statistically significant impact on SMEs' innovative performance. This result is supported by Hsu, Chen et al. (2012) based on their analysis of SMEs in Taiwan.

Network age

The network age has a positive impact on the innovative performance of the SMEs (Wincent et al. 2010, 2012), meaning that long-standing and well-established networks significantly contribute to innovation in SMEs.

Network and board characteristics

Network and board characteristics have also been examined. When mediated by board diversity and board education, the network size shows a negative impact on the SMEs' innovative performance (Wincent et al. 2010). Moderated by network, Wincent and his colleagues found that there is a "u-shape" relationship between board continuity and innovative performance of large networks; however, the change to innovative performance is fairly flat in small networks (a quasi- straight line) (Wincent et al. 2009).

2.4.6. Summary

The empirical evidence are summarised in Table 2.4.

Table 2.4 Summary of literature on the relationships between corporate governance and firm performance

Mechanisms	Constructs	Agency Theory	Stewardship Theory	Stakeholder Theory	Resource Dependence Theory	Institutional Theory	Network Governance Theory
Board of directors	Board roles	Monitor & control	Advice & counsel		Resource & network	Institution	Network
	CEO duality	—	+		+		+
	board size	—	+		+	+	+
	board independence	—	+		–	+	
	board expertise	+	+		+		+
	board sub-committees	+	+		+		
	board meetings	+	+				
	board ownership	–	+				
	board compensation	+					
managerial incentives	managerial ownership	–	+				
	managerial compensation	+					
	employment arrangements	+		+			
capital structure		+		+			
ownership structure							
auditing		+	+				

2.5. Gaps in existing research and motivation for this study

The limitations of existing research

Research into corporate governance of small firms alone is yet to be established. As such, there is a lack of evidence to conduct a meaningful analysis of comparative studies between corporate governance of small and large corporations. Audretsch and Lehmann (2012) who gathered 37 relevant articles and reviewed the state-of-the-art of research on corporate governance in small and medium sized firms argued that more attention should be given to small and medium sized firms.

The review of the existing literature indicates a number of limitations and gaps in the field. This includes:

i. Corporate governance research has been dedicated to and concerned with issues pertinent to the traditions of American corporations, most of which are listed on the stock market and are hiring thousands of employees.

ii. Most of the empirical literature suffers from a lack of clarity in definitions, for example, policy-relevant small firms or SME, corporate governance, and performance. Differences in the specification of the definitions hamper comparisons in studies. In addition, failing to control for other environmental variables makes it difficult to produce causal conclusions.

iii. Most empirical research is constrained by the availability of data. It is widely acknowledged that collecting data from small firms, in particular the non-listed ones, is extremely difficult.

iv. Refereed journal articles are published in “niche journals”, such as Small Business Economics, Entrepreneurship Theory and Practice, or the Journal of Business Venturing, or in management journals such as the Academy of Management Journal. However, the small business corporate governance research still suffers from being over-shadowed by research in business and economics that applies to larger corporations (Audretsch and Lehmann 2012).

v. Rigorous philosophical and theoretical foundations in existing research are often missing.

This study attempts to fill the gaps identified above and contribute to the literature and practice in a number of ways. The rationale and contribution of this study to the field is described below.

Rationale for this study

In reviewing academic literature and in finding several gaps, a rationale for this study is that:

1. An Australia-focused study will fill in the gaps of the US-Europe dominated small business corporate governance research;
2. Applying a legal definition of small corporations in this study will produce policy-relevant results;
3. A large scale survey of a ‘niche’ interest in corporate governance in Australia will deepen the understanding of small firms’ corporate governance in numerous aspects;
4. Misunderstandings and prejudice toward small firms have to be contested and corrected. Corporate governance is also of great significance to small firms, which comes in the form of financial opportunities, legal feasibilities and flexibilities and improvements in efficiency and productivity.

5. This study will discuss the fit between theories and empirical evidence in Australian small corporations.

2.6. Summary of this chapter

This chapter has reviewed literature on corporate governance theories and the relationship between corporate governance mechanisms and small firm performance. Gaps in the literature have been identified from a cross-comparison and analysis of theoretical and empirical studies. The next chapter will review regulations, particularly those concerned with corporate governance and regulations related to small firms. The reviews here will serve as a theoretical and empirical foundation for a meta-analysis and further development of a conceptual framework outlined in Chapter 5.

CHAPTER 3 LITERATURE REVIEW ON REGULATION AND SMALL FIRM PERFORMANCE

3.1. Introduction

Regulation has drawn attention from both academia and government sector from a host of disciplinary interests including law, economics, political science, management, history, psychology, social administration, accounting and finance (Baldwin et al. 2011). When it comes to the regulation of a firm's behaviour and transactions, different disciplines adopt varied approaches For example; the legal field uses law, Acts and provisions as the main instruments to curb business misconduct and to align diversified interests (Davies 2000). To facilitate self-regulation (Farrar 2008), legal, political and management regulators have developed guidelines to promote good practice in corporate governance (see Chapter 2 for more details). Likewise, accounting professional bodies have established financial reporting and auditing standards to improve the accountability of firms and top-level management, and the banking sector has produced Basel codes to safeguard bank operation and reduce liquidity risks (Brown, Beekes et al. 2011).

This chapter reviews both theories of regulation and academic studies that have focused on the relationship between regulation and small firm performance. In Section One, definitions of regulation are revisited, followed by a discussion identifying the need for regulation and the regulators, the regulation of corporate governance in Australia and the relevance of regulation to small firms.

Section Two critically evaluates theories of regulation. It examines three major types of theories often applied to regulation, which are Forces of Ideas Theory, Interest Theory and Institutional Theory.

Section Three examines six types of regulatory strategies including Coercion, Market-based approaches, Government compensation, Self-regulation, Responsive regulation and Network-based regulation.

Academic studies investigating the impact of regulation on small firm performance are reported in Section Four. Given the broad scope of regulation and the constraints on data availability for small firms, empirical evidence on the relationship between regulation and performance is yet to be established.

The last section summarises the theories of regulation and existing empirical studies on regulation-performance relationships. Gaps are identified and motivations for this study are also summarised.

3.1.1. Definition of regulation

Regulation has been defined in numerous ways to suit the convenience of regulators who design it. Earlier definitions have only focused on the control role of regulators. One dominant approach is to define regulation as a sustained and focused control exercised by a public agency over activities that are valued by a community (Selznick 1985).

The OECD (1997) defines regulation as rules and requirements that governments set forth to regulate enterprises and citizens. This definition specifies detailed categories of regulation, which includes laws, formal and informal orders and subordinate rules issued by governance, non-governmental organisations or self-regulatory organisational associations.

In Australia, regulation follows the OECD (1997) definition but extends to a larger scope. The Chairman of the Productivity Commission of Commonwealth Government of Australia, Gary Banks (2006) defines regulation as (1) a principle, rule or law designed to control or govern conduct of people and business; (2) the way particular regulations are implemented in practice. This definition incorporates not only legislation and formal regulation, but also quasi-regulation, such as codes of conduct and advisory instruments. This definition also provides a broad scope of regulation by adding the implementation of regulatory requirements into the consideration of regulation.

3.1.2. Categories of regulation

Under the Banks (2006) definition, a regulation falls into the following categories:

i. Social and environmental regulation which protects the public interest: (1) Health-related regulation, for example, General practice, Private health insurance, Pharmacy, Therapeutic products and medical devices and Aged care; (2) Labour market regulation, for example, Occupational health and safety, workers' compensation, skills mobility and licensing, business migration, education, childcare, employment reporting; (3) consumer-related regulation, for example, consumer protection, privacy, food regulation, chemicals and plastics, legal administration; and (4) environmental and building regulations.

ii. Economic and financial regulation which intends to secure market efficiency and maintain market order: (1) financial and corporate governance such as. cooperation and coordination between regulators, engagement with industry; (2) tax regulation such as sources and consequences of tax complexity, cumulative and specific burdens of tax compliance; (3)

superannuation regulation such as superannuation guarantees and superannuation taxation; and (4) trade-related regulation such as trade regulations and commonwealth procurement.

iii. Administrative regulations are the paper work and administrative formalities, commonly known as “red-tape”, which are required to facilitate the implementation of regulation in social, economic, financial and environmental aspects.

The regulatory compliance requirements for businesses in Australia includes: commonwealth laws, state and territory laws, local government laws, quasi-regulation, co-regulation and self-regulation (proposed by professional bodies and industry associations). The primary objective for government regulation is to ensure the transparency and accountability of business conduct (PC 2011).

3.1.3. Why regulate?

Motives for regulation, distinct from technical justifications, include monopolies and natural monopolies, windfall profits, externalities, information inadequacies, continuity and availability of service, anti-competitive and predatory pricing behaviour, public goods and moral hazards, unequal bargaining power, scarcity and rationing, rationalization and coordination, planning, human rights and social protection (Baldwin et al. 2011, p. 24) (Table 3.1). According to Baldwin et al. (2011), good regulation should gauge five criteria:

i. The legislative mandate, meaning that the regulatory action deserves parliamentary support and involves great details of interpretation around the implications, implementations and potential unintended consequences;

ii. Accountability, requiring regulators with imprecise mandates to gain support from the public, to whom they are accountable as per democratic institutions;

iii. Due process, which is fair, accessible and open to the public;

iv. Expertise, particularly when information asymmetry is a major concern and the regulatory issues are complex, expert judgment should be exercised; and

Table 3.1 Summary of motives toward regulation

Rationale	Main aims of regulation	Example
Monopolies and natural monpolies	Counter tendency to raise prices and lower output. Harness benefits of scale economies. Identify areas that are genuinely monopolistic.	Utilities.
Windfall profits	Transfer benefits of windfalls from firms to consumers or taxpayers.	Firm discovers unusually cheap source of supply.
Externalities	Compel producer or consumer to bear full costs of production, rather than pass on to third parties or society.	Pollution of river by factory.
Information inadequacies	Inform consumers to allow market to operate.	Pharmaceuticals. Food and drinks labelling.
Continuity and availability of service	Ensure socially desired (or protect minimal) level of 'essential' service.	Transport service to remote region.
Anti-competitive and predatory pricing behaviour	Prevent anti-competitive behaviour.	Below-cost pricing in transport.
Public goods and moral hazard	Share costs where benefits of activity are shared but free-rider problems exist.	Defence and security services. Health Services.
Unequal bargaining power	Protect vulnerable interests where market fails to do so.	Health and Safety at Work.
Scarcity and rationing	Public interest allocation of scarce commodities.	Petrol shortage.
Rationalization and coordination	Secure efficient production where transaction costs prevent market from obtaining network gains or efficiencies of scale. Standardization.	Disparate production in agriculture and fisheries.
Planning	Protect interests of future generations. Coordinate altruistic intentions.	Environment.
Human rights	Protection of weaker citizens.	Discrimination. Embryology.
Social protection	Social solidarity.	Broadcasting.

Source: Baldwin et al. (2011), p. 24

v. Efficiency, where Classical Economic Theory argues that there is always a trade-off between efficiency and social equity in the market allocation mechanism, also known as the 'Marshall dilemma'. Thus, new regulation should produce Pareto-Efficiency Improvements without sacrificing social equity.

3.1.4. Regulation of corporate governance in Australia

The Australian framework for regulation of corporate governance consists of three main components, namely 'hard law', 'soft law' and hybrid (Fig. 1). The hard law corresponds to the statutory regulation – Corporations Act 2001(Cth), which is the primary companies' legislation in Australia. The company law contains a number of provisions that directly and indirectly influences corporate governance in Australian firms.

The 'hard law'

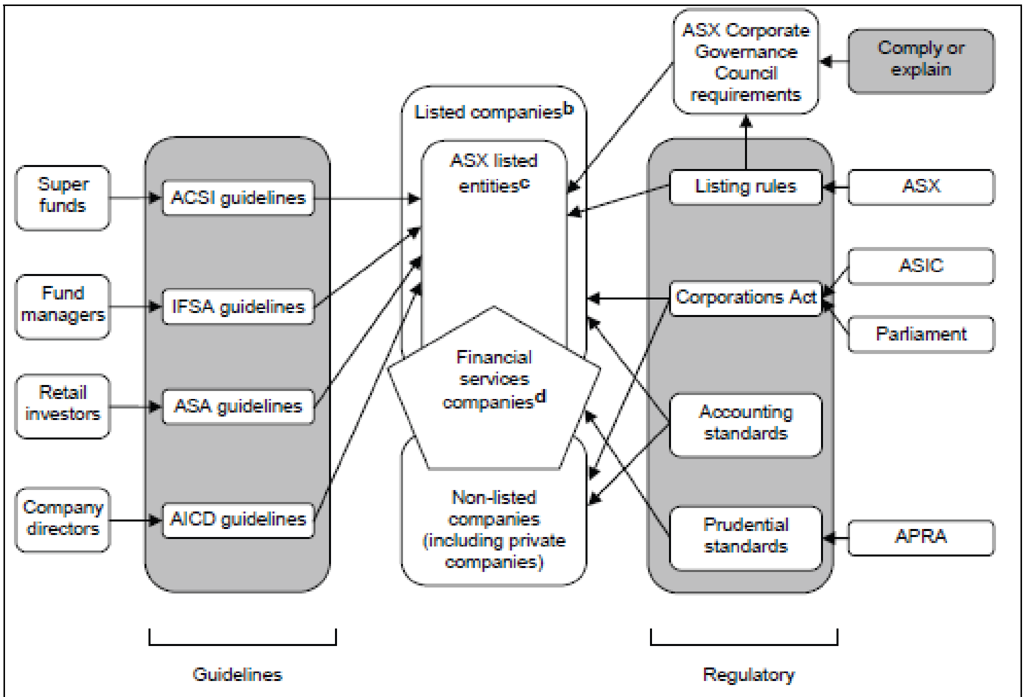
The 'hard laws' include Corporations Act 2001(Cth), statutory regulations other than the corporate laws which focus on the relationship between the company and its various stakeholders who operate and are influenced by the legal rules outside the company law (eg. Industrial relations, tax, environmental law, and banking and finance). Moreover, unlike pure common law based countries such as UK, Australia has judge-made law, in particular when it comes to self-regulation (Farrar 2003).

In order to meet the need of small firms, the consolidated version of the Corporations Act 2001 (Cth) s111J incorporates a section called 'small business guide'. The small business guide applies to proprietary companies limited by shares, which is the most common type of company used by small businesses. The small business guide summarises the main provisions under the Corporations Act 2001(Cth), the regulations made under the Corporations Act and ASIC practice notes, including (1) what registration means; (2) the company structure for small business; (3) setting up a new company; (4) continuous obligations when the companies is set up; (5) company directors and company secretaries; (6) shares and shareholders; (7) signing company documents; (8) funding for the company's operations; (9) returns to shareholders; (10) annual financial reports and audits; (11) disagreements within the company; and (12) companies in financial trouble. Violations incur sanctions accordingly.

The 'soft law'

The 'soft law' includes codes and guidelines published by professional bodies and industry associations as good practice of corporate governance. Businesses adopt the 'soft law' on a voluntary basis. Some 'soft law' serves as benchmarks, while others are developed to shape the internal arrangements and management for better performance.

The hybrid mechanism, also known as 'enforced self-regulation' (Ayres and Braithwaite 1992) occurs where the law delegates to private sector bodies (eg. self-regulatory organisations such as ASX) the task of formulating substantive rules, to which sanctions are attached. The hybrid mechanisms include ASX listing rules, ASX Corporate Governance Principles and Recommendations, Accounting standards, and auditing standards.



[a] Acronyms are as follows — ACSI: Australian Council of Super Investors; AICD: Australian Institute of Company Directors; APRA: Australian Prudential Regulation Authority; ASA: Australian Shareholders' Association; ASIC: Australian Securities and Investments Commission; ASX: Australian Securities Exchange; IFSA: Investment and Financial Services Association. [b] Listed public companies will predominantly be ASX-listed entities. Exceptions are companies listed on other Australian stock exchanges, such as the National Stock Exchange of Australia and the Bendigo Stock Exchange. [c] Most ASX listed entities would be listed public companies in the context of the Corporations Act. Exceptions include some listed trusts and companies incorporated outside Australia. [d] Some APRA-regulated banks and insurance companies would be ASX-listed entities. However many, including credit unions, building and friendly societies, and superannuation funds are not ASX listed.

Fig. 3.1 The Regulatory and Governance framework
Source: Australian Productivity Commission (2009), p. 127

3.1.5. Regulatory reforms in Australia

Major regulatory reforms to governance were inaugurated in Australia since 1995 (Table 3.2). Most of the regulatory reforms summarised in Table 2 endeavoured to reduce red tape, to increase market competition, to review regulatory requirements, and to introduce hybrid forms into the corporate governance system.

Table 3.2 Summary of the regulatory reforms in Australia

Year	Regulation	Comment
1995	National Competition Policy	State and Commonwealth Governments (COAG) agreed that new legislation should not restrict competition
1995	Regulatory Impact Statements	Introduced following the collapse of HIH
1996	Small Business Deregulation Taskforce	Survey by Australian Bureau of Statistics and Yellow pages. Report Reducing Redtape
1998	Regulatory Impact Statements strengthened	
2001	Corporations Act 2001	Commonwealth regulation of corporate law established
1998-2004	Corporate Law Economic Reform Commission (CLERP)	Regulation; fundraising, takeovers, executive remuneration, financial reporting, reporting, shareholder participation
2003	OECD	Report: From Red Tape to Smart Tape
2003	Australian Securities Exchange	ASX introduced Principles of Good Governance and Best Practice Recommendations
2003	Standards Australia International	Corporate Governance Standards announced
2005	COAG further regulatory reforms	COAG introduced new wave of reforms
2005	Victorian Office of Regulation Reform; Victorian Competition and Efficiency Commission	Allocated $42m to programs: Reducing the Regulatory Burden (est. $42b.)
2006	Competitions and Markets Advisory Committee	Corporate Social Responsibility Report
2006	OECD	Report: Cutting Red Tape: National Strategies for Administrative Simplification
2006	Australian Government	Taskforce on Reducing the Regulatory Burden on Business
2007-2010	Productivity Commission	Research Reports of Annual Review of Regulatory Burdens on Business:
2009	National Consumer Protection Bill	Introduced licensing and responsible lending obligations for financial lenders, brokers
2009	Henry Review of Taxation	
2010	Cooper Review	Review of superannuation system.

Source: Armstrong, Li and Clarke et al. (2011), p. 33

3.1.6. Relevance of regulation to small corporations

Small firms often most heavily bear the cost of regulations. From an institutional perspective, small firms are shaped by institutions, while they are constrained by the institutions as well. Given the characteristics of small firms, small firms are far more disadvantaged compared with their larger counterparts; for example, small scale organisations in terms of financial and human capital, have minimal influence on the market, small firms do not have the power to substantially lobby the government for their preferred policies and regulations.

Small firms are often in a far worse situation to their capacity to respond to regulatory requirements, compared to larger companies. Small firms do not have in house experts to handle regulatory compliance requirements. Instead, they would rather hand over regulatory related issues to their accountants and lawyers (Adams et al. 2011). The Australian Productivity Commission (2006) has reported that most executives and senior management teams spend more than 25% of their time meeting numerous regulatory compliance requirements, which hampers them from undertaking their core businesses. Thus, small firms are bearing disproportionate regulatory costs.

3.2. Theories of regulation

There are three major theories explaining regulation, namely: Force of Ideas Theory, Interest Theory, and Institutional Theory.

3.2.1. Force of Ideas Theory

A common framework used to understand regulation is Force of Ideas Theory. In discussing the impact of ideas, ideologies, and beliefs, a number of different line of thought can be detected in the wider literature on public policy and regulation. One line points to changing (party-) political ideologies that shape regulation. This phenomenon has been particularly prominent in discussions regarding 'deregulation' in the US and in wider public sector reforms elsewhere. A second line stresses the inherent plurality of rationalities or worldviews that characterize any debate regarding regulatory instruments. A third line emphasizes the importance of deliberation and conversations (Baldwin et al. 2011).

The ‘Power of Ideas’ approach focuses on the drivers of the design of regulatory instruments. This stresses the importance of the broader intellectual climate that shapes regulatory instruments, and which emphasizes understanding deliberations and discourses, as well as the interactions and communication patterns that operate within regulatory domains and which structure regulatory actions. It is a broad approach that might have difficulties in explaining why certain ideas take root, how ideas can be separated conceptually from interests, and in accounting for the patchiness of ‘deregulation’ (which has led observers to prefer the term ‘regulatory reform’).

In so far as it is conceded that ideas possess a force of their own, however, the ‘power of ideas’ accounts do qualify the economic theory of regulation’s emphasis on the market as the key factor in understanding regulatory progressions. They emphasize the importance of plural rationalities in shaping regulation and they also highlight also the prevalence of fads and fashions in regulatory politics (Baldwin et al. 2011).

The main criticisms toward Ideas Theory are that it may be hard to separate the force of ideas from the role of economic interests.

3.2.2. Interest Theory

Based on whose interests count in the regulatory design, Interest Theory can be divided into two main theories: the public interest theory and interest group theory (Baldwin, Cave et al. 2011).

Public Interest Theory

Public interest theories centre on the idea that those seeking to institute or develop regulation do so in pursuit of public interest-related objectives (rather than group, sector, or individual self-interests). Proponents of regulation are thus seen as acting as benevolent agents for the public interest. The purpose of regulation is to achieve certain publicly desired results in circumstances where, for instance, the market would fail to yield these.

Consistent with such a vision is an emphasis on the trustworthiness and disinterestedness of expert regulators in whose public-spiritedness and efficiency the public can have confidence. It is a vision that implies a highly benevolent view of political processes. It assumes some form of objective knowledge that can establish the presence of ‘market failures’ and that can respond with appropriate instruments.

The ‘public interest’ world is a world in which bureaucracies do not protect or expand their turf, in which politicians do not seek to enhance their electoral or other career prospects, in which decision-making rules do not determine decisions, and a world in which business and other interest groups do not seek special exemptions or privileges. In short, it is a world of few transaction costs and institutional biases. Instead, regulation is based on some form of dispassionate expertise and objective standards. On such a view there can, for example, be a non error-prone and un-slanted statement on whether or not industry is investing in infrastructure in order to protect security of supply. The public interest approach also assumes the possibility of unproblematic enforcement and compliance.

Not surprisingly, a number of problems, theoretical, practical, and political, beset this public interest view of the regulatory process. A first difficulty is that an agreed conception of the public interest may be hard to identify. A further problem stems from doubts concerning the disinterestedness, expertise, and efficiency that the public interest approach attributes to regulators (Stigler 1971).

Interest Group Theory

A second broad approach to regulation stresses the extent to which regulatory developments are driven not by the pursuit of public interest but by the particularistic concerns of interest groups. This approach has most prominently been associated with the so-called 'economic theory of regulation' (often also linked to labels such as private interest, Chicago/Virginia school, public choice, special interest and 'capture' theory).

The economic theory of regulation builds on the assumption that actors are inherently self-regarding and orientated at maximizing their own (material) interest. It assumes that all parties involved in regulation seek to maximize their utility (self-interest) (politicians, for instance, seeking votes to maximize their cash incomes); it assumes that all parties are as well informed as possible and learn from experience; and it also assumes that regulation is costless .

3.2.3. Institutional Theory

Institutional Theory has become such a broad church that it is hard to find anyone who would not claim to be an institutionalist. However, an almost universal agreement that 'institutions matter' does not suggest a consensus on all aspects of institutional behaviour. There are key differences in perspectives on institutions, ranging from those researchers that emphasize the importance of formal rules in shaping behaviour, to those stressing the importance of political rules of the games in shaping diverse actors' behaviours, to those that regard all human action as embedded in their social context. Institutionalists, therefore, do not necessarily agree on where preferences come from, but they do agree on the notion that institutional structure and arrangements, as well as social processes, significantly shape regulation. In other words, there are more issues driving regulatory developments than mere aggregations of individual preferences. Some commentators apply a number of well-worn distinctions between different approaches towards institutionalism.

There are three main strains in the institutionalism literature: those that focus respectively on 'inter-institutional relations' (especially regarding institutional design questions); those primarily interested in 'intra-institutional forces' (especially the evolution of regulatory regimes over time); and those that emphasize the network and 'regulatory space' understandings of regulation (Baldwin et al. 2011).

3.2.4. Summary of regulatory theories

The economic nature of small corporations determines that regulation toward small corporations is a microeconomic policy issue. The market-economy ideology has set force the Australian economy. However, the privilege of lobbying has enabled large corporations to capture the regulatory designs which intend to cater to the public interests. Hence the small corporations may hardly be taken into account in the policy debates unless they are considered as an interest group, to which the regulatory reforms can cater to their interests. Furthermore, relevant to small corporations are the institutional arrangements, which may include inter-institutional relationships design, intra-instructional forces analysis and the interaction between network and regulation.

To sum up, the understanding of small corporations related regulation may require combining the Force of Ideas Theory, the Interest Theory and the Institutional Theory.

3.3. Regulatory strategies

There are mainly six types of regulatory strategies toward firms, covering Coercion, Incentive-based approaches, Government compensation, Self-regulation, Responsive regulation and Network-based regulation (Armstrong, Li and Clarke et al. 2011).

3.3.1. Coercion

The essence of command and control (C & C) regulation is the exercise of influence by imposing standards backed by criminal sanctions. Thus, the Health and Safety Executive may bring criminal prosecutions against occupiers who breach health and safety regulations. The force of law is used to prohibit certain forms of conduct, to demand some positive actions, or to lay down conditions for entry into a sector.

Regulators who operate C & C techniques are sometimes equipped with rule-making powers (as is often the case in the USA). In the UK, however, it is common for regulatory standards to be set by government departments through primary or secondary legislation and then enforced by regulatory bureaucracies. C & C thus involves the setting of standards within a rule; it often entails some kind of licensing process to screen entry to an activity, and may set out to control not merely the quality of a service or the manner of production but also the allocation of resources, products, or commodities and the prices charged to consumers or the profits made by enterprises.

The strengths of C & C regulation (as compared to techniques based, say, on the use of economic incentives such as taxes or subsidies) are that the force of law can be used to impose fixed standards with immediacy and to prohibit activity not conforming to such standards. In political terms, the regulator or government is seen to be acting forcefully and to be taking a clear stand:

by designating some forms of behaviour as unacceptable; by excluding dangerous parties from relevant areas; by protecting the public; and establishing penalties for those engaging in offensive conduct. Some forms of behaviour can thus be outlawed completely and the ill-qualified can be stopped from practising activities likely to produce harm. The public, as a result, can be assured that the might of the law is being used both practically and symbolically in their aid.

C & C regulation is not, however, problem-free and, during the 1980s in particular, a number of North American socio-legal scholars and economists alleged a series of weaknesses. Such concerns were echoed by many politicians on both sides of the Atlantic—particularly those predisposed to doubt the value of governmental rather than market-based modes of influence.

Four main issues relating to the coercion approach is regulatory capture, legalism, standard setting, and enforcement (Baldwin and Black 2008).

3.3.2. Incentive -based approaches

Regulating by means of economic incentives might be thought to offer an escape from highly restrictive, rule-bound, C&C regimes. According to the incentives approach, the potential mischief causer can be induced to behave in accordance with the public interest by the state or a regulator imposing negative or positive taxes or deploying grants and subsidies from the public purse. Thus, not only can taxes be used to penalize polluters, but rewards can be given for reductions in pollution, or financial assistance can be given to those who build pollution-reducing mechanisms into their production or operational processes. An example of such an incentive strategy at the broadest level was the differential tax on leaded and unleaded petrol that was introduced into Britain in 1987.

They are also said to leave managers free to manage. It is up to the regulated firm, not the bureaucrat or regulator, to balance the costs of polluting against those of abatement in a particular context and to devise means of reducing the mischief most efficiently. Managers are, accordingly, able to be more flexible concerning their modes of production than most C & C regimes allow.

Incentive-based regimes are, additionally, claimed to be cheaper to administer than commands and to involve relatively light burdens of information collection and compliance costs. They, moreover, are said by proponents to encourage individual regulated firms to reduce harmful conduct as much as possible (to give an 'incentive to zero'), not merely down to the level that is demanded by the standard stipulated in a C & C regime—a standard liable, in any event, to be fairly lax because C & C regulators tend, for political reasons, to have to set a general standard soft enough to be met by poorer performers in the industry without causing financial crises or unacceptable unemployment.

The advantages of incentive regimes can, however, be exaggerated and a number of cautionary points should be borne in mind. Such systems often have to be put into effect by means of highly complex systems of rules (the field of taxation, for instance, is not one renowned for simplicity). A core difficulty with incentive regimes may be predicting the effect on the ground of a given incentive.

3.3.3. Government compensation

Economic incentives to avoid undesirable behaviour can be created not merely by systems of taxation and subsidy but also by schemes of compensation or insurance that link premiums paid to performance records. One field in which a good deal of research into insurance-based incentives has been conducted is that of the working environment. The compensation may come in a number of ways, for instance, credit guarantee by government agencies to facilitate small firms' accessing to finance.

3.3.4. Self-regulation

Fiscal pressures prevent government to monitor every activity of the corporations in that governments are not able to afford it. Thus, self-regulation becomes a cheaper solution and a more attractive alternative (Braithwaite 1982). Self-regulation can be seen as taking place when a group of firms or individuals exert control over its own membership and their behaviour. In Britain, it is encountered in a number of professions and sports and in sectors such as advertising, insurance, and the press. A host of arrangements can be seen as self-regulatory and variations in the characteristics of self-regulatory regimes can be identified (Baldwin, Cave et al. 2011).

A first variable is the governmental nature of self-regulation. An association may self-regulate in a purely private sense—in pursuit of the private ends of its membership—or it may act governmentally in so far as public policy tasks are delegated to private actors or institutions. Both forms of activity may, indeed, be combined. The process of self- regulation may, moreover, be constrained governmentally in a number of ways—for instance by statutory rules; oversight by a governmental agency; systems in which ministers approve or draft rules; procedures for the public enforcement of self-regulatory rules; or mechanisms of participation or accountability. Self-regulation may appear to lack any state involvement, but in reality it may constitute a response to threats by government that if nothing is done state action will follow. A second variable concerns the extent of the role played by self-regulators. A full role may involve the promulgation of rules, the enforcement of these on the ground, and the monitoring of the whole regulatory process.

Self-regulation, however, may be restricted to one of these functions— where, for instance, rules are drafted by a self-regulatory organization but are enforced and monitored by a public agency. The degree of binding legal force that attaches to self-regulatory rules is a third variable to be noted. Self-regulation may operate in an informal, non-binding, voluntary manner, or it may involve rules of full legal force that are enforceable in the courts. Finally, self-regulatory regimes may vary in their coverage of an industrial sector—they may apply to all those who participate in an activity (perhaps because screening or licensing of entry is applied), or they may cover only those who join an association voluntarily.

3.3.5. Enforced self-regulation for small corporations

Braithwaite (1982) coined the term "enforce self-regulation", which refers to the situation that the regulator imposes a requirement in order to achieve certain policy ends on the business while the businesses responds accordingly by determining and implementing their own rules and procedures. A critical element for enforced self-regulation is its internal control systems of the regulated to achieve the goal of the regulator (Ayres and Braithwaite 1992).

The difference between enforced self-regulation and pure self-regulation is the role regulators play. In self-regulation, it is the industry or firms to be regulated which take the initiative to design the mechanisms as well as implementation (Braithwaite 1982); while for enforced self-regulation, the regulators setup expectations and the regulated design internal mechanisms to gauge the regulators' objectives. However, the self-regulation and enforced self-regulation share some limitations. Both regulatory regimes, for instance, require employees to understand how self-assessment actually works, but the employees may lack the initiative to exercise assessment and control (Fairman and Yapp 2005).

Moreover, small firms may encounter difficulties in implementing the pure self-regulatory regimes, in that the implementation of self-regulation depends on empowering employees, favourable market conditions to motivate employees for self-regulation, knowledge sharing within the company, and capacity for innovation and change, most of which are missing in the small firms (Aalders and Wilthagen 1997; Fairman and Yapp 2005).

3.3.6. Responsive regulation and network-based regulation

Responsive regulation has been recognised as the best way to promote regulatory compliance (Nielsen and Parker 2009). Institutional theorists call for responsive regulation and network-based regulation as more efficient vehicles to enhance the collaboration between the regulators and the regulated in order to achieve certain policy objectives (Braithwaite et al. 2007).

Responsive regulation focuses on designing for more flexible regulatory enforcement (Ayres and Braithwaite 1992). Ayres and Braithwaite (1992) developed a pyramid of regulatory alternatives ranging from deterrent to cooperative regulatory enforcement strategies, where responsive regulation can be interpreted in two ways: tit-for-tat responsive regulation and restorative justice responsive regulation (Nielsen and Parker 2009).

In order to demystify the complexity of responsive regulation, Braithwaite (2011) summarised the essence of responsive regulation in nine heuristics, as follows

i. Think in context rather than to be dominated with a preconceived theory, including the responsive regulation itself. The gist of responsive regulation is to be responsive to the contextual insight rather than to be flexible about the strategic options in the pyramid;

ii. Listen actively and structure dialogue that involves stakeholders and settles agreements around outcomes, monitoring, commitment and motivation;

iii. Engage parties resisting the regulatory requirements, respect them and construe the resistance as an opportunity of regulatory reform;

iv. Praise those who commit to continuous innovation and improvement and help leaders to promote excellence;

v. Support and education are the preferred approach to achieve outcomes and build capacity;

vi. Signal but not threaten a range of sanctions to which you can escalate; signal that the ultimate punishments are formidable and are used when necessary, though as a last resort;

vii. As one move up the regulatory pyramid, engage wider networks of partners for the purpose of the network governance;

viii. Elicit active responsibilities, which mean 'challenging actors to take responsibility for making things right into the future' (Braithwaite 2011; p. 510); when active responsibilities fail, render to passive responsibilities;

ix. Evaluate outcomes and costs for regulatory practice; communicate the achievements and lessons learned.

Network-based regulation, reflected in the partnership principles of Ayres and Braithwaite's pyramidal escalation, provides a cheaper alternative for regulators to escalate to more expensive regulatory options by involving higher level network partners. Those new network partners may potential exert more pressured on the regulated (Braithwaite 2011).

3.3.7. Criticisms of responsive regulation and network-based regulation

The responsive regulatory theory is designed in developed economies, while most of the critiques of it are also framed within the context of developed economies (Black 1997;

Gunningham and Grabosky 1998; Haines 1997; Haines 2003). Criticisms mainly fall into three categories: (1) in practice, it may not be politically feasible for regulators to escalate step by step up the regulatory pyramid; in addition, the "tit-for-tat" responsive regulatory may be wasted if the compliance is driven by industry culture rather than responding to the regulatory requirements; (2) in concept, the more punitive strategies may stand in the way of the voluntary 'self-regulation'; and (3) in principle, responsive regulatory has been criticised for its lack of fairness, proportionality and consistency (Baldwin and Black 2008).

3.3. Empirical studies on regulation and performance of small firms

This study is only able to obtain one study which takes a systematic approach to look into the impact of regulation and performance in companies employing less than 250 staff in the United Kingdom (UK) (Anyadike-Danes et al. 2008). Their study took a new approach, which involves 124 qualitative interviews with small business owners and 1205 small businesses by telephone interview, to analyse the relationship between regulation and small business performance. Their interviews with the 124 small business owners found that regulation generates multiple influences which can be enabling and motivating as well as constraining.

These influences, operating simultaneously, shape the activities of small business owners and other stakeholders whose actions underpin small business performance, regardless of the owner and manager's awareness of such regulations. The impact of regulation on business performance depends on how business owners and other stakeholders respond to specific regulations. Agents' adaptations to regulation, and thus the business performance outcomes that result, depend on firms' internal resources and capabilities, and on the external product, labour and capital market conditions.

The report (Anyadike-Danes et al. 2008) has for the first time introduced the latent variable technique to measure regulation in the small corporation's literature. Their analysis is of significant conceptual and empirical depth to the construct of regulation. However, as they acknowledged, given that they used the subjective instruments, the robustness of which is yet to be tested, they failed to find any explicit relationship based on the multivariate Structural Equation Modelling approach (SEM). The explorative nature also weakened the power of causality testing based on the explorative analysis.

3.4.1. The positive impact of regulation on small firm performance

Proponents of regulation argue that the regulation has economic, social and environmental benefits, including sustaining a stable market economy, protecting the investors, employees, citizens, and the community and maintaining the market confidence and trust for business activities (Radaelli and Meuwese 2009).

Anyadike-Danes et al. (2008) found that business owners vary in their capacity to discover, interpret and adapt to regulation. Those with greater resources – finance, equipment, management capability, workforce knowledge and skills – are better placed to deal positively with regulation.

3.4.2. The negative impact of regulation on small firm performance

Critics of regulation insist that regulations incur unnecessary burdens to small firms, thus impeding start-up, investment, innovation, employment growth, hence affect whole national economic performance (Arnold et al. 2008, 2011; Fiori et al. 2012). Moreover, small firms suffer disproportionately from state regulation and are disadvantaged by the unintended consequences of regulations aimed at large companies (Baldwin and Black 2008; Baldwin et al. 2011).

Anyadike-Danes et al. (2008) found that where businesses lack the resources to develop new practices and products, their capacity to adapt to regulation is constrained. Smaller businesses also vary in the business objectives they seek to achieve and these also shape how they adapt to regulation.

3.4.3. Empirical studies

Empirical studies into the impact of regulation and performance of small firms at the micro-(firm) level can be divided into three strands, namely business burden studies, compliance cost studies, and business decision making and competitive studies (Kitching 2006). Kitching (2006) undertook a systematic review to explore the relationship between regulation and performance of small firms, with a particular interest in the UK.

Business burden studies

The 'business burden' studies normally include quantitative surveys on business owners' perceptions of regulation as a burden or barrier or obstacle or extra cost to business performance (or growth or success). Some studies ask the respondents to rank the regulation amongst all the barriers to business performance. The UK Small Business Service Annual Survey of small businesses incorporated 7,505 businesses, which employ less than 250 employees in the 2004-05 survey, and found that 31% of the owners cite regulation as an obstacle to their business success (Atkinson and Curtis 2004).

Firm size is identified as a mediator constraining the impact of regulation on performance. These studies argue that smaller businesses suffer from greater impact of regulations compared to those in larger corporations (Atkinson and Hurstfield 2004). The main reason is that smaller firms lack the resources and capacity to cope with regulatory requirements, thus regulatory burden is having a more dramatic impact on them. However, other research found a more nuanced relationship: businesses not employing people and micro firms (1-9 employees) are less likely to report regulation as an obstacle to business success. This may because they have not perceived the influence of regulation or they lack the awareness about the loosely defined regulation in the surveys (Carter and Auken 2006; Carter and Shaw 2006). However, studies on regulatory burden have not identified a deterministic relationship between firm size and regulation (Kitching 2006).

Compliance cost studies

Another body of studies attempts to investigate the costs and benefits of regulations. Compliance cost analysis goes beyond a survey of business owners' perceptions on regulation by highlighting and focusing on the importance of time and the opportunity costs associated with meeting regulatory obligations. Given that it is difficult to estimate potential benefits, compliance costs are used as a proxy for business regulation. Compliance costs are normally quantified by calculating various components of regulation related costs, for example, administrative costs, and red-tape. Compliance costs are mainly measured by two methods, time that a business has to spend on meeting regulatory requirements and the dollar value of regulatory costs, or as a proportion of annual turnover (Atkinson and Hurstfield 2004).

A UK study on regulation and paper work found that owners working alone reported that they spend 8.4 hours per person per month on regulation and paper work; while in businesses with more than 25 employees, owners spent 1.8 hours only (Crafts 2006). However, the inverse relationship between compliance costs and business size is not always linear. Some studies have found that the proportionate costs vary amongst the smallest firms. The result may reflect lower regulation awareness among owners of the very smallest businesses (Chittenden et al. 2005; Chittenden et al. 2010).

Business decision-making studies

The regulatory compliance cost analysis, though providing a better proxy of regulatory requirements compared to regulatory burden studies, is subject to limitations in being a static analysis approach. A dynamic approach is adopted in some studies focusing on how regulation generates changes of business behaviour and performance. A UK Household Survey of Entrepreneurship shows that a pervasive anti-regulation discourse in the society is a genuine constraint that influences business start-ups in the UK (Lomax et al. 2007).

Regulation does not have uniform consequences for small business owners. The impact of regulation depends on how the action of other stakeholders including competitors, suppliers, employees, infrastructure providers and regulatory authorities causally influence the behaviour of small firm owners (Blackburn et al. 2002; Tabone and Baldacchino 2003; Kitching 2006; Saridakis et al. 2008).

Various studies argue for the benefits of regulation for small business owners' activities. Tabone and Baldacchino (2003) found that the statutory audit requirements in UK generate benefits to the businesses by disciplining the business owners and protecting the businesses from misconduct. Blackburn and Hurt (2002) argue that employment regulations can benefit small employers by providing guidelines and clarification in setting employment conditions. However, the formalisations of the contractual arrangements undermine the flexibility of existing informal workplace relationships in small firms (Saridakis et al. 2008).

3.4. Gaps in existing research and rationale for this study

As proposed by Anyadike-Danes et al. (2008), '… the conduct of future research seeks to capture some measure of the costs of regulation or administrative burden'. Below summarised the limitations of extant research on regulation and its impact on the performance of small corporations, hence justifies the rationale of this study.

3.5.1. Limitations of existing research on regulation

The following gaps are identified in existing research and practice:

i. Regulatory strategies are designed in an isolated fashion which mainly concentrates on a particular industry, or a specific interest group, for example, corporate governance requirements derived based on listed companies. Due to a lack or unwillingness of communication among regulators, there are overlaps between regulatory requirements promulgated by each regulator, thus incurring significant unintended consequences and negative externality to the other stakeholders. For example, small corporations have to comply with corporate governance requirements according to the Corporations Act 2001 (s45a) in Australia.

ii. A consensus has yet to be reached in practice by the regulators on the definition of small corporations, the definition and measure of regulation, or the regulatory approach toward small firms.

iii. Only financial performance of small firms is considered in the regulatory debate, while social performance has been largely ignored.

3.5.2. Limitations of existing research on the relationship between regulation and firm performance

The existing research, as critically examined by Kitching (2006), suffers from the following limitations:

i. Inadequate conceptualisation of "regulation" and methodological shortcomings encourages superficial and misleading results. In particular, for studies focusing on regulatory burden, the underlying assumption is that regulation has a negative impact on performance. Thus, the study of select methodologies caters to producing expected results.

ii. The impact of regulation on firm performance is yet to be determined. Most research fails to consider the mediating impact of environmental contingencies or a business capacity to adapt to the regulatory requirements.

iii. Existing research largely fails to consider a causal linkage between regulation and performance of small firms. Though Kitching and colleagues (Kitching 2006; Kitching 2007; Anyadike-Danes, Athayde et al. 2008) endeavours to uncover the causal impact of regulation on performance of small firms in the UK, the performance is only measured by business growth and regulation and is derived simply by a data-driven approach in an exploratory way.

iv. The conditions that support a positive impact (or minimise a negative impact) of regulation on performance of small firms is yet to be established.

3.5.3. Rationale for this study

Given the existing gaps identified above, this study makes the following contributions to the field. It does this as:

i. To take a holistic approach toward a better understanding of the relationships among governance, regulation and performance;

ii. To explore regulatory compliance costs in general, rather than focusing on isolated aspects of business in small firms. Note that as small firms have difficulties in being distinguished in their approach to one form of regulation from another, this study adopts a static approach. Regulatory cost in terms of time and dollar value spent on meeting compliance requirements are used as a proxy for regulatory compliance costs;

iii. Both financial and social performance is considered in the analysis. The study goes beyond growth concerns, and focuses on both financial and social aspects of the firms.

v. The role corporate governance and government regulation plays in shaping the financial and social performance is also explored. The study aims to assist in developing a responsive regulatory framework for small business governance and regulation, which calls for better collaboration and communication among regulators and enables small firms to enjoy more efficiency and flexibility in meeting the regulatory requirements.

3.6. Summary of this chapter

This Chapter reviewed the literature on regulation. It first defined regulation, then offered a classification of regulation and a review of the rationale of having regulation. This discussion was followed by a review of the regulation of corporate governance and regulatory reforms in Australia, then of the relevance of regulation to small corporations..

Three major theories of regulation were reviewed, including the Force of Ideas Theory, Interest Theory, and Institutional Theory, all of which are relevant to the regulation of small corporations in Australia.

The regulatory strategies were reviewed, including the coercion, incentive-based approaches, government compensation, self-regulation and its relevance to small corporations. Two recent theories namely the responsive regulation theory and the network-based regulation which synthesise current theories were critically examined,.

Empirical research on regulation and performance of small corporations was also reviewed. Though not much research focuses on the overall impact of regulation on performance of small corporations, sporadic studies found conflicting results on the relationship in focus. Some found a positive relationship (Radaelli and Meuwese 2009), some a negative one (Arnold et al. 2008, 2011; Fiori et al. 2012), and some found no relationship (Anyadike-Danes et al. 2008).

Limitations of the current research on regulation and on its impact on performance of small corporations were analysed, and serve as a motivation for this study. Chapter 4 will discuss the context of the study.

CHAPTER FOUR THE CONTEXT OF THE STUDY

4.1. Introduction

This chapter provides a context to the study. It starts with a discussion of the status quo of small corporations in Australia and their contributions to the Australian economy, and it then provides an analysis of government regulation, corporate governance and the difficulties facing small corporations in Australia. Key terms are also introduced in section 6 with an acknowledgement in Section 7 acknowledged of the research support from the ARC Linkage project team. The chapter concludes with a summary of the context of small corporations in Australia.

4.2. Small corporations in Australia

Small corporations are those with less than 50 shareholders and which meet at least two of the following criteria: they have consolidated revenue of less than $25 million per year, gross assets of less than $12.5 million, and fewer than 50 full-time employees. This definition derives from s45A(2) Corporations Act 2001 (Cth) (Corporations Act 2001 (Cth) s 45 2001). Under this definition, ‘small corporations’ make up the vast majority of the Australian market ─ some 1.38 million companies ─ and are vitally important in economic, social and cultural contexts. They employ more than five million members of the Australian workforce (Armstrong, Li and Clarke et al. 2011). Small corporations have been referred to as the ‘engine room of the Australian economy’ (Clarke 2007).

While the Act has a clear definition, both regulators and scholars are yet to agree upon a simple definition of a small corporation. They do agree though that small corporations encompass a wide range of entities: one-person firms, family businesses, SMEs (small and medium enterprises), and small proprietary companies.

Small businesses are the engine room of the Australian economy. Demographics speak of the widespread impact that small businesses has on economic growth. During 2008-09, there were 1.96 million small businesses actively operating, accounting for 95.20% of all businesses; 0.75 million small businesses were employers, accounting for 88.39% of all businesses providing employment; small businesses employ 4,764,000 people in Australia, taking up 47.65% of total number of people been employed; 293,681 small businesses entered the market, equivalent to 99.20% of the total number of business entries; 311,227 businesses exited the market, accounting for 98.74 of the total number of business exits (ABS 2010).

In monetary terms, small businesses are the backbone of the Australian economy. Small business generated $772,057 million income from sales and service, accounting for 31.85% of all the salary and service income; small business paid $116,386 million for wages and salaries, accounting for 29.57% of all the wages and salaries paid economy-wide; small businesses generated $109,264 million operating profit before tax, accounting for 40.17% of profit generated by all the businesses; small businesses contributed $290,348 million value-added to the economy, accounting for 34.46% of the total value-added generated by all businesses (ABS 2010) .

Evidence from the longitudinal data analysis of small businesses in Australia

To the best knowledge of the author, there are two major longitudinal datasets with some bearings on small businesses in Australia, one is the ABS Business Longitudinal data, and the other is the Comprehensive Australian Study of Entrepreneurial Emergence data. The formal is more focused on understanding the productivity, efficiency and innovation determination; while the latter is solely focusing on start-ups and the publications available are mainly descriptive in nature.

Li et al. (2011) applied the ABS Business Longitudinal Data 2005-07 to analyse the financing behaviour of small businesses and found that: (1) financing has significantly positive impacts on the performance of small businesses in Australia; (2) equity and debt financing are used as alternatives, comparatively, equity financing is preferred; (3) capital purchases are largely funded by debt financing, while non-capital purchases and salary expenses are funded by equity financing; and (4) equity financing is more often used by firms with increasing capital purchases and declining non-capital purchases, while debt financing is used by firms with the opposite trends. However, the paper also found that there are more financing needs than offers which may be supplied by financial institutions or government agencies, hence exists an unmet needs for small business financing.

4.3. Government regulation

Despite the impact small business has on the economy, small business has largely been ignored in recent governance and regulation reforms in Australia. Due to the resource constraints, in particular a lack of access to finance and lack of in-house experts, small businesses are not benefiting from the spill-over effect of the policy reforms, rather they are bearing more unnecessary compliance burdens (Clarke 2007). Thus, it becomes an imperative task for scholars to understand and to build the evidence base so as to understand how small businesses are actually performing in Australia (Clarke 2007).

Government and their regulators, legal and economic theorists and others like to portray regulation as benign and helpful to business. A common depiction is that regulators are the friends and the guide of the start-up and small corporations, with regulation being viewed by the regulated as a necessary evil - the cost of doing business (Kitching 2006). For many small business owners, the time and resources spent dealing with regulation is time spent away from core business.

The US scholar Robert Summers (1971) identifies regulation as a 'technique element' of the law. He refers to five 'technique elements' or basic approaches in law. One of these is the administrative-regulatory approach. As Farrar notes in summarising the model (2010, p.39):

> '*it basically exists to regulate wholesome activity rather than prohibiting anti-social forms of behaviour. It is designed to operate preventively before a grievance has arisen*.'

There are, in turn, three basic steps which taken together comprise the administrative-regulatory approach. They are: first, the adoption of a set of regulatory standards; second, relevant communication with the whole of the regulated cohort; and third, taking measures to ensure compliance with the set of regulations (Farrar 2010, p. 49-50).

The roles played by the leading federal regulators Australian Securities & Investment Commission (ASIC), Australian Competition and Consumer Commission (ACCC), Australian Taxation Office (ATO) and Australian Prudential Regulation Authority (APRA) respectively reflect this basic law paradigm in regulating the corporate sector in Australia.

4.3.1 Legal and economic approaches to regulation

Regulation involves both economic and legal theories relevant to the firm and the market. Despite the approaches offered by free market economy advocates such as Summers (1969), it can be argued that more work has been done in relation to economic theories in this regard. Theory of the firm scholarship dates back to R.H Coase whose work has taken on wide international application (1932). Coase's work can be applied to all firms given that his definition of the firm in modern economic theory is an organization which transforms inputs into outputs. This definition is so broad as to capture micro as well as behemoth organizations.

The law, in so far as modern Australian regulation is concerned predominantly reflects a 'large firm' view of the world. The law also operates at a national (rather than international) level, with distinctive border and jurisdiction issues at play. In contrast, economics is a much more international and integrated project. The Corporations Act 2001 (Cth) (Corporations Act 2001 (Cth) 2001) provides a complex scheme of regulations designed for large (Mroczkowski and Tanewski) firms. It is predicated on the assumption of firms possessing in-house expertise, or being able to access the same via lawyers, accountants and other compliance experts. There are some references (ie. Section 45) to small corporations in the Act such as on the sole director firm and guides for small businesses, but the Act is overwhelmingly complex, and this makes it far more difficult for a small firm to comply with it.

4.3.2 Regulation and law reform

Even the law making and law reform process in modern Australia is likely to be dominated by reference to a firm's resources. In the recent debates on the mining tax, the three biggest mining firms were given the opportunity to negotiate directly with senior members of the Government. As such, they gained special rights to seek to resolve the political impasse at the Federal level. This exclusive club was apparent in public-political terms that second tier and third tier firms resorted to complaining loudly, and to being shut out of the process. In regulation and regulation reform, the law appears instinctively to stratify the market into layers relevant to firm size and political capacity.

This reflex towards big business works against the interests of many small firms who lack political resources. A double bind is that the regulations operate in effect as a contract between an individual firm and the State. This means that small, resource stretched firms are atomised and isolated in their dealings with regulators and the complex matrix of regulation. From a legal perspective, the phrase ‘regulatory burden’ has real resonance for most small corporations, as they struggle to compete in the national ‘regulatory politics.’ (Milhaupt 2004, p.232). As Milhaupt (2004, p.240) notes, “cross industry (‘peak’) associations and industry organizations provide a forum for negotiations with political agents and constrain the actions of individual member firms.”. It is this balancing act between speaking with one united voice, and actually being heard by Government, which neatly describes the role of COSBOA, and other peak bodies, in the law reform arena.

4.4. Corporate governance in small businesses in Australia

Corporate Governance in Small Business

Governance refers to the decision-making and control exercised by the boards of organisations. Although the term “Corporate Governance” is universally recognised, there is no one acceptable definition of its usage. It is essentially about the control and direction of companies, exercised by their directors and those holding power and authority.

In general, corporate governance is concerned with the structures and processes for decision-making, accountability, control and behaviour at the top of organisations. Corporate governance is especially concerned with holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as closely as possible the interests of individuals, corporations and society (Cadbury 2000).

Numerous guidelines and standards for good governance have been developed. For the most part they are directed at ‘big’ corporations. Decision-making refers to all those matters which affect the vision, performance and long term sustainability of an organisation. The lean governance structures in small business mean that decisions can be quickly made and implemented.

Governance of small businesses is mainly concerned with improving the performance and allowing the commensurate benefits to flow to stakeholders such as owners and employees. (Burgess et al. 2009). Due to the particular characteristics of small businesses, the ways they deal with issues relating to corporate governance are different from larger businesses. Many are not interested in economic growth, rather survival on a day-to-day basis and to provide the owners and their employees with a comfortable living (Scupola and Kubon 2005).

However in many small businesses only one or two individuals, mainly the owners and/or managers, make critical decisions on finance, accounting, personnel, purchasing, processing or servicing, and marketing. They sell products and services without the aid of internal specialists and with specific knowledge in only one or two areas. For most small businesses, governance is a combination of the views of the owners and the manner in which they run the business (Burgess et al. 2009)

Much of the debate in academic literature on governance has centred on the separation of the roles of Chair and CEO, the appointment of independent directors, and more recently, the diversity of board members (Adams et al. 2011). The arguments for separation of the Chair and CEO are drawn from agency theory. The argument is that there is a separation of ownership from control of companies leading to a conflict of interests between owners and managers. Based on the same theory is the requirement for the performance of boards and management to be assessed, and that this is a role for shareholders. As most small businesses are owner managed or family owned, this argument is often irrelevant to small businesses, until the second or even third generation of their businesses. Where agency theory could apply is when the business has a combination of inside owners and smaller outside investors. The minority shareholders could be disadvantaged if resources were directed to the advantage of the families and disadvantage of the other investors.

Diversity on boards has also been explored. Research shows that even in large companies, diversity in terms of gender, age and nationality is poor (Calvert Investments, 2013). Research into small businesses has found that in the past women's contribution to the businesses was not recognised and that, unlike male family members, they were not groomed nor given the same opportunities to learn to be leaders of small businesses (Barrett and Moores 2009). In relation to the above issues, independent boards and independent directors are seen as essential for achieving transparency and accountability in large companies. In small companies, a board and independent directors are not regarded as a value but as a cost that is unaffordable to a small business.

Regulation of corporate governance

Regulation of the governance of small business is largely captured in the Corporations Law. However, companies listed on the securities exchange also must meet the ASX Guidelines for Corporate Governance. Many professional associations, as well as Standards Australia International, have published guidelines on standards of best practice (Armstrong 2004). While these regulations are not supported by law, their compliance is usually required for membership of the issuing body, such as listing on the Australian Securities Exchange (ASX) or membership of National Institute of Accountants (NIA) or Chartered Professional Accountants (CPA).

4.5. Governance and regulation of small corporations in Australia: status quo and challenges

Small corporations were severely affected by the 2008 global financial crisis (ADB 2009). The Asia Development Bank (2009) report observed that export-oriented sectors were the direct victims of the financial turmoil in the respective industries. The “contagion effect” spilt over to other sectors on the same supplier chain in the same industry. Making matters worse, in response to the economic downturn, the access of small corporations to credit has been particularly restricted. On the one hand, small corporations lack sufficient funding for innovation and technology advancement and, on the other hand, fierce competition on both domestic and global markets demands the constant upgrading of technology. Such a dilemma puts small corporations in a disadvantaged position. In addition, heavy taxation burdens, red-tape and regulatory compliance pressures have also been challenges to the growth of small corporations (PC 2008).

A pilot survey was designed to understand the status quo of the governance and regulation of small corporations in Australia as well as the challenges facing them. During the aftermath of the 2008 Global Financial Crisis, Armstrong et al. (2011) interviewed seventeen CEOs of small corporations and nine directors of small business associations in Victoria in 2010 by a semi-structured interview schedule. The interview served partly as the foundation for the design of the questionnaire for this study.

The interview found a few themes, including industry, business development stage, sources of advice about regulation, cost on meeting regulatory compliance requirements, different types of regulatory compliance requirements, types of difficulties facing business operation, succession planning, role of different stakeholders in the decision making process and the corporate governance of small corporations or small business members.

The small corporations involved in the interview are mainly in the professional service industry (Armstrong et al. 2011). The small corporations are mainly at the growth-stage, established stage or expansion stage. The majority of the small corporations do not have a board of directors; neither do they have a strategic plan.

The regulatory compliance requirements mainly come from the Corporations Act 2001 (Cth) which is administered by the Australian Securities and Investment Commission (ASIC), recording keeping for tax purposes (ie. Goods and Services Tax or GST), Directors' duties, information disclosure, Occupational Health and Safety (OHS), Superannuation management, workplace relationships, maternity leave, quality assurance for products and services, and environmental protection. The small corporations from their interview, in particular those from in the service industries, call for stricter regulation toward the monopolies in the industry and the electricity, water and petrol industries.

Their study found that the regulatory compliance requirements are mainly obtained from lawyers, accountants, industry associations, government agencies and other stakeholders such as employees or business partners. The majority of the small corporations simply hand over their regulatory issues to their lawyers and accountants, who requires extra cost to the small corporations and divert their attention from performing their core business. The small corporations estimated that, on average, each firm spent about $5,000 on meeting the regulatory compliance requirements.

The small corporations found that there are six key stakeholders that influence their decision making in small corporations in Australia, namely customers, suppliers, employees, investors, philanthropy and environment.

The pilot survey and interviews found that small corporations in Australia face seventeen types of difficulties which incur extra costs to the business operations, including access to financing (ie. Collateral required or availability of funding for small corporations), cost of financing in terms of interests and charges, contract violation by customers and suppliers, cost of electricity, cost of transportation, access to land, title or leasing of land, rates of taxation, tax administration, customs and trade regulations, business licensing and permits, labour regulations, skills and education of available workers, uncertainty about regulatory policies, compliance with new laws, anti-competitive practices of competitors and Trade Practice Act.

4.6. Definitions of key constructs used in this study

Small corporations

In order to provide a policy relevant definition, this study adopts the definition of small corporation derived from s 45A(2) Corporations Act 2001 (Cth). Small corporations are those with less than 50 shareholders which meet at least two of the following criteria:

i. consolidated revenue of less than $25 million per year;

ii. gross assets of less than $12.5 million; and

iii. fewer than 50 full-time employees.

Corporate governance

Given that the stakeholder theory has more relevance to the role that firms play in the economic society, this study adopts the du Plesis et al (2010, p.10) definition, which describes corporate governance as:

> *The system of regulating and overseeing corporate conduct and of balancing the interests of all internal stakeholders and other parties (external stakeholders, governments and local communities) who can be affected by the corporation's conduct, in order to ensure responsible behaviour by corporations and to achieve the maximum level of efficiency and profitability for a corporation.*

Regulation

This study adopts the Banks' definition in the Regulatory Taskforce report (2006) that regulation is (1) a principle, rule or law designed to control or govern conduct of people and business; (2) the way particular regulations are implemented in practice.

Financial performance

Financial performance is defined as the accounting measures for the financial performance of a small firm, total sales, total assets, net profit. Firm growth is also captured by using total sales growth and net profit growth (Heugens, van Essen et al. 2009).

Social performance

Social performance is defined as the extent to which firms consider the interests of other stakeholders, as suggested by the corporate social responsibility studies, including customers, suppliers, competitors, investors, and community (Chen and Delmas 2010).

4.7. Summary

This chapter has provided the context of the study on governance and regulation of small firms in Australia. The role of small firms as the engine room of the Australian economy was first explored through a summary of the evidence on the contribution of small firms to employment, percentage of overall employers within the larger Australian economy, and their economic value-added. The important role of small businesses in Australia was revealed in a range of statistics.

With reference to the economic and social importance of small business to the Australian economy, it was argued that small firms have been a forgotten market player in public policy. Of the many barriers facing small firms, failure to catch up with the corporate governance practice and failure to cope with the government regulation in various forms was discussed. The last sections provided working definitions of corporate governance, regulation, financial and social performance, which will be the main focus in the conceptual framework development in the next chapter.

CHAPTER FIVE ADOPTING THE EVIDENCE-BASED APPROACH TO DEVELOP A CONCEPTUAL FRAMEWORK

5.1. Introduction

Based on the literature review of corporate governance and performance of small firms in Chapter Two, and regulation and performance in Chapter Three, this chapter develops the conceptual framework. Statistical hypotheses are established based on a series of meta-analyses, whenever applicable. The meta-analysis is a rigid evidence-based approach and it systematically synthesizes prior empirical research results on the relationships in focus. The conceptual framework covers six main relationships, namely corporate governance and financial performance, corporate governance and social performance, regulation and financial performance, regulation and social performance, corporate governance and regulation, financial performance and social performance.

5.2. Methodology for developing the conceptual framework

Given that the investigation into the relationship between corporate governance, regulation and firm performance warrants policy significance, an evidence-based approach, including systematic review and meta-analysis, will be adopted to develop the conceptual framework. The systematic review and meta-analysis are applied here so that evidence from existing literature can serve as a basis for statistical hypotheses. Thus the focus for this chapter is to develop statistical hypotheses based on the evidence-based approach rather than to provide summative inferences on the statistical hypotheses.

5.2.1. Evidence-based approach

Evidence-based research originated in medical and health research. It has been used to assess the impacts of interventions, with evidence informing decision making. It has drawn an increasing interest of researchers and policy decision makers in the past two decades. Evidence-based practice can be broadly defined as a process that uses rigorous and tested evidence in the design, implementation and refinement of policy to meet designated policy objectives, whilst placing transparency and accountability in the centre of whole process.

The broad definition stresses three characteristics of evidence-based practice, namely (1) evidence should be broad, tested, rigorous, and ideally capable of replication; (2) evidence should be robust and avoid common methodological pitfalls; and (3) the entire process should be transparent and contestable (PC 2010). Former Australian Prime Minister Kevin Rudd expressed a uninformed version of the definition for evidence-based policy. He suggested that the task of evidence-based practice is to provide a 'rational' or 'objective' guide to decision-making, unswayed by the distorting influences of tradition, private interest, ideology, or the personal biases of those in power (Argyrous 2009).

The 'evidence-based movement' was fuelled by new policy developments in the UK, and was heralded by the then Blair-led Labour Government and its establishment of the UK Centre for Evidence Based Policy and Practice as well as the Economic and Social Research Council (Marston and Watts 2003). Blair's philosophy of 'what counts is what works' has triggered debate in UK, Europe, US, Canada, Australia and New Zealand on more effective public governance. These two agencies, together with the Cabinet Office Centre for Management and Policy Studies, have clear and extensive funding commitments toward evidence-based practice and training of the relevant expertise. Bush and Obama administrations in the US also joined the movement by the designating the Office of Management and Budgeting in the White House to undertake the evidence-based evaluation for government funded projects.

Leigh (2009) and the Australian Productivity Commission (2009) articulated a set of tools that decision-makers can use to evaluate the best available evidence, including

i. Existing evidence, eg. systematic review, meta-analysis, confirmed theories;

ii. Experimental evidence, eg. randomised policy trials, quasi-experimental studies, pre-post analysis;

iii. Quantitative evidence, eg. cost-benefit analysis, General Equilibrium modelling, statistics, surveys, performance measures;

iv. Qualitative evidence, eg. qualitative research, observational studies, case studies;

v. Descriptive evidence, eg. expert opinion, anecdote.

Evidence-based practice has also attracted criticisms, including (1) selection bias, the evidence is gleaned from only published reports and journal articles, while unpublished ones are ignored; (2) research evidence, ultimately a social construct, can never be objective; and (3) evidence-based research may be a threat to the research independence, given its preference for practicality and policy pertinence (Argyrous 2009).

Acknowledging its limitations, evidence-based approach has enjoyed popularity amongst government departments and agencies in Australia, for instance, the Queensland state government, Productivity Commission and Australian Bureau of Statistics. However, there is still a gap in using an evidence-based approach to facilitate decision making in governance and regulation related issues of small firms. To date, this is the first study to explore the hard evidence base in the Australian context toward small firms.

5.2.2. Systematic review

Systematic review, an evidence-based approach, attempts to identify, appraise and synthesize all the empirical evidence that meets pre-specified eligibility criteria to answer a given research question. Researchers conducting systematic reviews use explicit methods aimed at minimizing bias, in order to produce more reliable findings that can be used to inform decision making (Cochrane 2011). Compared to a traditional narrative review, the systematic review identifies all the available and accessible literature and synthesizes the evidence, exempting the literature review from subjectivity and selection bias.

Criticisms toward systematic review include reporting and publication bias, selection bias and language bias. The reporting and publication bias mainly comes from the investigators and journal editors/reviewers. The selection bias is due to the inclusion of publicly available literature, including both published and unpublished work. Only literature written in English is reviewed.

5.2.3. Meta-analysis

Meta-analysis, a summative method of systematic review, is the analysis of the original data from a number of different studies after it has been pooled into a single dataset and after accounting for differences in the research designs, number of subjects, size of effects and confidence intervals. Such pooling of a large number of small studies increases statistical power and avoids the issue of 'vote counting'. The ability to conduct meta-analysis within a systematic review is touted as one of the major strengths of the systematic review strategy and has contributed to the positive view of systematic reviews and their adoption by other disciplines (Cochrane 2011).

The application of meta-analysis rests on two pre-requisites, namely the study has to be empirical and there should be more than one studies focusing on the same relationship (Cochrane 2011). Given the nature and availability of the data, the meta-analysis is used only when these two conditions are met.

5.2.4. Meta-analysis procedure

The procedure of meta-analysis includes sampling, selection criteria for the inclusion of studies, coding of the effect sizes and the computation method.

Sampling

To identify the population of studies on board size and performance of small firms, the author used five complementary strategies, suggested by (Van Essen and Van Oosterhout 2008; van Essen, Oosterhout et al. 2012). First, six databases were searched using key terms, “board”, “board of directors”, “board size”, “board characteristics”, “governance”, and “corporate governance”, married with “SMEs”, “small and medium-sized enterprises”, “small firm”, “small business” , “non-listed firm”, “non-listed business”, “family business”. The databases include (1) JSTOR; (2) ProQuest ; (3) ABI/INFORM Global; (4) EconLit; (5) SSRN; (6) Google Scholar. Second, the manually searched the most relevant journals in the fields of accounting, economics, finance and management, suggested by the Australian Research Council’s ERA Ranking. Third, top journals in the field of Entrepreneurship and Small Business Management were searched, eg. Journal of Business Venturing, Entrepreneurship: Theory and Practice, International Small Business Journal, Entrepreneurship and Regional Development, Small Business Economics, Journal of Small Business Management and Family Business Review. Fourth, top journals in the field of Governance were searched, eg. Journal of Business Ethics, Corporate Governance: An International Review, Governance: An International Journal of Policy, Administration and Institutions. Fifth, after collecting an initial set of studies, a “snow-balling” technique was used to cross-check the reference that cited the original journals using Scopus and Google Scholar. This yielded an initial sample of 81 papers. Given that the research focus is on the correlation of board size and firm performance, each article was checked against five criteria, specified as follows:

(1) The paper is not an earlier version of another paper included in the sample;

(2) The paper is an empirical study that includes either a regression or a correlation analysis, as long as the impact size is estimable;

(3) The sample used in the empirical research must be a cohort of small firms, or have a small firm cohort, whose effect size are reported separately and can be obtained. Thus, the sample includes small business, Small and Medium-sized Enterprises (SMEs) and family SMEs;

(4) Board size must be a separate variable and must be identifiable;

(5) The full text of the article must be obtainable.

Coding and analysis

Two main types of data are encountered in the sample: correlation coefficients with sample size and regression results (either a t-statistics or p-value) with sample size. A commercial coding package, Comprehensive Meta-Analysis was used. The build in functions and consistency in correcting estimation errors exempt the coding from human calculation errors. HOMA procedure is computed in STATA12SE environment. Observation with missing values is dropped.

HOMA procedure

Pearson product-moment correlation coefficient r and partial correlation coefficient $r_{xy,z}$, are commonly used in meta-analysis, given that they are scale-free, can be easily interpreted and computed, using the HOMA procedure in STATA. In the study, where multiple measures of firm performance are provided, all the available measurements from the sample were included in the study. In order to account for the differences in precision across effect sizes and variability in the population, the HOMA procedure was adopted (Hedges and Olkin 1985), which treats the inverse variance weight w as the optimal measure of precision for a given effect size. These weights will help to produce appropriate estimate for the meta-analytic mean effect size (van Essen, Oosterhout et al. 2012). The HOMA procedure will be used to produce the summative results of the relationships in focus.

5.2.5. Characteristics of primary studies

Key terms used in the meta-analytic procedure are defined in Table 5.1.

Table 5.1 Description of key terms

Terms	Description
ID	A unique serial number assigned to each article
Author-year	Author(s)-year published/publicly available
N	Number of firm-year observations
Type of firm	Types of firm in focus, eg. small firm, SMEs, family firm
Published	Published work = 1, unpublished work = 0
year	Year published/publicly available
Cross-sectional	Type of data used in the analysis, Cross sectional data = 1, Otherwise = 0
Data collection	Data collection method, eg. survey, interview, database
Country	Country in which the sample was drawn
Data-year	Year in which the data was collected for the given sample
Measurement of CFP	Accounting measurements, eg. ROA, ROE, ROI, share price, market-to-book ratio, operating cash flow, R&D (van Essen et al. 2012)
Measurement of CSP	Owner/manager's perception of strategic performance, stakeholder involvement, board performance, internationalisation and growth opportunities (Orlitzky et al. 2003)
Methodology	Methodology used in the analysis, eg. Ordinary Least Squares, Panel data regression, Hierarchical regression

The most important study characteristics, eg. Author-year, study sample size N, type of the firm, published work or not, year published/publicly available, cross sectional data or panel data, country in which sample was drawn, year in which data was collected, measurement of corporate financial performance ,measurement of corporate social performance (CSP), and analytical method(s), are listed in Table 5.2 5.

Table 5.2 Summary of Studies included in the Meta-analysis

ID	Author-Year	N	Type of firm	Published	Year	Cross-sectional	Data collection	Country	Data-Year	Measurement of CFP	Measurement of CSP	Methodology
1	Abor and Biekpe(2007)	720	SMEs	1	2007	0	Annual reports	Ghana	1998-2003	ROA		GLS
2	Arosa, Iturralde and Maseda(2010)	369	Nonlisted family SMEs	1	2010	1	Survey	Spain	2007	ROA	Growth opportunity	OLS
3	Arosa, Iturralde and Maseda(2010b)	586	Nonlisted firms	1	2010	1	Survey	Spain	2007	ROA	Growth opportunity	OLS
4	Arosa, Iturralde and Maseda(2012)	307	SMEs	1	2012	1	Survey	Spain	2007	ROA	Growth opportunity	OLS
5	Bennedsen, Kongsted and Nielsen(2008)	6850	SMEs	1	2008	1	Survey	Denmark	1999	ROA		IV
6	Borch and Huse (1993）	104	Joint stock small hotels	1	1993	1	Survey	Norway and Sweden			Professional motivation	OLS
7	Brunninge, Nordqvist and Wiklund(2007)	889	SMEs	1	2007	0	Telephone interview	Sweden	1997-2000		Strategic performance	Hierarchical Regression
8	Calabrò and Mussolino(2011)	101	Family SMES	1	2011	0	Survey	Norway	2003/04, 2005/06		Export intensity	OLS
9	Cowling(2003)	427	Small firms	1	2003	0	Survey	UK	1995		Productivity	OLS
10	Di Pietra et al.(2008)	568	Listed companies	1	2008	0	Database	Italy	1993-2000	Share price		Panel OLS
11	Dickson (2011)	2054	SMEs	1	2011		Survey	Multiple			Uncertainty, export intensity, entrepreneurial orientation	Hierarchical Logistic Regression

ID	Author-Year	N	Type of firm	Published	Year	Cross-sectional	Data collection	Country	Data-Year	Measurement of CFP	Measurement of CSP	Methodology
12	Eisenberg, Sundgren and Wells(1998)	879	SMEs	1	1998	0	Database	Finland	1992, 1994	ROA		OLS
13	Fiegener(2005)	2382	small private corporations	1	2005	1	Survey	USA			Board strategic participation	Logistic regression
14	Gabrielsson and Winlund (2000)	302	SMEs	1	2000	1	Survey	Sweden	1997		Board performance	OLS
15	Gabrielsson(2007)	135	small companies	1	2007	1	Survey	Sweden	2000	Sales growth, ROE	Export activity, high-tech production	Correlation analysis, OLS
16	García-Ramos and Olalla(2012)	539	family business	1	2012	0	Database	Spain, Portugue, Italy	2001-2007	Tobin's Q		IV GMM
17	García-Ramos and García-Olalla(2011)	539	family business	1	2011	0	Database	Spain, Portugue, Italy	2001-2007	Market-to-book ratio		IV GMM
18	George, Wiklund and Zahra(2005)	889	SMEs	1	2005	1	Survey and interview	Sweden	1997, 2000		Scope of Internationalisation	Zero-inflated Negative Binomial Regression
19	Gul, Srinidhi and Ng(2011)	1226	Non-financial companies	1	2011	0	Database	Multiple	2002-2007	Stock price informativeness		IV, Panel data regression
20	Hamad and Karoui(2011)	50	SMEs	1	2011	1	Survey	Tunisia		ROS, ROI, ROE		OLS

ID	Author-Year	N	Type of firm	Published	Year	Cross-sectional	Data collection	Country	Data-Year	Measurement of CFP	Measurement of CSP	Methodology
21	Hansson, Liljeblom and Martikainen(2011)	404	family SMEs	1	2011	1	Survey	Finland	2009	ROI		OLS
22	Ho, Wu and Xu(2011)	719	Electronics companies	1	2011	0	Database	Taiwan province of China	2001-2005	ROA		OLS
23	Hsu, Chen and Cheng(2012)	187	SMEs	1	2012	0	Database	Taiwan province of China	2000-2009	ROA	Scope of Internationalisation	Panel OLS
24	Hung and Chen(2009)	496	Listed SMEs	1	2009	0	Database	Taiwan province of China	1999-2006		Effects of internal ownership on firm value	Threshold regression, Morck, Shleifer, and Vishny's model
25	Huse et al.(2011)	347	Small firms	1	2011	1	Survey	Norway	2004		Board performance	OLS
26	Ibrahim, Samad and Amir(2011)	474	Listed family businesses	1	2011	0	Database	Malaysia	1991-2005	Tobin's Q, ROA, ROE		OLS
27	Imoniana and Soares(2010)	20	Listed SMEs	1	2010	1	Survey	Brazil	2006		Classification of the administrative board	Multinomial logit regression
28	Kula(2005)	386	small and non-listed stock ownership companies	1	2005	1	Survey	Turkey	2003	Firm performance index		OLS

ID	Author-Year	N	Type of firm	Published	Year	Cross-sectional	Data collection	Country	Data-Year	Measurement of CFP	Measurement of CSP	Methodology
29	Kyereboah-Coleman and Amidu(2008)	44	SMEs	1	2008	0	Database and survey	Ghana	1996-2004	ROA		Panel OLS
30	Larmou and Vafeas(2010)	257	Smaller firms	1	2010	0	Database	USA	1994-2000	Stock returns		Panel OLS
31	Machold et al.(2011)	140	Small firms	1	2011	1	Survey	Norway	2004-2005		Board's strategic involvement	OLS
32	O'Connell and Cramer(2010)	44	Listed small firms	1	2010	1	Database	Ireland	2001	RET, Tobin's Q, ROA		OLS, 2SLS
33	Pearce II, Howton and Howton(2002)	116	SMEs	1	2002	0	Database	USA	1996-1998	Operating Cash Flows/Total Assets (OCF/TA), Industry adjusted OCF/TA		OLS, Logistic regression
34	Pindado et al. (2008)	4333	Family business	0	2008	0	Database	Westerm Europe	2000-2006	Market-to-book ratio		GMM
35	Pugliese and Wenstøp(2007)	497	Small firms	1	2007	1	Survey	Norway	2004		Strategic performance	OLS
36	Raja and Kumar(2007)	40	Listed SMEs	1	2007	1	Database	India	2005	Tobin's Q		OLS
37	Randoy and Goel(2003)	204	Listed SMEs	1	2003	0	Database	Norway	1996-1998	Tobin's Q, ROA		OLS
38	Rashid and Lodh(2011)	769	Listed SMEs	0	2011	0	Database	Bangladesh	2000-2008	Tobin's Q, ROA	Growth	OLS

ID	Author-Year	N	Type of firm	Published	Year	Cross-sectional	Data collection	Country	Data-Year	Measurement of CFP	Measurement of CSP	Methodology
39	Uhlaner, Floren and Geerlings(2007)	233	Privately-held firms	1	2007	1	Survey	Switzerland	2005	Financial performance	Owner commitment, collective goals	OLS
40	Valenti, Luce and Clifton(2011)	87	Mid-sized listed corporations	1	2011	1	Database	USA	2000-2005	ROA, ROE		OLS, Logit regression
41	Wang(2011)	318	SMEs	1	2011	0	Database	China	2006-2008	ROA, ROE		OLS
42	Wincent et al.(2010)	53	Small firms	1	2010	0	Survey	Sweden	2000-2004	R&D spending	External funding efficiency	OLS
43	Wincent, Anokhin and Boter(2009)	53	Small firms	1	2009	0	Survey	Sweden	2000-2004		Innovative performance of a strategic small-firm network	OLS
44	Wincent, Anokhin and Örtqvist(2010)	53	Small firms	1	2010	0	Survey	Sweden	2000-2004		Total innovation, radical innovation, incremental innovation	OLS
45	Zahra, Neubaum and Naldi(2007)	384	SMEs	1	2007	1	Survey	USA	2004		Human capital, proprietary, relational resources	OLS

5.2.6. Moderators identified from prior studies

Moderators identified from prior studies in the meta-analyses include industry, development stage, age, size, and whether the firm has a board (see a list of the reference in Table 5.2). Given the sample size, respondents were classified into two categories, service industry or no service industry. The development stages were reduced to three categories, namely start-ups, established and declining. The age of the company was measured by the number of years from the establishment of the firm. Size was measured by number of employees.

5.3. Corporate governance and financial performance of small firms

Academic literature identifies eight main types of corporate governance mechanisms pertinent to the small firms, namely, board size, board independence, board interest alignment, board meeting frequency, ownership structure, directors' network, succession planning and independent auditing (Gillan 2006).

Financial performance is measured by the accounting indicators of the firms, including return on assets (ROA), return on equity (ROE), return on investment (ROI), Tobin's Q, share price, operating cash flow, market-to-book ratio and R&D spending (Orlitzky et al. 2003; van Essen et al. 2012).

5.3.1. Board size and financial performance of small firms: a meta-analysis

Board size, defined as the number of directors sitting on the board, is a critical factor influencing the appointment of subcommittees and the board's involvement with external directors (Brown, Vetterlein et al. 2010; Brown, Beekes et al. 2011). However, the endogeneity issue between the board size and firm performance hampers researchers from making valid causality deductions.

The endogeneity debate flags a measurement issue for small business performance (Ayyagari, Beck et al. 2007; Ayyagari, Demirguc-Kunt et al. 2011; Beck, Demirgüç-kunt et al. 2011).

The board of directors are valuable human capital, entering into the production function as a factor (Bammens, Voordeckers et al. 2011). The Resource Dependency Theory (RDT) argues that the external environment as well as the interaction between external and internal factors significantly influence the competitiveness of the firm, hence the board of directors can serve as an internal-external nexus (Pfeffer and Salancik 2003; Dalziel, Gentry et al. 2011). The Resource Based View (RBV) suggests that a firm's competitive advantage lies in the application of the bundle of valuable resources at the firm's disposal, of which the directors are a unique form (Wernerfelt 1984).

A widely cited paper by Darlton et al (1999) utilised the meta-analysis approach to summarise the literature published before 1999 and they found that board size is generally negatively correlated with financial performance. Nevertheless, they also found that firm size, serving as a moderating factor, might positively contribute to the correlation between board size and financial performance. However, they failed to provide specific analysis for the small firm cohort in the data (Dalton, Daily et al. 1999). Another paper by Bennedsen et al (2008) attempted to discover the causal impact of board size on performance in SMEs applying Instrumental Variable (IV) on cross-sectional survey data. It confirmed the negative relationship between board size and firm financial performance, supporting the precedents' argument that agency problems prevail in boards with seven or more members (Lipton and Lorsch 1992; Jensen 1993; Yermack 1996; Bennedsen, Kongsted et al. 2008). However, the explanatory power of the identified relationship in Bennedsen et al (2008) may be challenged because that the data collected in 1999 is somewhat out-dated and their sample was only based on one country – Denmark. Moreover, Lehn et al.

(2005) reviewed the literature on size and composition of the boards based on articles published during the period of 1935-2000 and found no systematic relationship between board characteristics and performance. The findings were based on the premise that firms maximize value and this point was validated for the great majority of firms.

Empirical research on the correlation between board size and financial performance of small firms is mixed. Arosa and colleagues examined the determinants of ROA of Spanish non-listed SMEs and found a positive correlation between board size and firm performance (Arosa, Iturralde et al. 2010). Calabro and Mussolino (2011) found a positive correlation between board size and export intensity. Bennedsen et al (2008), on the contrary, used a larger dataset of 7,000 firms and an advanced Instrumental Variable technique, and found a negative relationship. Huse et al. (2011) reported a negative impact of board size on ROI and total task involvement.

A total number of 23 articles were included in the meta-analysis of the relationship between board size and financial performance, with 63 effect sizes and 30166 firm-year observations (Table 5.3).

Table 5.3 Mapping between variables and articles included in the meta-analysis

ID	board size		board independence		meeting frequency		network		Ownership concentration		CFP VS. CSP
	CFP	CSP	CFP	CSP	CFP	CSP	CFP	CSP	CFP	CSP	
1	x										
2	x	x	x	x							x
3									x	x	x
4	x	x	x	x	x	x					x
5	x										
6								x			
7		x				x					
8		x		x							
9		x									
10	x						x				
11								x			
12		x									
13		x		x							
14		x		x		x					
15	x	x	x	x							
16			x								
17	x		x								
18			x	x							
19	x										
20	x		x								
21	x										
22			x								
23											x
24	x										
25		x		x		x					

ID	board size		board independence		meeting frequency		network		Ownership concentration		CFP VS. CSP
	CFP	**CSP**	**CFP**	**CSP**	**CFP**	**CSP**	**CFP**	**CSP**	**CFP**	**CSP**	
26	x		x								
27				x							
28	x		x								
29	x		x								
30	x		x								
31		x									
32	x										
33	x										
34									x		
35	x	x			x	x					
36											
37											
38	x	x	x	x							x
39							x				x
40	x		x								
41	x		x								
42	x	x									
43		x				x					
44		x		x		x		x			
45								x			

Remark:

1. x — the article is included in the meta-analysis to calculate the respective effect size.
2. The ID for each article in Table 3 corresponds to the same as the ID in Table 2.

The moderators inferred from the prior literature include legal form, industry, development stage, Full-time Equivalent Employees (FTEs) and membership of industry association.

The results of meta-analysis on the relationship between board size and corporate financial performance are reported in Table 5.4. The point estimate for the effect size is -0.0136.

Table 5.4 HOMA Results for the relationship of board size and financial performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	63	30116	-0.0073	-0.0186	0.0040	-1.2634	0.2064
Random effects	63	30116	-0.0136	-0.0397	0.0125	-1.0232	0.3062
Q-value	**df (Q)**	**P-value**	**I-squared**				
246.1093	62	0	74.80794				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
6.64E-03	2.55E-03	6.48E-06	0.081457				

Data was collected from different countries over a number of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. Hence the hypothesis is:

H1: There is a negative relationship between board size and corporate financial performance (Fig. 5.1).

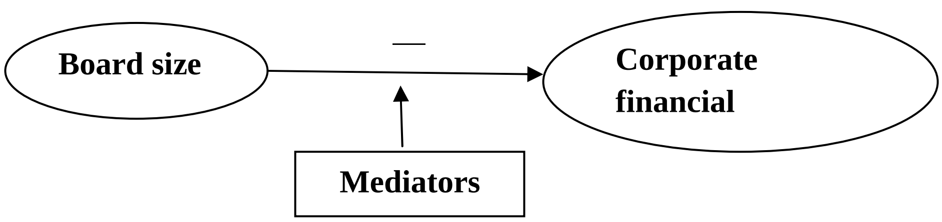


Figure 5.1 Hypothesized relationship between board size and corporate financial performance

5.2.2. Board independence and financial performance of small firms: a meta-analysis

Board independence is measured by the number of outsider or independent directors on the board (Arosa et al. 2010). A total number of 15 articles were included in the meta-analysis of the relationship between board independence and financial performance, with 46 effect sizes and 13585 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between board independence and corporate financial performance are reported in Table 5.5. The point estimate for the effect size was 0.0217.

Table 5.5 HOMA Results for the relationship of board independence and financial performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	46	16308	-0.0011	-0.0165	0.0143	-0.1373	0.8908
Random effects	46	16308	0.0217	-0.0152	0.0585	1.1516	0.2495
Q-value	**df (Q)**	**P-value**	**I-squared**				
218.6512	45	0	79.41928				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
1.11E-02	3.54E-03	1.25E-05	0.105581				

Given that the data were collected from different countries over many years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. Hence the hypothesis is

H2: There is a positive relationship between board independence and corporate financial performance (Fig. 5.2).

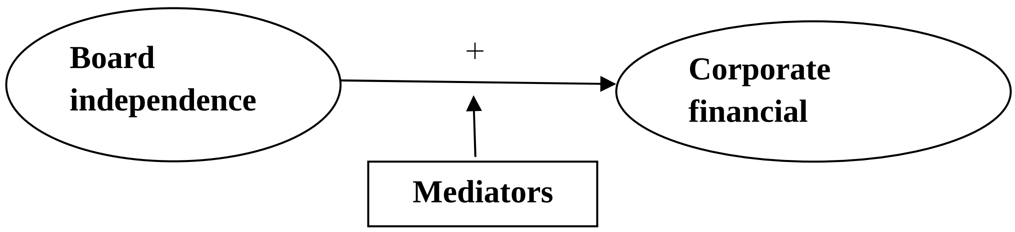


Figure 5.2 Hypothesized relationship between board independence and corporate financial performance

5.2.3. Board meeting frequency and financial performance of small firms: a meta-analysis

Board meeting frequency, measured by the number of meetings the board holds on average each year, is an indicator of board involvement and diligence in strategic decision-making (Arosa et al. 2012). A total of 2 articles were included in the meta-analysis of the relationship between board size and financial performance, with 2 effect sizes and 804 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between board meeting frequency and corporate financial performance are reported in Table 5.6. The point estimate for the effect size is 0.0017.

Table 5.6 HOMA Results for the relationship of meeting frequency and financial performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	2	804	0.0220	-0.0473	0.0911	0.6219	0.5340
Random effects	2	804	0.0017	-0.1896	0.1928	0.0171	0.9864
Q-value	**df (Q)**	**P-value**	**I-squared**				
7.3511	1.0000	0.0067	86.3966				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0169	0.0276	0.0008	0.1299				

Given that the data was collected from different countries across a wide range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. Hence the hypothesis is

H3: There is a positive relationship between board size and corporate financial performance (Fig. 5.3).

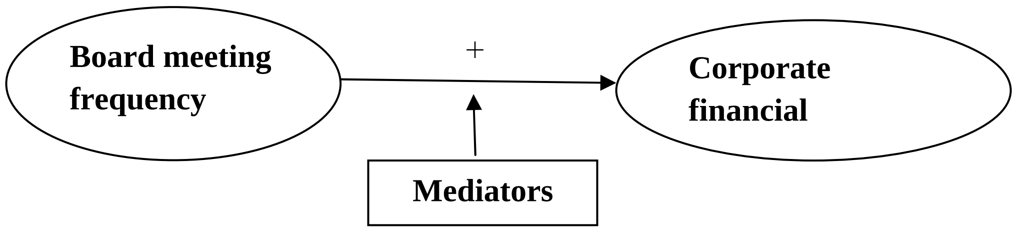


Figure 5.3 Hypothesized relationships between board meeting frequency and corporate financial performance

5.2.4. Ownership concentration and financial performance of small firms: a meta-analysis

Compared to large corporations, the ownership structure in small firms is relatively simpler (Arosa et al. 2012). Ownership concentration, measured by the proportion of shares owned by the largest shareholder, has been identified in the literature as a determinant of financial performance of small firms (Pindado et al. 2008). A total number of 2 articles were included in the meta-analysis of the relationship between ownership concentration and financial performance, with 4 effect sizes and 13585 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between ownership concentration and corporate financial performance are reported in Table 5.7. The point estimate for the effect size is 0.0281.

Table 5.7 HOMA Results for the relationship of ownership concentration and financial performance

Total effects	**No. of effect size**	**No. of observations**	**Point estimate**	**Lower limit**	**Upper limit**	**z-value**	**p-value**
Fixed effects	4	13585	0.0281	0.0113	0.0449	3.2707	0.0011
Random effects	4	13585	0.0281	0.0113	0.0449	3.2707	0.0011
Q-value	**df (Q)**	**P-value**	**I-squared**				
0.7297	3.0000	0.8662	0.0000				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0000	0.0003	0.0000	0.0000				

Given that the Q-statistic is insignificant, the fixed effect model was chosen. Moreover, the hypothesis proposed is that:

H4: There is a positive relationship between ownership concentration and corporate financial performance (Fig.5. 4).

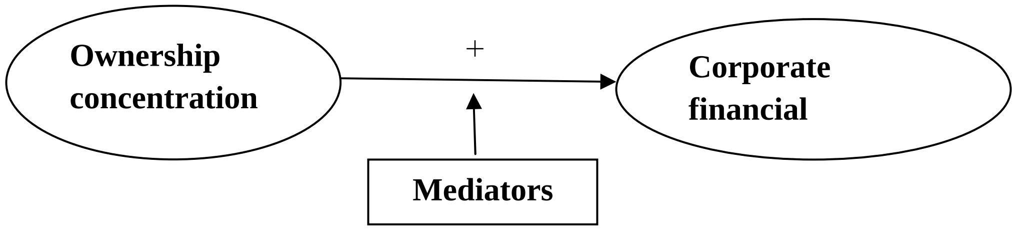


Figure 5.4 Hypothesized relationship between ownership concentration and corporate financial performance

5.2.5. Directors' network and financial performance of small firms: a meta-analysis

Network governance theory argues that the organization's network as well as networks established by individuals, particularly directors, are vital resources to the survival and growth of small firms (Di Pietra et al. 2008). The frequency that directors use their personal network for the development of the business and network size are used as the measure of the directors' network (Uhlaner et al. 2007). 2 articles were included in the meta-analysis of the relationship between directors' network and financial performance, with 4 effect sizes and 2272 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between a directors' network and corporate financial performance are reported in Table 5.8. The point estimate for the effect size is -0.0325.

Table 5.8 HOMA Results for the relationship of director's network and financial performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	4	2272	-0.0325	-0.0736	0.0087	-1.547	0.1219
Random effects	4	2272	-0.0325	-0.1712	0.1074	-0.455	0.6495
Q-value	**df (Q)**	**P-value**	**I-squared**				
34.7514	3.0000	0.0000	91.3673				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0187	0.0167	0.0003	0.1369				

Given that the data were collected from different countries over a range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. The hypothesis formulated is:

H5: There is a negative relationship between directors' network and corporate financial performance (Fig. 5.5).

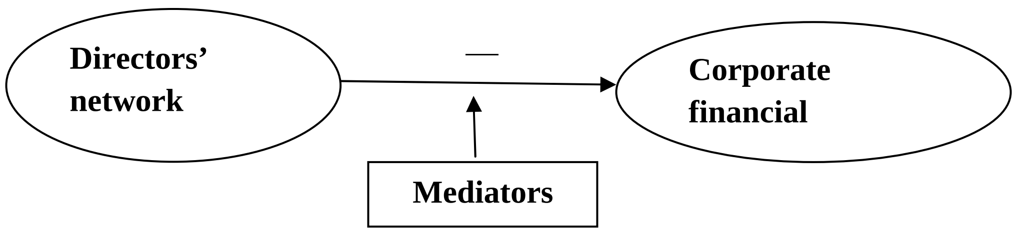


Figure 5.5 Hypothesized relationship between directors' network and corporate financial performance

5.2.6. Board interest alignment and financial performance of small firms

Muth and Donaldson (1998) used Stewardship Theory and offers opposing prediction to the Agency Theory on the structure of effective boards and their financial performance in large listed companies in Australia. They argue that directors are stewards of the company and they act in the best interest of the company as well as for their own professional satisfaction. Thus, financial performance will improve in firms which align the interests of board with the owners. They developed a five-scale indicator to measure the level of alignment between the board and owners: 1 = retired executives; 2 = suppliers, consultants; 3 = no ties/ no relevant shareholding; 4 = shareholders; 5 = founders/family members acting as executives. Therefore, the hypothesized relationship between board interest alignment and financial performance of small firms is as follows:

H6: There is a positive relationship between board's interest alignment and corporate financial performance (Fig. 5.6).

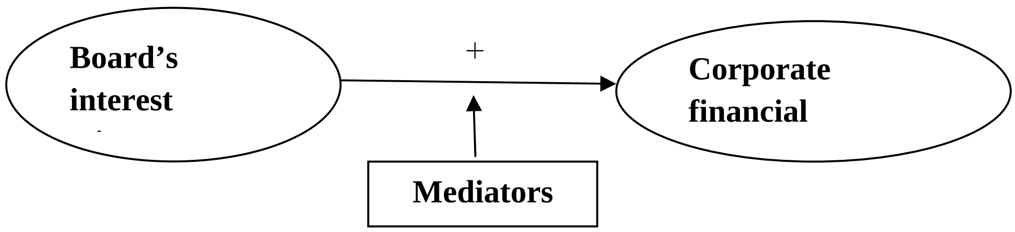


Figure 5.6 Hypothesized relationship between board's interest alignment and corporate financial performance

5.2.7. Succession planning and financial performance of small firms

Worldwide, a large number of small firms are family controlled businesses, thus succession from the CEO/owner/manager to the heirs is of great relevance to the financial performance of small firms. Cucculelli and Micucci (2008) surveyed 229 Italian companies with business succession taking place during 1996-2000. They found that succession decreases the growth rate of sales, a phenomenon confirmed by Brown and Caylor (2009). Moreover, Brown and Caylor, in an analysis of data from listed companies in the US, found that a board approved CEO succession plan has positive impacts on ROE, net profit margin, Tobin's Q, dividends yield and share repurchases.

Thus, the hypothesized relationships between succession planning and financial performance are as follows:

H7: Succession planning has a positive relationship with financial performance (Fig. 5.7).

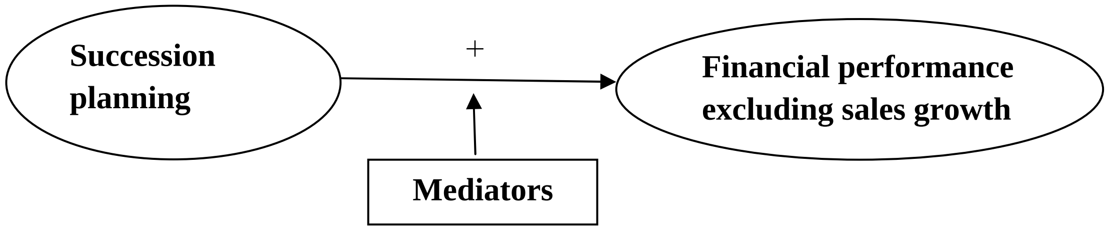


Figure 5.7 Hypothesized relationship between succession planning and financial performance

5.2.8. Independent audit and financial performance of small firms

Independent audit, or external audit, is defined as a systematic process of objectively obtaining and evaluating accounts or financial records of economic units based on established criteria. External auditors may audit the financial statements, regulatory compliance and business operations (Dalkiliç et al. 2012). The Australian Auditing and Assurance Standards Board (2007) mentioned in their report that the independent audit has a number of benefits to SMEs:

- fraud/misappropriation deterrent;
- preparation of annual financial report in compliance with the applicable accounting framework;
- independent health check especially the consideration of going concern;
- enhancement of reporting skills of organizations;
- exposure to a range of independent experts on matters such as risk management, information systems, internal control and corporate governance; and
- enhancement of corporate governance where a management letter on control deficiencies was issued.

Thus, the hypothesis is as follows:

H8: Independent auditing has a positive relationship with financial performance (Fig. 5.8).

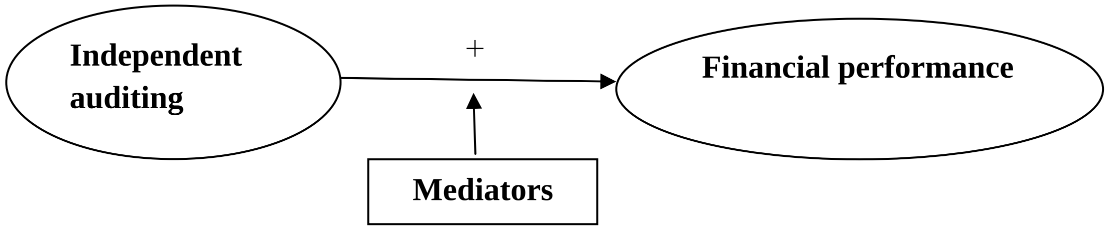


Figure 5.8 Hypothesized relationship between independent auditing and financial performance

5.2.9. Summary

The systematic review and meta-analysis synthesized the empirical evidence in the literature and the hypotheses for the relationship between components of corporate governance and financial performance in small firms. The conceptual framework is summarised in Figure 5.9.

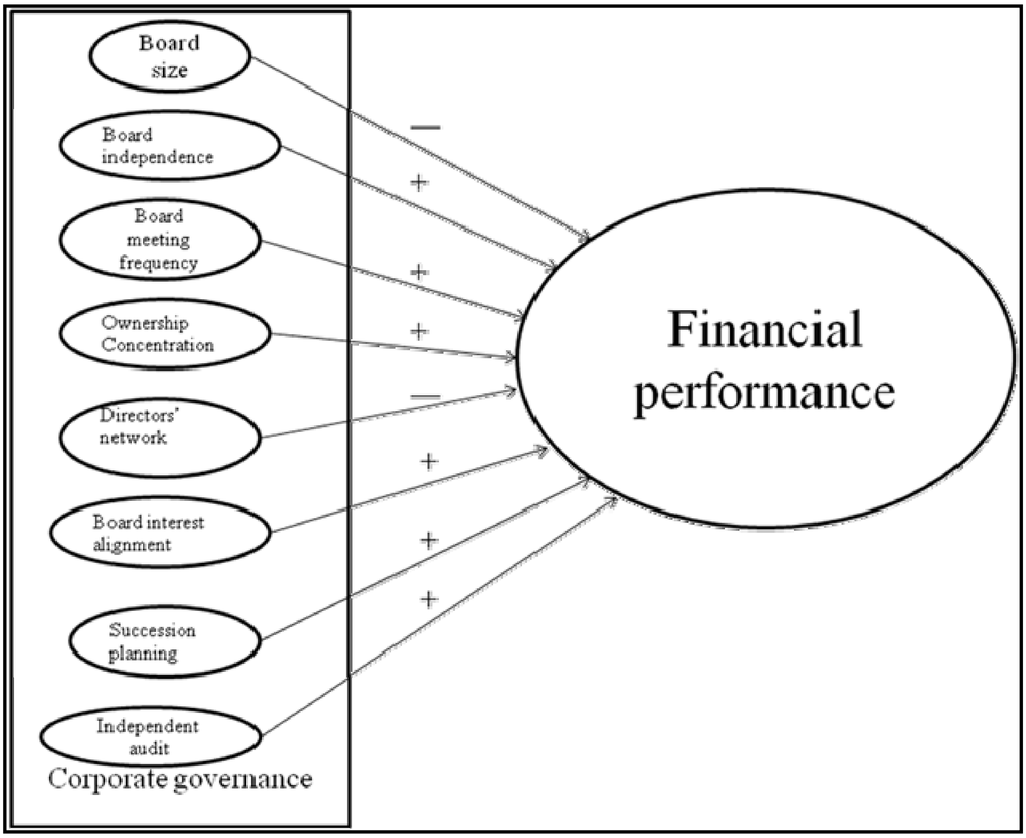


Figure 5.9 Conceptual framework on corporate governance and financial performance of small firms

The Agency Theory, Stewardship Theory, Stakeholder Theory, from different perspectives, all argue that corporate governance mechanisms (as a bundle) have a positive relationship with performance (Clarke 2004). Thus,the relationship between the latent variables of 'corporate governance' and 'financial performance' of small firms can be hypothesized as:

H9 Corporate governance has a positive relationship with financial performance of small firms.

5.3. Corporate governance and social performance of small firms

Contingency Theorists argue that the performance of business organisations is largely determined by their strategies and operations in market and non-market environments (Donaldson 2001). The non-market environments may be captured by one construct – CSR, which can be defined as:

> *a business organization's configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships (Wood 1991, p.693).*

Four types of broad measurement strategies have been used to quantify CSR in the literature of large corporations, namely (1) CSR disclosures; (2) CSR reputation ratings; (3) CSR process, observable outcomes and social audits; and (4) managerial principles, values and perceptions (Orlitzky et al. 2003). The small business literature on CSR is mainly concerned with the fourth type.

5.3.1. Board size and social performance of small firms: a meta-analysis

A total number of 16 articles were included in the meta-analysis of the relationship between board size and social performance, with 40 effect sizes and 19246 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between board size and corporate social performance are reported in Table 5.9. The point estimate for the effect size is 0.0432.

Table 5.9 HOMA Results for the relationship of board size and social performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	40	19246	0.0528	0.0386	0.0669	7.3059	0.0000
Random effects	40	19246	0.0432	-0.0043	0.0906	1.7829	0.0746
Q-value	**df (Q)**	**P-value**	**I-squared**				
401.8723	39	0	90.29543				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0200	0.0067	0.0000	0.1414				

Given that the data were collected from different countries across a wide range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. Hence the hypothesis is

H10: There is a positive relationship between board size and corporate social performance (Fig. 5.10).

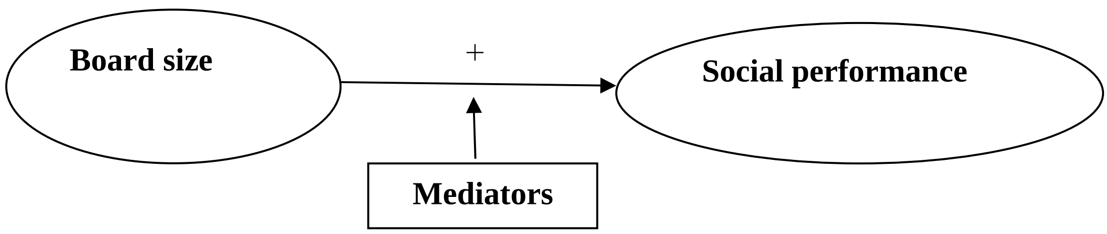


Figure 5.10 Hypothesized relationship between board size and social performance

5.3.2. Board independence and social performance of small firms: a meta-analysis

A total number of 11 articles were included in the meta-analysis of the relationship between board size and financial performance, with 25 effect sizes and 11907 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between board independence and corporate social performance are reported in Table 5.10. The point estimate for the effect size is 0.0669.

Table 5.10 HOMA Results for the relationship of board independence and social performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	25	11907	0.0517	0.0345	0.0689	5.8706	0.0000
Random effects	25	11907	0.0669	0.0048	0.1284	2.1126	0.0346
Q-value	**df (Q)**	**P-value**	**I-squared**				
273.2909	24.0000	0.0000	91.2182				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0214	0.0095	0.0001	0.1462				

Given that the data were collected from different countries across a wide range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. Hence the hypothesis is

H11: There is a positive relationship between board independence and corporate social performance (Fig. 5.11).

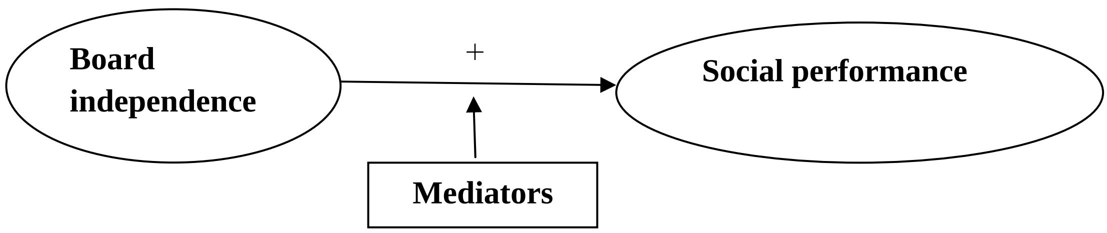


Figure 5.11 Hypothesized relationship between board independence and social performance

5.3.3. Board meeting frequency and social performance of small firms: a meta-analysis

A total number of 23 articles were included in the meta-analysis of the relationship between board size and financial performance, with 23 effect sizes and 8298 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between board meeting frequency and corporate social performance are reported in Table 5.11. The point estimate for the effect size is 0.1355.

Table 5.11 HOMA Results for the relationship of meeting frequency and social performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	23	8298	0.0960	0.0746	0.1174	8.7380	0.0000
Random effects	23	8298	0.1355	0.0747	0.1952	4.3463	0.0000
Q-value	**df (Q)**	**P-value**	**I-squared**				
163.2906	22.0000	0.0000	86.5271				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0182	0.0071	0.0000	0.1350				

Given that the data were collected from different countries across a wide range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model is chosen. Hence the hypothesis is:

H12: There is a positive relationship between board meeting frequency and corporate social performance (Fig. 5.12).

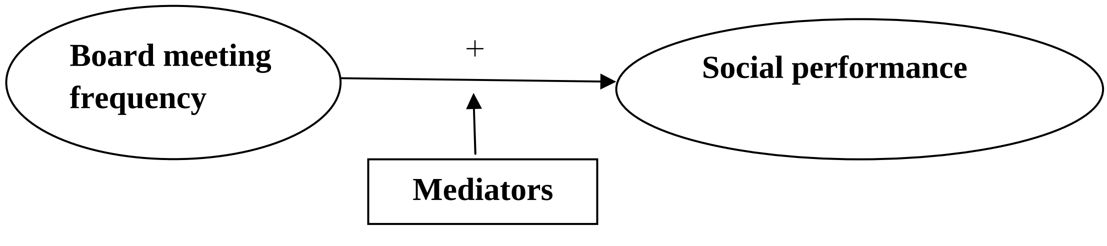


Figure 5.12 Hypothesized relationship between board meeting frequency and social performance

5.3.4. Ownership concentration and social performance of small firms: a meta-analysis

Only one article was included in the meta-analysis of the relationship between ownership concentration and social performance of small firms, with one effect size and 586 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between ownership concentration and corporate social performance are reported in Table 5.12. The point estimate for the effect size is -0.004.

Table 5.12 HOMA Results for the relationship of ownership concentration and social performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	1	586	-0.0040	-0.0850	0.0770	-0.0966	0.9231
Random effects	1	586	-0.0040	-0.0850	0.0770	-0.0966	0.9231

Q-value	df (Q)	P-value	I-squared
0.0000	0.0000	1.0000	0.0000

Tau Squared	Standard Error	Variance	Tau
0.0000	0.0000	0.0000	0.0000

In relation to ownership concentration and social performance, the hypothesis is:

H13: There is a negative relationship between ownership concentration and corporate social performance (Fig. 5.13).

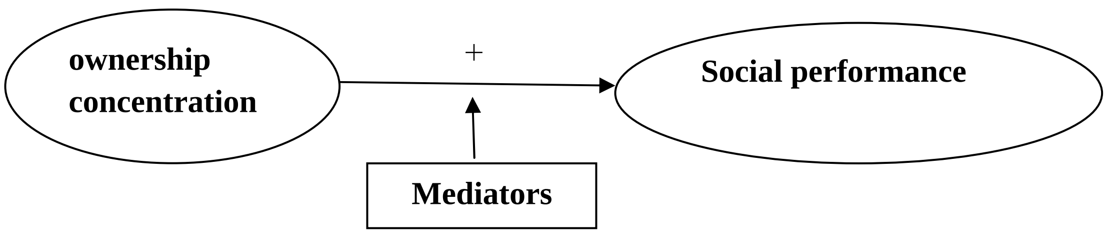


Figure 5.13 Hypothesized relationship between ownership concentration and social performance

5.3.5. Directors' network and social performance of small firms: a meta-analysis

A total number of 4 articles were included in the meta-analysis of the relationship between board size and financial performance, with 22 effect sizes and 30166 firm-year observations (Table 5.3).

The results of meta-analysis on the relationship between board size and corporate financial performance are reported in Table 5.13. The point estimate for the effect size is 0.1387.

Table 5.13 HOMA Results for the relationship of director's network and social performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	22	9323	0.1055	0.0853	0.1256	10.1849	0.0000
Random effects	22	9323	0.1387	0.0636	0.2124	3.6022	0.0003
Q-value	**df (Q)**	**P-value**	**I-squared**				
171.3971	21.0000	0.0000	87.7477				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0202	0.0142	0.0002	0.1423				

Given that the data were collected from different countries across a wide range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model was chosen. Hence the hypothesis is

H14: There is a positive relationship between a director's network and corporate social performance (Fig. 5.14).

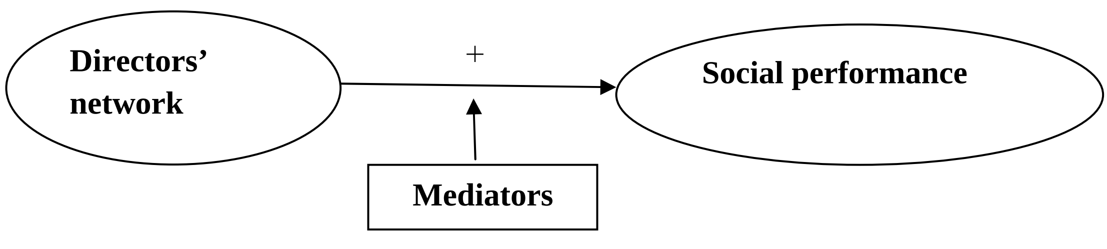


Figure 5.14 Hypothesized relationship between directors' network and social performance

5.3.6. Board interest alignment and social performance of small firms

The instrumental stakeholder theory suggests a positive relationship between various stakeholders and the firm performance in that the satisfaction of stakeholders is instrumental to organisational development (Donaldson and Preston 1995). The Stakeholder-Agency Theory adds to the argument that reciprocal and bilateral stakeholder- management relationships established via negotiation and contracting processes serve as monitoring and enforcement mechanisms and prevents managers from hampering the organisational goals (Jones 1995). Moreover, a well-balanced stakeholder-management relationship may potentially ease the coordination of the business operation. Consequently, it may bolster a firm's competitive advantage in that limited resource can be prioritized for optimal use (Orlitzky et al. 2003). Hence, the relationship between board interest alignment and social performance can be hypothesized as:

H15 The board interest alignment has a positive relationship with social performance (Fig. 5.15).

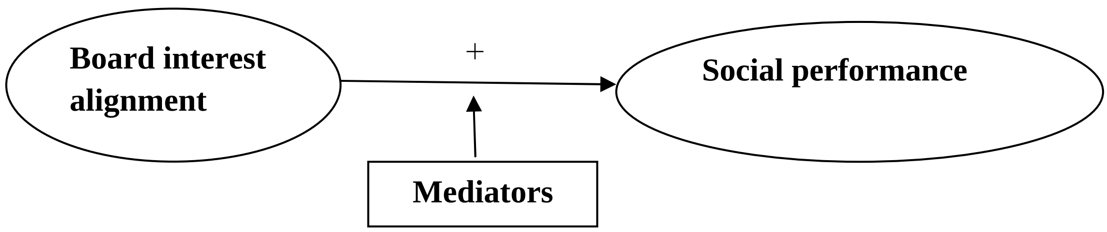


Figure 5.15 Hypothesized relationship between board interest alignment and social performance

5.3.7. Succession planning and social performance of small firms

Succession planning may enhance the chances of a smooth and effective transition of leadership in businesses. As a consequence, the likelihood of cooperations among stakeholders in business may increase (Wang et al. 2004). Thus, the relationship between succession planning and social performance can be hypothesized as follows:

H16 Succession planning has a positive relationship with the social performance (Fig. 5.16).

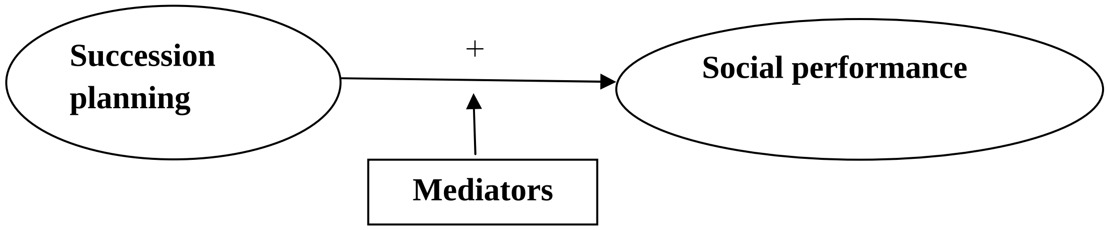


Figure 5.16 Hypothesized relationship between succession planning and social performance

5.3.8. Independent audit and social performance of small firms

An external audit is able to identify the potential errors, frauds and weaknesses in the existing financial system. Improved financial information helps firms to better allocate their scarce resources and better engage with its potential customers and suppliers (Dalkilic et al. 2012). Thus, the proposed relationship between independent audit and social performance is H17 The independent audit has a positive relationship with social performance (Fig. 5.17).

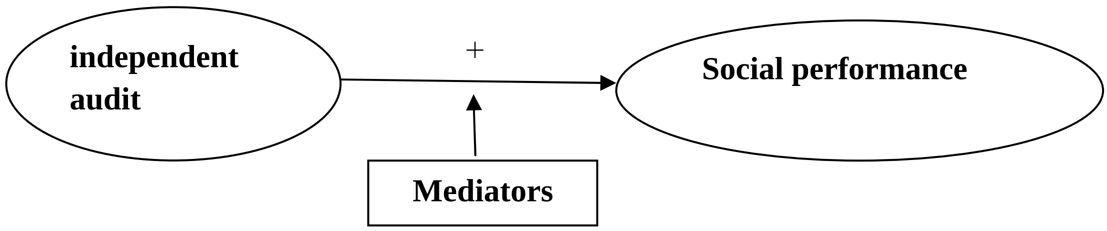


Figure 5.17 Hypothesized relationship between independent audit and social performance

5.3.9. Summary

The aforementioned hypotheses can be summarised as follows (Fig. 5.18):

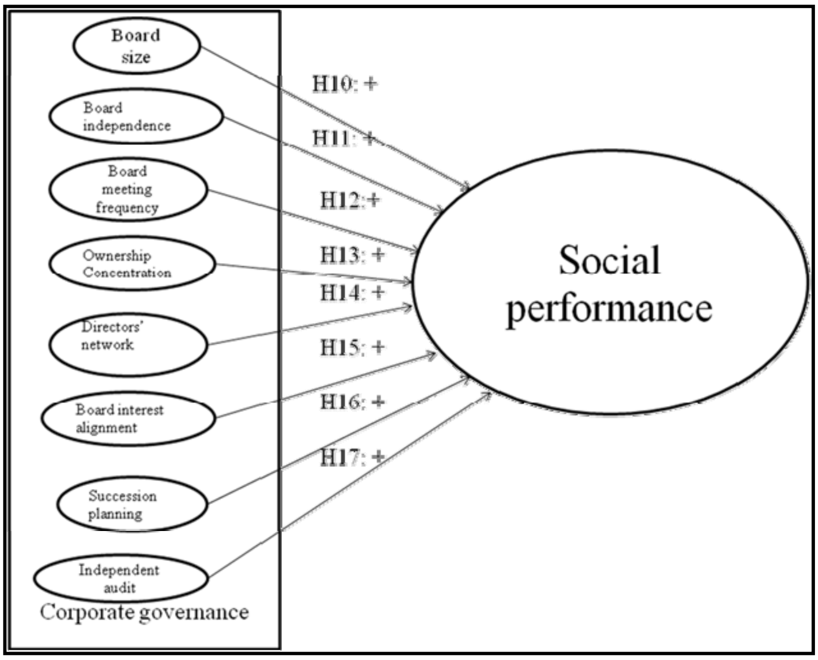


Figure 5.18 Conceptual framework between corporate governance and social performance

In Fig. 5.18, as proposed in the statistical hypothese, all the components of corporate governance has a positive relationship with social performance (H10-H17), thus the relationship between corporate governance and social performance can be proposed as

H18 Corporate governance has a positive relationship with social performance of small firms.

The meta-analyses results are summarised in Table 5.14.

Table 5.14 HOMA Results by performance measures

	Financial performance							Social performance						
Variables	**K**	**N**	**Mean**	**z**	**p**	**CI 95%**	**I-squared**	**K**	**N**	**Mean**	**z**	**p**	**CI 95%**	**I-squared**
Board size	63	30116	-0.0136	-1.0232	0.3062	-0.0397/0.0125	74.80794	40	19246	0.0432	1.7829	0.0746	-0.0043/0.0906	90.29543
Board independence	46	16308	0.0217	1.1516	0.2495	-0.0152/0.0585	79.41928	25	11907	0.0669*	2.1126	0.0346	0.0048/0.1284	91.2182
Board meeting frequency	2	804	0.0017	0.0171	0.9864	-0.1896/0.1928	86.3966	23	30116	0.1355***	4.3463	0.0000	0.0747/0.1952	86.5271
Ownership concentration	4	13585	0.0281***	3.2707	0.0011	0.0113/0.0449	0	1	586	-0.0040	-0.0966	0.9231	-0.0850/0.0770	0
Directors' network	4	-0.0325	-0.1712	-0.4545	0.6495	-0.1712/0.1074	91.3673	22	9323	0.1387***	3.6022	0.0003	0.0636/0.2124	87.7477

6. Remark:
7. k — number of effect sizes
8. N — number of firm-year observations
9. Mean — estimated effect size, * — 10% significance level; * *— 5% significance level; *** — 1% significance level;
10. z — z value for the effect size
11. p — p value for the effect size
12. CI — 95% confidence interval
13. I-squared — % of the observed variance is due to the real differences in the effect size, or the existence of heterogeneity

5.5. Social performance and financial performance:a meta-analysis

Six articles were included in the meta-analysis of the relationship between board size and financial performance, with 15 effect sizes and 5920 firm-year observations (Table 5.15).

The results of meta-analysis on the relationship between corporate financial and corporate social performance are reported in Table 5.15. The point estimate for the effect size is 0.0763.

Table 5.15 HOMA Results for the relationship of financial and social performance

Total effects	No. of effect size	No. of observations	Point estimate	Lower limit	Upper limit	z-value	p-value
Fixed effects	15	5920	0.0892	0.0638	0.1145	6.8584	0.0000
Random effects	15	5920	0.0763	-0.0489	0.1991	1.1951	0.2321
Q-value	**df (Q)**	**P-value**	**I-squared**				
321.8219	14.0000	0.0000	95.6498				
Tau Squared	**Standard Error**	**Variance**	**Tau**				
0.0578	0.0265	0.0007	0.2404				

Given that the data were collected from different countries across a wide range of years (Table 5.2), heterogeneity of the effect sizes may be a concern, which is confirmed by the Q-value (statistically significant) and I-square (larger than 0.1) (Borenstein et al. 2007). Thus, the random effect model was chosen. The hypothesis is:

H19: There is a positive relationship between corporate financial and social performance (Fig. 5.19).

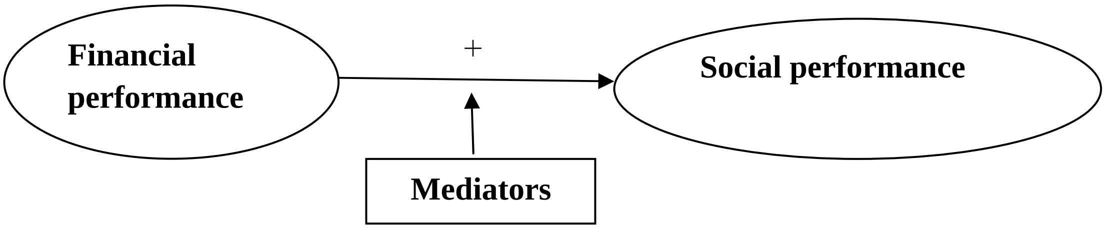


Figure 5.19 Hypothesized relationship between corporate financial and social performance

5.6. Regulation and financial performance

Kitching (2006) undertook a systematic review to investigate the impact of regulation on small business performance. As mentioned in Chapter 3, three streams of the literature on the regulation and performance of small firms have been identified, including business burden, compliance costs, and the adaptation of business owners to regulation. Hereby, the causal relationship between regulation and firm performance can be direct impact or indirectly mediated by other factors (Fig. 5.20).

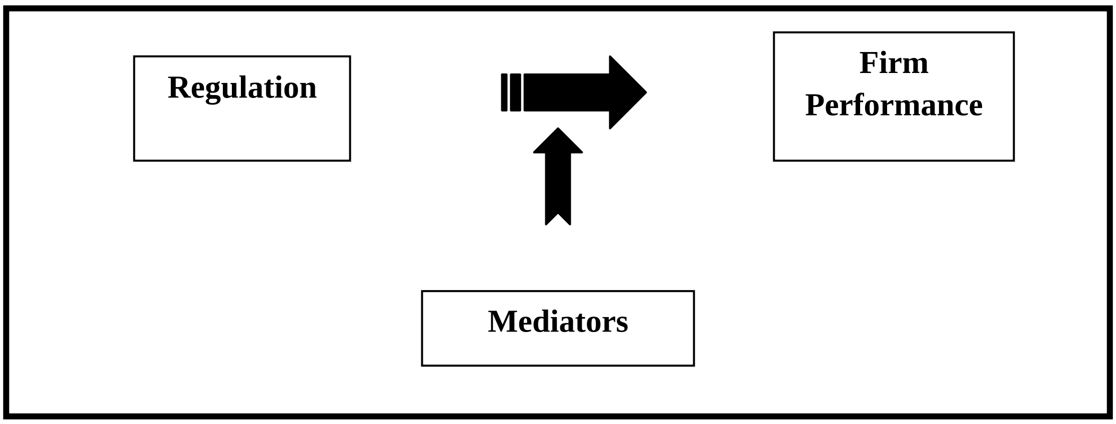


Figure 5.20 Realist View of Causation (adapted from Hills 2008)

The business burden studies present quantitative surveys that have found that regulation as well as regulatory changes are ‘burdens/barriers/obstacles’ to business performance, innovation and growth, indicating the existence of a negative impact (Atkinson and Hurstfield 2004; Cosh and Hughes 2003). Furthermore, the constraining impact of regulation is inversely related to business size, meaning that small businesses face greater regulatory burdens (Cartel et al. 2006).

Compliance cost studies argue that there is a direct cost of ‘red tape’ for meeting regulation compliance requirements and an opportunity cost in diverting scarce resources. Examples include executives’ scarce business time, away from productive, profit-generating activities in order to discover, interpret and comply with regulatory obligations (Kauser et al. 2005). Moreover, a study conducted by Business New Zealand/KPMG (2005) illustrated that small businesses incurs a higher proportionate of costs than larger companies in both monetary terms and labour time estimates.

The literature on the adaption of business owners to regulation argues that the change of regulations enables and generates changes to the behaviour and performance of business owner/managers (Kitching 2006). However, this strand of literature fails to consider that catering to the changes of regulatory requirements costs time and effort and deviates from the core business of small firms and, unintentionally introduces extra financial burdens.

Thus, the following hypotheses can be proposed

H20: There is a positive relationship between corporate financial and social performance (Fig. 5. 21).

H21: The impact of regulation on the financial performance is larger in smaller firms than in big firms (Fig. 5. 21).

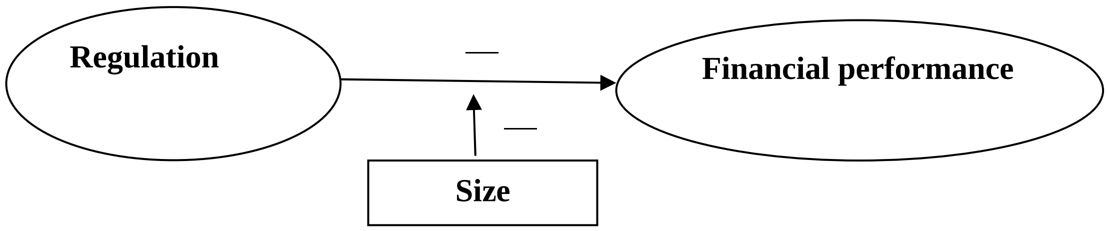


Figure 5.21 Hypothesized relationship between regulation and financial performance

5.7. Regulation and social performance

The impact of regulation on performance, as shown in Fig. 20, can be mediated by internal and external conditions. Internal conditions refer to any factors or mechanisms within the firm including resource, owner/managers' capacity, motivation of managers and employees. External conditions refer to the factors beyond the enterprise, including other stakeholders, for example, suppliers, consumers, product, labour and capital markets. All stakeholders are in competition for resources and markets. If the owner of a small firm is not able to respond to the regulatory requirements prompt, he/she may lose the competition. Consequently, the performance of the firm may decline and the relationships with stakeholders may be impaired (Hills 2008).

Thus, the relationship between regulation and social performance can be proposed as:

H22: There is a negative relationship between regulation and social performance (Fig. 5. 22).

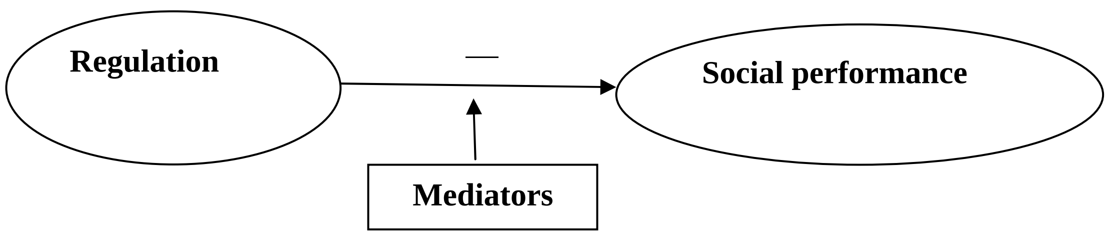


Figure 5.22 Hypothesized relationship between regulation and social performance

5.8. Corporate governance and regulation

The New Institutional Theory argues that it is institutions that shape the landscape of the business world (North 1997). Therefore, firms are only regulation-takers. In Australia, the

Corporations Act (2001) has laid the foundations for the basic requirement of corporate governance for all the business entities registered with Australian Securities and Investment Commission (ASIC). The Corporations Act (2001) serves as a legal means to safeguard the corporate governance practice so that the potential business risk can be minimised. In addition, regulators have also promulgated guidelines and good practice in order to promote corporate governance, for example,. the 'comply or explain' approach adopted by the Australian Stock Exchange (ASX). Thus, the impact of regulation on corporate governance can be proposed as:

H23: The regulation has a positive impact on corporate governance (Fig. 5. 23).

Though firms may perceive regulation as a burden to the business operation, firms with sound corporate governance framework may incur less regulatory compliance cost, comparing with those which do not have proper corporate governance practice (Brown et al. 2011). This argument is well supported by the Resource Dependence Theory, which explains that corporate governance mechanisms, for example, the board of directors, can serve as scarce and valuable resource to the firm and the diversified expertise can improve the owner/manager's understanding about regulatory requirement (Chapter 2).

Thus, corporate governance may reduce regulatory compliance requirements.

H24: Corporate governance has a negative impact on regulation (Fig. 5. 23).

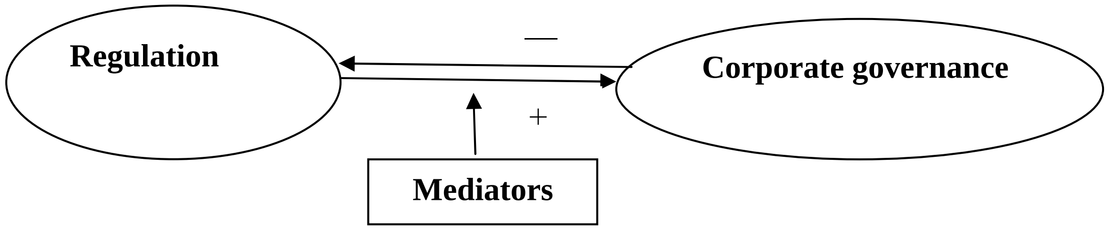


Figure 5.23 Hypothesized relationship between regulation and corporate governance

5.9. Summary of the conceptual framework

This chapter applied an evidence-based method, in particular, a systematic review and meta-analysis, to investigate the relationships found in previous research on four constructs pertinent to small firms: corporate governance, regulation, financial performance and social performance. From this analysis, a conceptual framework was developed (Fig. 5.24) and statistical hypotheses proposed (H1-H24) (Table 5.16). The conceptual framework only includes the hypothesised relationship among these four constructs, while relationships between the components of corporate governance and financial performance have been presented in Fig. 9 and components of corporate governance and social performance in Fig. 18.

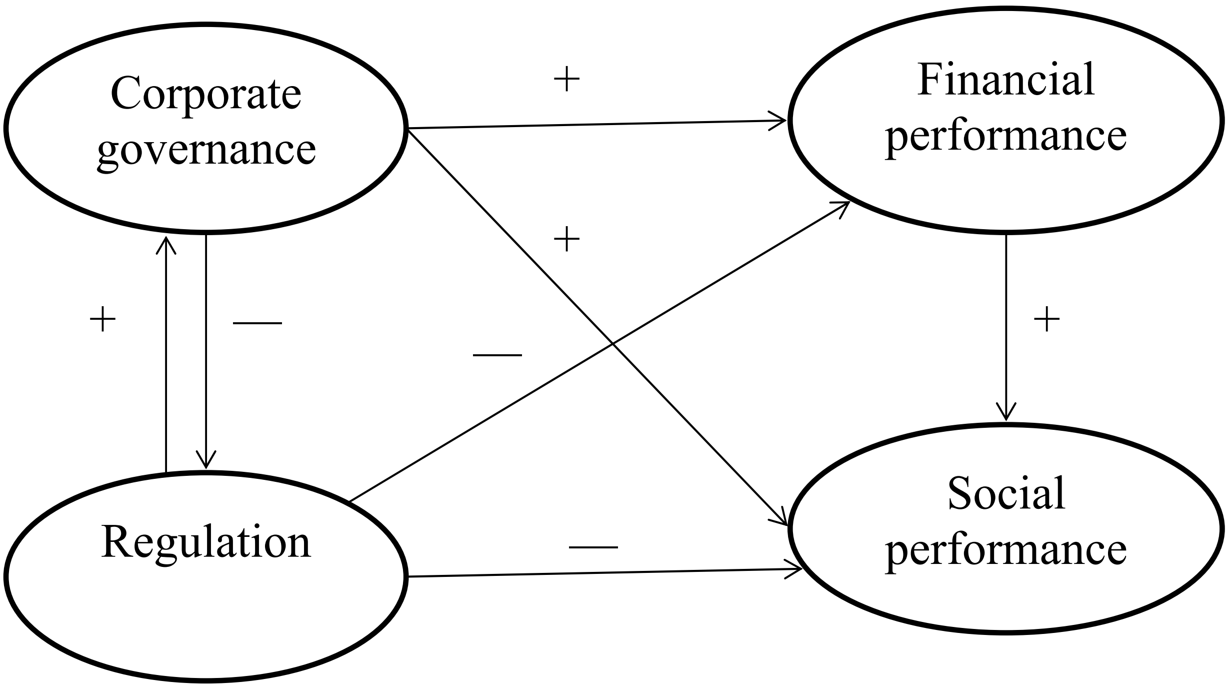


Figure 5. 24 Conceptual framework

Based on the conceptual framework, the next Chapter will embark on developing the measurement and specifications methodology for the hypothesised relationships.

Table 5.16 Summary of the statistical hypotheses

Hypothesis No.	Relationship	Expected sign
1	Board size and financial performance	-
2	Board independence and financial performance	+
3	Board meeting frequency and financial performance	+
4	Ownership structure and financial performance	+
5	Director's network and financial performance	-
6	Board interest alignment and financial performance	+
7	Succession planning and financial performance	+
8	Independent audit and financial performance	+
9	Corporate governance and financial performance	+
10	Board size and social performance	+
11	Board independence and social performance	+
12	Board meeting frequency and social performance	+
13	Ownership structure and social l performance	+
14	Director's network and social performance	+
15	Board interest alignment and social performance	+
16	Succession planning and social performance	+
17	Independent audit and social performance	+
18	Corporate governance and social performance	+
19	Social and financial performance	+
20	Regulation and financial performance	-
21	The mediating effect of size on the impact of regulation on financial performance	-
22	Regulation and social performance	-
23	Regulation on Corporate governance	+
24	Corporate governance on regulation	-

CHAPTER 6 METHODOLOGY

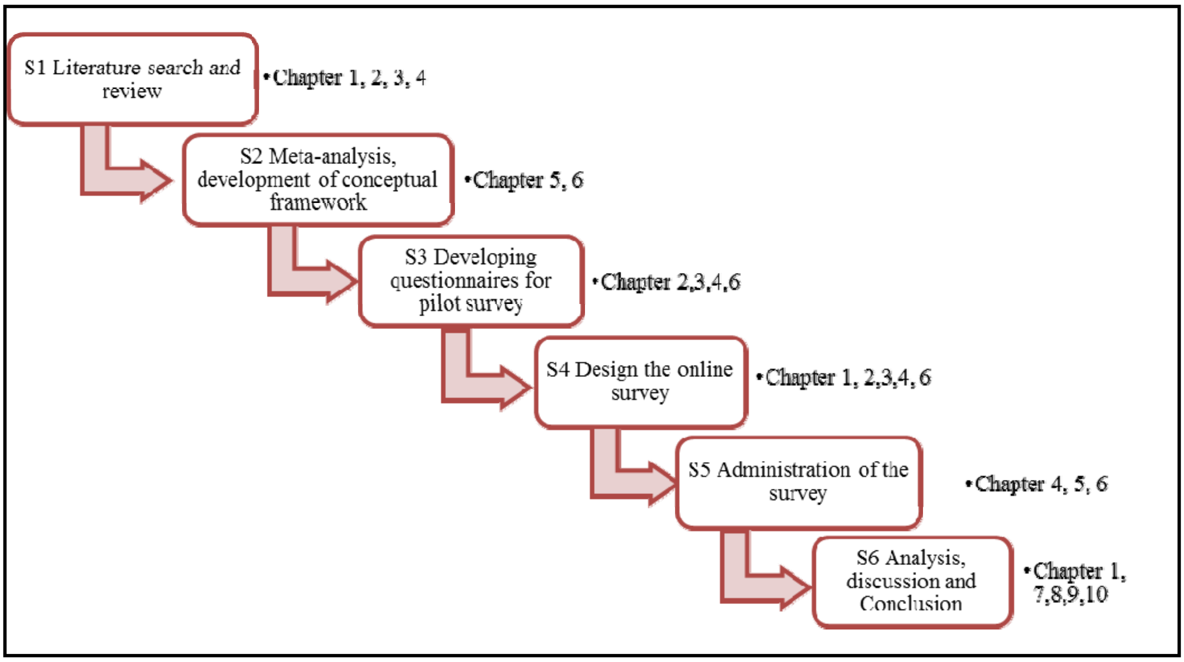


Figure 6.1 Flow chart of the research design

6.1. Introduction

Chapter Five outlined the conceptual framework for this research and developed the research questions and hypotheses to be tested in Chapter Seven. Chapter Six discussed the research design and methodology used to undertake this study, which steers different stages of the whole research project, including research questions, the literature review, conceptual framework, data collection, data analysis and discussion.

The research design is conducted in a positivist paradigm using quantitative research methods. The design was adopted to explore the research questions and hypotheses and to meet the research objectives and aims, outlined in the introduction chapter. Unlike data from listed companies, data collection from small firms is considerably harder and more expense to acquire, constraining the availability of data collection methods. A survey approach to testing the statistical hypotheses was considered necessary in order to generate preliminary data on the status quo of corporate governance, regulation and performance of small corporations in Australia across a range of constructs.

Given that this is the first study in Australia to apply the legal definition of the Corporations Act (2001 Cth) to small corporations, there is no prior knowledge or data specifically on the characteristics of the small corporations. Thus the sample frame is unknown and the firms fall into a definition of a small corporation that has to be determined *ex post*, hence large corporations were dropped from the response cohort. Balancing practical matters such as cost, timeline and data availability, this study adopts a convenient survey approach to collect data using the online survey tool, Surveymonkey[2] (Cavana et al. 2001).

The research design is described in section 6.2 of this Chapter. It recognises that there are numerous measurement systems for corporate governance, regulation and performance within organisations (Audretsch and Lehmann 2011). The design incorporates the measurement of the relationship study between the different measurement of corporate governance, regulation and performance identified in Chapter 5. These relationships were explored using a quantitative approach, based on research instruments derived from instruments used in previous empirical studies. Section 6.2 also outlines the process adopted to select the sample groups used in both stages four and five of the study and the problems encountered in securing the participation of small firms.

The research was designed in six stages to ensure it is undertaken in a sequential and ordered manner, the flow chart of which are provided in Figure 6.1. This Chapter presents the methodology adopted for each stage in the sequence in which it was conducted:

i. Stage one comprised the literature search and review.
ii. Stage two involved a meta-analysis of the empirical literature and the development of the statistical hypotheses and conceptual framework.

[2] **www.surveymonkey.com**

iii. Stage three involved the development of questionnaire instruments based on the findings from stage one and two, which were later piloted to 26 CEOs of small firms and directors of industry associations.

iv. The results from the pilot surveys, as well as the findings from stage one and two, were used to assist the design of the questionnaire instrument in stage four of the study, which is outlined in the section 6.6 of this chapter. The pre-testing of the questionnaire and the reliability and validity were undertaken by the author before sending it out.

v. Stage five of the study involved the administration of the questionnaire.

vi. Stage six provides the detailed methods of collation, analysis and discussions of the results, outlined in section 6.8.

The data analysis method is specified in section 6.9, which includes econometric modelling and structural equation modelling (SEM). Econometric modelling will be used to test the hypotheses 1-9 and 11-18, which involves a relationship between individual corporate governance and regulation measures on performance. SEM is applied to estimating the relationships among latent variables, covering corporate governance, regulation, financial performance and social performance. The extension to the latent variable modelling also marked this study as a new approach to investigating the impact of corporate governance bundles as well as regulations on the performance of small firms.

The Chapter also discussed the process undertaken for ethics committee approval and the confidentiality of respondent information obtained during the project in the rest of the sections.

6.2. Research design

The philosophical foundation for this study is positivism. The development of the research design requires decisions to be made about the purpose of the study, the study setting, unit of analysis and time horizon (Cavana et al. 2001).

The research was a non-contrived, cross-sectional study. The purpose of the study was primary hypothesis testing as to explain the nature of the relationships between the different constructs. To the extent that the study was interested in delineating between the internal and external situations associated with corporate financial and social performance, it can be described as a confirmative causal analysis. Hence, the study was scoped to test the hypothesized causal relationships based on prior research and avoid seeking for causality based on data-driven analysis.

Positivism

Positivism serves as the fundamental philosophical basis for this study. Positivism has been selected primarily because it fits with the requirements of causality testing suggested by theories and prior empirical research. Moreover, it has been recognised as a rigid evidence-based approach, which produces more objective results. It is hence found to be an appropriate research epistemology for this study. An extension of the positivist research results is via the meta-analysis procedure to summarise findings based on prior positive analysis.

Selection of the research sample groups

A random sample is ideal for the survey analysis if the sample frame is set. However, given that small corporations have yet to be substantially examined in the research literature, there were no prior sample frames, which could be used to inform this study. This researcher did not have the luxury of benefiting from a census conducted by government bodies before the survey. Due to the lack of sample frame and given the time and resource constraints, the web survey was recognised as the best option (Bethlehem and Biffignandi 2012).

A convenient sample was obtained by promoting the call for responses to the survey via newsletters of industry associations, university industry networks and the industry research partners such as Federal Department of Treasury and COSBOA. The link for the survey was created and embedded in newsletters and emails which were sent to the peak industry associations such as COSBOA, VACC and VECCI. Through the newsletters and promotion via the industry associations as well as the industry connections of research partners and industry partners namely the Federal Treasury, COSBOA, Victoria University, University of Western Sydney, University of Canberra, Southern Cross University and University of Technology Sydney, the research team invited small corporations' participants to respond to the web survey. The survey also asked the respondents to provide their post codes, which are used to map back to the local government areas for the calculation of the sample weights.

The final sample is consisted of 391 respondents. Applying the small corporations' definition from the Corporations' Act 2001(Cth) to the sample, four companies were ruled out, which yields a sample of 387 observations.

Given the nature of the convenient sample, it is subject to self-selection bias, non-normality and missing value problems. The self-selection bias had been compensated by applying sample weights, proxy by the inverted proportion of small corporations in each local government areas calculated from the post codes and the ABS Regional Profile data. Non-normality had been corrected by introducing innovative statistical estimators — Robust Weighted Least Squares Approach (WLSMV). And missing value problem had been addressed by modelling the patterns of the missing values and filling in the missing values using the full-information maximum likelihood (FIML) methods. The effects of the analysing approximately normally distributed ordered categorical data and non-normal ordered categorical data are briefly discussed below. A detailed statistical treatment of the non-normality issue has been provided by Hancock and Mueller (2006).

Effects of analysing approximately normally distributed ordered categorical data

Researchers often ignore the categorical nature of the data if ordinal data are used in the modelling and assume that the same methodology as the normally distributed continuous data. The fundamental difference from the traditional analysis of continuous data is that the ordinal data requires the construction of a covariance matrix based on Pearson product-moment correlational techniques. If few categories are used the maximum likelihood estimation is employed, the model fit indices, parameter estimates, and standard errors can be biased (Hancock and Mueller 2006).

Effects of analysing non-normal ordered categorical data

Ordinal data are considered by some researchers as non-normal (Hancock and Mueller 2006). However, if the observed data have more than five categories and are approximately normal, then using the traditional maximum likelihood approach does not necessary incur any severe bias in the fit indices, parameter estimates, or standard errors. It will only be problematic if the observed data, as well as the underlying latent construct, has less than five categories. The less the categories, the less likely the data will proxy normal distribution. Hence advanced estimators have to be used to compensate for the bias incurred. The robust weighted least squares approach (WLSMV) will be applied to all the modelling process for this thesis to reduce the impact of non-normal distributions.

The purpose of study

This study is confirmative in nature and is intended to determine the impact of governance and regulation on performance of small firms in Australia. The goal of the study is to empirically estimate the impacts of governance and regulation factors on performance and to develop policy instruments with a view to improving the performance of small corporations.

The study setting

This study uses a non-contrived cross section data; which is first hand data and was collected in the natural environment. There was minimal research interference. The participants are able to exit the questionnaire at any time they wish.

The unit of analysis

The unit of the analysis for this study was individual small corporations in Australia. Data for analysis was collected by a structured questionnaire. The details of the interview schedule and questionnaire is set out below and attached in the appendix 3.

Time horizon

The project was undertaken between March 2010 and November 2011, which coincided with the aftermath period of the 2008 Global Financial Crisis (GFC). The pilot interviews were conducted during March – November 2010. And main data collected using the structured questionnaire was between November 2010 and November 2011.

6.3. Stage 1: Literature search

Stage one of the research involved a review of the academic literature pertinent to the theories of governance and regulation and empirical studies. The databases outlined in Table 6.1 were used for the literature searching purpose. The databases were accessed through the Victoria University Library and various internet search engines, such as Google Scholar. The initial search used key words such as ‘corporate governance’, ‘governance’, ‘board of directors’, ‘board duality’, ‘board independence’, ‘board network’, ‘regulation’, ‘regulatory compliance’ together with ‘non-listed companies’, ‘unlisted companies’, ‘small firms’, ‘family business’, and ‘small and medium-sized enterprises (SMEs)’. The search for relevant articles from selected journals was based on an issue by issue searching strategy. Then a ‘snowballing’ approach was adopted to identify relevant articles published in other venues.

Table 6.1 Databases used in the literature search

Database	Source
JSTOR	VU library
ProQuest	
ABI/INFORM Global	
EconLit	
SSRN	
Google Scholar	
Entrepreneurship and Small Business Management related journals *: Journal of Business Venturing, Entrepreneurship: Theory and Practice, International Small Business Journal, Entrepreneurship and Regional Development, Small Business Economics, Journal of Small Business Management, and Family Business Review	
Governance related journals *: Journal of Business Ethics, Corporate Governance: An International Review, Governance: An International Journal of Policy, Administration and Institutions	

Note: * The author manually searched the most relevant journals in the fields of accounting, economics, finance and management, suggested by the Australian Research Council's ERA Ranking. In addition, the author also searched top journals in the field of Entrepreneurship, Small Business Management and Governance.

Searches of the academic literature were conducted intensively between October 2009 and December 2012. Literature updates have been on a continuous basis thereafter until March 2014.

6.4. Stage 2: Identifying the key factors and relationships in focus

Research questions were concerned with identifying the relationships between governance and regulation factors and the performance of small firms. Hypotheses developed in Chapter 5 were tested based on the data collected from the structured questionnaire.

Based on the existing theories reviewed in Chapter 2 and Chapter 3, a meta-analysis approach has been adopted to ascertain the relationship between variables. Prior empirical studies have also been systematically reviewed and serve as an evidence base for the development of statistical hypotheses. In particular, Chapter 2 and 3 provides the theoretical foundations for the establishment of causal relationships between constructs, while Chapter 5 estimated the hypothesised sign and magnitude of the relationships. This is the most important exercise in causality focused studies, given that the causal relationships solidly rest on theoretical deductions rather than on data-driven inferences.

The theoretical literature identifies a number of variables impacting corporate governance mechanisms, including board size, duality, board independence, board networks, interest alignment, board meeting frequency, and independent audit. Financial performance can be measured by accounting indicators including total assets, total sales, total net profit, and net profit growth. CSR can also be measured by components such as customers, suppliers, employees, philanthropy, and environment. Regulatory mechanisms include ASIC regulation, record keeping, directors' duties, information disclosure, Occupational Health and Safety (OHS), superannuation, work relationship, maternity leave, quality assurance, and environmental protection.

6.5. Stage 3: Pilot interviews with the CEOs and Managers and Heads of Industry Associations

In order to obtain in-depth information about the status quo of small firms' operation, governance and regulation, a semi-structured interview was used. The interview schedule was developed based on main issues identified from the literature and expert judgement. Twenty six respondents were recruited through industry associations and confirmation of participation by themselves, seventeen of whom are small corporations and the rest are industry associations.

Sample of the pilot interview

The CEOs/Managers as well as Heads of Industry Associations were recommended by COSBOA. The research team sent out an email to invite participation in the study. At least two moderators were involved in the interview process, in order to make sure that the recording is objective and reduced any potential bias. The results were recorded by two separate researchers and double-checked for validation.

Two versions of the questionnaires were used, one for the small corporations and one for the industry associations. Seventeen small corporations were recruited via the recommendation of their industry associations and agreement to participate by themselves. Approximately one hour interviews have been conducted with the interviewees either in person or by phone. Two interview experts were recruited to undertake the interview, both of whom are native English speakers and are experienced in communicating with senior executives in organisations.

The results of the pilot interview were reported in Armstrong et al. (2011). The report identifies a number of themes pertinent to the governance, regulation and performance of small corporations, including industry, business development stage, sources of advice about regulation, cost on meeting regulatory compliance requirements, different types of regulatory compliance requirements, types of difficulties facing business operation, succession planning, role of different stakeholders in the decision making process and the corporate governance of small corporations or small business members. These themes serve as the foundation for the development of the large scale questionnaire in Stage 4.

6.6. Stage 4: Design of the main research questionnaire

As a result of the literature review and pilot interview, findings were incorporated in the development of final instruments. This was composed of five different sections: the demographics, regulation, governance, business operation and institutional factors. The instruments were cross-validated by an advisory panel consisted of domain experts[3].

6.6.1. The design of the main research instrument

The research instruments were drawn from a number of sources including existing academic research papers, World Bank Business Environment and Enterprise Performance Survey and related publications. Modifications of the research instruments were also made from suggestions in the pilot interviews and from domain exports. Details of the source of each section in the questionnaire are provided as follows.

6.6.2. Section 1: The Demographic Questionnaire

The instruments for the Demographic Questionnaire were adapted from the World Bank Business Environment and Enterprise Performance Survey Section One. Questions in regards to the industry association, development stage of the firm, position of the respondent and years in the position and suggestions from the literature and by domain experts.

The demographic questionnaire included questions for both the small corporations and their managers or owners. The firm-level questions included age (year in which the business started operations), legal status, industry in which the business operates following the Australian and New Zealand Standard Industrial Classification (ANZSIC) (ABS 2006) by division, the geographical location, and whether or not the company is listed on the stock exchange.

The development stage on the business life cycle was found to be a critical factor determining its financial performance (Filatotchev 2006; Roche 2010), and seven stages were specified, including:

[3] The advisory panel members at Victoria University are Professor Anona Armstrong, Professor Andrew Clarke, , Professor Colin Clark, Professor Neil Andrews, and Professor John Breen. Comments from Emeritus Professor Harry Glasbeek is also appreciated.

i. Seed stage when the business is just a thought or an idea;

ii. Start-up stage when the business is born and exists legally;

iii. Growth stage, when the business has made it through the toddler years and now is a child;

iv. Established stage when the business has now matured with a place in the market and loyal customers;

v. Expansion stage, when a new period of growth into new markets and distribution channels;

vi. Decline stage when changes in the economy, society, or market conditions can decrease sales and profits; and

vii. Exit stage when there is big opportunity for the business to cash out all the efforts.

The number of sites can be used as a proxy for the complexity of the organisational operations (Hsu et al. 2012). Industry association is recognised as a proxy for business networks (Wincent et al. 2009).

Characteristics of the owner or manager include the position of the manager, which is also used to code for the duality of directors when cross tabulating with the board characteristics data; years of which he or she has been in the role; highest level of education obtained; age; and gender.

6.6.3. Section 2: The Regulation Questionnaire

The Regulation Questionnaire was mainly derived based on findings from the semi-structured interviews with the CEOs/Managers and heads of the industry associations. Additional questions were added to capture the details of regulation, including the Constitutions or

Replaceable Rules, time and money spent on meeting compliance requirements. The questions relate to Constitutions or Replaceable Rules suggested by the domain experts, while questions on regulatory compliance were derived from the literature.

According to the Corporations Act 2001, all corporations have to have either a constitution or use the Replaceable Rules provided by the Australian Securities and Investment Commission (ASIC). The Replaceable Rules are normally used the default arrangement. Question has also been asked about whether or not small corporations have encountered any difficulties with regards to the Replaceable rules and whether they have an overdraft in precaution for liquidity issues in the future. Whether the small corporation is a franchise or not is also of critical legal implication.

Regulation relates to the source of advice on regulatory compliance requirements, financial costs of regulatory compliance and difficulties encountered with specific regulatory requirements. The regulatory compliance advice normally comes from one of the four major sources for small corporations, namely industry associations, lawyers, accountants and government agencies. Regulatory compliance costs include the cost of the four advice sources, day equivalent that the small corporations spent on meeting regulatory compliance requirements and the corresponding dollar value estimation.

Regulatory compliance requirements can be specified as ASIC regulation, record keeping for tax purposes, directors' duties, information disclosure, occupational health and safety, superannuation management, workplace relationships, maternity leave, quality assurance and environmental protection.

6.6.4. Section 3: The Business Operation Questionnaire

The Business Operation Questionnaire was mainly developed based on expert opinion, existing literature, with reference to the World Bank Business Environment and Enterprise Performance Survey Section Two.

Given that small corporations may be reluctant to disclose their financial information, the financial data, including the total assets, total sales, net profit, sales growth rate and net profit growth rate are collected in ranges and percentages.

Another aspect of the business operations concerns the types and proportion of sales and the time it takes to collect cash from major customers, including government or government agencies, large domestic firms, small and medium size businesses, multinationals located in Australia, parent company or affiliated subsidiaries, not for profit organisations, overseas companies and others. In this case, full time equivalent employees can be used as a proxy for the company size.

Seventeen factors have been found to be potential barriers and the proportion of cost to total costs associated with the business operations, including access to financing, cost of financing, contract violations by customers and suppliers, cost of electricity, cost of transportation, access to land, title or leasing of land, rates of taxation, tax administration, customs and trade regulations, business licensing and permits, labour regulations, skills and education of available workers, uncertainty about regulatory policies, compliance with new laws, anti-competitive practices of competitors, and the Trade Practice Act.

The next set of questions focus on the involvement and importance of key stakeholders in major business decision making, including customers, suppliers, employees, financial investors, philanthropy and environment.

Questions also addresses the adoption of information and communication techniques (ICT), financial expenses on innovation, whether the small corporation has a strategic plan, whether it provides any formal training to its permanent employees, whether the technology is advanced comparing with their major competitors in the market, and major means to acquire technological innovation.

6.6.5. Section 4: The Corporate Governance Questionnaire

The Corporate Governance Questionnaire was developed based on the factors identified in the literature and suggestions from domain experts. The first and foremost question is whether the small corporation has a board of directors. If yes, how many do they have? How many are executive directors or independent directors or female directors?

The director selection may come from one of the seven sources, which measures the interest alignment between the director and the owner and manager, including founders or family members as executives and directors, shareholders with significant amounts of shares, shareholders without significant amount of shares, suppliers, consultants, retired executives, or no relationship with the firm at all.

The average age of the directors is used as a proxy for the personal calibre of directors. The number of shareholders is one criterion for being a small corporation under the Corporations Act 2001 definition.

Other factors pertinent to the performance of the board include board meeting frequency, the extent to which the directors use their own network, the shareholding of the largest shareholder, whether the small corporation has a success plan, and whether the small corporation is independently audited.

The information disclosure is one mechanism that is designed to curb managers' self-dealing. The small corporations may disclose to government or regulators, industry associations, public, shareholders, bank and financial sources, or others. The information they may disclose includes the financial and operating results of the corporation, major share ownership and voting rights, and potential risk factors.

6.6.6. Section 5: The Institutional Factors Questionnaire

The Institutional Factors Questionnaire was developed based on New Institutional Theory and related empirical studies. The questions concentrate on asset specificity, frequency and uncertainties. Given that transactions play a less important role in terms of the scale and frequency of business in small corporations, the Institutional Factors Questionnaire was only used to inform quantitative analysis but was not included in the major quantitative analysis.

6.7. Stage 5: Questionnaire data collection

Given that the small corporation's definition has never been used for data collection purposes nationwide, the sample frame is not readily available. Thus, this study took a purposive survey approach, targeting at small firms whichever is reachable. A number of venues were used to publicise an invitation to small firms' to participate in the survey, including newsletters in industry associations, alumni and business networks. The respondents were mainly located in Melbourne and Sydney, however, constrained only by their access to the internet given that the survey was online.

A commercial web survey tool, Survey Monkey, was used to collect data. The confidentially of the respondent is guaranteed and no respondent is traceable. The link for the survey was created and embedded in newsletters and emails which were sent to the peak industry associations such as COSBOA, VACC and VECCI. Through the newsletters and promotion through the industry connections of Victoria University, the research team invited small corporations' participants to respond to the web survey. Web survey has many advantages when compared with traditional pen and paper surveys. Firstly, recruitment of the participants may be exhibitive without a sample frame. Web surveys incur no cost as those for interviewers, printing and mailing. Secondly, the tendency to agree with statements in questions, regardless of their content, is less frequent in self-administered modes of data collection (Bethlehem and Biffignandi 2011). In particular, for content with sensitive issues or min those that may be perceived as having adverse consequences on participants, web surveys offer more privacy and confidentiality and may result in more objective responses. Thirdly, 'do not know' can be offered as an option for respondents to avoid personal or sensitive questions. Fourthly, respondents are more likely to give a socially desirable answer in paper-based interviews and questionnaires, while the web survey may be able to obtain objective answers. Fifthly, the web survey can introduce some smart techniques to improve the respondents' experience, such as providing checking for potential errors and designing automatic routines in order to navigate particular respondents skipping irrelevant sections. Last but not least, a web survey can be undertaken quickly and the respondents are not obliged to send the questionnaires back by post, which may be lost or misplaced occasionally.

Online surveys, however, may be subject to self-selection bias and may hamper the generalizability of the sample results to the population. A solution to this problem is to use sampling weights to each observation as a proxy for random selection. The random sampling weights, calculated using the proportion of small businesses (defined as less than 20 employees by the ABS definition) of all the businesses in each local postal areas. The sampling weights are used as proxies for self-selected sampling weights used in this study. The web survey had a question to capture the postal code of each respondent. The ABS Regional Profile data was also used to gather data for small business counts in each postal area. The sampling weight was calculated as the reciprocal of the small business count in the corresponding postal area.

6.8. Stage 6: Data analysis and methodology

6.8.1. Data collation

The data was first transformed into an excel format and then stored in STATA 12.1. The data analysis is mainly based on the quantitative data. The questionnaire also probed for in-depth qualitative information on some specific questions; such questions include details of industry associations, regulatory burdens and proposals to relieve regulatory burdens. The invitation letters were sent to CEOs of industry associations recommended by COSBOA. Respondents were selected to sit for the pilot survey. Based on the feedback from the pilot survey, the author consulted a number of domain experts for further comments with regards to the style, setting up of questions, potential impediments for the administration of the survey and brevity issue.

The revised version was circulated three rounds amongst the ARC linkage project team for further feedback and comments. Then a web version was developed and a link was created. The research tried his best to reach out to the industry associations, ie. COSBOA, VACC, VECCI, in order to solicit the interest for potential small corporations to participate.

The survey was administered online and data were collected anonymously. The confidentiality is not a concern for the small corporation respondents. The data was cleaned and used for quantitative modelling in SEM.

6.8.2. Methods for data analysis

Structural Equation Models (SEM) was the major tool used in the analysis of quantitative data. This study aimed to test the adequacy of pre-determined models based on prior theories and research using the confirmatory factor analysis. In addition, this study was designed to test relationships among latent variables and other variables, applying simultaneous regression equations.

The SEM is recognised in the field as an appropriate analytical approach for confirmative causal relationship analysis because of its huge capacity to handle many commonly employed statistical models, such as analysis of variance, analysis of covariance, multiple regression, factor analysis, path analysis, econometrics models of simultaneous equation and non-recursive modelling, multilevel modelling, and latent variable modelling. Hence, SEM can be viewed as an ‘umbrella’ tool encompassing a set of multivariate statistical approaches including conventional and recent development approaches. It is a widely used approach in social sciences because of its capacity to deal with latent variables.

The primary goal of an SEM analysis is to confirm research hypotheses about the observed means, variances, and covariances of a set of variables. SEM is viewed as a general model of many commonly employed statistical models, such as analysis of variance, analysis of covariance, multiple regression, factor analysis, path analysis, econometric models of simultaneous equation and non-recursive modelling (Tabachnick and Fidell 2007). Thus, SEM has been recognised as an appropriate method for addressing the modelling requirements of this study.

The Null Hypothesis in SEM

In SEM, an input matrix is the variance covariance matrix computed from the original data. The model implied matrix is the variance covariance matrix inferred by the estimates from the general SEM models. The null hypothesis for SEM is that the input matrix equals the matrix implied by the general SEM models. The equation for this null hypothesis in the sample is:

$$H_0 : S = \Sigma(\theta)$$

The equation states simply that the variance covariance matrix (S) is not statistically different from the implied covariance matrix $\Sigma(\theta)$, which is reproduced based on parameter estimates. In other words, one has to accept the null hypothesis of no difference (Bowen and Guo 2012).

Preparation steps and analysis decisions

Before applying the SEM, there are four preparation steps, suggested by Bowen and Guo (2012), including

i. Assess sample size adequacy.

Kline (2005) gives absolute and relative guidelines on the ratio of cases to estimated parameters. He suggests that fewer than 100 cases is a ‘small sample’, 100 to 200 is ‘medium’ and over 200 is ‘large’. In relative terms, Kline suggests that a 20:1 case-to-parameter ratio is desirable, 10:1 is ‘more realistic’ and 5:1 is ‘doubtful’. Given that the study has 390 observations, which is larger than 200, this study have a ‘large’ sample.

ii. Decide how to handle missing data.

The literature frequently discusses three types of causes of ‘missingness’, namely missing completely at random (MCAR), missing at random (MAR), and missing not at random (MNAR) (Graham 2009). MCAR is a restrictive form of missingness, and typically it is difficult for researchers to discern its presence in empirical settings. MAR refers to a pattern of missingness that depends on observed data, but not on the values of the outcome of interest. MNAR is a pattern of missingness that is systematic or that is based on values of the outcome variable of interest. The survey data for this study is a combination of MNAR for the outcomes variables of interest and MAR for the rest of the exogenous variables.

There are several common methods for dealing with missing data, including: (a) likewise deletion or analysis based on complete cases, (b) pairwise deletion, that is, calculating a correlation or covariance matrix such as that employed by SEM by using complete cases for each pair of variables, (c) mean substitution by replacing missing values of a variable by its sample mean of the complete cases, (d) incorporation of a missingness dummy variable in the analysis in addition to the specially coded missing value, (e) regression-based single imputation, and (f) imputation of categorical values based on data from cases with similar response patterns on other variables.

Recent developments originated from Little and Rubin's (2002) seminal work on missing data, includes three procedures on data integrity, namely (a) the expectation maximization algorithm (EM), (b) multiple imputation (MI) under the normal model, and (c) full-information maximum likelihood (FIML) methods. Graham (2009) compared the traditional and new methods for handing missing values and found that FIML outperformed all the comparison methods in that FIML offers good estimates of standard errors and permits researchers to perform hypothesis testing without serious bias.

Thus, this study adopted the FIML methods to deal with the missingness issue in the survey data, which is good practice in empirical research. FIML is a default missingness handling method in Mplus, for estimators other than maximum likelihood. This study flags missing values with '-999'. Hence Mplus calls for FIML whenever '-999' presents.

iii. Choose the proper estimation method for the measurement level and distributional characteristics of variables.

The measurement level and distributional characteristics of variables are essential checks for multivariate analysis. Though SEM accommodates all measurement levels and distributions, special analysis properties much be called upon for variables not meeting the default assumptions. Ignoring these issues can lead to biased results and inaccurate conclusions, and reduce the credibility of results (Bowen and Guo 2012).

There are four types of statistical measurement, namely nominal, ordinal, interval and ratio. In order to reduce the respondents' sensitivity concern about releasing financial data, the variables in this study were mainly interval in nature, but could also be treated as ratio data given that the zero property holds. Given that more than 5 levels of measurement are used for the outcome variables, it is appropriate to treat them as continuous variables (Byrne 2012).

Default SEM procedures assume that observed variables have normal distributions, which has a skewness value of 0 and a kurtosis value of 3. Kline (2005) indicated that a skewness value of 3 or -3 can be regarded as greater 'extreme' skewness and +/- 20 can be indicative of 'problematic' kurtosis. This study applies these cut off points to assess the normality of univariate distribution.

To identify the univariate and multivariate outliers, this study uses the Mahalanobis distance statistics. Any variables with a p-value of 0.001 is regarded as an outlier.

This study applies the variance inflation factor (VIF) to assess for multicollinearity. VIF values greater than 10 indicate a potentially harmful multicollinearity problem (Kline 2005).

Kline (2005) offers five strategies to address non-normal distributions: (a) normalise the non-normally distributed variables with data transformations, then analyse the transformed data with standard maximum likelihood estimation; (b) use a corrected normal theory method such as the Satorra-Bentler approach to adjust estimated standard errors and perform a revised version of model chi-square test; (c) use an estimator that does not assume multivariate normal distribution; (d) create a special correlation matrix that takes into account the measurement level of variables, and analyse it and an appropriate weight matrix with a weighted least square estimation procedures; and (e) to use bootstrapping to obtain a more accurate standard error estimates based on multiple sample of available data[4]. The fourth option is especially recommended by many SEM experts in that it enables the estimators to handle dichotomous, ordered categorical, unordered categorical and count variables. Hence this study adopts the fourth option, which is a built-in option for various estimators in Mplus.

Another potential data problem is known as 'ill-scaling', meaning that the ratio of the greatest to the smallest variance of observed variables in a dataset is greater than 10. The ill-scaling problem had been corrected by multiplying a variable with a constant, which essentially does not change the correlation of variables.

The data structure is simple so that there is no need to consider issues related to hierarchical data.

iv. Finalise variables and data files for analysis

Processing the raw data through the aforementioned three steps, the raw data is then saved in a text file. The data does not have variable names as required by the Mplus input formats, which has to be specified in Mplus in the modelling process. The data format is convenient for using FIML to handle missing values in Mplus. So far, the data is clean and is ready for SEM.

Byrne (2012) strongly recommend that SEM modelling be undertaken in the following two stages: fitting the measurement model first, then fitting the structural equation model. For each stage, four major steps should be followed, including (i) model specification, (2) model estimation, (3) evaluation of results, and (4) model modifications.

[4] The fifth approach is described by Bollen (1989).

To ensure bias in analysis is reduced, the discussion and policy recommendations with explore issues surrounding the quantitative data and qualitative data.

6.9. Ethics approval and confidentiality of participation information

This section of the Chapter discusses ethics committee approvals for the research and how the confidential information and data of individual respondents was handled. The ethics approval was gained from the Human Research Ethics Committee, Faculty of Business and Law, Victoria University for stage four and for stage five. Copies of memos relating to the Ethics Committee approvals are appended in the Appendix 2.

Deontological principles dominated the ethical standards adopted in the research. These include treating subjects with respect and dignity; allowing autonomy in their decision-making, especially those concerning whether or not to participate, or interrupting during the course of answering the questionnaire; and having concern for their well-being and avoiding group-think (Lefkowitz 2003).

As all respondents to the study were over 18 years of age and professionals living in Australia, it was assumed that they were literate in English and that no translation of information was required.

In the study design, the author also considered that any respondent who had completed either the pilot or main survey online was in effect consenting to participation. The focus, therefore, was on ensuring respondents had sufficient information about the study so that they could make an informed decision as to whether or not to participate and to understand what rights they had to confidentiality.

In terms of confidentiality, the physical documents relating to the respondents were kept in locked filing cabinets in a locked room in the Principal Supervisor's office. Where data was transcribed in a digital form it was protected by passwords on computer, although it was understood that data stored on servers connected to the internet posed more risks to the confidentiality of respondents than data stored in locked filing cabinets (Nosek, Banaji & Greenwald 2002).

6.10. Summary

This chapter provided a discussion of methodology. It included methodological details on the design and operation of this study. Research results on the impact of corporate governance on financial performance of non-listed small corporations will be reported in Chapter 7 and those on regulation in Chapter 8.

CHAPTER SEVEN RESULTS THE IMPACT OF CORPORATE GOVERNANCE ON PERFORMANCE OF NON-LISTED SMALL CORPORATIONS IN AUSTRALIA

7.1. Introduction

In Chapter 5, the author applied meta-analyses to summarise the research findings on the impact of each individual corporate governance mechanism of small firm performance, based on which the conceptual framework was developed. Chapter 6 provided details about the methodology for surveying and data analysis. This chapter, Chapter 7, reports the results from the major survey on small corporations. Characteristics of the small corporation and characteristics of the owners and/or managers respondents of small corporations are summarised first.

The performance and corporate governance of the small corporations were analysed and a performance measurement model was developed, followed by the path analysis model evaluating the impact of each individual corporate governance mechanisms on corporate governance and measurement model of corporate governance for small corporations. The structural equation modelling assessed the impact of corporate governance as a bundle of mechanisms on the performance of small corporations. The last sector summarises the results related to corporate governance and performance of small corporations.

7.2. Data screening

This section describes how characteristics of data were examined for consistency with distributional assumptions. First, individual variables were checked for normality by means of both univariate and multivariate procedures. Then, data assumptions were checked for variates, by means of both univariate and multivariate procedures.

Data Screening of Individual Variables

Outliers. A single low outlier with $z < -4$ was observed for only 12 of the 59 variables. Further, the 12 outliers came from different cases. Since there was minimal evidence of univariate outliers, the initial decision was to retain all data. Next, Mahalanobis D^2 distances were generated for each case using SPSS Regression with case number as the dependent variable and all non-demographic measures as independent variables. Higher D^2 values represent potential multivariate outliers.

Examination of D^2 values for all cases suggests the presence of four multivariate outliers, which were dropped from the analysis, thus the remaining 387 observations were retained for analysis.

Normality. Ten of the 59 variables were moderately negatively skewed, with skewness < -1, although none of these had skewness < -2. The standard error of skewness was 0.125, so these ten variables were statistically significantly skewed at the 5% level. Fourteen variables had positive kurtosis > 1. More seriously, four showed negative kurtosis < -1.

The power of univariate tests is not severely affected if non-normality is solely due to skewness, however excessive kurtosis does seem to have an effect (Sharma, 1996). In particular, negative kurtosis (a flat distribution) has a more severe effect. Thus there was evidence of some univariate nonnormality (3 out of 59 variables with moderate negative kurtosis). These three variables are total assets, total sales and net profits. The log transformation was applied to compensate for the nonnormality problem.

Multivariate normality of the individual variables was checked following the procedure described in Sharma (1996: 380-382). The correlation coefficient between the Ordered Mahalanobis Distances and Chi-square is 0.985. This value exceeds the critical value of

0.983 (alpha = .05, n = 74), so the data likely came from a multivariate normal distribution (Sharma, 1996).

In summary, some individual variables had moderately non-normal distributions, although overall the data appeared to have a multivariate normal distribution. This is unusual since evidence of univariate non-normality often (but not always) suggests multivariate non-normality. In the present context, since most of the variables are ordinal with limited discrete values, and since both hypothesis testing in this study was multivariate in nature and less than 10% of the variables had moderate negative kurtosis, normality of the individual variables was assumed.

Homoscedasticity and Homogeneity of Variance were reviewed. Most individual variables were measured at the ordinal level, so homoscedasticity was not evaluated by means of bivariate plots. Levene's test of homogeneity of variance was assessed for the categorical variables: legal form (two categories: company; non-company); development stage (three categories: growing; established; and declining); membership of industry association (two categories: member; non-member); number of full-time equivalent employees (FTEs) (five categories: 1; 2-5; 6-19; 20-49; 50 and above) and Industry (two categories: service industry sector; non-service sectors). Levene's test of homogeneity of variance was not significant. Thus, variances of dependent variables across categories of the predictor variables were found to be similar.

Data screening of variates

Normality. First, skewness and kurtosis values were assessed, and the general shapes of histograms were examined. None of the values had an absolute value greater than one, indicating little suggestion of univariate nonnormality.

A Kolmogorov Smirnov z test was conducted to provide additional evidence of univariate normality (Tabachnick & Fidell, 2007:80). Generally, a z-value above 2.58 signals that normality can be rejected at the 1% level of significance (Hair et al., 2006). Normality of the variates was then tested from a multivariate perspective.

The correlation coefficient between the Ordered Mahalanobis Distances and Chi-square is 0.995. This value exceeded the critical value of 0.926 (alpha = .05, n = 12), so the data likely have a multivariate normal distribution (Sharma, 1996).

Homoscedasticity, Homogeneity of Variance, and Box's M Test. Four dependent variates - , corporate governance, financial performance, CSR, and government regulation - were regressed with the other five categorical variates (including legal form, industry, development stage, FTEs and membership of industry association) in order to examine for homoscedasticity. All indicated that the variability in dependent variate scores was roughly the same at all values of each predictor variate.

Homogeneity of variance statistics for five categorical variables, namely legal form, industry, development stage, FTEs, and membership of industry association. The Levene statistic was generally not significant, indicating that homogenous variances may be assumed.

Finally, a Box's M test was performed by specifying all four dependent variates in a multivariate assessment of the homogeneity of variance-covariance matrices. None of the results were significant.

In sum, there was little evidence to suggest that the assumption of homoscedasticity was not reasonably satisfied by the dataset.

Linearity and Multicollinearity

Multicollinearity is a problem that occurs when variables are highly correlated (>.90); the sizes of error terms become inflated (Tabachnick & Fidell, 2007). Correlations between the variates were calculated. None of the correlations were above 0.80, thus this preliminary analysis did not suggest that any of the variates were redundant. Finally, scatterplots were examined and little suggestion of excessive non-linearity was found.

In summary, individual variables and variates were tested for basic distributional assumptions before testing relationships between constructs. Overall, the data screening process concluded that the data was suitable for further multivariate analysis.

7.3. Descriptive statistics of corporate governance and performance

7.3.1. Characteristics of small corporations

The survey collected effectively 387 responses from small corporations around Australia between June 2010 – June 2011. The data collection period happened to fall in the aftermath of the 2008 Global Financial Crisis (GFC), which provides a timely snapshot of those businesses that survived the 2008 GFC. The basic characteristics of small corporations in the sample are summarised in Table 7.1.

Of all the respondents, about two thirds of the respondents (66%) employ less than five full-time equivalent employees (FTEs), and are called micro businesses by the ABS definition (ABS 2000). Essentially, the sample is a micro-business majority sample. A quarter of small corporations (26%) employ five to nineteen employees. About fifteen per cent of the small corporations' respondents employ more than 20 employees. Approximately half of the sample failed to specify the number of employees in their corporations.

Approximately two thirds of the corporations in the sample (59%) have less than half a million dollars of total assets. One third of the small corporations (35%) have a total asset valued between half a million to five million dollars. Only twelve corporations (6%) have a total asset between five million to twenty-five million dollars. Thus, the majority of the small corporations in the sample (94%) have total assets with a value under five million dollars.

More than half of the small corporations (53%) started their business before the Asian Financial Crisis in 1998. More than a third of the small corporations were established during the period of 1998 to 2008. After 2008, forty-three corporations (11%) were started.

Approximately three quarters (71%) of the small corporations are companies; the other quarter is either partnerships or sole traders. This research project treats all forms of private entities as small corporations as long as they fits the definition of small corporations in the Corporations Act 2001 (Cth) (S45A).

The industries have been merged into three categories, the production industries, the trade and transportation industry and Personal, Financial & Business Services. The production industries include Agriculture, Forestry and Fishing, Manufacturing and Construction. The trade and transportation industry include Wholesale Trade, Retail Trade and Transport, Postal and Warehousing. The other service industries include Electricity, Gas, Water and Waste Services, Accommodation and Food Services, Information Media and Telecommunications, Financial and Insurance Services, Rental, Hiring and Real Estate Services, Professional, Scientific and Technical Services, Administrative and Support Services, Public Administration and Safety, Education and Training, Health Care and Social Assistance, Arts and Recreation Services and Other Services. The sample does not have any respondents from the Mining sector. The respondents from Personal, Financial & Business Services industries dominate the sample (65%). Approximately a quarter of the respondents (22%) come from the Trade and Transportation industries. Only forty-nine (13%) respondents come from the Production industries.

Of all the respondents, 60% (231) are located in New South Wales (NSW), 27% (105) in Victoria and 13% (50) in the other States or Territories. The sample has a strong presence of small corporations from Victoria and NSW.

Small corporations were asked to map their business development status in the seven-stage business development cycle, including Seed Stage (when a business is just a thought or an idea). Start-Up Stage (when a business is born and now exists legally.); Growth Stage (a business has made it through the toddler years and is now a child.); Established Stage (a business has now matured with a place in the market and loyal customers.); Expansion Stage (a new period of growth into new markets and distribution channels.); Decline Stage (changes in the economy, society, or market conditions can decrease sales and profits.); Exit Stage (this is the big opportunity for your business to cash out on all the effort.). One in two respondents' firms (191, or 50%) were at the established stage; four out of five small corporations are either at the Growth Stage, or Established Stage of the Expansion Stage. Sixteen small corporations (4%) were at the start-up stage, thirty-eight small corporations (10%) were now facing a decline of their business, while nineteen small corporations (5%) were exiting.

Approximately four out of five small corporations (78%) have one business site. Thirty-nine (10%) small corporations have two sites. Forty-five small corporations (12%) have more than two sites.

It is obvious that two out of three firms been surveyed are micro-businesses and 29% of them are unincorporated firms. The proportion of the micro-businesses in the sample is consistent with that in the ABS data (ABS 2010). To the best knowledge of the author, the data on the unincorporated firm is the first firm-level data which is collected in Australia. Rather than confounding the analysis of corporate governance and government regulation, such diversified sample offers a unique opportunity to analyse the impact of firm heterogeneity on the governance, regulation and performance of small corporations. Consequently, the "one size fits all" model of the prescribed regulation and corporate governance requirements can be contested.

Table 7.1 Characteristics of small corporations

	Percentage	Unweighted number
Employment size		
less than 5	66%	127
5-19	26%	50
20-49	8%	16
50+	7%	13
Total assets		
Under $100k	27%	53
$100k-$500k	32%	62
$500k-$1m	20%	38
$1m - $5m	15%	29
$5m-$25m	6%	12
Business start date		
Prior to 1998	53%	206
1998-2008	36%	138
After 2008	11%	43
Legal status		
Company	71%	270
Partnerships	9%	36
Sole trader	16%	60
Others	4%	15
Industry		
Production	13%	49
Trade and transportation	22%	86
Personal, Financial & Business Services	65%	250
Business location		
Victoria	27%	105
New South Wales	60%	231
Other states	13%	50
Development stage		
Start-Up Stage	4%	16
Growth Stage	14%	53
Established Stage	50%	191

Expansion Stage	17%	64
Decline Stage	10%	38
Exit Stage	5%	19
Number of business sites		
1	78%	298
2	10%	39
More than 2	12%	45

Table 7.1 Characteristics of small corporations (Cont'd)

Industry association membership		
Yes	73%	281
No	27%	102

Approximately three out of four small corporations (73%) are members of at least one industry associations. The other quarter (27%) of small corporations do not have an industry association membership.

To sum up, a small corporation in the sample has the following characteristics:

i. Have less than 20 employees.
ii. Have total assets of less than one million dollars.
iii. Established prior to 2008.
iv. Exist in the legal form of companies.
v. In the Personal, Financial & Business Services industries.
vi. Located in NSW or Victoria.
vii. Either growing or established or expanding.
viii. Have one business site.
ix. Is a member of at least one industry association.

7.3.2. Characteristics of the owners and/or managers

The survey was addressed to the owners and/or managers of small corporations[5]. The respondents of the survey are owners and/or managers or employees who are assuming management roles of the small corporations. The characteristics of the owners and/or managers are summarised in Table 7.2.

Of all the respondents, 77% (297) are owner and managers; 17% (64) are managers only; 2% (6) are owners only; and 4% (17) are employees in management roles.

One in two respondents (51%) has been in the position for more than ten years. Approximately a quarter of the small corporations' respondents have been in the position for less than five years. One in five respondents (20%) has been in the position for five to ten years.

In terms of the highest educational level the respondents have obtained so far, approximately one in two (46%) holds a tertiary degree, including Bachelor's degree, Master's Degree, or Doctor's Degree; one in three (32%) have a certificate or diploma; one in five (21%) have below secondary education.

Of all the respondents, 34% (131) are aged between 50 to 60 years old; 32% (123) are aged between 40 to 50 years old; 22% (83) are above 60 years old; 12% (46) are 40 years or younger. Two thirds of the sample is represented by respondents aged between 40 to 60 years old.

Three quarters of the respondents (72%) are male and the other quarter are female (28%).

To sum up, the respondents of the survey has the following characteristics:

[5] The introduction section specifies the respondents' type are owners and/managers or person in management roles. Thus the respondents can opt in by themselves.

i. Owner and manager
ii. More than five years in the current position
iii. Holds at least a certificate/diploma or tertiary degree
iv. Aged between forty and sixty years old
v. The owner/manager is male.

Table 7.2 Characteristics of owners and/or managers

	Percentage	Unweighted number
Position		
Owner manager	77%	297
Owner only	2%	6
Manager only	17%	64
Others	4%	17
Years of experience		
Less than 5 years	28%	107
5-10 years	20%	78
More than 10 years	51%	196
Highest education level		
Tertiary degree	46%	176
Certificates and diploma	32%	123
Secondary school or below	21%	81
Age		
Under 40	12%	46
40-50	32%	123
50-60	34%	131
Above 60	22%	83
Gender		
Male	72%	277
Female	28%	107

7.3.3. Performance of small corporations

This study measures both financial performance and corporate social responsibility (CSR) of small corporations. The financial performance, as a latent construct, is measured by total assets, annual turnover, net profit, sales growth rate, and net profit growth rate. The CSR is a latent construct for CSR, measured by the importance of major key aspects affecting business decision making, including customers, suppliers, investors, employees, philanthropy and environment.

Financial performance

An overview of financial performance of small corporations was provided, followed by a breakdown of financial performance with respect to the development stage, membership of industry associations, legal status, and industry.

An overview of financial performance

The financial performance indicators, including total assets, annual turnover, net profit, sales growth rate, and net profit growth rate, are summarised in Table 7.3.

Four out of five small corporations (79%) have a total asset base of under $1 million. 95% of the small corporations has less than $5 million in total assets.

Table 7.3 Financial performance

	Percentage	Unweighted number
Total assets		
Under $100k	27%	53
$100k-$500k	32%	62
$500k-$1m	20%	38
$1m - $5m	15%	29
$5m-$25m	6%	12
Annual turnover		
Under $100k	10%	19
$100k-$500k	34%	67
$500k-$1m	19%	37
$1m - $5m	26%	51
$5m-$25m	9%	18
Above $25m	2%	4
Net profit		
Under $100k	69%	132
$100k-$500k	20%	39
$500k-$1m	6%	11
$1m - $5m	5%	9
Sales growth		
0	21%	41
Under 5%	29%	57
5%-9%	21%	41
10%-19%	18%	36
Above 20%	12%	23
Net profit growth		
0	21%	41
Under 5%	36%	69
5%-9%	19%	36
10%-19%	13%	25
Above 20%	12%	23

As for annual turnover (or total sales) during the 2010/11 financial year, approximately ninety per cent of the small corporations have total sales under $5 million. 9% of the small corporations (18) have an annual turnover of values between $5 and $25 million. Four firms (2%) generated more than $25 million revenue from sales. The polynomial trend lines show that the annual turnover has a quasi-normal 'bell-shaped' distribution, while net profit is significantly skewed to the left tail (Fig. 7.1).

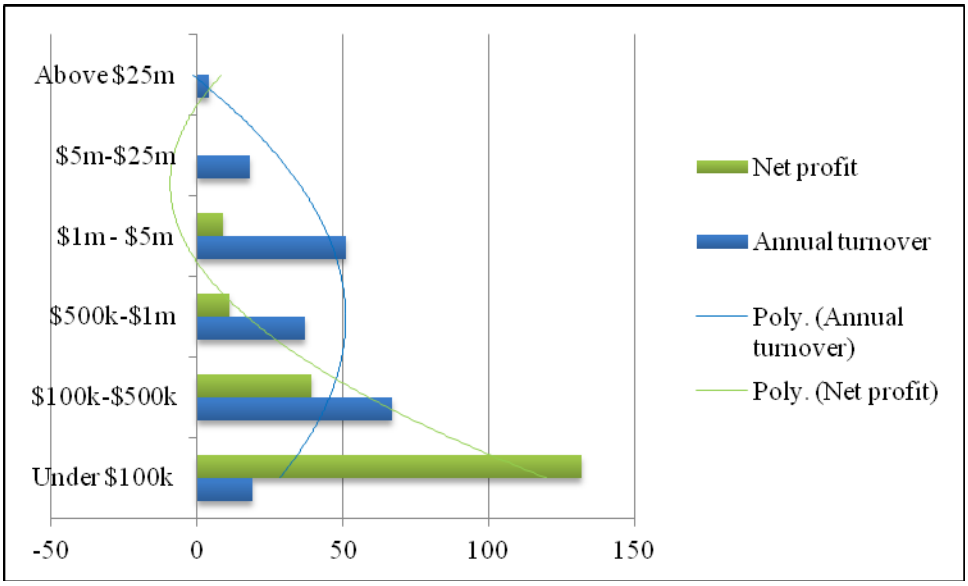


Fig. 7.1 Number of firms by net profit and annual turnover

The sales growth rate and net profit growth rate are measured in percentages. Of all the respondents, sales and net profit in one out of five (21%) corporations did not grow at all in the 2010/11 financial year. One in two small corporations has less than 5% sales growth and net profit growth. One in five small corporations has between 5% and 9% in sales growth and net profit growth. Approximately a third of the small corporations have sales growth above 10% and a quarter of the small corporations have net profit growth above 10%. The distribution of sales growth and net profit growth follow similar trends (Fig. 7.2).

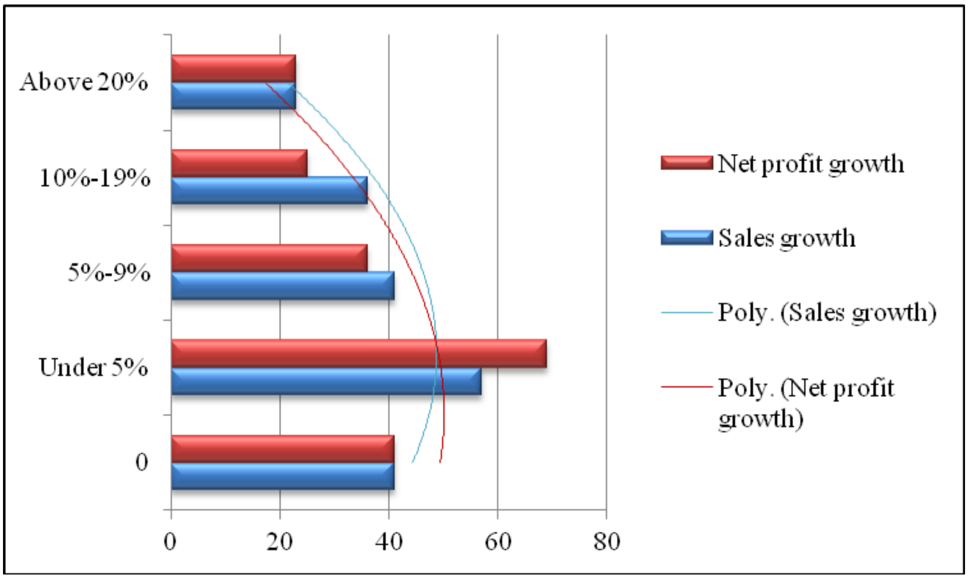


Fig. 7.2 Number of firms by net profit growth rate and sales growth rate

Financial performance by number of FTEs

A two-way graph and a regression trend-line show that, on average, small corporations with more FTEs tends to have more total assets (Fig. 7.3a), higher total sales values (Fig. 7.3b) and higher net profits (Fig. 7.3c). The fitted straight line is steeper for total sales, indicating that sales matters more for total sales, comparing to total assets and net profits. On average, larger small corporations are more likely to perform better in absolute values that their smaller counterparts.

The trend-line of total sales growth rate and net profit growth rate were relatively flat, meaning that the sales growth rates and net profit growth rates are relatively stable and does not vary with the number of FTEs. The straight trend lines for net sales growth rate slopes slightly downward while the net profit growth slopes slightly upward, meaning that on average net sales growth rate tends to be lower in small corporations with more FTEs, while net profit growth rate tends to be higher in small corporations with more FTEs.

The financial performance measures were cross-tabulated with number of FTs to explore the heterogeneity of financial performance varied by number of FTEs (Table 7.4). The characteristics of the financial performance were summarised below by number of FTEs.

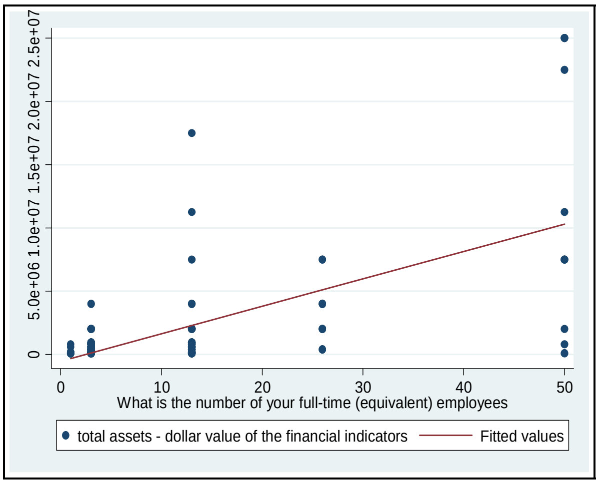


Fig. 7.3a Total assets versus number of FTEs

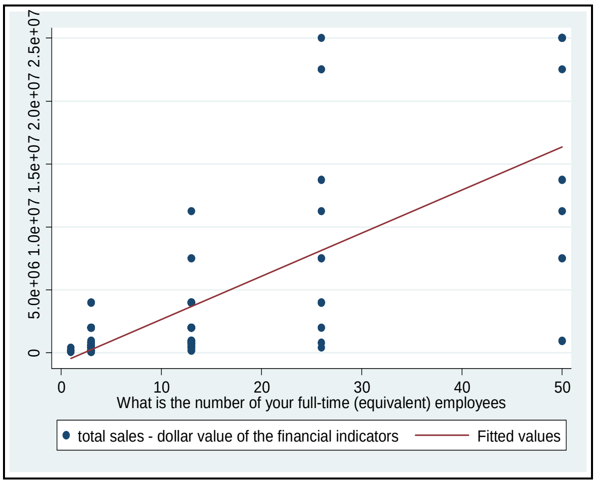


Fig. 7.3b Total sales versus number of FTEs

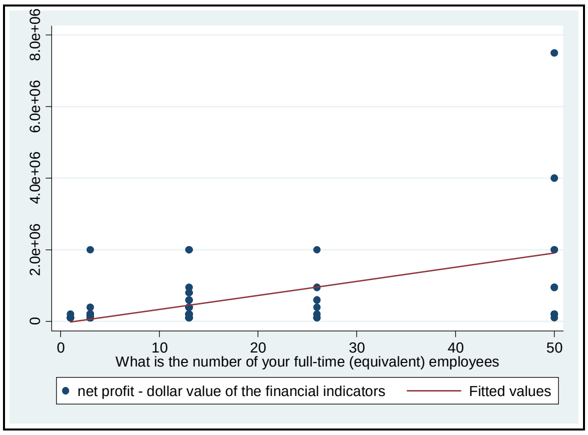


Fig. 7.3c Net profit versus number of FTEs

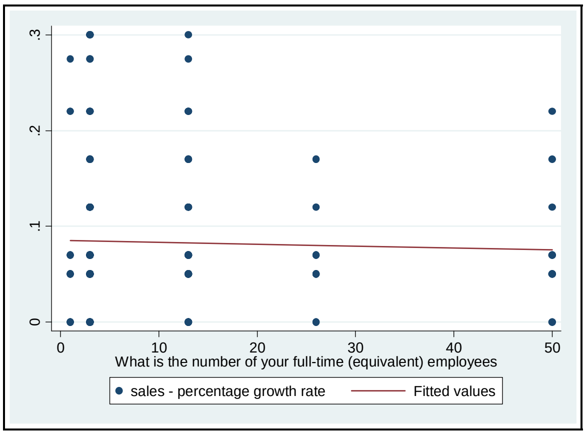


Fig. 7.3d Net sales growth rate versus number of FTEs

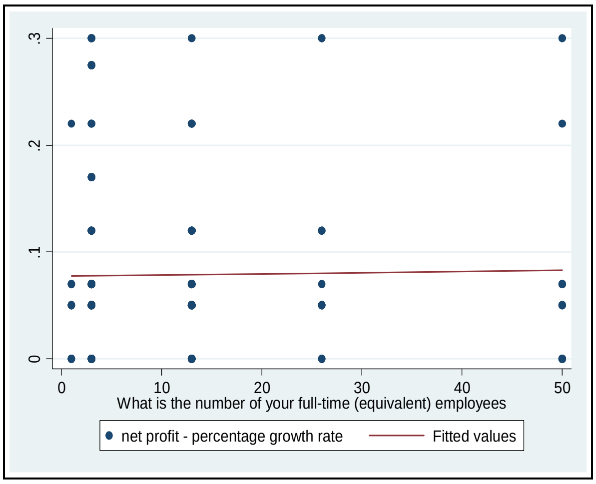


Fig. 7.3e Net profit growth rate versus number of FTEs

For small corporations with less than 5 FTEs, 87% have a total asset below $500,000; 63% have total sales valued between $100,000 and $500,000; 87.5% have net profits below

$100,000; approximately 80% has sales growth at a rate below 10% and 18.75% has sales growth at a rate above 20%; approximately 93%% have net profit growth at a rate below 10% and only one firm has a net profit growth rate above 20%.

For small corporations employing 5 to 19 FTEs, 77% has a total asset below $500,000 and 23% between $500,000 and $1 million; 73% has a total sales valued between $100,000 and $1 million; nearly all of them have a net profit of less than $500,000; 51% has a sales growth at a rate under 5%, and 13% have a sales growth rate of more than 20%; and 57% has a net profit growth rate under 5%, and 13% has a net profit growth rate of more than 20%.

For small corporations employing 20 to 49 FTEs, 71% have more total assets valued between $1 million to $5 million; 86% have total sales between $1 million and $25 million; 92% have a net profit less than $1 million; sales growth rate were relatively evenly distributed below 20%; 53% have a net profit growth rate under 5% and 40% have grown their net profit by more than 10%.

For small corporations employing more than 50 FTEs, 73% have total assets valued between $5 million to $25 million; 91% have sales valued between $5 million to $25 million; the net profit, sales growth rate and net profit growth rates were distributed relatively evenly.

Table 7.4 Financial performance indicators by FTEs

		Number of employees											
		Under 5		5-19		10-19		20-49		Above 50		Total	
Total assets	Under $100k	9	56%	32	33%	6	13%	0	0%	1	9%	48	26%
	$100k-$500k	5	31%	43	44%	11	23%	2	14%	0	0%	61	33%
	$500k-$1m	2	13%	16	16%	17	36%	0	0%	1	9%	36	19%
	$1m - $5m	0	0%	7	7%	10	21%	10	71%	1	9%	28	15%
	$5m-$25m	0	0%	0	0%	3	6%	2	14%	8	73%	13	7%
	Total	16	100%	98	100%	47	100%	14	100%	11	100%	186	100%
Total sales	Under $100k	6	38%	11	11%	0	0%	0	0%	0	0%	17	9%
	$100k-$500k	10	62%	50	51%	5	10%	1	7%	0	0%	66	35%
	$500k-$1m	0	0%	22	22%	12	25%	1	7%	1	9%	36	19%
	$1m - $5m	0	0%	13	13%	28	58%	5	33%	0	0%	46	25%
	$5m-$25m	0	0%	0	0%	3	6%	8	53%	10	91%	21	11%
	Total	16	100%	98	100%	48	100%	15	100%	11	100%	186	100%
Net profits	Under $100k	14	87.50%	79	84%	25	53%	5	38%	1	9%	124	69%
	$100k-$500k	2	12.50%	14	15%	15	32%	3	23%	3	27%	37	20%
	$500k-$1m	0	0.00%	0	0%	5	11%	4	31%	2	18%	11	6%
	$1m - $5m	0	0.00%	1	1%	2	4%	1	8%	3	27%	7	4%
	$5m-$25m	0	0.00%	0	0%	0	0%	0	0%	2	18%	2	1%
	Total	16	100.00%	94	100%	47	100%	13	100%	11	100%	181	100%
Sales growth rate	0	5	31.25%	21	22%	7	14%	3	20%	2	17%	38	20%
	Under 5%	5	31.25%	28	29%	14	200%	5	33%	4	33%	56	30%
	5%-9%	3	18.75%	16	17%	13	68%	3	20%	3	25%	38	20%
	10%-19%	0	0.00%	18	19%	9	100%	4	27%	2	17%	33	18%
	Above 20%	3	18.75%	12	13%	6	75%	0	0%	1	8%	22	12%
	Total	16	100.00%	95	100%	49	100%	15	100%	12	100%	187	100%
Net profit growth rate	0	5	35.71%	21	22%	7	15%	3	20%	4	36%	40	22%
	Under 5%	5	35.71%	33	35%	19	40%	5	33%	3	27%	65	36%
	5%-9%	3	21.43%	17	18%	9	19%	1	7%	2	18%	32	17%
	10%-19%	0	0.00%	12	13%	8	17%	4	27%	0	0%	24	13%
	Above 20%	1	7.14%	12	13%	5	10%	2	13%	2	18%	22	12%
	Total	14	100.00%	95	100%	48	100%	15	100%	11	100%	183	100%

Financial performance indicators by development stage

On average, small corporations at the established stage tends to have the highest total assets per FTE of $164, 705 and total sales per FTE of $251,592.5; those at the growth stage tend to have the lowest total assets per FTE and total sales per FTE, but the highest net profit per

FTE, sales growth rate and net profit growth rate; those at the declining stage has the lowest net profit per FTE, sales growth rate and net profit growth rate (Table 7.5).

Table 7.5 Mean of financial performance indicators by development stage

Development stage	Growth		Established		Declining		Total	
	# of Observations	Mean	# of Observations	Mean	# of Observations	Mean	# of Observations	Mean
Mean of total assets per FTE	33	90,112.66	127	164,705	26	145,293.9	186	148,758
Mean of total sales per FTE	32	124,318.9	128	251,592.5	26	164,636.1	186	217,541
Mean of net profit per FTE	30	46,573.5	125	45,230.56	26	35,333.33	181	44,031.5
Sales growth rate	31	0.10	139	0.09	27	0.04	197	0.08
Net profit growth rate	31	0.09	135	0.08	27	0.05	193	0.08

Financial performance indicators by industry association membership

On average, small corporations that are members of industry associations tend to have lower average total assets per FTE, average sales per FTE, average net profit per FTE, sales growth rate and net profit growth rate (Table 7.6).

Table 7.6 Mean of financial performance indicators by industry association membership

Industry association membership	No		Yes	
	# of Observations	Mean	# of Observations	Mean
average total assets per FTE	46	162040.1	140	144393.2
average total sales per FTE	45	254401.7	141	205776.7
average net profit per FTE	43	44944.54	138	43746.93
Sales growth rate	47	0.11	150	0.07
Net profit growth rate	45	0.11	148	0.07

Financial performance indicators by legal status

On average, small corporations in the legal form of companies have higher average total assets per FTE and average net profit per FTE. While small corporations in other legal forms, for example, partnerships or sole traders, have higher average sales per FTE, sales growth rate and net profit growth rate (Table 7.7).

Table 7.7 Financial indicators by legal status

Legal status	Company		Other legal forms	
	# of Observations	Mean	# of Observations	Mean
average assets per FTE	52	183605	134	135235
average sales per FTE	53	208079	133	221311
average net profit per FTE	52	61097.6	129	37152.1
Sales growth rate	57	0.078	140	0.084
Net profit growth rate	52	0.068	141	0.082

On average, the total assets per FTE and sales per FTE were larger in the service sector compared with those in other sectors (Table 7.8). However, the net profit per FTE, sales growth rate and net profit growth rate were higher in the service sector, with a mean of \$50,027.06, 9%, and 8% respectively.

Table 7.8 Mean of financial indicators by industry

Industry	Service sector		Production, logistics and trade	
	# of Observations	Mean	# of Observations	Mean
average assets per FTE	112	136,071.20	74	167,958.40
average sales per FTE	111	148,475.40	75	319,757.60
average net profit per FTE	108	50,027.06	73	35,161.22
average sales growth rate	113	0.09	84	0.08
average net profit growth rate	111	0.08	82	0.07

To sum up, small corporations with a large firm size (measured by more FTEs) tend to have better financial performance. Though the production, logistics and trade sector had accumulated larger assets per FTE and attracted more sales per FTE, the service sector surpassed it by generating more average net profits per FTE, higher reported sales growth rates and a higher net profit growth rate. This indicates a strong growth impetus of small corporations in the service sector in Australia.

CSR

An overview of CSR of small corporations was provided, followed by a breakdown of CSR with respect to its development stage, membership of industry associations, legal status, and industry.

When asked about the importance of the CSR components in making business decisions, 89.2% of the respondents perceived their customers are very important; 65.9% nominated employees as a very important component; 28.5% responded that environment is very important; and 12.5% found philanthropy to be a very important factor. 23.9% of the respondents found philanthropy irrelevant, as do 20.5% of them on investors (Table 7.9).

In total, 98.4% of respondents perceived customers as either very important or important; the proportion declined to 94.9% for employees, 77.7% for suppliers, 73.8% for environment, 72.5% for investors, and 42% for philanthropy.

Table 7.9 Importance of CSR components to business decision making

	Very important	Important	Neutral	Not so important	Not important at all	Not applicable	Total
customers	89.2% (165)	9.2% (17)	1.1% (2)	0.5% (1)	0.0% (0)	0.0% (0)	185
suppliers	39.5% (60)	38.2% (58)	10.5% (16)	9.2% (14)	0.7% (1)	2.0% (3)	152
employees	65.9% (116)	29.0% (51)	2.8% (5)	1.1% (2)	0.0% (0)	1.1% (2)	176
investors	34.1% (30)	28.4% (25)	13.6% (12)	2.3% (2)	1.1% (1)	20.5% (18)	88
philanthropy (incl. volunteering)	12.5% (11)	29.5% (26)	18.2% (16)	14.8% (13)	1.1% (1)	23.9% (21)	88
environment	28.5% (39)	45.3% (62)	15.3% (21)	2.2% (3)	4.4% (6)	4.4% (6)	137

The means of assets per FTE, sales per FTE, net profit per FTE, sales growth rate and net profit growth rate were calculated for small corporations considering each CSR component as either a very important or an important to be considered in their business decision making. Small corporations with more resources (measured by average assets per FTE in Table 7.10) tend to consider environment as an important factor. While smaller firms (with the lowest average assets per FTE), were inclined to select investors as a major factor.

Small corporations with high average sales per FTE preferred to take into account suppliers and employees more than the other CSR components, while those with low sales per FTE tend to consider investor and philanthropy as important considerations (Table 7.10).

Small corporations gain the most net profit per FTE by considering the environmental factors in their business decision making. However, putting investors as a key factor of business decision making reduces the net profit per FTE.

Comparatively, small corporations putting employees at the centre of business decision making have the highest sales growth rate; while those focusing on investors tend to have faster net profit growth.

Table 7.10 Means of financial indicators by CSR components

	Customers	Suppliers	Employees	Investor	Philanthropy	Environment
average assets per FTE	148,544.60	161,845.10	151,217.50	139,853.40	146,931.30	170,742.10
average sales per FTE	218,148.60	227,830.30	225,131.50	194,284.70	181,103.70	212,350.30
average net profit per FTE	45,029.48	42,572.50	43,150.62	37,490.84	44,420.75	48,813.11
Sales growth rate	0.0797514	0.0767323	0.0798538	0.0793662	0.0739216	0.0761712
Net profit growth rate	0.0765537	0.0779365	0.0784226	0.0824648	0.0720408	0.0749537

Given that the CSR components are measured on a five-point Likert Scales, the median was yielded in reference to three business development stages, namely growing, established and declining stage (Table 7.11). Overall, all the firms found customers to be a very important factor for their business decision making, followed by employees, suppliers and the environment. Small corporations seem to ignore the importance of investors and philanthropy, regardless of the business development stage.

Small corporations at the growing stage ranked customers as the most important component, followed by suppliers, employees and environment but investors and philanthropy as not so important; those at the established and declining stages ranked customers and employees as the most important, suppliers and environment as important, and investor and philanthropy as not so important.

Table 7.11 Median of CSR indicators by business development stage

Stage	Growing		Established		Declining	
	No. of observations	Median	No. of observations	Median	No. of observations	Median
Customers	37	5	136	5	28	5
Suppliers	36	4	133	4	28	4
Employees	37	4	135	5	28	5
Investor	36	2	130	2	26	2
philanthropy	36	2	131	2	27	2
Environment	36	4	134	4	27	4

Small corporation members of industry associations considered customers and employees as two very important factors influencing their business decision-making (Table 7.12). They considered suppliers and the environment as important factors, and investors and philanthropy not so important.

Small corporations that have no affiliation with their industry associations rank customers as a very important factor, suppliers and employees as important factors, the environment as not important or unimportant, investors and philanthropy not so important.

Table 7.12 Median of CSR indicators by industry associations

Industry association	Yes		No	
	No. of observations	Median	No. of observations	Median
Customers	154	5	47	5
Suppliers	151	4	46	4
Employees	153	5	47	4
Investor	147	2	45	2
philanthropy	149	2	45	2
Environment	150	4	46	3

Regardless of the legal form, all the small corporations who responded to this question nominated customers and employees as very important factors in their business decision making, suppliers as an important factor, investors and philanthropy as not so important factors. Small corporations in legal forms other than the company rank environment as an important factor, while small corporations registered as companies found the environment a neutral factor to their business decision making (Table 7.13).

Table 7.13 Median of CSR indicators by legal form

Legal form	Company		Other forms	
	No. of observations	Median	No. of observations	Median
Customers	144	5	57	5
Suppliers	143	4	54	4
Employees	143	5	57	5
Investor	140	2	52	2
philanthropy	141	2	53	2
Environment	143	3	53	4

Small corporations which respond to the questions on industry sectors and importance of CSR components rank customers and employees as very importance factors for their business decision making, suppliers as important factor, and investors and philanthropy as not so important (Table 7.14). Comparatively, small corporations in the service sector care less about the environment than those in the other sectors.

Table 7.14 Median of CSR indicators by industry sectors

Industry	Service sector		Production, transportation and trade	
	No. of observations	Median	No. of observations	Median
Customers	118	5	83	5
Suppliers	115	4	82	4
Employees	118	5	82	5
Investor	115	2	77	2
philanthropy	115	2	79	2
Environment	117	3	79	4

7.3.4. Corporate governance of small corporations

79 small corporations in the sample have a board of directors. The summary statistics for the corporate governance of small corporations are based on this subsample. An overview of corporate governance small corporations was provided, followed by the breakdown of

corporate governance with respect to development stage, membership of industry associations, legal status, and industry.

A small corporation with board of directors in the research normally have the following characteristics (Table 7.15):

i. Two directors on average, but ranging from one director to more than ten directors;
ii. No independent directors, some have up to ten independent directors;
iii. Two executive directors, some have up to six executive directors;
iv. One female director on average, some have up to eight female directors;
v. Hold four board meeting annually, some board meet more than four times a year;
vi. Board of directors sometimes use their social networks for business purposes, but some directors use their social networks more often;
vii. Aged 55 years old;
viii. More than 45% of the shares were held by the largest shareholder;
ix. Founder/family members serve as executive directors;
x. CEO is also the chairman of the board;
xi. Audited by independent parties;
xii. Have no succession plan.

In terms of the development stages, most established small corporations tend to have more directors sitting on the board, more independent directors, more executive directors, presence of female directors, more frequent board meetings, less often to use directors' networks for business purposes, older directors, less concentrated share ownership by the largest shareholder, the selection of directors were from multiple sources, the CEO was served by a person different from the chairman of the board, audited by an independent party (Table 7.16).

When corporate governance mechanisms are mapped to the number of FTEs in small corporations (Table 7.17), those with a larger number of FTEs had more directors sitting on their board. For instance, there are, on average, two directors in small corporations with less than 20 employees, while four directors in small corporations employ more than 20 but less than 50 employees and six directors in small corporations employ more than 50 employees. The number of independent directors follows a similar pattern. On average, there is no independent director sitting on a board in small corporations employing less than 20 employees, while one independent director in those employing 20 to 49 employees, and three independent directors in those employing more than 50 employees. Fewer women served as directors in small corporations employing 20 to 49 persons.

Small corporations with more than 20 employees tend to hold board meetings more frequently, that is, more than four times a year. Small corporations of very small firm sizes (employing 1 or less FTE), or very large firm sizes (employing more than 50 FTEs) generally used the directors' network for business purposes less often. The larger the size of small corporations (with more FTEs), the higher the proportion of shares held by the largest shareholder. Small corporations with more than 50 FTEs had the separation of CEO and chairman. Small corporations with more FTEs tend to be audited by an independent party. Larger sized small corporations (employing more than 20 FTEs) are more likely to have succession plans.

Table 7.15 Descriptive statistics of corporate governance components

	Median	Standard deviation	10%	25%	50%	75%	90%	Min	Max
No. of directors	2	2.033	1	2	2	3	6	1	10
No. of independent directors	0	1.920	0	0	0	1	3	0	10
No. of executive directors	2	1.125	1	2	2	3	4	1	6
No. of female directors	1	1.218	0	0	1	1	2	0	8
No. of board meetings	4	1.736	1	2	4	5	5	0	5
Use of board network	3	1.278	1	2	3	4	4	0	4
Average age of directors	55	5.648	50	50	55	55	64	50	67
Proportion of shares held by the largest shareholder	0.455	0.092	0.355	0.455	0.455	0.5	0.5	0.08	0.5
Alignment of interest	7	1.525	6	7	7	7	7	1	7
CEO is also the chairman	1	0.473	0	0	1	1	1	0	1
Independent audit	1	0.500	1	1	1	0	0	1	0
Succession planning	0	0.496	1	1	0	0	0	1	0

Table 7.16 Corporate governance by development stage

Business development stage	Growing		Established		Declining	
	Mean	Median	Mean	Median	Mean	Median
No. of directors	2.222	2	3.278	3	1.857	2
No. of independent directors	0.529	0	1.039	0	0.429	0
No. of executive directors	2.353	2	2.615	3	2.429	3
No. of female directors	0.529	0	0.885	1	0.571	1
No. of board meetings	2.833	3	3.549	4	2.714	2
Use of board network	3.056	3	2.750	3	3.000	4
Average age of directors	55.056	55	55.654	55	54.143	55
Proportion of shares held by the largest shareholder	0.458	0.455	0.431	0.455	0.470	0.455
Alignment of interest	6.889	7	6.222	7	6.857	7
CEO is also the chairman	0.778	1	0.611	1	0.857	1
Independent audit	1.611	0	1.380	1	1.500	0
Succession planning	0.563	0	1.592	0	0.600	0

Table 7.17 Corporate governance by FTEs

No. of FTEs	1		2-5		6-19		20-49		Above 50	
	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median
No. of directors	1.67	2	1.89	2	3.04	2	3.50	4	5.78	6
No. of independent directors	0.00	0	0.27	0	0.74	0	1.14	1	3.50	3
No. of executive directors	2.67	3	2.12	2	2.79	3	2.71	2	2.75	3
No. of female directors	1.00	1	0.69	1	0.89	1	0.43	0	1.13	1
No. of board meetings	2.67	2	2.46	2	3.46	4	5.00	5	4.22	5
Use of board network	2.67	2	2.88	3	2.93	3	3.14	3	2.22	2
Average age of directors	56.33	55	54.77	55	55.32	55	56.14	55	55.67	55
Proportion of shares held by the largest shareholder	0.46	0.46	0.44	0.46	0.44	0.46	0.45	0.5	0.42	0.5
Alignment of interest	7.00	7	6.67	7	6.21	7	7.00	7	5.44	7
CEO is also the chairman	1.00	1	0.93	1	0.57	1	0.50	1	0.22	0
Independent audit	0.00	0	0.28	0	0.39	0	0.50	1	0.69	1
Succession planning	0.00	0	0.27	0	0.36	0	0.58	1	0.63	1

Small corporations which are members of industry associations, compared to those non-members, have larger boards (more directors), more independent directors, less executive directors, board meets less often, and have a succession plan (Table 7.18).

Table 7.18 Corporate governance by membership of industry associations

Membership of industry associations	Yes		No	
	Mean	Median	Mean	Median
No. of directors	3.35	2	2.76	2
No. of independent directors	0.95	1	0.84	0
No. of executive directors	2.45	2	2.57	3
No. of female directors	0.95	1	0.71	1
No. of board meetings	3.05	3	3.39	4
Use of board network	2.55	3	2.95	3
Average age of directors	57.25	55	54.72	55
Proportion of shares held by the largest shareholder	0.43	0.46	0.45	0.46
Alignment of interest	6.45	7	6.42	7
CEO is also the chairman	0.70	1	0.66	1
Independent audit	0.59	1	0.69	1
Succession planning	0.67	1	0.46	0

Comparing corporate governance in small corporations in different legal forms, those in the form of corporations are more likely to have larger boards, more independent directors, less female directors, more frequent board meetings, less use of directors' personal networks for business purposes, higher concentration of share ownership, more diversified sources of directors, and to be audited independently (Table 7.19).

Table 7.19 Corporate governance by legal forms

Legal status	Company		Other legal forms	
	Mean	Median	Mean	Median
No. of directors	3.73	2	2.78	2
No. of independent directors	1.40	1	0.78	0
No. of executive directors	2.73	2	2.51	2
No. of female directors	1.09	0	0.72	1
No. of board meetings	3.60	5	3.26	4
Use of board network	2.00	2	2.97	3
Average age of directors	55.10	55	55.42	55
Proportion of shares held by the largest shareholder	0.49	0.5	0.44	0.46
Alignment of interest	4.45	6	6.75	7
CEO is also the chairman	0.64	1	0.68	1
Independent audit	0.61	1	0.49	0
Succession planning	0.63	0	0.58	0

Small corporations in the service sector, compared with those in other industry sectors, are more likely to have larger boards (larger means of number of directors), more independent directors, more executive directors, more female directors, more frequent board meetings, to be independently audited and less likely to have a succession plan (Table 7.20).

Table 7.20 Corporate governance by industry sector

Industry	Service sector		Production, Transportation and Trade	
	Mean	Median	Mean	Median
No. of directors	3.11	2	2.43	2
No. of independent directors	1.00	0	0.55	0
No. of executive directors	2.69	3	2.18	2
No. of female directors	0.83	1	0.64	0
No. of board meetings	3.67	4	2.33	2
Use of board network	3.00	3	2.45	3
Average age of directors	55.04	55	56.23	55
Proportion of shares held by the largest shareholder	0.44	0.455	0.44	0.455
Alignment of interest	6.21	7	6.96	7
CEO is also the chairman	0.71	1	0.57	1
Independent audit	0.42	1	0.32	0
Succession planning	0.38	0	0.60	1

7.4. Correlation coefficients

Spearman's correlation coefficients were calculated to estimate the preliminary relationships among measurement variables for corporate governance, financial performance (Table 7.21) and CSR (Table 7.22-23).

The company's total assets is positively correlated with total sales, net profit, board size, board independence, and negatively correlated with block-holding, and duality. Total sales is positively correlated with net profit, board size, board independence, and negatively correlated with duality. Net profit is negatively correlated with duality. Sales growth is positively correlated with net profit growth and duality, but negatively correlated with executive directors. Net profit growth is positively correlated with duality. Board size is positively correlated with board independence, executive directors, female directors and frequency of board meetings, but negatively correlated with block-holding and duality. Board independence is positively correlated with frequency of board meetings, but negatively correlated with duality. Executive directors are negatively correlated with block-holding.

Board meeting frequency is negatively correlated with interest alignment and succession planning. Average age of directors is negatively correlated with the frequency of using director's personal networks. Succession is positively correlated with alignment of interest.

For CSR components, small business owner/managers' perception on customers is positively correlated with employees, philanthropy and environment; suppliers is positively correlated with employees and environment; employees is positively correlated with investors and environment; investors is positively correlated with philanthropy; and, philanthropy is positively correlated with environment (Table 7.22).

Larger board size is associated with more importance of investors and philanthropy. Small corporations' perception on the importance of suppliers is negatively correlated with board independence and succession planning. Owner/managers of small corporations in which the CEO is also the chairman of the board of directors in the sample tend to value customers more and see them as more important. The number of executive directors is positively correlated with the owner/managers' perception on employees. The small corporations which have less separation of ownership and control tend to have higher net profit (Table 7.21).

Table 7.21 Spearman's Correlation coefficients between financial performance and corporate governance

	Serial number	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
total assets	1	1																
total sales	2	0.6891*	1															
net profit	3	0.5401*	0.5736*	1														
sales grow	4	-0.0009	0.0517	0.1712*	1													
net profit growth	5	0.0554	0.0449	0.1712*	0.7137*	1												
board size	6	0.4640*	0.4703*	0.4572*	0.0886	0.0805	1											
board independence	7	0.4458*	0.3892*	0.4269*	0.1024	0.0734	0.5584*	1										
executive directors	8	-0.0407	-0.0536	0.0005	-0.104	-0.1165	0.3394*	-0.1966	1									
female directors	9	0.054	-0.0376	0.0942	0.1921	0.1962	0.3653*	0.1695	0.1918	1								
Average age of directors	10	0.0019	0.1209	0.1138	0.0452	-0.0662	0.0136	0.0372	-0.085	-0.146	1							
Block-holding	11	-0.0484	-0.028	-0.0112	-0.1661	-0.0885	-0.1908	0.2474	-0.231	-0.005	-0.0072	1						
succession plan	12	-0.251*	-0.1285	0.0476	-0.131	-0.069	-0.1538	-0.1397	-0.079	0.0469	0.1531	0.0469	1					
Independent audit	13	-0.2106	-0.1217	-0.1245	-0.0688	-0.1362	-0.260*	-0.250*	-0.123	-0.167	-0.1324	-0.147	0.1355	1				
interest alignment	14	0.0527	0.1950*	0.2938*	0.0666	0.087	-0.2077	-0.1146	0.0577	-0.009	0.0137	0.0954	0.1349	0.1215	1			
duality	15	-0.1155	-0.0026	0.0932	0.1674*	0.1781*	-0.461*	-0.432*	-0.043	-0.127	-0.1885	-0.206	-0.076	0.0808	0.7724*	1		
meeting frequency	16	0.2902*	0.3144*	0.2484*	0.2370*	0.2131	0.5651*	0.3837*	0.2026	0.0464	-0.1438	-0.008	-0.321*	-0.282*	-0.281*	-0.0838	1	
board network	17	-0.1222	-0.0893	-0.056	-0.0853	-0.0955	-0.2064	-0.2293	0.1798	-0.12	-0.230*	-0.066	-0.2014	0.1697	0.1694	0.3254*	0.05	1

*p< 0.05

Table 7.22 Spearman's correlation coefficients between CSR and corporate governance

	Serial number	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18
customers	1	1																	
suppliers	2	0.2569*	1																
employees	3	0.2783*	0.1761*	1															
investors	4	0.0775	-0.0019	0.2399*	1														
philanthropy	5	0.1857*	0.0449	0.118	0.2669*	1													
environment	6	0.2948*	0.3259*	0.2419*	0.1144	0.2884*	1												
board size	7	0.0294	-0.1169	0.0131	0.2520*	0.2519*	0.0946	1											
board independence	8	0.0275	-0.251*	0.0043	-0.0295	0.0465	-0.053	0.5584*	1										
executive directors	9	-0.0317	0.0106	-0.0128	0.3040*	0.1577	0.0225	0.3394*	-0.1966	1									
female directors	10	0.0185	-0.2	-0.0343	0.021	0.0265	-0.047	0.3653*	0.1695	0.1918	1								
Average age of directors	11	-0.0763	0.0912	-0.363*	-0.1799	-0.0792	-0.112	0.0136	0.0372	-0.085	-0.146	1							
Block-holding	12	-0.0445	0.1398	-0.1172	0.0201	-0.1741	-0.164	-0.1908	0.2474	-0.231	-0.005	-0.007	1						
succession plan	13	-0.082	-0.27*	-0.0981	-0.1669	-0.116	-0.4*	-0.1538	-0.1397	-0.079	0.0469	0.1531	0.0469	1					
Independent audit	14	-0.018	-0.1081	0.0619	0.016	-0.1522	-0.061	-0.260*	-0.250*	-0.123	-0.167	-0.132	-0.147	0.1355	1				
interest alignment	15	0.0621	-0.073	-0.0171	0.1334	0.1468*	-0.052	0.2077	-0.1146	0.0577	-0.009	0.0137	0.0954	0.1349	0.1215	1			
duality	16	0.1430*	-0.034	0.0353	0.0128	0.1709*	-0.051	0.4671*	-0.432*	-0.043	-0.127	-0.188	-0.206	-0.076	0.0808	0.7724*	1		
meeting frequency	17	0.1449	-0.0424	0.0386	0.2053	0.2246	0.0221	0.5651*	0.3837*	0.2026	0.0464	-0.144	-0.008	-0.32*	-0.29*	-0.281*	-0.0838	1	
board network	18	-0.0643	0.0007	0.078	0.1511	-0.0277	-0.077	-0.2064	-0.2293	0.1798	-0.12	-0.23*	-0.066	-0.20	0.1697	0.1694	0.3254*	0.0495	1

*p< 0.05

Table 7.23 Spearman's correlation coefficients between financial performance and CSR

	Serial number	1	2	3	4	5	6	7	8	9	10	11
total assets	1	1										
total sales	2	0.6891*	1									
net profit	3	0.5401*	0.5736*	1								
sales growth	4	-0.0009	0.0517	0.1712*	1							
net profit grow	5	0.0554	0.0449	0.1712*	0.7137*	1						
customers	6	-0.0649	-0.0075	0.021	-0.0527	-0.0323	1					
suppliers	7	0.0467	0.0307	-0.106	-0.1137	-0.0425	0.2569*	1				
employees	8	0.0467	0.1592*	0.1454	-0.0919	-0.0267	0.2783*	0.1761*	1			
investors	9	0.2392*	0.2267*	0.1973*	-0.0359	0.0007	0.0775	-0.0019	0.2399*	1		
philanthropy	10	0.0571	-0.0533	0.0782	0.0158	0.044	0.1857*	0.0449	0.118	0.2669*	1	
environment	11	0.0509	-0.015	-0.0342	-0.079	-0.0007	0.2948*	0.3259*	0.2419*	0.1144	0.2884*	1

*p< 0.05

7.5. Measurement model for financial performance and CSR

Measurement model for financial performance

Confirmatory factor analysis was performed where four measures of financial performance, namely total assets (assets), total sales (sales), net profit, and net profit growth derived from the literature in Chapter 4 were allowed to correlate freely with each other but were uncorrelated with measurement errors from other indicators (Byrne, 2001)[6]. The path diagram together with standardised parameter estimates is shown in Figure 7.4.

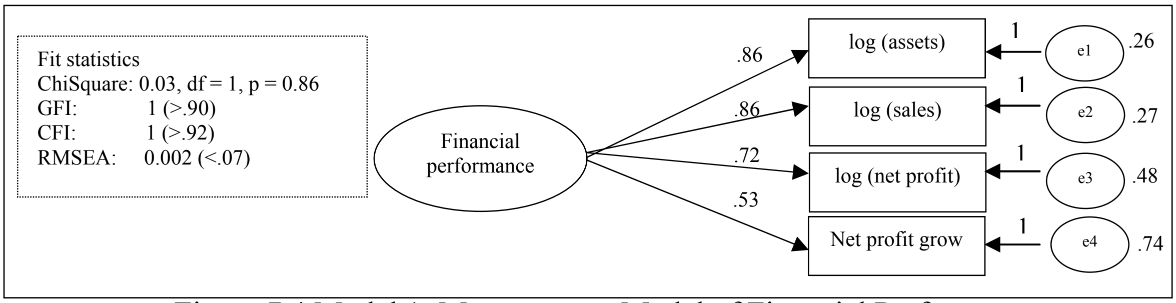


Figure 7.4 Model 1: Measurement Model of Financial Performance

The measurement model (Figure 7.4) hypothesized that four hypothesized financial performance dimensions of namely total assets (assets), total sales (sales), net profit, and net profit growth were correlated. Included in the model was a factor measuring overall financial performance as perceived by the respondent. This is an unobserved construct and is thus enclosed by ovals. Four measures (enclosed by rectangles) were specified, each with a nonzero loading on the factor it was designed to measure, and zero loading on other factors. Thus each indicator was identified with a unique construct. Error variables (enclosed by ovals because they are not directly observed) represent a composite of any influences on the observed measures that are not measured in this study. For example, in Figure 7.4 the single-headed arrow leading from financial performance to total assets shows that total assets scores depend only in part on financial performance; specifically the hypothetical 'financial performance' construct accounts for 70% of the variance in scores for item total assets.

[6] For the sake of brevity of presentation, the correlations between the measures are hidden in Figure 7.4.

Alternatively, the path coefficient (loading) that describes the impact of total assets on financial performance is 0.86 (Arbuckle, 1995).

Goodness of fit index

A goodness of fit check was undertaken. There is 1 degree of freedom (6 distinct sample moments less 4 parameters and 1 construct variance estimated. The construct variance is not shown for visual clarity). Thus normed chi-square = 0.86, GFI = 1, CFI = 1 all suggested the model is plausible. The RMSEA index is acceptably low at 0.002. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). Thus for the financial performance measurement model, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. There was, thus, evidence to suggest that the financial performance measurement model had adequate overall goodness-of-fit.

In determining construct validity, the CFA provided a test of convergent validity for each of the sets of items that measured each construct. All path estimates were significant at the 1% level, and loadings between measured variables and factors were generally greater than 0.5. Indicators loaded significantly on their hypothesized construct, indicating adequate levels of convergent validity (Bagozzi & Phillips, 1982; Barki & Hartwick, 2001).

Nested models to test dimensionality were also examined. The plausibility of one dimension of financial performance for SMEs (as opposed to, for example, a multiple dimension model) was assessed in a nested modelling process. Thus, a further test of the measurement model was made by comparing two nested models (Barki & Hartwick, 2003), as described in Chapter 6. The first model loaded all items onto a single factor, hypothesizing that the items do not differentiate any underlying dimensions. The second model assumed two factors and hypothesized that the items have different dimensions hence the financial performance is a multi-level latent variables measured by other latent variables related to financial performance. The Chi-square difference was calculated between Model 1 and its alternative and the test result was not significant, implying that the two-level model does not produce a better fit. In other words, Model 1 had a relatively better fit (as reported above). Thus, the financial performance of small corporations is a uni-dimensional construct that can be measured by four indicators, namely total assets, total sales, net profit, and net profit growth rates.

The factor weights indicate that the financial performance of small corporations may well be measured by total sales, total assets and net profits. However, the net profit growth and net sales growth play a less important role. The net profit growth has been included in the analysis to address the model identification issue.

Measurement model for CSR

The measurement model of CSR is specified in Fig. 5. In the prior literature, as reviewed in Chapter 2, CSR can be measured by the small corporation own/managers' perceptions on five dimensions, namely customers, suppliers, employees, philanthropy and environment. The goodness of fit indices confirms a good fit between the data and underlying model.

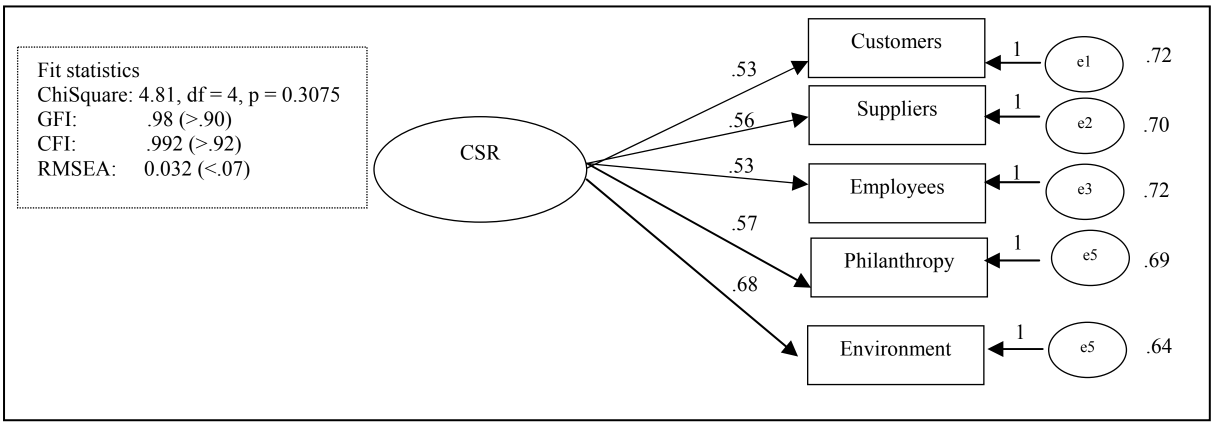


Fig. 7.5 Model 2: Measurement model of CSR

The measurement model (Figure 7.5) hypothesized that five CSR dimensions were correlated. Included in the model was a factor measuring overall CSR as perceived by the respondent. This is an unobserved construct and is thus enclosed by ovals. Five measures (enclosed by rectangles) were specified, each with a nonzero loading on the factor it was designed to measure, and zero loading on other factors. Thus each indicator was identified with a unique construct. Error variables (enclosed by ovals because they are not directly observed) represent a composite of any influences on the observed measures that are not measured in this study.

Goodness of fit index

There are 4 degrees of freedom (the construct variance is not shown for visual clarity). The normed chi-square = 0.31, GFI = 0.980, CFI = 0.992 all suggested the model is plausible. The RMSEA index is acceptably low at 0.032. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). Thus, for the financial performance measurement model, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. Evidence suggested that the financial performance measurement model had adequate overall goodness-of-fit.

Construct validity

The CFA provided a test of convergent validity for each of the sets of items that measured each construct. All path estimates were significant at the 1% level, and loadings between measured variables and factors were generally greater than 0.5. Indicators loaded significantly on their hypothesized construct, indicating adequate levels of convergent validity (Bagozzi & Phillips, 1982; Barki & Hartwick, 2001).

Nested models to test dimensionality

The plausibility of one dimension of growth fitness for SMEs (as opposed to, for example, a multiple dimension model) was assessed in a nested modelling process. A further test of the measurement model was made by comparing two nested models (Barki & Hartwick, 2003), as described in Chapter 6. The first model loaded all items onto a single factor, hypothesizing that the items do not differentiate any underlying dimensions. The second model assumed two levels of factors and hypothesized that the items have different dimensions hence the CSR is a multi-level latent variables measured by other latent variables related to IT. As anticipated, the first model has a relatively good fit (as reported above). Thus, the CSR of small corporations is a single level construct that can be measured by five indicators, which are customers, suppliers, employees, philanthropy and environment. The factor weights indicate that the CSR is a five factor model and each factor has relatively similar weights.

7.6. Measurement model for corporate governance

In the prior study as reviewed in Chapter 2, corporate governance can be measured by seven indicators, namely board size, duality (the CEO is also chair of the board), board independence, interest alignment, meeting frequency, board network and independent audit (Fig. 7.6). The fit statistics indicate a satisfactory fit of the model specified in Fig. 7.6.

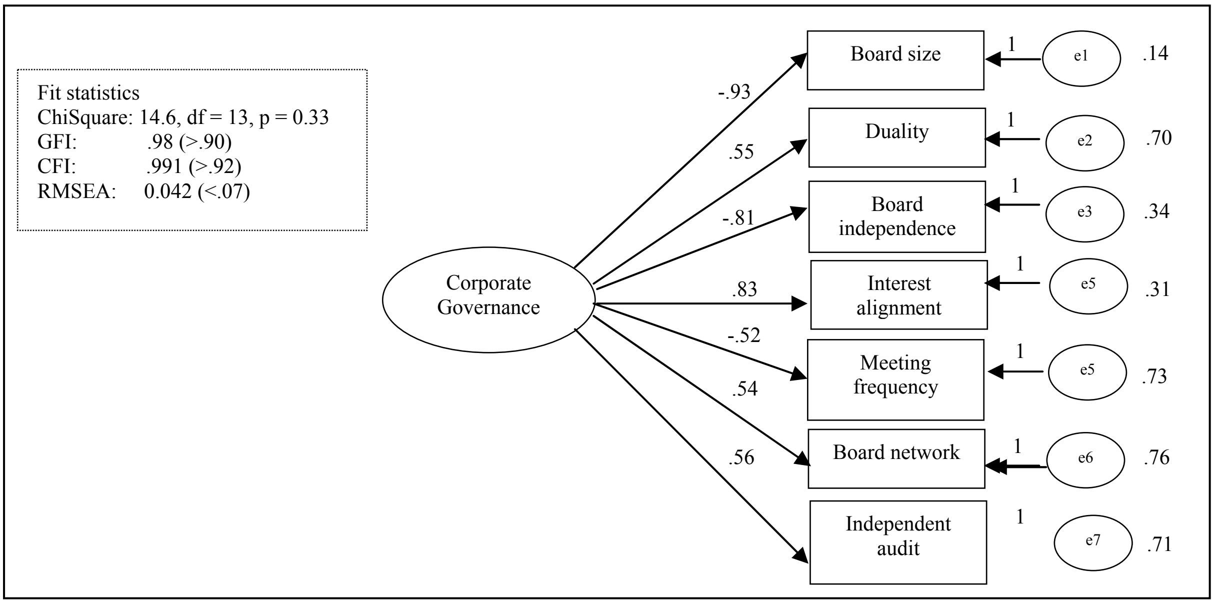


Fig. 7.6 Model 3: Measurement model of corporate governance

Corporate governance is an unobserved construct and is thus enclosed by ovals. Seven measures (enclosed by rectangles) were specified, each with a nonzero loading on the factor was designed to measure, and zero loading on other factors. Thus each indicator was identified with a unique construct. Error variables (enclosed by ovals because they are not directly observed) represent a composite of any influences on the observed measures that are not measured in this study.

Goodness of fit index

There are 13 degree of freedom (the construct variance is not shown for visual clarity). Thus normed chi-square = 0.33, GFI = 0.980, CFI = 0.991 all suggested the model is plausible. The RMSEA index is acceptably low at 0.042. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). Thus, for the financial performance measurement model, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. There was thus evidence to suggest that the financial performance measurement model had adequate overall goodness-of-fit.

Construct validity. The CFA provided a test of convergent validity for each of the sets of items that measured each construct. All path estimates were significant at the 1% level, and loadings between measured variables and factors were generally greater than 0.5. Indicators loaded significantly on their hypothesized construct, indicating adequate levels of convergent validity (Bagozzi & Phillips, 1982; Barki & Hartwick, 2001).

Nested models to test dimensionality. The plausibility of one dimension of corporate governance for small corporations (as opposed to, for example, a multiple dimension model) was assessed in a nested modelling process. A further test of the measurement model was made by comparing two nested models (Barki & Hartwick, 2003), as described in Chapter 6. The first model loaded all items onto a single factor, indicating that the items do not differentiate any underlying dimensions. The second model assumed two levels of factors and hypothesized that the items have different dimensions hence the corporate governance is a multi-level latent variables measured by other latent variables related to financial performance. As anticipated, the single level model had a relatively better fit (as reported above). Thus, the corporate governance of small corporations is a uni-dimensional construct that can be measured by sever indicators, namely board size, duality (the CEO is also chair of the board), board independence, interest alignment, meeting frequency, board network and independent audit.

One may challenge the relevance of corporate governance to the micro-business, particularly the one-man business, which accounts for 66% of the sample. The measurement model of corporate governance in Model 3, on the other hand, offers an explanation to such query. If the corporate governance construct were to be measured by the observed variables identified from the literature of large corporations, then well governed small corporations favour smaller boards of directors, less independent boards of directors and less frequent board meeting if there are any, more presence of CEOs as chairman of the board, more interest alignment between managers and owners, more use of the directors' networks for the business purposes and more independent audits.

Comparatively, the board size and board independence seems to be two daunting counter-productive mechanisms that small corporations have learned from large listed companies. The weights of board size and board independence are so high that the impact of the positively factors have been severely diluted. However, it clearly shows that less independence of the board of directors, smaller boards, increased duality of CEO and chair, less interest disparity between managers and owners and the use of networks as alternative governance mechanisms play fairly important roles in mainstream "ordinary" Australian small corporations.

7.7. Impact of corporate governance on financial performance of small corporations

The measurement models for financial performance and corporate governance were specified in Fig. 7.4 and Fig. 7.6. The Structural Equation Model (SEM) was applied to assess the impact of corporate governance on small corporations' financial performance. The standardised SEM results indicate that corporate governance has a negative impact on the financial performance of small corporations. The standardised regression (which is also correlation) between the two latent variables — corporate governance and financial performance is - 0.40 which is negative and statistically significant, meaning that firms with better corporate governance structure in place tends to perform better in financial terms (Fig. 7.7). The fit indices indicate that the model is satisfactory in meeting the fit criteria for a SEM.

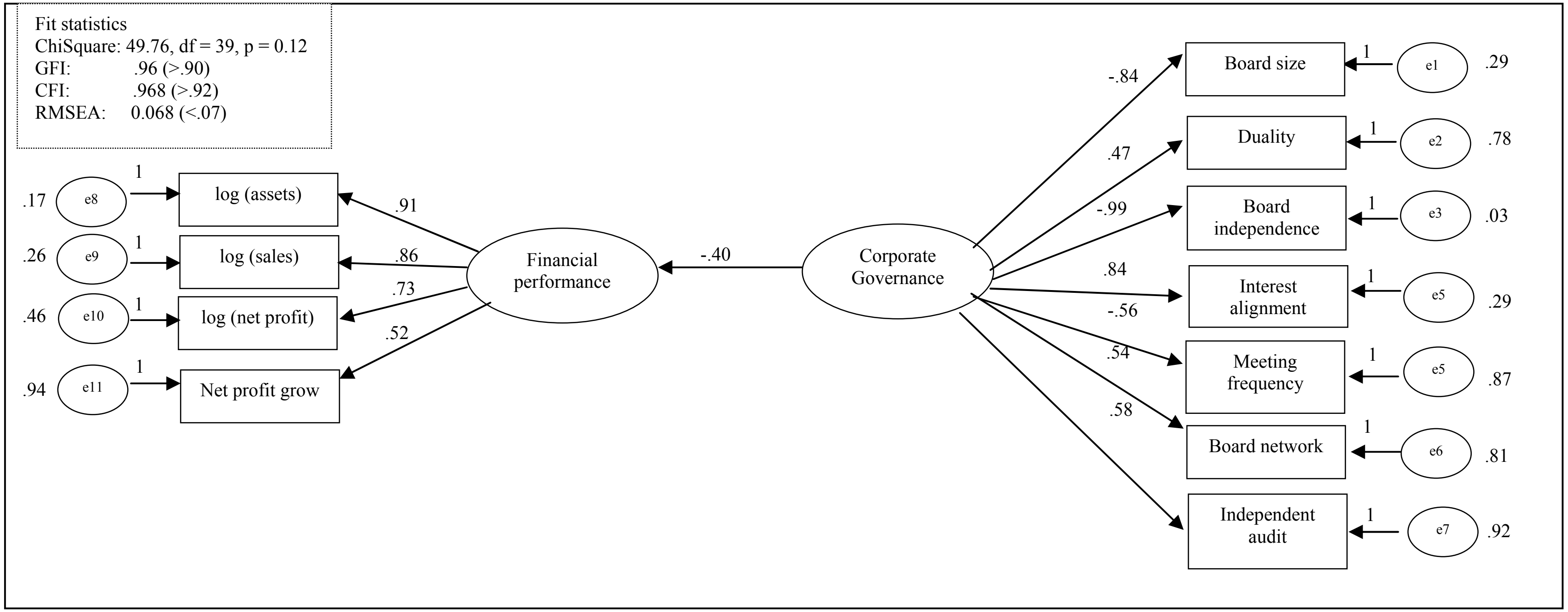


Fig. 7.7 Model 4: Corporate governance on financial performance

7. Corporate governance on CSR

Based on the measurement model of corporate governance and CSR, a SEM was applied to estimate the impact of corporate governance on the CSR of small corporations. The results show that the corporate governance has a negative impact on the CSR. However, the standardised regression result (which essentially is the correlation coefficient) is 0.13 is not statistically significant.

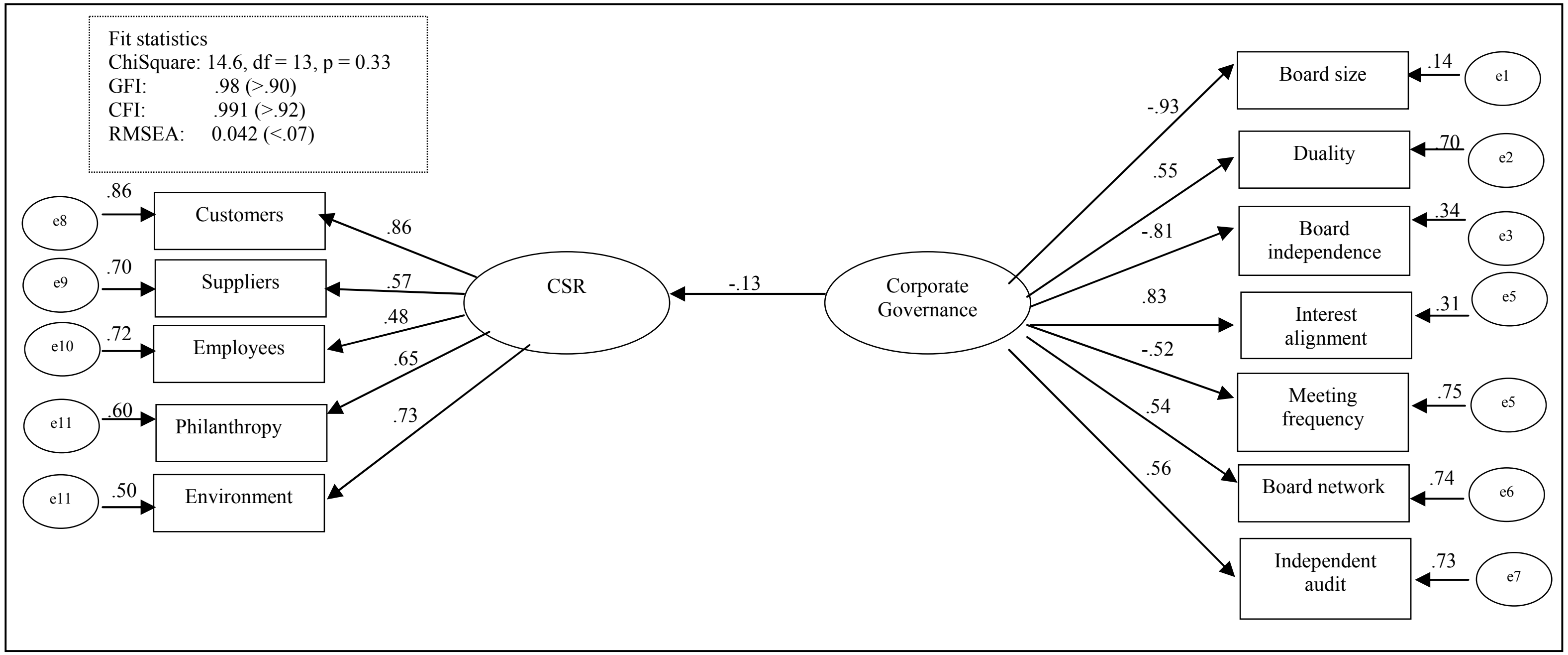


Fig. 7.8 Model 5: Impact of corporate governance on CSR

8. CSR on Financial performance

The SEM is applied to estimate the impact of CSR on financial performance. The results show that the CSR has a negative impact on the financial performance measured by accounting terms. The standardised regression coefficient is 0.4, which is statistically significant and negative, indicating that small corporations with better CSR tend to have poor financial performance.

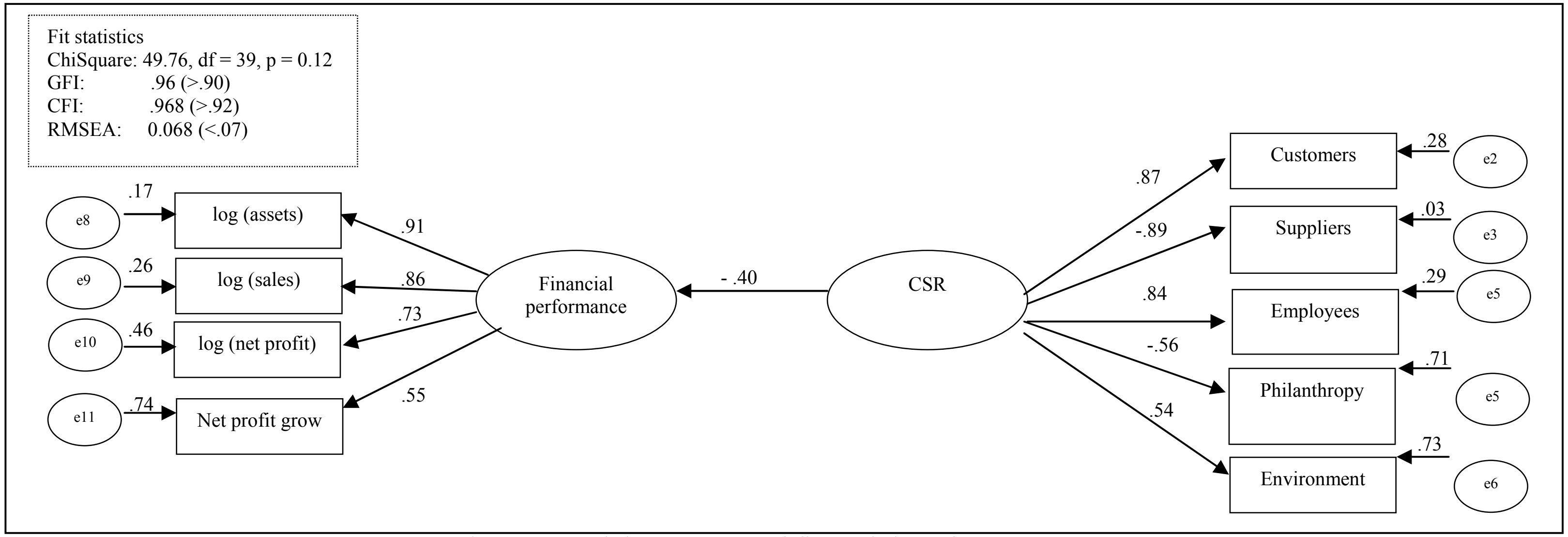


Fig. 7.9 Model 6: Impact of financial performance on CSR

7.8. Mediation and moderation effects via path analysis

As specified in Chapter 5, mediators were introduced in the path analysis in order to estimate the direct and indirect effects of individual corporate governance variables on financial and social performance.

In order to analyse the specific impact of each governance mechanism on the performance of small corporations, a path analysis approach was applied in this study to examine the multivariate relationship among variables. It is used to analyse the direct, indirect effects and interaction among variables in the integrated models developed in Chapter 5. The path analysis results are presented in Table 7.24. The model exhibited a good fit as measured by various model fit indices. The model also shows the direct and indirect effects among variables. Overall, the strength of indirect effects, although present, is not as strong as the direct effects (Table 7.25). These governance mechanisms therefore complement each other in contributing to the formation of collaborative governance arrangements.

Statistical hypotheses H1-H21 have been verified by the SEM model given that the total effects are statistically significant.

The total effect of board size on performance is 0.246, meaning that one standard deviation scaling up of the board size will increase the financial performance by 0.246 standard deviations.

Searching for mediators was informed by previous literature. Five factors were identified as mediators, including legal form, industry, and membership of an industry association, development stage and size (measured by FTEs). Missing value correction technique in Stata 12.0, Maximum Likelihood with Missing Values (MLMV), has been applied to compensate for the missingness of values for variables in the data.

Table 7.24 Results of the Path Analysis

Hypotheses		Direct effect				Indirect effect				Total effect			
		Std. R.W.	t-value	S.E.	Sign. Level	Std. R.W.	t-value	S.E.	Sign. Level	Std. R.W.	t-value	S.E.	Sign. Level
Financial performance													
Board size	H1	0.239	9.548	0.025	***	0.006	1.42	0.005		0.246	9.801	0.025	***
Independence	H2	1.569	8.208	0.191	***	-0.002	-0.079	0.028		1.567	8.303	0.189	***
Board meeting frequency	H3	0.239	9.919	0.024	***	0.003	0.899	0.004		0.242	9.978	0.024	***
Ownership concentration	H4	-0.461	-5.483	0.084	***	0.013	0.813	0.016		-0.448	-5.342	0.084	***
Directors' network	H5	0.258	7.895	0.033	***	-0.006	-0.825	0.007		0.253	7.751	0.033	***
Board interest alignment	H6	0.189	8.409	0.023	***	-0.001	-0.258	0.004		0.188	8.257	0.023	***
Succession planning	H7	0.898	5.527	0.162	***	-0.015	-0.547	0.027		0.883	5.33	0.166	***
Independent audit	H8	0.922	6.927	0.133	***	0.024	1.272	0.019		0.946	6.968	0.136	***
Corporate governance	H9	-0.397	10.813	0.037	***	-0.112	5.621	0.02	***	-0.51	13.694	0.037	***
Social performance													
Board size	H10	0.318	9.301	0.034	***	0.005	0.889	0.006		0.322	9.49	0.034	***
Independence	H11	2.103	9.226	0.228	***	0	0.005	0.026		2.103	9.18	0.229	***
Board meeting frequency	H12	0.307	9.144	0.034	***	0.003	0.807	0.004		0.31	9.187	0.034	***
Ownership concentration	H13	-0.587	-6.994	0.084	***	0.01	0.743	0.014		-0.577	-6.942	0.083	***
Directors' network	H14	0.366	8.485	0.043	***	-0.005	0.006	-0.775		0.361	8.516	0.042	***
Board interest alignment	H15	0.262	8.724	0.03	***	-0.001	-0.311	0.003		0.261	8.711	0.03	***
Succession planning	H16	1.296	5.949	0.218	***	-0.012	-0.51	0.023		1.284	5.871	0.219	***
Independent audit	H17	1.241	7.829	0.159	***	0.018	0.805	0.022		1.259	7.962	0.158	***
Corporate governance	H18	-0.505	10.662	0.047	***	-0.094	4.758	0.02	***	-0.599	13.676	0.044	***
Financial performance	H19	-0.653	27.399	0.024	***	-0.058	6.539	0.009	***	-0.711	33.992	0.021	***
Size													
Governance on financial performance	H20	-1.532	46.42	0.033	***	0.983	4.681	0.210	***	-0.549	2.815	0.195	***
Regulation on financial performance	H21	0.178	4.12	0.043	***	0.333	23.825	0.014	***	0.511	13.669	0.037	***

Model fit indices:

P	df	CFI	RMSEA
0.1468	77	1	0.053

Note: Std. R.W. – Standardised regression weight; S.E. – standard error. * - 10% significance level; **5% significance level; ***- 1% significance level.

The size effects on the corporate governance – financial performance link

The moderation effect of size on corporate governance – financial performance link is – 1.532, which is negative and statistically significant. The number of FTE influences the slope of the regression of financial performance against corporate governance and has multiplier effect on the relationships in focus. Given that the impact of governance on financial performance relationship is – 0.4, the mediation effect of size means that the larger the firms, the extent to which governance negatively influence the financial performance reduces as the firm size increases at an accelerated rate. If the FTE increase by one scaling level, the effect size increases by 0.613, which are the multiplicative function of the moderation effect and effect size in focus, meaning that the corporate governance has a positive impact on financial performance once the FTE is larger.

The overall effect size for FTE on corporate governance – financial performance link is – 0.549, meaning that if FTE increases by one scaling levels, the impact of corporate governance on financial performance increases by 0.22, which is a multiplicative function of the moderation effect and the effect size. Putting it in another way, in small corporations with the less FTEs, the corporate governance mechanisms negatively influences the financial performance. However, when the FTE increases to a certain level, the impact of corporate governance on financial performance may eventually become positive.

7.9. Summary

This chapter provided results of the research project, covering survey data analysis, descriptive statistics, correlation analysis, SEM and path analysis. The SEM results enabled us to make decisions toward the null hypotheses, which are summarised in Table 7.26. The latent variable models showed that the corporate governance has a negative and statistically significant impact on financial performance. In addition, corporate governance has a negative impact on social performance, but the impact is not statistically significant. The financial performance has a positive impact on social performance.

Chapter 8 will report the results related to government regulation. Chapter 9 will focus on the discussion of the results and their implications with regards to the theories and prior empirical research pertinent to corporate governance.

Table 7.25 Summary of statistical hypotheses tests results

Hypothesis No.	Relationship	Expected sign	Results	Decision on null hypothesis
H1	Board size and financial performance	-	+	Reject
H2	Board independence and financial performance	+	+	Accept
H3	Board meeting frequency and financial performance	+	+	Accept
H4	Ownership structure and financial performance	+	-	Reject
H5	Director's network and financial performance	-	+	Reject
H6	Board interest alignment and financial performance	+	+	Accept
H7	Succession planning and financial performance	+	+	Accept
H8	Independent audit and financial performance	+	+	Accept
H9	Corporate governance and financial performance	+	+	Accept
H10	Board size and social performance	+	+	Accept
H11	Board independence and social performance	+	+	Accept
H12	Board meeting frequency and social performance	+	+	Accept
H13	Ownership structure and social performance	+	-	Reject
H14	Director's network and social performance	+	+	Accept
H15	Board interest alignment and social performance	+	+	Accept
H16	Succession planning and social performance	+	+	Accept
H17	Independent audit and social performance	+	+	Accept
H18	Corporate governance and social performance	+	-	Reject
H19	Social and financial performance	+	+	Accept
H20	Regulation and financial performance	-	+	Reject
H21	The mediating effect of size on the impact of regulation on financial performance	-	+	Reject
H22	Regulation and social performance	-	+	Reject
H23	Regulation on Corporate governance	+	+	Accept
H24	Corporate governance on regulation	-	+	Reject

CHAPTER EIGHT RESULTS THE IMPACT OF REGULATION ON PERFORMANCE OF NON-LISTED SMALL CORPORATIONS IN AUSTRALIA

8.1. Introduction

Chapter 3 reviewed theories and empirical studies on government regulation, followed by the development of the hypothesis on the relationship between regulation and performance of small corporations in Chapter 5 This chapter reports the results on the measurement model of regulation, the impact of regulation on financial performance, CSR, and corporate governance of small corporations in Australia, and the mediation effects on the relationship between responsive regulation and firm performance. The last section summarises the results on regulation related models.

8.2. Data screening

The regulatory compliance requirements data was examined for consistency with distributional assumptions. First, individual variables were checked for normality by means of both univariate and multivariate procedures. Then data assumptions were checked for variates, by means of both univariate and multivariate procedures.

Mahalanobis D^2 distances were generated for each case using SPSS Regression with case number as the dependent variable and all non-demographic measures as independent variables. For observations with higher D^2 values were identified with potential multivariate outliers, yielding 387 observations for the data analysis.

Normality. All the ten regulation indicators were moderately negatively skewed, with skewness < -1, although none of these had skewness < -2. The standard error of skewness was 0.1, so these ten variables were statistically significantly skewed at the 5% level.

The power of univariate tests is not severely affected if non-normality is solely due to skewness; however, excessive kurtosis does seem to have an effect (Sharma, 1996). In particular, negative kurtosis (a flat distribution) has a more severe effect. However, none of the regulation variables has negative kurtosis. Thus, the univariate normality is assumed for each regulation indicator.

Multivariate normality of the individual variables was checked following the procedure described in Sharma (1996: 380-382). The correlation coefficient between the Ordered Mahalanobis Distances and Chi-square is 0.99. This value exceeds the critical value of 0.983 (alpha = .05, n = 74), so the data likely came from a multivariate normal distribution (Sharma, 1996).

In summary, some individual variables had moderately non-normal distributions, although overall the data appeared to have a multivariate normal distribution. This is unusual since evidence of univariate non-normality often (but not always) suggests multivariate non-normality. In the present context, since most of the variables are ordinal with limited discrete values, since hypothesis testing in this study was multivariate in nature, and since less than 10% of the variables had moderate negative kurtosis, normality of the individual variables was assumed.

Homoscedasticity and Homogeneity of Variance. Most individual variables were measured at the ordinal level, so homoscedasticity was not evaluated by means of bivariate plots. Levene's test of homogeneity of variance was used instead. It assessed the homogeity of each regulation indicator against the control variables, such as legal form (two categories: company; non-company); development stage (three categories: growing; established; and declining); membership of industry association (two categories: member; non-member); number of full-time equivalent employees (FTEs) (five categories: 1; 2-5; 6-19; 20-49; 50

and above) and Industry (two categories: service industry sector; non-service sectors). Levene's test of homogeneity of variance was not significant. Thus variances of dependent variables across categories of the regulation indicators were found to be similar.

Data screening of variates

Normality. First, skewness and kurtosis values were assessed, and the general shapes of histograms were examined. None of the values have an absolute value greater than one, indicating little suggestion of univariate nonnormality.

A Kolmogorov Smirnov z test was conducted to provide additional evidence of univariate normality (Tabachnick & Fidell, 2007:80). Generally, a z-value above 2.58 signals that normality can be rejected at the 1% level of significance (Hair et al., 2006). Normality of the variates was then tested from a multivariate perspective.

The correlation coefficient between the Ordered Mahalanobis Distances and Chi-square is 0.93. This value exceeded the critical value of 0.926 (alpha = .05, n = 12), so the data likely have a multivariate normal distribution (Sharma, 1996).

Homoscedasticity, Homogeneity of Variance, and Box's M Test. Four dependent variates, namely corporate governance, financial performance, CSR, and government regulation were regressed with the other five categorical variates (including legal form, industry, development stage, FTEs and membership of industry association) in order to examine for homoscedasticity. All indicated that the variability in dependent variate scores was roughly the same at all values of each predictor variate.

Homogeneity of variance statistics for five categorical variables, namely legal form, industry, development stage, FTEs, and membership of industry association. The Levene statistic was generally not significant, indicating that homogenous variances may be assumed.

Finally, a Box's M test was performed by specifying all four dependent variates in a multivariate assessment of the homogeneity of variance-covariance matrices. None of the results were significant.

In sum, there was little evidence to suggest that the assumption of homoscedasticity was not reasonably satisfied by the dataset.

Linearity and Multicollinearity

Multicollinearity is a problem that occurs when variables are highly correlated (>.90); the sizes of error terms become inflated (Tabachnick & Fidell, 2007). Correlations between the variates were calculated. None of the correlations were above 0.80, thus this preliminary analysis did not suggest that any of the variates were redundant. Finally, scatterplots were examined and little suggestion of excessive non-linearity was found.

In summary, individual variables and variates were tested for basic distributional assumptions before testing relationships between constructs. Overall, the data screening process concluded that the data was suitable for further multivariate analysis.

Given that the regulatory variables are ordinal in nature, the spearman correlation coefficients were used to analyse the correlations.

8.3. Summary statistics of regulation

Table 8.1 reports the summary data of respondents' perceived difficulty level for ten aspects of regulation, specifically including ASIC regulation, record keeping for tax purposes, Directors' duties, Information disclosure, Occupational Health and Safety, Superannuation management, Workplace relationships, Maternity leave, Quality assurance, and Environmental protections.

Of all the respondents,

i. **ASIC regulation** 33.8% find ASIC regulation not a difficulty at all; 13.7% find it either difficult or most difficult.

ii. **Record keeping for tax purposes** 14.1% find record keeping for tax purposes not difficult at all; while 41.3% find it either difficult or most difficult.

iii. **Directors' duties** 19.7% find it not difficult at all; while 18.1% find it either difficult or most difficult.

iv. **Information disclosure**s 22.8% find it not difficult at all; while 22.8% find it either difficult or most difficult.

v. **Occupational Health and Safety** 16.1% find it not difficult at all; while 37.7% find it either difficult or most difficult.

vi. **Superannuation management** 18.3% find it not difficult at all; while 28.1% find it either difficult or most difficult.

vii. **Workplace relationships** 17.4% find it not difficult at all; while 26.5% find it either difficult or most difficult.

viii. **Maternity leave** 32.1% find it not difficult at all; while 13.9% find it either difficult or most difficult.

ix. **Quality assurances** 20.4% find it not difficult at all; while 24% find it either difficult or most difficult.

x. **Environmental protections** 22.4% find it not difficult at all; while 22.5% find it either difficult or most difficult.

Ranking the abovementioned summary data, the top three regulatory requirements that incurs difficulty or most difficulties to small corporations are record keeping for taxation purposes, occupational health and safety and superannuation management; and the least three difficult regulatory requirements are ASIC regulation, maternity leave and environmental protections (Table 8.1).

Table 8.1 Summaries of responses by difficulty level

	1 = not difficult at all	2= not so difficult	3 = neutral	4 = difficult	5 = most difficult	Not applicable	Total
ASIC regulation	33.8% (101)	22.1% (66)	17.1% (51)	9.7% (29)	4.0% (12)	13.4% (40)	299
Record keeping for tax purposes	14.1% (43)	18.4% (56)	25.6% (78)	24.6% (75)	16.7% (51)	0.7% (2)	305
Directors' duties	19.7% (60)	25.0% (76)	24.7% (75)	10.9% (33)	7.2% (22)	12.5% (38)	304
Information Disclosure	22.8% (69)	18.5% (56)	25.4% (77)	15.5% (47)	7.3% (22)	10.6% (32)	303
Occupational Health and Safety	16.1% (49)	20.0% (61)	23.6% (72)	17.4% (53)	20.3% (62)	2.6% (8)	305
Superannuation management	18.3% (56)	25.2% (77)	24.2% (74)	18.6% (57)	9.5% (29)	4.2% (13)	306
Workplace relationships	17.4% (53)	25.2% (77)	24.9% (76)	15.7% (48)	10.8% (33)	5.9% (18)	305
Maternity leave	32.1% (97)	13.2% (40)	11.3% (34)	7.3% (22)	6.6% (20)	29.5% (89)	302
Quality assurance	20.4% (62)	19.4% (59)	26.3% (80)	14.8% (45)	9.2% (28)	9.9% (30)	304
Environmental protections	22.4% (68)	23.4% (71)	21.5% (65)	13.9% (42)	8.6% (26)	10.2% (31)	303

The descriptive statistics of business perceived regulation

More than a quarter of the respondents find that certain regulations are difficulties to their business operations. Such regulations include record keeping for tax purposes, Information disclosure, occupational health and safety, workplace relations and quality assurance. 10% of the respondents find ASIC regulation, Directors’ duties, and maternity leaves of particular difficulty to them (Table 8.2).

Table 8.2 Descriptive statistics of regulation

	median	Standard deviation	p10	p25	p50	p75	p90	min	max
ASIC regulation	2	1.20	1	1	2	3	4	1	5
Record keeping for tax purposes	4	1.29	1	2	4	4	5	1	5
Directors' duties	2	1.20	1	2	2	3	4	1	5
Information Disclosure	3	1.26	1	1	3	4	4	1	5
Occupational Health and Safety	4	1.37	1	2	4	4	5	1	5
Superannuation management	4	1.25	1	2	4	4	4	1	5
Workplace relationships	3	1.26	1	2	3	4	5	1	5
Maternity leave	2	1.36	1	1	2	3	4	1	5
Quality assurance	3	1.27	1	2	3	4	5	1	5
Environmental protections	2	1.28	1	1	2	3	4	1	5

When comparing the difficulties incurred by regulatory requirements by legal forms between companies and other legal forms, companies are facing more difficulties than the latter in regulations such as ASIC regulation, record keeping for tax purposes, information disclosure and quality assurance; however, companies are facing less difficulties for director’s duties and environmental protections; and the difficulties faced by the company and non-company business entities are similar in regulations such as Occupational Health and Safety, superannuation, workplace relationships and maternity leave (Table 8.3).

Table 8.3 Comparison of difficulties incurred by regulatory requirements by legal forms

	Legal form	1*	2	3	4	5
ASIC regulation	Other legal forms	38% (20)	27% (14)	23% (12)	8% (4)	4% (2)
	Company	39% (81)	25% (52)	19% (39)	12% (24)	5% (10)
Record keeping for tax purposes	Other legal forms	16% (15)	19% (17)	26% (24)	22% (20)	16% (15)
	Company	13% (28)	18% (39)	26% (54)	26% (54)	17% (36)
Directors' duties	Other legal forms	29% (17)	17% (10)	28% (16)	12% (7)	14% (8)
	Company	21% (43)	32% (66)	29% (59)	12% (25)	7% (14)
Information disclosure	Other legal forms	28% (18)	18% (12)	34% (22)	11% (7)	9% (6)
	Company	25% (51)	21% (44)	27% (55)	19% (39)	8% (16)
Occupational Health and Safety	Other legal forms	19% (16)	17% (15)	23% (20)	21% (18)	20% (17)
	Company	16% (33)	22% (46)	25% (52)	16% (34)	21% (45)
Superannuation	Other legal forms	17% (14)	32% (26)	23% (19)	20% (16)	9% (7)
	Company	20% (41)	24% (51)	26% (55)	20% (41)	10% (22)
Workplace relationships	Other legal forms	18% (14)	24% (19)	29% (23)	18% (14)	10% (8)
	Company	19% (39)	28% (58)	25% (53)	16% (33)	12% (25)
Maternity leave	Other legal forms	43% (21)	14% (7)	20% (10)	10% (5)	12% (6)
	Company	47% (76)	20% (33)	15% (24)	10% (16)	9% (14)
Quality assurance	Other legal forms	25% (19)	21% (16)	32% (24)	12% (9)	9% (7)
	Company	22% (43)	22% (43)	28% (55)	18% (36)	11% (21)
Environmental protections	Other legal forms	16% (12)	24% (18)	29% (22)	20% (15)	11% (8)
	Company	29% (56)	27% (53)	22% (43)	13% (26)	9% (18)

* Difficulties incurred by regulatory requirements: 1= Not difficult at all; 2= Not so difficult; 3= Neutral; 4 = Difficult; and 5 = Most difficult.

Comparing the service companies with the non-service companies, the difficulties faced by non-service companies are more severe when it comes to regulations such as record keeping for tax purposes, occupational health and safety, superannuation management, and environmental protections, while less so in quality assurance (Table 8.4).

Business entities which are members of industry associations find it less difficult to comply with ASIC regulation, record keeping for tax purposes and superannuation management, while more difficult for information disclosure, occupational health and safety and environmental protection (Table 8.5).

Comparing the difficulties of regulatory requirements by business development stage, it is obvious that the established businesses find it the least difficult to deal with nearly all the regulatory requirements except information disclosure and occupational health and safety. Start-ups are having the most difficulties with record keeping for tax purposes, quality assurance and information disclosure. The declining businesses are facing the most difficulties in regulations such as Director's duties, superannuation management, workplace relationships, maternity leave and environmental protections (Table 8.6).

The difficulties incurred by regulatory requirements are compared based on the number of employees (also used as one of the proxies for firm size in the literature). For ASIC regulation, the companies with only one employee or more than 50 employees find the compliance particularly difficult. For record keeping for tax purposes, companies with more than 20 employees find it difficult. For Directors' duties, companies with either one employee or more than 50 employees find it difficult. For information disclosure, companies with more than 50 employees find it extremely difficult, followed by companies with 6 to 19 employees and those with 20-49 employees. For occupational health and safety, companies employing more than 20 employees find it particularly difficult. For superannuation management, companies with more than 50 employees find it difficult. For workplace relationships, companies with more than 20 employees find it difficult. For maternity leave, companies with more than 50 employees find it difficult. For quality assurance, companies with more than 6 employees find it difficult. For environmental protections, companies with more than 20 employees find it difficult (Table 8.7).

When comparing the difficulties incurred regulatory requirements between companies with and without a board, those with a board find it particularly difficult with ASIC regulation, information disclosure, workplace relationships and quality assurance, but less so in superannuation management, maternity leave and environmental protections (Table 8.8).

Table 8.4 Comparison of difficulties incurred by regulatory requirements by industry sector

	Industry	1	2	3	4	5
ASIC regulation	Service	40% (61)	25% (38)	19% (30)	11% (17)	5% (8)
	Non-service	38% (40)	27% (28)	20% (21)	11% (11)	4% (4)
Record keeping tax purposes	Service	17% (31)	19% (35)	28% (50)	19% (34)	17% (30)
	Non-service	10% (12)	17% (21)	23% (28)	33% (40)	17% (21)
Directors' duties	Service	28% (44)	25% (40)	28% (45)	11% (17)	8% (12)
	Non-service	15% (16)	34% (36)	28% (30)	14% (15)	9% (10)
Information disclosure	Service	28% (46)	18% (29)	29% (47)	18% (30)	7% (12)
	Non-service	22% (23)	25% (27)	28% (30)	15% (16)	9% (10)
Occupational Health and Safety	Service	20% (36)	25% (45)	25% (45)	15% (27)	14% (24)
	Non-service	11% (13)	13% (16)	23% (27)	21% (25)	32% (38)
Superannuation	Service	20% (34)	30% (53)	24% (42)	18% (32)	7% (13)
	Non-service	18% (21)	20% (24)	27% (32)	21% (25)	14% (16)
Workplace relationships	Service	19% (33)	28% (48)	25% (42)	17% (29)	11% (19)
	Non-service	17% (20)	25% (29)	30% (34)	16% (18)	12% (14)
Maternity leave	Service	46% (61)	17% (23)	17% (22)	11% (15)	8% (11)
	Non-service	45% (36)	21% (17)	15% (12)	8% (6)	11% (9)
Quality assurance	Service	20% (33)	22% (37)	28% (46)	19% (32)	11% (18)
	Non-service	27% (29)	21% (22)	31% (33)	12% (13)	9% (10)
Environmental protections	Service	33% (52)	27% (43)	22% (35)	10% (16)	7% (11)
	Non-service	14% (16)	25% (28)	26% (30)	22% (25)	13% (15)

* Difficulties incurred by regulatory requirements: 1= Not difficult at all; 2= Not so difficult; 3= Neutral; 4 = Difficult; and 5 = Most difficult.

Table 8.5 Comparison of difficulties incurred by regulatory requirements by membership of industry association

	Membership of industry association	1	2	3	4	5
ASIC regulation	No	44% (27)	15% (9)	23% (14)	16% (10)	3% (2)
	Yes	38% (73)	28% (55)	19% (37)	9% (18)	5% (10)
Record keeping for tax purposes	No	17% (13)	15% (11)	23% (17)	25% (19)	20% (15)
	Yes	13% (30)	19% (43)	27% (60)	25% (55)	16% (36)
Directors' duties	No	30% (20)	26% (17)	24% (16)	12% (8)	8% (5)
	Yes	20% (40)	29% (57)	30% (58)	12% (24)	9% (17)
Information disclosure	No	37% (25)	19% (13)	25% (17)	13% (9)	4% (3)
	Yes	22% (44)	21% (41)	30% (60)	18% (36)	10% (19)
Occupational Health and Safety	No	17% (13)	25% (19)	31% (23)	11% (8)	16% (12)
	Yes	16% (35)	19% (41)	22% (49)	20% (44)	22% (49)
Superannuation	No	18% (13)	31% (23)	20% (15)	18% (13)	14% (10)
	Yes	19% (40)	25% (53)	27% (59)	20% (44)	9% (19)
Workplace relationships	No	18% (13)	29% (21)	27% (20)	18% (13)	8% (6)
	Yes	19% (39)	26% (55)	26% (55)	16% (34)	13% (27)
Maternity leave	No	49% (26)	15% (8)	13% (7)	11% (6)	11% (6)
	Yes	45% (70)	20% (31)	17% (26)	10% (15)	9% (14)
Quality assurance	No	25% (18)	24% (17)	24% (17)	15% (11)	13% (9)
	Yes	22% (44)	21% (41)	31% (62)	17% (33)	9% (18)
Environmental protections	No	29% (19)	35% (23)	18% (12)	12% (8)	6% (4)
	Yes	24% (49)	24% (48)	26% (53)	16% (32)	10% (21)

* Difficulties incurred by regulatory requirements: 1= Not difficult at all; 2= Not so difficult; 3= Neutral; 4 = Difficult; and 5 = Most difficult.

Table 8.6 Comparison of difficulties incurred by regulatory requirements by development stage

	Development stage on business life cycle	1	2	3	4	5
ASIC regulation	Start-ups	31% (15)	27% (13)	23% (11)	13% (6)	6% (3)
	Established	43% (75)	23% (39)	20% (34)	10% (17)	5% (8)
	Declining	30% (11)	38% (14)	16% (6)	14% (5)	3% (1)
Record keeping for tax purposes	Start-ups	16% (9)	14% (8)	23% (13)	27% (15)	20% (11)
	Established	16% (31)	20% (39)	26% (51)	24% (47)	16% (31)
	Declining	6% (3)	19% (9)	30% (14)	26% (12)	19% (9)
Directors' duties	Start-ups	27% (13)	20% (10)	33% (16)	10% (5)	10% (5)
	Established	23% (42)	29% (53)	28% (50)	12% (21)	8% (14)
	Declining	14% (5)	36% (13)	25% (9)	17% (6)	8% (3)
Information disclosure	Start-ups	28% (14)	16% (8)	24% (12)	24% (12)	8% (4)
	Established	26% (47)	22% (40)	29% (52)	14% (26)	8% (15)
	Declining	20% (8)	20% (8)	33% (13)	20% (8)	8% (3)
Occupational Health and Safety	Start-ups	25% (13)	17% (9)	32% (17)	9% (5)	17% (9)
	Established	15% (29)	22% (44)	21% (41)	20% (39)	22% (44)
	Declining	15% (7)	17% (8)	30% (14)	17% (8)	20% (9)
Superannuation	Start-ups	20% (10)	32% (16)	18% (9)	22% (11)	8% (4)
	Established	20% (39)	26% (50)	27% (52)	19% (38)	8% (16)
	Declining	13% (6)	23% (11)	28% (13)	17% (8)	19% (9)
Workplace relationships	Start-ups	25% (13)	20% (10)	29% (15)	10% (5)	16% (8)
	Established	17% (32)	30% (58)	25% (48)	17% (33)	10% (20)
	Declining	18% (8)	20% (9)	30% (13)	20% (9)	11% (5)
Maternity leave	Start-ups	50% (19)	13% (5)	13% (5)	8% (3)	16% (6)
	Established	44% (65)	23% (34)	17% (25)	10% (15)	6% (9)
	Declining	50% (13)	4% (1)	15% (4)	12% (3)	19% (5)
Quality assurance	Start-ups	21% (10)	19% (9)	25% (12)	21% (10)	15% (7)
	Established	22% (41)	24% (45)	28% (51)	16% (30)	9% (17)
	Declining	27% (11)	12% (5)	39% (16)	12% (5)	10% (4)
Environmental protections	Start-ups	30% (14)	23% (11)	23% (11)	13% (6)	11% (5)
	Established	26% (47)	29% (53)	23% (42)	14% (26)	9% (16)
	Declining	18% (7)	18% (7)	30% (12)	23% (9)	13% (5)

* Difficulties incurred by regulatory requirements: 1= Not difficult at all; 2= Not so difficult; 3= Neutral; 4 = Difficult; and 5 = Most difficult.

Table 8.7 Comparison of difficulties incurred by regulatory requirements number of employees

	Number of Employees	1	2	3	4	5
ASIC regulation	1	33% (3)	0% (0)	33% (3)	22% (2)	11% (1)
	2-5	37% (33)	33% (30)	16% (14)	11% (10)	3% (3)
	6-19	40% (19)	17% (8)	28% (13)	11% (5)	4% (2)
	20-49	50% (7)	29% (4)	14% (2)	0% (0)	7% (1)
	above 50	33% (4)	17% (2)	17% (2)	25% (3)	8% (1)
Record keeping for tax purposes	1	22% (4)	17% (3)	22% (4)	22% (4)	17% (3)
	2-5	7% (8)	19% (21)	30% (32)	25% (27)	19% (20)
	6-19	19% (9)	19% (9)	23% (11)	25% (12)	15% (7)
	20-49	13% (2)	6% (1)	19% (3)	50% (8)	13% (2)
	above 50	0% (0)	0% (0)	27% (3)	36% (4)	36% (4)
Directors' duties	1	46% (6)	8% (1)	15% (2)	23% (3)	8% (1)
	2-5	23% (21)	24% (22)	34% (31)	11% (10)	8% (7)
	6-19	24% (12)	22% (11)	31% (15)	12% (6)	10% (5)
	20-49	7% (1)	43% (6)	29% (4)	21% (3)	0% (0)
	above 50	8% (1)	8% (1)	42% (5)	17% (2)	25% (3)
Information disclosure	1	43% (6)	36% (5)	7% (1)	7% (1)	7% (1)
	2-5	23% (21)	19% (18)	31% (29)	20% (19)	6% (6)
	6-19	21% (10)	17% (8)	27% (13)	21% (10)	15% (7)
	20-49	21% (3)	21% (3)	29% (4)	21% (3)	7% (1)
	above 50	8% (1)	17% (2)	33% (4)	25% (3)	17% (2)
Occupational Health and Safety	1	33% (6)	6% (1)	22% (4)	22% (4)	17% (3)
	2-5	16% (17)	24% (25)	26% (27)	18% (19)	15% (16)
	6-19	10% (5)	27% (13)	24% (12)	16% (8)	22% (11)
	20-49	6% (1)	13% (2)	13% (2)	13% (2)	56% (9)
	above 50	0% (0)	8% (1)	17% (2)	33% (4)	42% (5)
Superannuation	1	20% (3)	27% (4)	13% (2)	27% (4)	13% (2)
	2-5	12% (13)	33% (35)	28% (29)	19% (20)	8% (8)
	6-19	20% (10)	24% (12)	24% (12)	16% (8)	14% (7)
	20-49	31% (5)	19% (3)	19% (3)	19% (3)	13% (2)
	above 50	0% (0)	25% (3)	33% (4)	33% (4)	8% (1)
Workplace relationships	1	27% (4)	13% (2)	27% (4)	13% (2)	20% (3)
	2-5	17% (17)	29% (30)	30% (31)	17% (17)	7% (7)
	6-19	12% (6)	24% (12)	24% (12)	20% (10)	18% (9)
	20-49	6% (1)	19% (3)	25% (4)	19% (3)	31% (5)
	above 50	0% (0)	17% (2)	8% (1)	58% (7)	17% (2)
Maternity leave	1	64% (7)	9% (1)	9% (1)	0% (0)	18% (2)
	2-5	49% (33)	18% (12)	10% (7)	13% (9)	9% (6)
	6-19	41% (16)	23% (9)	23% (9)	3% (1)	10% (4)
	20-49	36% (5)	21% (3)	14% (2)	21% (3)	7% (1)
	above 50	8% (1)	17% (2)	25% (3)	33% (4)	17% (2)

(Continued)

Table 8.7 Comparison of difficulties incurred by regulatory requirements by membership of industry association (Continued)

	Number of Employees	1	2	3	4	5
Quality assurance	1	29% (4)	29% (4)	29% (4)	14% (2)	0% (0)
	2-5	20% (19)	24% (23)	32% (31)	19% (18)	6% (6)
	6-19	20% (9)	24% (11)	15% (7)	26% (12)	15% (7)
	20-49	7% (1)	27% (4)	33% (5)	13% (2)	20% (3)
	above 50	8% (1)	8% (1)	42% (5)	8% (1)	33% (4)
Environmental protections	1	21% (3)	14% (2)	36% (5)	21% (3)	7% (1)
	2-5	23% (21)	28% (26)	29% (27)	15% (14)	5% (5)
	6-19	27% (13)	27% (13)	22% (11)	12% (6)	12% (6)
	20-49	13% (2)	27% (4)	13% (2)	27% (4)	20% (3)
	above 50	8% (1)	17% (2)	25% (3)	25% (3)	25% (3)

* Difficulties incurred by regulatory requirements: 1= Not difficult at all; 2= Not so difficult; 3= Neutral; 4 = Difficult; and 5 = Most difficult.

Table 8.8 Comparison of difficulties incurred by regulatory requirements by whether has a board

	Has a board of directors?	1	2	3	4	5
ASIC regulation	No	38% (70)	28% (51)	21% (38)	9% (17)	4% (8)
	Yes	42% (31)	20% (15)	18% (13)	15% (11)	5% (4)
Record keeping for tax purposes	No	13% (30)	20% (45)	26% (58)	24% (53)	17% (39)
	Yes	17% (13)	14% (11)	26% (20)	27% (21)	16% (12)
Directors' duties	No	21% (40)	31% (59)	28% (54)	12% (22)	8% (15)
	Yes	27% (20)	23% (17)	28% (21)	13% (10)	9% (7)
Information disclosure	No	25% (49)	23% (44)	31% (61)	14% (27)	7% (13)
	Yes	26% (20)	16% (12)	21% (16)	25% (19)	12% (9)
Occupational Health and Safety	No	17% (38)	20% (43)	24% (53)	18% (39)	21% (46)
	Yes	14% (11)	23% (18)	25% (19)	17% (13)	21% (16)
Superannuation	No	19% (41)	25% (54)	25% (54)	21% (45)	10% (22)
	Yes	18% (14)	30% (23)	26% (20)	16% (12)	9% (7)
Workplace relationships	No	20% (42)	26% (55)	29% (62)	14% (30)	10% (22)
	Yes	15% (11)	29% (22)	19% (14)	23% (17)	15% (11)
Maternity leave	No	46% (70)	18% (27)	14% (22)	12% (18)	10% (15)
	Yes	45% (27)	22% (13)	20% (12)	5% (3)	8% (5)
Quality assurance	No	23% (47)	22% (44)	30% (60)	15% (31)	9% (19)
	Yes	21% (15)	21% (15)	26% (19)	19% (14)	13% (9)
Environmental protections	No	26% (51)	23% (46)	24% (48)	16% (31)	11% (22)
	Yes	23% (17)	34% (25)	23% (17)	14% (10)	5% (4)

* Difficulties incurred by regulatory requirements: 1= Not difficult at all; 2= Not so difficult; 3= Neutral; 4 = Difficult; and 5 = Most difficult.

8.4. Correlation coefficients between financial performance indicators and regulatory requirement

Given that the variables used to measure regulatory difficulties are ordinal data in nature, the Spearman correlation coefficient is used to test the correlations between financial performance indicators and regulatory compliance requirements, social performance indicators and regulatory compliance requirements, and corporate governance mechanisms and regulatory compliance requirements.

8.4.1. Financial performance and regulatory compliance requirements

The regulatory requirements serve as stimulus for the financial performance measured by total assets, total sales and net profit, meaning that the better the financial performance the higher the regulatory compliance costs, except that the difficulties incurred by ASIC regulation has a negative impact which means that stricter ASIC regulatory requirements prohibits better financial performance. The regulatory compliance difficulties perceived by the small businesses deter the net profit growth, except that the stricter quality assurance contributes to net profit growth. Ranked by the effect size, the top five deterrents of the net profit growth are superannuation management, ASIC regulation, maternity leave, environmental protection and occupational health and safety, all of which exceed the value of 0.1 (Table 8.9).

Small corporations which may have difficulty with ASIC regulations may also have difficulty with information disclosure (correlation coefficient is 0.53 and statistically significant). Correlation coefficients larger than 0.50 is perceived as large effect[7] (Cohen 1988), hence .05 is used here as a cutting off point to identify large effects. Those having difficulties with record keeping for tax purpose also have difficulty with director's duties, OHS and

[7] According to Cohen (1988), effect size < 0.1 = trivial effect; 0.1-0.3 = small effect; 0.3 – 0.5 = moderate effects; > 0.5 = large effect.

superannuation management. Those having difficulty with directors' duties also have difficulty with information disclosure, quality assurance and environmental protection. Those having difficulties with information disclosure also have difficulties with quality assurance and environmental protection. Those having difficulties with OHS also have difficulties with superannuation management, workplace relations and environmental protection (Table 8.9).

8.4.2. Social performance indicators and regulatory compliance requirements

Small corporations which consider customers in their key business decision making find it more difficult to comply with regulatory requirements such as directors' duty and environmental protection, but less difficult in superannuation management and maternity leave. Those that consider suppliers find it difficult in superannuation management and environmental protection, but less difficult with ASIC regulation and maternity leave. Those that consider employees find it more difficult to comply with directors' duties, information disclosure, workplace relations and quality assurance, but less with record keeping for tax purposes. Those that consider philanthropy find it more difficulty with ASIC regulation, but less with superannuation management, OHS, record keeping for tax purpose, maternity leave and environmental protection. Those that consider the environment find it more difficult to deal with ASIC regulation, information disclosure, OHS, workplace relations and environmental protection (Table 8.10).

8.4.3. Corporate governance mechanisms and regulatory compliance requirements

Small corporations which are independently audited find it more difficult to comply with regulatory requirements such as OHS, superannuation management, workplace relation and maternity leave, but less with director's duty or information disclosure. Those with high interest alignments, meaning that the owner and manager are closely related or is the same person, tends to have less difficulty in all kinds of regulatory requirements. Those that have a chairman who is also the CEO find it more difficult to comply with ASIC regulations, directors' duty and superannuation management, but less with OHS, workplace relations and quality assurance.

Those which have a larger number of directors serving on the board find it more difficult with OHS, workplace relation, maternity leave, quality assurance and environment, but less with record keeping for tax purpose. Those that have more independent directors serving on the board tend to have more difficulties with regulatory requirements. Those with a board and that meet more frequently tend to have more difficulty with regulatory compliance requirements except ASIC regulation. Those whose board of directors use their personal network for business purposes tend to have more difficulties with regulatory compliance requirements such as ASIC regulation and record keeping for tax purpose, but less with OHS, workplace relations and quality assurance (Table 8.11).

Table 8.9 Correlation between financial performance indicators and regulations

	No.	1	2	3	4	5	6	7	8	9	10	11	12	13	14
total assets	1	1													
total sales	2	0.6812*	1												
net profit	3	0.6146*	0.6303*	1											
net profit growth	4	0.0273	0.0061	0.2186*	1										
ASIC regulation	5	0.0134	-0.0459	0.0087	-0.1381	1									
record keeping for tax purpose	6	0.1262	0.1212	0.1025	-0.0618	0.2607*	1								
directors' duty	7	0.1067	0.11	0.1716	-0.009	0.4844*	0.5460*	1							
information disclosure	8	0.0468	0.1252	0.1345	-0.0397	0.5333*	0.4539*	0.6919*	1						
OHS	9	0.2048*	0.2659*	0.0653	-0.1025	0.2106*	0.5030*	0.4543*	0.4398*	1					
superannuation management	10	0.118	0.1155	0.0899	-0.1536	0.2918*	0.5664*	0.3454*	0.3282*	0.5027*	1				
workplace relation	11	0.2139*	0.2066*	0.175	-0.0637	0.3163*	0.4981*	0.4539*	0.4619*	0.6495*	0.6860*	1			
maternity leave	12	0.1840*	0.1656	0.0996	-0.1168	0.2626*	0.3203*	0.3519*	0.2769*	0.4503*	0.4640*	0.5810*	1		
quality assurance	13	0.1662	0.1532	0.0803	0.0319	0.3690*	0.4436*	0.5455*	0.5633*	0.4650*	0.4310*	0.5608*	0.4493*	1	
environment protection	14	0.175	0.2117*	0.0752	-0.1142	0.4087*	0.4580*	0.5191*	0.5166*	0.6614*	0.5114*	0.6107*	0.5819*	0.5808*	1

*denotes that the corresponding Spearman correlation coefficient is statistically significant at 5% significance level.

Table 8.10 Correlation between social performance indicators and regulatory requirements

	No.	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
customers	1	1														
suppliers	2	0.2377*	1													
employees	3	0.3186*	0.0671	1												
philanthropy	4	0.1983*	0.0718	0.0109	1											
environment	5	0.2663*	0.3327*	0.2159*	0.2794*	1										
ASIC regulation	6	0.0096	-0.0311	0.0504	0.1163	0.1292	1									
record keeping for tax purpose	7	0.0974	0.044	-0.0206	-0.0642	0.0078	0.3420*	1								
directors' duty	8	0.1482	0.0258	0.1929*	0.0571	0.0615	0.5276*	0.5542*	1							
information disclosure	9	0.0041	-0.0043	0.2028*	0.0999	0.1141	0.5711*	0.4660*	0.6914*	1						
OHS	10	0.0593	0.089	0.0091	-0.0811	0.1985*	0.2334*	0.4690*	0.4502*	0.4058*	1					
superannuation management	11	-0.0407	0.111	-0.0004	-0.1227	0.0605	0.3054*	0.5405*	0.3554*	0.3532*	0.4488*	1				
workplace relation	12	0.0958	0.0477	0.1682	-0.0114	0.2594*	0.3869*	0.4870*	0.4652*	0.4827*	0.6154*	0.6144*	1			
maternity leave	13	-0.0634	-0.0817	0.075	-0.0519	-0.0036	0.3509*	0.3077*	0.3574*	0.3131*	0.4098*	0.4068*	0.5705*	1		
quality assurance	14	0.0458	0.0857	0.1085	0.0228	0.0379	0.4090*	0.4578*	0.5403*	0.5586*	0.4766*	0.4079*	0.6011*	0.4849*	1	
environment protection	15	0.1073	0.1129	0.0267	-0.0266	0.2187*	0.4356*	0.4721*	0.5366*	0.5184*	0.6285*	0.4934*	0.6027*	0.5940*	0.5623*	1

*denotes that the corresponding Spearman correlation coefficient is statistically significant at 5% significance level.

Table 8.11 Correlation coefficient between corporate governance mechanisms and regulatory requirements

		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
independent audit	1	1																
interest alignment	2	-0.0414	1															
duality	3	-0.0315	0.1632	1														
board size	4	-0.0746	-0.1974	-0.4249*	1													
board independence	5	-0.1903	-0.2314	-0.4298*	0.5083*	1												
board meeting frequency	6	-0.2247	-0.3628*	0.0293	0.4317*	0.4116*	1											
board network	7	0.0082	0.2225	0.2808*	-0.1809	-0.2313	0.0625	1										
ASIC regulation	8	0.0335	-0.0475	0.0836	0.0142	0.0074	-0.0347	0.1261	1									
record keeping for tax purpose	9	0.0905	0.0219	0	-0.011	0.1616	0.0749	0.2565	0.4106*	1								
directors' duty	10	-0.0107	-0.0267	0.0816	0.0706	0.1968	0.2485	0.0647	0.4011*	0.5900*	1							
information disclosure	11	-0.036	-0.0673	-0.0208	0.0115	0.1715	0.152	0.0084	0.6275*	0.4477*	0.5707*	1						
OHS	12	0.1169	-0.0894	-0.2028	0.3369*	0.2802*	0.1171	-0.2321	0.2172	0.4324*	0.3777*	0.2308	1					
superannuation management	13	0.1147	-0.0202	0.0415	0.0853	0.1692	0.1762	0.083	0.273	0.6036*	0.3447*	0.3234*	0.4608*	1				
workplace relation	14	0.1533	-0.2086	-0.0582	0.1983	0.2841*	0.2953*	-0.055	0.3765*	0.5157*	0.5308*	0.4623*	0.6352*	0.6233*	1			
maternity leave	15	0.1153	-0.1937	0.0188	0.1995	0.072	0.1899	0.0887	0.3376*	0.3335*	0.3795*	0.3624*	0.4109*	0.2900*	0.5507*	1		
quality assurance	16	0.0279	-0.2656	-0.0772	0.2431	0.1752	0.2081	-0.0943	0.3087*	0.3482*	0.5684*	0.4110*	0.4682*	0.2391	0.5609*	0.6540*	1	
environment protection	17	-0.008	-0.1218	0.0236	0.1728	0.2004	0.1851	0.0235	0.3189*	0.4665*	0.6041*	0.4934*	0.6256*	0.4289*	0.6396*	0.6025*	0.6037*	1

8.5. Measurement Model for Regulation

The literature review in Chapter 3 on small corporations and related regulation has identified ten dimensions of regulation. These were ASIC regulation, record keeping for tax purpose, directors' duties, information disclosure, OHS, superannuation, workplace relations, maternity leave, quality assurance and environmental protection. The measurement model hypothesized that regulation can be measured by each of these ten items, each of which also measures level of difficulty as perceived by the respondents (Figure 8.1). The items were allowed to correlate freely with each other but were uncorrelated with measurement errors from other indicators (Byrne, 2001). The path diagram together with standardised parameter estimates is shown in Figure 8.1.

Included in the model was a factor measuring overall regulation as perceived by the respondents. This is unobserved construct and is thus enclosed by ovals. Ten measures (enclosed by rectangles) were specified using a five-point Likert Scale, each with a nonzero loading on the factor it was designed to measure, and a zero loading on other factors. Thus, each indicator was identified with a unique construct. Error variables (enclosed by ovals because they are not directly observed) represent a composite of any influences on the observed measures that are not measured in this study. For example, in Figure 8.1 the single-headed arrow leading from regulation to ASIC regulatory compliance requirements (ASIC) shows that regulation depended only in part on ASIC; specifically the hypothetical 'Regulation' construct accounts for 27% of the variance in scores for item ASIC. Alternatively, the path coefficient (loading) that describes the impact of ASIC on Regulation is 0.57 (Arbuckle, 1995).

Goodness of fit index

There are 82 degrees of freedom (the construct variance is not shown for visual clarity). Thus normed chi-square = 0.195, GFI = 0.98, CFI = 0.99 all suggested the model is plausible. The

RMSEA index is acceptably low at 0.028. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). Thus for the financial performance measurement model, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. There was, therefore, evidence to suggest that the financial performance measurement model had adequate overall goodness-of-fit.

Construct validity was also examined. The CFA provided a test of convergent validity for each of the sets of items that measured each construct. All path estimates were significant at the 1% level, and loadings between measured variables and factors were generally greater than 0.5. Indicators loaded significantly on their hypothesized construct, indicating adequate levels of convergent validity (Bagozzi & Phillips, 1982; Barki & Hartwick, 2001).

Nested models to test dimensionality was a further consideration. The plausibility of one level of regulation model for SMEs (as opposed to, for example, a multiple dimension model) was assessed in a nested modelling process. A further test of the measurement model was made by comparing two nested models (Barki & Hartwick, 2003), as described in Chapter 6. The first model loaded all items onto a single factor, hypothesizing that the items do not differentiate any underlying dimensions. The second model assumed a two-level model and hypothesized that the items have different dimensions hence regulation is a multi-level latent variables measured by other latent variables related to regulation. The third model assumed a three-level model by explorative factor analysis. The chi-square difference statistics were calculated between the two-level model and single level model, the three-level model and the single level model. The Chi-square difference tests were not statistically significant, implying that Model 1 had a relatively better fit (as reported above). Thus, regulation of small corporations is a single level construct that can be measured by ten indicators, namely ASIC regulation, record keeping for tax purpose, directors' duties, information disclosure, OHS, superannuation, workplace relations, maternity leave, quality assurance and environmental protection.

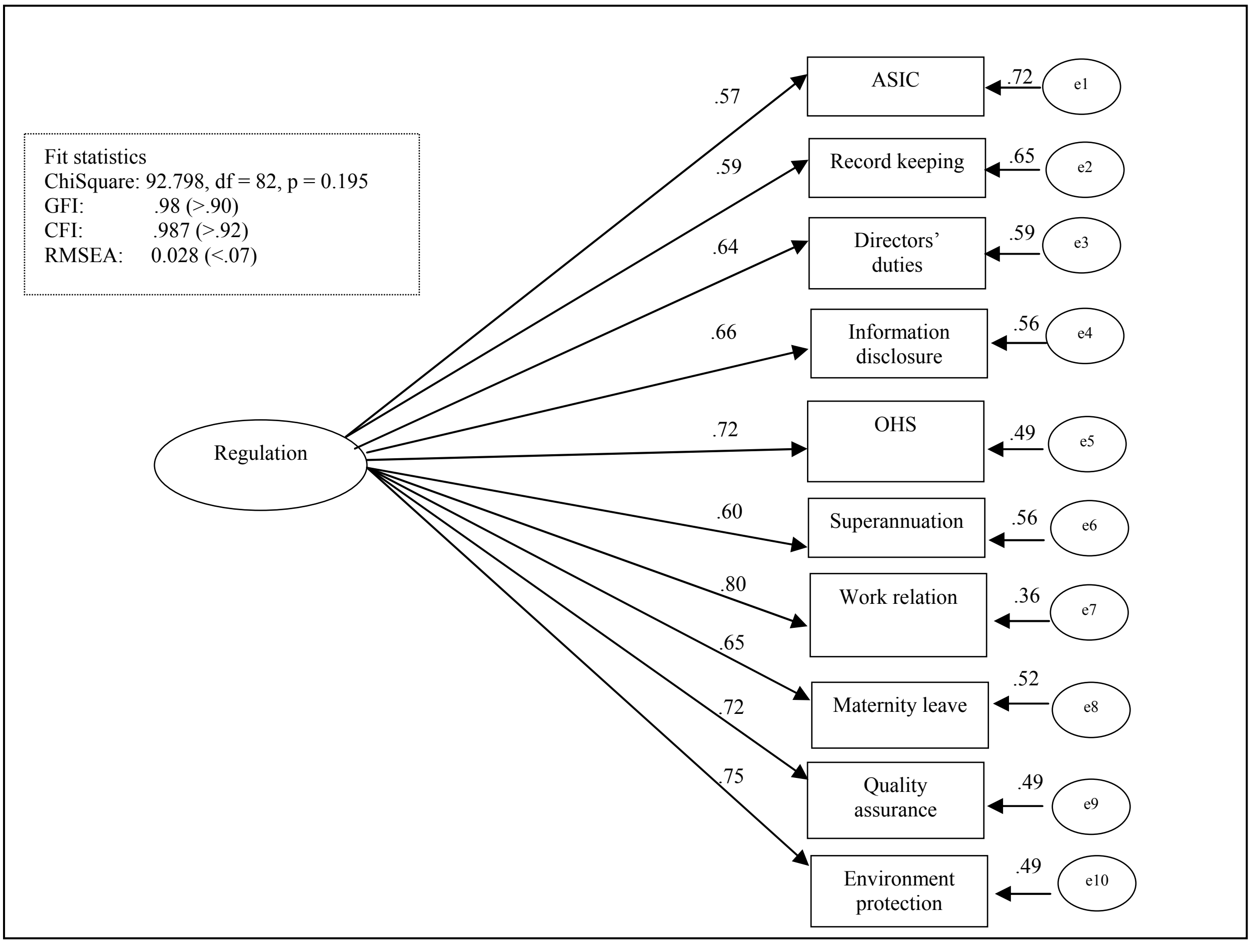


Figure 8.1: Model 7: Measurement Model of Regulation

Based on the factor weights in the measure model of regulation, work relation is the most prominent factor, followed by environmental protection, quality assurance for products and services, and OHS. Comparatively, ASIC regulations were surprisingly found as the least difficult regulatory compliance requirements.

8.6. SEM of Regulation and Financial Performance

The statistical hypothesis H20 developed in Chapter 5 specifically addressed research question R2: What relationships, if any, are there between regulation and financial performance for small corporations in Australia? The existing small business literature finds support for a negative impact of regulation on financial performance. Model 8, specified in

Figure 8.2, shows the parameters that resulted from the SEM analysis of relationships between regulation and financial performance.

There are 63 degrees of freedom (the construct variance is not shown for visual clarity). The normed chi-square = 0.38, GFI = 0.98, CFI = 0.99 all suggested the model is plausible. The RMSEA index is acceptably low at 0.012. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). For Model 8, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. There was, therefore, evidence to suggest that Model 8 had adequate overall goodness-of-fit (Figure 8.2).

The effect size of regulation on financial performance is 0.26 and is classified as a small effect according to Cohen (1988). The effect size is positive and statistically significant.

The size effects on the government regulation – financial performance link

According to the results in Table 7.24, the direct effect size of FTE on government regulation – financial performance link is 0.178, which is positive and statistically significant, meaning that a one scaling unit increase in FTE increases the effect size of government regulation to financial performance by 0.046, which is a multiplicative function of the moderation effect and the effect size.

The overall moderation effect is 0.511, meaning that one scaling unit increase in TTE overall increases the effect size of government regulation to financial performance by 0.133. In other words, for larger companies, the positive impact of regulation on financial performance is more prevailing that those micro- businesses.

8.7. SEM of Regulation and CSR

The statistical hypothesis H22 developed in Chapter 5 specifically addressed research question R2: What relationships, if any, are there between regulation and CSR for small corporations in Australia? The existing small business literature finds support for a negative impact of regulation on CSR. Model 9, specified in Figure 8.3, shows the parameters that resulted from the SEM analysis of relationships between regulation and financial performance.

There are 73 degrees of freedom (the construct variance is not shown for visual clarity). The normed chi-square = 0.55, GFI = 0.99, CFI = 1 all suggested the model is plausible. The RMSEA index is acceptably low at 0. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). Thus, for Model 8, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. There was thus evidence to suggest that Model 9 had adequate overall goodness-of-fit (Figure 8.3).

The effect size of regulation on CSR is 0.29 and is a small effect according to Cohen (1988), though it is close to below the cutting off point 0.3 that it failed to be qualified as a moderate effect. The effect size is positive and statistically significant.

8.8. SEM of Regulation and Corporate Governance

The statistical hypothesis H23 developed in Chapter 5 specifically addressed research question R2: What relationships, if any, are there between regulation and corporate governance for small corporations in Australia? The small business literature finds support for a positive impact of regulation on corporate governance. Model 10, specified in Figure 8.3, shows the parameters that resulted from the SEM analysis of relationships between regulation and financial performance.

There are 110 degrees of freedom (the construct variance is not shown for visual clarity). Thus normed chi-square = 0.62, GFI = 1, CFI = 1 all suggested the model is plausible. The RMSEA index is acceptably low at 0. As described in Chapter 6, a confidence interval provides a test of close fit (C.I. straddles 0.05), and not-close fit (entire C.I. lies above 0.05). Thus for Model 8, a hypothesis of close fit < 0.05 was accepted, and not-close fit < 0.05 was rejected. There was thus evidence to suggest that Model 9 had adequate overall goodness-of-fit (Figure 8.3).

The effect size of regulation on corporate governance is 0.36 and is a moderate effect according to Cohen (1988). The effect size is negative and statistically significant.

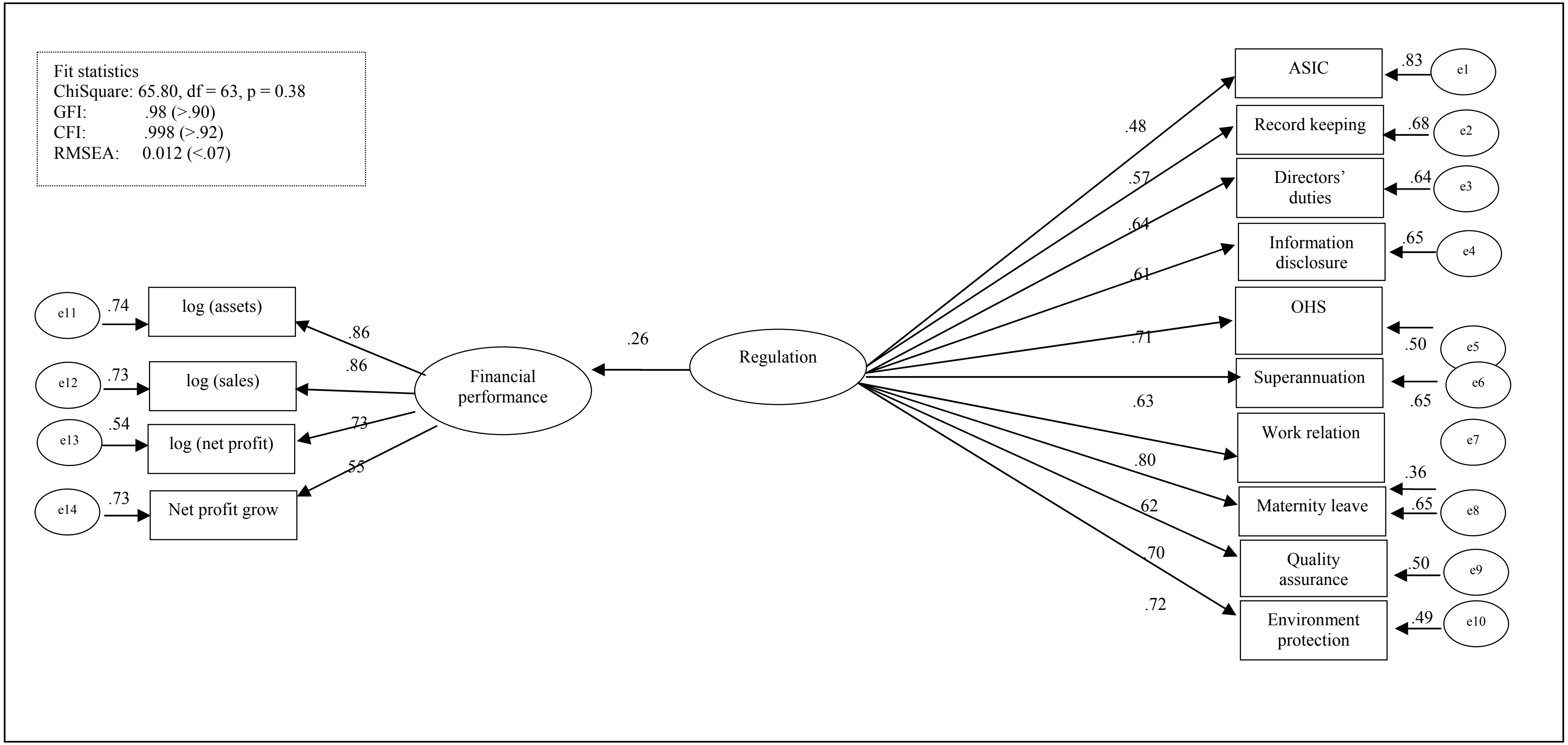


Figure 8.2 Model 8: Impact of Regulation on Financial Performance

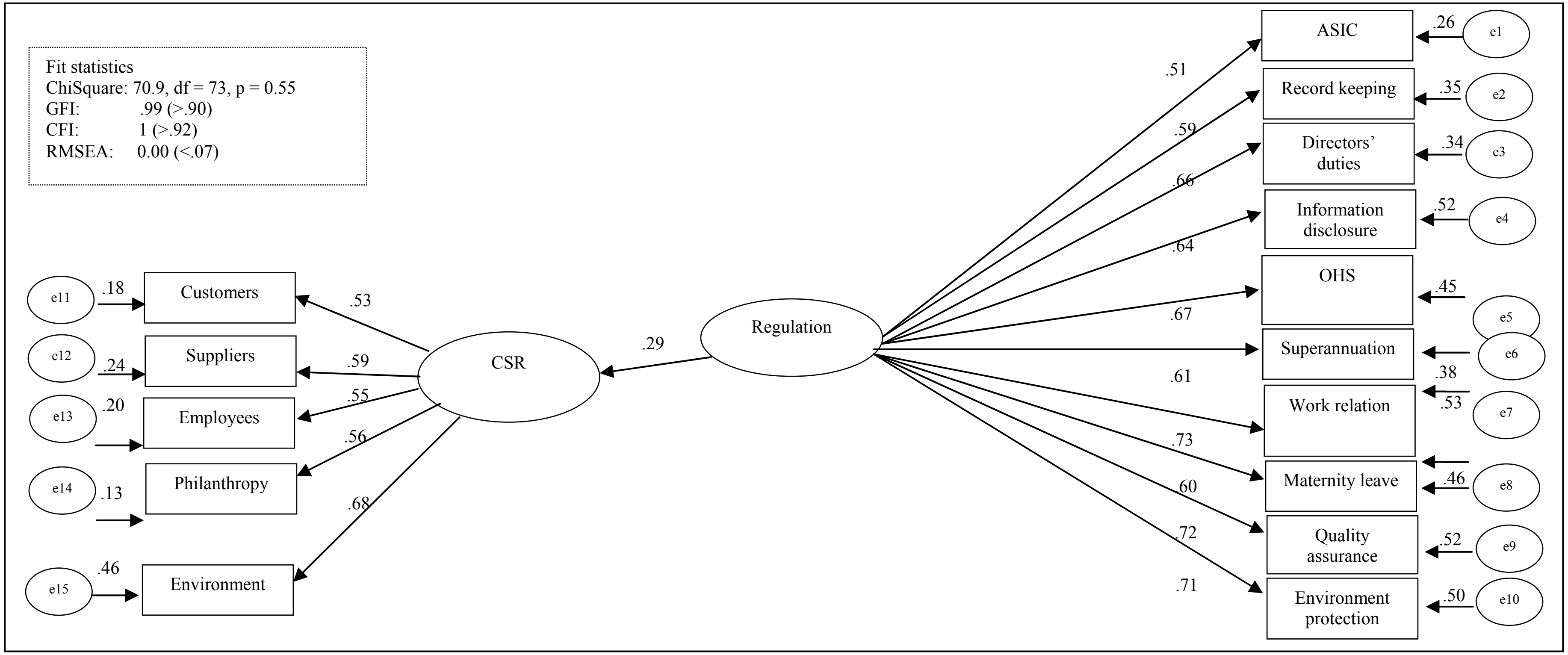


Figure 8.3 Model 9: Impact of Regulation on CSR

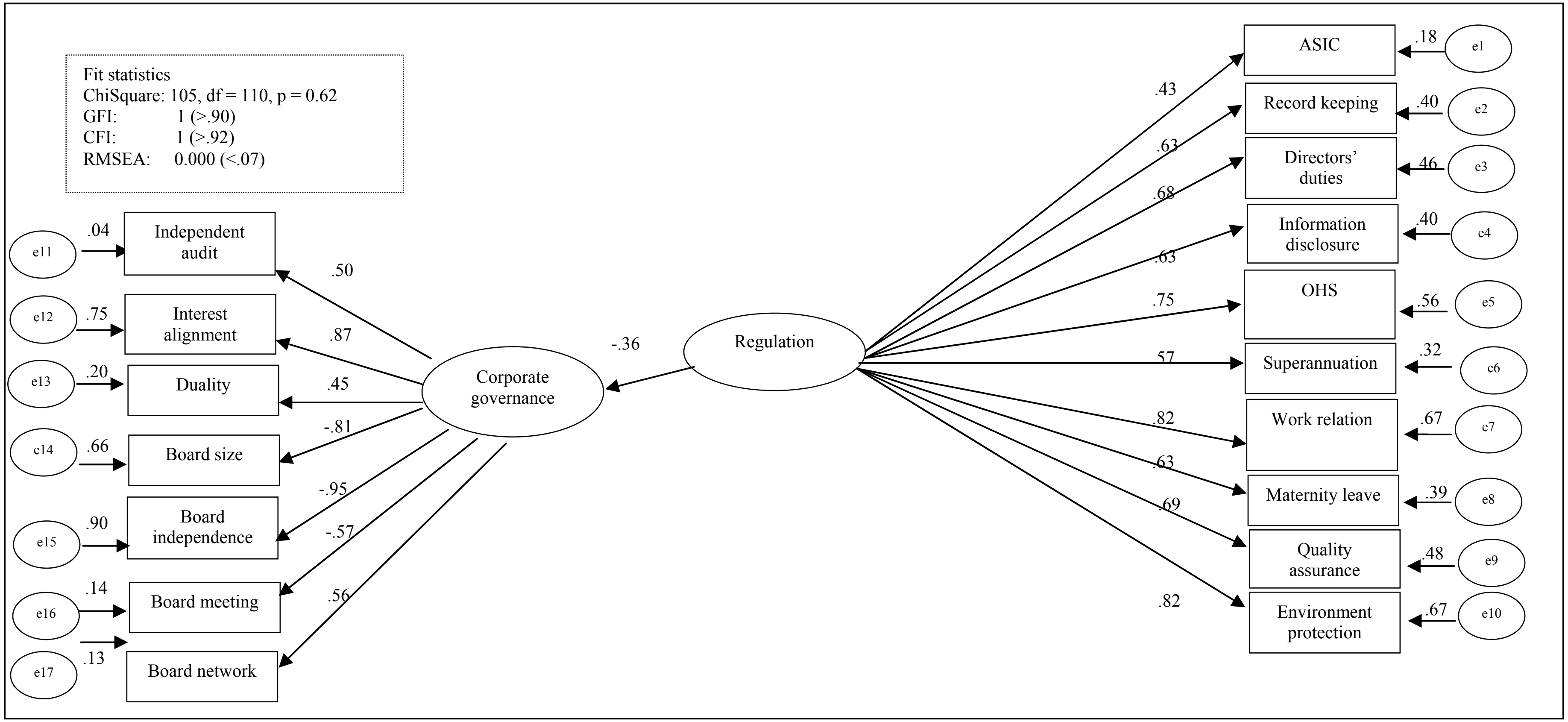


Figure 8.4 Model 10: Impact of Regulation on Corporate governance

8.9. Summary

The CFA model (Model 7) finds that regulation is a first order construct which can be measured by ten indicators, namely ASIC regulation, record keeping for tax purpose, directors' duties, information disclosure, OHS, superannuation, workplace relations, maternity leave, quality assurance and environmental protection.

The SEM models found that regulation has a positive impact on the financial performance (Model 8) and CSR (Model 9), but a negative impact on the corporate governance (Model 10).

CHAPTER NINE DISCUSSION

9.1. Introduction

This chapter discusses the research findings from Chapter 7 and 8, theories and empirical studies in prior research to review in Chapter 2 and Chapter 3.

The Chapter is structured around the sub- research questions of the research question:

- 'What relationship, if any, is there between corporate governance, government regulation and performance of small corporations in Australia?'
- Section 2 to 4 addresses Sub-question 1- 'What is the relationship, if any, is there between corporate governance and performance of small corporations in Australia?';
- Section 5 analysed Sub-question 2 – 'How to develop a corporate governance framework for the small corporations in Australia in order to improve performance';
- Section 6 and 7 discussed Sub-question 3 – 'What is the relationship, if any, between government regulation and performance of small corporations in Australia';
- Section 8 discussed Sub-question 4 – 'What relationship, if any, is there between corporate governance and government regulation?'
- Section 9 discussed Sub-question 5 – 'How to develop a responsive regulatory system for small corporations in Australia?'

In further introducing this Chapter, in specific, Section 2 discussed the performance measurement of small corporations, covering the financial performance, the CSR and the relationship between financial performance and CSR; Section 3 discussed the corporate governance in small corporations; Section 4 discussed the impact of corporate governance on the performance of small corporations; Section 5 analysed the regulatory policy alternative: private ordering – network based governance; Section 6 discussed the measurement of regulation of small corporations; Section 7 discussed the impact of regulation on the performance of small corporations; Section 8 discussed the impact of regulation on corporate governance; Section 9 developed a responsive regulatory system for small corporations in Australia; and, Section 10 ends with a brief summary.

9.1.1. Performance of small corporations

Sub-research question 1 involved the measurement of performance of small corporations in Australia during 2010-11. This section discussed the measurement of financial performance and CSR for small corporations and the relationship.

9.1.2. Financial Performance

Based on the prior literature reviewed in Chapter 2, the confirmative factor analysis found that four indicators can be used to measure financial performance of small corporations in Australia, namely the total assets, total sales, net profit and net profit growth (Model 1 in Fig. 7.4). The findings are consistent with Murphy et al. (1996) and cover four dimensions of the financial performance measurement of small corporations, namely size (measured by total assets), profit (measured by net profit), efficiency (proxy by total assets, total sales and net profit) and growth (measured by net profit growth). As shown in Fig. 7.4, financial performance is better measured by total assets, total sales and net profit. It is evident that growth plays a less important role in the financial performance than survival, given that this sample is dominated by micro- businesses.

9.1.3. CSR

Based on the prior literature, the confirmative factor analysis found that five indicators can be used to measure CSR of small corporations in Australia, namely the small corporation owner/managers' perceptions in key business decision making on the importance of customers, suppliers, employees, philanthropy, and environment (Model 2 in Fig. 7.5). The findings are consistent with and cover five of the six dimensions of the CSR measures widely accepted by the large corporations' literature (Kumar and Zattoni 2013). However, investors were not perceived as a major component for CSR. This conforms with the literature that small corporations are less attractive to investors compared with their larger counterparts; hence, the investors play a less important role in small corporations. Unfortunately, the role investors' play in small business financing is yet to be identified. However, this does flag another agency problem between the owner/managers and the investors, in which the investors may deserve more protection. This may merit further investigation in the future (Wright et al 2013).

9.1.4. Impact of CSR on financial performance of small corporations

As reported in Chapter 8, CSR has a negative impact on the financial performance of small corporations, implying that better CSR incurs extra costs for small corporations. This finding rejects the view that organizational effectiveness may be a broad concept encompassing both financial and social performance as complements (Andrews 1987; Judge 1994; Orlitzky et al. 2003). Instead, the result accepts the idea that CSR is necessarily inconsistent with shareholder wealth maximization (Friedman 1970). Given the conflicting nature of CSR and financial performance in this context, the bottom-line considerations may constitute barriers to outcomes desired by the public, which, in turn, makes it rational to introduce government intervention, serving as the "the public interest" (Orlitzky et al. 2003). This may go against the notion of libertarians such as Friedman who argued that government regulation on the CSR may not necessary obsolete.

Contrary to the results of many studies on small corporations, Orlitzky et al. (2003) synthesized the relationship from a meta-analysis and found a positive relationship between the CSR and CFP. They argued that the relationship should be bidirectional and simultaneous and may be confounded by reputation issues. McWilliams and Siegel (2000) found that most academic studies on the CSR and CFP link are mis-specified and once a problem is corrected, CSR has a neutral impact on CFP. Margolis et al. (2007) also find a positive relationship between CSR and CFP but such a relationship is inconsistent when different measures are used. They called for further efforts to find the mechanism governing the companies pursuing CSR, CFP subsequent to CSR, and pursuing both simultaneously.

The negative impact of CSR on financial performance of small corporations challenged the meta-analysis in Section 5.5 in Chapter 5 of this thesis. The results confirmed the causality relationship from CSR to financial performance and contradicted with the financial performance foster CSR argument. Hence, the results support the substitution effects between CSR and financial performance of small corporations.

A negative relationship between CSR and CFP can also be explained by the Resource-dependency Theory. This theory posits that small corporations do not enjoy the luxury of access to the resources that their larger counterparts do, hence are not able to afford both CFP and CSR simultaneously but have to trade-off CSR for CFP. It is also worth noting that the results strongly support the Stakeholder Theory, treating non-shareholding stakeholders such as investors, employees, community, environment and the philanthropy, as legitimate stakeholders. It is obvious that the market is able to account for accounting-based financial performance at the cost of jeopardising social performance, as indicated by the negative relationship.

Alternatively, it may be explained by the 'Principal-Principal Conflicts Theory', which argues that due to the concentration of ownership and control and poor institutional protections for minority shareholder rights, both external governance mechanisms such as institutional arrangements in the forms of law and regulations and internal governance mechanisms such as diluting the voting rights. This is pertinent to the CSR and financial performance debate. External stakeholders serve as minority 'shareholders' in obtaining a return for the social dividends in the form of granting the right for the small corporations to operate in exchange for quality products and a better environment. Quite opposite to this, a reality for many small corporations is that they consider the community's right to a lesser extent than their financial performance. This is especially true because they are supported by institutional design that encourages the small corporations to opt in/out in of taking into account CSR in their decision making. The author would suggest (1) CSR should be a performance measure for small corporations as well and it should be regulated; and (2) a more interactive model between small corporations and other stakeholders, in particular regulators, should be introduced. This point is discussed later in the responsive regulatory model section of this chapter.

Empirical research has also lead to conflicting results between the relationship between CSR and financial performance (Corporate Financial Performance or CFP), recent results of which been reported by a recent meta-analysis by Malhotra et al. (2013). They have summarised 56 studies published between 2002 and 2012 and reported that the link between CSR and CFP may be positive, negative, neutral, or curvilinear. In terms of the causal directions in the CSR and CFP link, they further argue that the literature has produced mixed results, some arguing that CSR causes CFP, some that CFP causes CSR and some for bidirectional relationships. However, studies generally agree that boundary conditions influencing CSR, CFP and the CSR-CFP link have yet to be explored in depth.

9.2. Corporate governance in small corporations

Based on existing research with a particular focus on large corporations, Gillan (2006) has classified corporate governance strategies as internal and external governance mechanisms.. For small corporations, adopting the same dichotomous approach, the literature has proposed a textbook model of corporate governance developed for large corporations and publicly-listed companies can simply be adapted to fit the requirements of the smaller enterprises (Gabrielsson and Huse 2002). Ingley and Karoui (2010) contends that the corporate governance in small businesses assumes both control and service roles; hence, the board composition, board characteristics and board network are key components of small business governance.

Based on the prior literature reviewed in Chapter 2, the confirmative factor analysis found that seven indicators can be used to measure corporate governance of small corporations in Australia, namely the number of directors on the board (board size), the separation of the chairman of the board and CEO, a number of independent directors on the board, the extent to which owner's interest aligns with managers, number of meetings held by the board in 2010-11, the extent to which boards use their networks to support business operations, and whether or not the firm is independently audited.

These findings are consistent with the measurement literature on corporate governance of small business. They are based on the previously discussed seven dimensions of corporate governance measures. However, competing theories such as Agency Theory, Stewardship Theory, do produce conflicting results. Agency Theory, for instance, argues that the board of directors serve as the controller of companies, thus its independence is a requirement to guaranteeing a controlling role (Jensen and Meckling 1976). Stewardship Theory, on the other hand, counters the view of management self-interest, arguing that managers are stewards of the resources entrusted to them and can be trusted to maximise profits on behalf of the shareholders (Donaldson 1990, 1991, 1994; Kiel and Nicholson 2003). Advocates for the Stewardship Theory continue to argue that external directors in particular are not necessary because they cannot provide firm-specific in-depth knowledge, skills, knowledge, time, resources or expertise to monitor management (Donaldson and Davis 1994).

9.2.1. Uniqueness of corporate governance in small corporations

Numerous corporate governance guidelines and good practices have been developed to improve the corporate governance of small corporations. Some have proven that the corporate governance mechanisms borrowed from large corporations are effective (Bennedsen et al. 2008), some believe it is unnecessary as it reduces the financial performance of small corporations (Hansson et al. 2010). However, it remains an open debate in the literature about the need for corporate governance in small corporations.

Without a thorough understanding of small corporations and their institutional contexts, borrowing the corporate governance mechanisms from large corporations may simply be a ‘window dressing’ and will not do any good to the financial and social performance of small corporations’ shareholders or owners. So what are the characteristics that small corporations possess that separate them from large corporations?

As pointed out by Armstrong, Li, Clarke et al. (2012), the majority of small corporations have some distinct characteristics, which are not shared with their larger counterparts. Such characteristics, particularly relevant to corporate governance mechanisms include relatively concentrated ownership structure, family ownership, little, if any, separation between ownership and management, lack of resource to hire professionals and directors, lack of resource to set up corporate governance structures. So what are the real corporate governance problems in small corporations?

Davis (2000) nominated three types of agency conflicts between: 1. owners and managers; 2. controlling shareholders and minority shareholders; and 3. shareholders and non-shareholding stakeholders. Type 1 conflict is the main theme of the corporate governance debate in large corporations and it can be compensated by signing *ex ante* contracts. As discussed in the distinct characteristics of small corporations, the separation of ownership and management is a minimal issue; hence type 1 conflict is not a major issue. What concerns small corporations, and offers opportunities for corporate governance research, is the type 2 and type 3 conflicts, both of which can hardly be secured by the *ex ante* contracts given that one can never predict the uncertainties involved in the contracts (McCarthery and Vermeulen 2008).

Type 2 conflict has been interpreted in the literature as principal-principal conflict (Su et al. 2008). The remedy is concentrated ownership, venture capital ownership and family ownership, as family business groups did in Japan and South Korea, but this may substitute or even jeopardise the remedies offered by the Agency Theory, for instance, board independence (Becher and Frye 2012).

Type 3 conflict may involve the employee involvement and protection (Labor law). However, consumer protection and quality assurance (Tort Law) is beyond internal governance and is expected to be solved through regulation rather than by governance mechanisms (Davis 2000;

Peng et al. 2008). However, it is yet to be confirmed as to whether or not regulation serves as a substitute or complementary mechanism to corporate governance (Adams and Ferreira 2006).

Based on the aforementioned justification, corporate governance is a relevant theme to small corporations. But would corporate governance in small corporations in Australia exhibit any differences? It may, due to the institutional structure and the market environment. The relationship between corporate governance and government regulation requirements are exhibited in Figure 1.

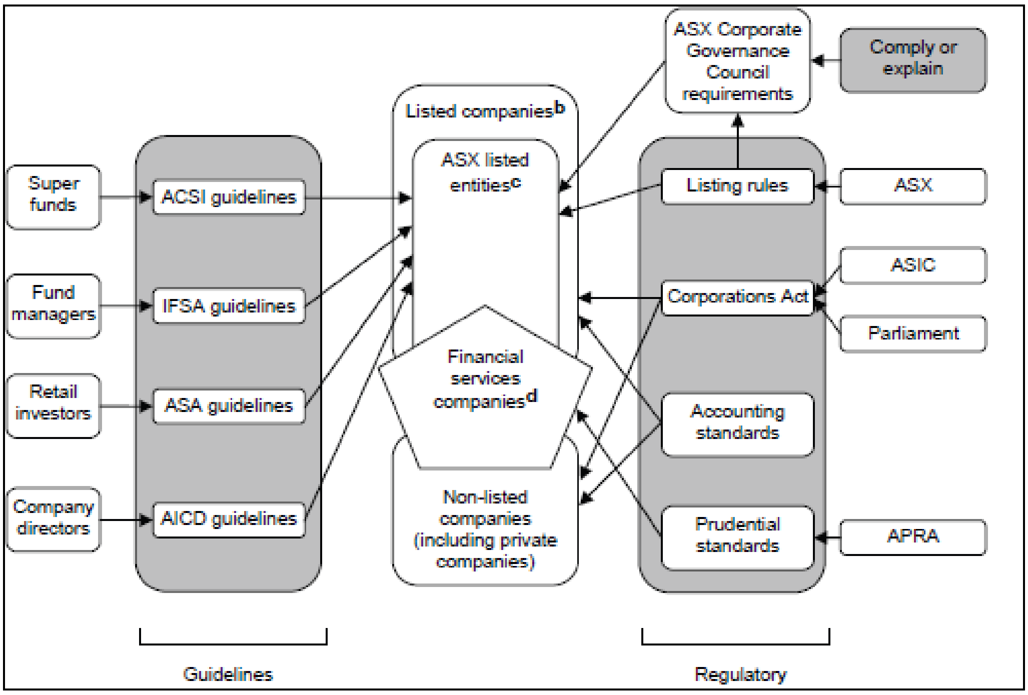


Fig. 9.1 Corporate governance and government regulation requirements in Australia

Small corporations are required to abide by the Corporations Act 2001(Cth), which is also called the Hard Law (Productivity Commission 2008). In addition, depending on the industry, small corporations may face industry-specific regulations, also called soft laws. From the market perspective, most of the small corporations face a monopolistic market, which amongst themselves are a quasi-competitive market (reviewed by numerous task force reports by the Productivity Commission and Australian Competition and Consumers Commission, such as Service Industry, the Manufacturing Industry). The combined effect of hard law, soft law and market structure may determine interaction between corporate governance and government regulation in small corporations in Australia.

9.2.2. Impact of corporate governance on the performance of small corporations

This study adopts two separate measures for performance of small corporations, namely the financial performance and the CSR. The impacts of corporate governance on financial performance and on CSR are discussed respectively. The results of the SEM model on the impact of corporate governance on the performance answers RQ1: what is the relationship, if there is any, between corporate governance and performance of small corporations?

The impact of corporate governance on financial performance

Empirical results from the SEM model in Chapter 8 found a negative impact of corporate governance on the financial performance of small corporations, which challenges the well-established theories on corporate governance in the large corporations' literature. The effect size is 0.4, indicating a medium effect. The results provide an answer to RQ1a: what is the relationship, if there is any, between corporate governance and financial performance of small corporations?

According to the Cadbury Report (1990) and the OECD (2004), corporations with sound governance systems yield good financial performance. The result from this study seems to contradict those in the well-cited literature of large corporations.

However, considering the disparities between small corporations and their larger counterparts, this result does not conflict with the existing literature, but complements them in four ways:

i. Though the literature is flooded with literature investigating the impact of a separate corporate governance mechanism on firm performance (Bhagat and Bolton 2008; Dalton et al. 1998; Zahra and Pearce 1989), treatment of corporate governance mechanisms as a bundle is fairly recent and is 'limited' (Rediker and Seth 1995; Hoskisson et al. 2009; Ward et al. 2009).

   Ward et al. (2009) points out that government mechanisms may serve as either complements or substitutes to one another. Hence, the estimation of the overall effect requires the corporate governance mechanism to be treated as a bundle (Mock 2007). Moreover, there is still a dearth of research into corporate governance bundles in small corporations. The SEM is recognised as the one of the most common techniques to empirically analyse the corporate governance mechanism as a bundle – a latent construct which can be measured by its indicators (Bowen and Guo 2013).

   This research project provides new evidence that the corporate governance bundle, measured by variables populated in the large corporations' literature, impedes the financial performance of small corporations. Why is this so? Admittedly, the literature has yet to provide evidence-based solutions for corporate governance in small corporations, with this study being the first to look into such issues. In addition, there may be three reasons, to be discussed below, the first reason is that the existing theory fails to consider the differences between large corporations and small corporations; the second reason is that small corporations are yet to incorporate governance practice in order to improve their financial performance, provided that the regulatory bodies are able to develop small corporations-tailored corporate governance guidelines; and, the third reason is that the same corporate governance, for instance, the board of directors, may play different roles in small corporations than their larger counterparts.

ii. The research finding of this project adds to the Agency Theory that multiple facets of the interest conflicts in the small corporations should be considered. Agency Theory has been used predominantly in justifying the existence of agency costs in large corporations between the owner and managers and in identifying ways to reduce it. Quite oppositely, small corporations do not have dispersed ownership structures and, consequently, the interest conflict between owner and managers is not the only major issue (Li et al. 2013). The main interest conflicts are between the shareholders and the other stakeholders, between dominating owners and the other owner/managers, as well as between family owners and other types of owners. In this regard, the Stakeholder Theory may be more sensible to justify the importance of corporate governance issues in small corporations (Wright et al. 2013).

iii. Small corporations passively react to corporate governance related regulations. In the responses to the open-end questions, small corporations' owner/managers point out that the ASIC regulation, in particular on director's duties and registration requirements are burdens to them, but with which they have to comply. Evidently, more discussion has yet to happen between the small corporations and ASIC in order to design small corporations-suited corporate governance practices in a view to improving their financial performance rather than compliance.

iv. It calls for an extended view about the role of the board of directors in a firm. Board's role in the Agency Theory, the Stakeholder Theory and the Network Theory has been classified mainly as control and monitoring (Ingley and Karoui 2012). Boards in small corporations offer more than the controlling role, but also resource roles (Armstrong et al. 2012). Board of directors also provide knowledge, skills, resource and social connections, which are all valuable assets to the financial performance of small corporations.

The moderating effect of size on the corporate governance- financial performance link

The results reported in Chapter 7, Section 7.8 revealed that size moderating the corporate governance and financial performance in a negative way. For those small corporations which have relatively more FTEs, corporate governance may have a positive impact on financial performance. When the firm size grows, the agency cost becomes a major concern and hence the corporate governance will add value to the financial performance.

But for those at the very small end, corporate governance has a negative impact on financial performance. If firm size is extremely small, ie. the micro-businesses in the sample, the corporate governance mechanisms prescribed by the regulatory bodies will be a drain on the financial performance, while alternative governance mechanisms have to be sought for. For micro-businesses, the governance issues will no longer be the agency cost, rather it will be issues such as resource constraints, network governance and risk management.

The impact of corporate governance on CSR

The study finds a negative relationship between corporate governance and CSR. The effect size is 0.13, which indicates a small effect. This contradicts the literature that suggests corporate governance should be able to improve CSR. The results provide answer to RQ1b: what is the relationship, if there is any, between corporate governance and CSR of small corporations?

There may be two relevant strands of explanations. One explanation is that the corporate governance measures failed to incorporate mechanisms relevant to the non-shareholding stakeholders; hence a non-positive impact should be expected. Moreover, CSR has been perceived as a less critical factor pertinent to the financial performance of large corporations. As discussed above, stakeholders' interests, partially presented by CSR, are of great significance to small corporations. Strengthening the shareholders' interest by improving corporate governance will certainly weaken CSR performance.

Another explanation may be relevant to the relationship between financial performance and CSR, which may be complementing or substitutive. As discussed in Section 2.3 in this chapter, the financial performance and CSR has a negative relationship, implying that the financial performance and CSR may compete for resources. It becomes natural that corporate governance compliance and practice absorbs more attention for financial performance from the owner/managers, hence reducing the CSR performance.

9.2.3. Corporate governance mechanisms for small corporations in Australia

Given the distinct features of small corporations and the institutional context in Australia, the proposed corporate governance mechanisms are best tailored to meet the needs of small corporations in Australia. Such mechanisms include multi-purpose of the corporate governance in small corporations, the role and selection of board of directions, family cycle and business cycle governance, networks and industry associations, corporate social responsibility, risk management and market mechanisms, and corporate governance as a dynamic process.

i. Corporate governance in small corporations serve multiple purposes

Corporate governance in small corporations serves multiple purposes. Such purposes include, but are not limited to, minority shareholder protection, value creation and value added, improvement in financial performance and CSR (Ingleey and Karoui 2013; OECD 2012). Small corporations may have to develop a holistic view that incorporates the financial performance, social performance, innovation and growth in the performance measurement system.

ii. Board of directors' role and structure

Board of directors in small corporations serve both controlling and service roles. They fill in the gaps in resource and expertise and they expand business opportunities by making use of their personal and professional networks. Ideally, the board of directors should possess a specialisation in areas which are critical to the core business of the small corporations and have relevant industry expertise (Ingley and Karoui 2013).

Given the nature of blockholding and family ownership, small corporations may focus more on the diversity of the expertise and required industry experience of directions, while give a lesser weight to the independence of the board (Adams and Ferrreira 2006).

iii. Family cycle governance and business cycle governance

The majority of small corporations are family owned (Armstrong et al. 2012). The corporate governance issue hence is complicated with the consideration of the family cycles and business cycles. Toms (2012) discussed the life cycle of corporate governance. Business type specific discussions include Bertoni et al. (2012) in High-tech firms, Uhlaner (2012) on family business, Filatotchev and Allcock (2012) on IPOs, Wu and Tihanyi (2012) on multinational firms and international firms, Yiu et al. (2012) on business groups, and Ayotte et al. (2012) on financial distress and bankruptcy. Given the complexity of the family cycle and business cycle, which may require benchmarking across the whole industry or sector, small corporations may have to resort to specialists for help in this regard.

Family governance is concerned with a number of issues, including succession planning, sustainability and social responsibility, and major events such as marriage and divorce of key family members.

iv. Network and industry associations

Recent development in Network Theory has pinpointed the importance of networks in business development (Street and Cameron 2007; Perry 2012). Network and industry associations serve as a nexus for information exchange and sharing good practice amongst small corporations.

v. Corporate social responsibility, risk management and market mechanisms

External corporate governance mechanisms have to be considered as an integrated part of the corporate governance framework. This includes corporate social responsibility, risk management and market mechanisms. Corporate social responsibility refers to the involvement and taking into account the key stakeholders in major business decision-making. Such stakeholders include employees, customers, suppliers, investors, environment, and philanthropy. Risk management may involve sound risk control systems, such as internal auditing, reporting and external auditing. Market mechanisms may include the competition in the labour market for qualified employees, directors and executives, the product market and the financial market.

vi. The corporate governance as a dynamic process

The Contingency Theory argues that strategic management, in the form of corporate governance, is a dynamic process and should be contingent on the contextual factors such as industry landscape and development stage. The majority of the businesses in the sample are at the established stage, where their governance needs would be more based on the consolidation of the market position and product development; while those at the start up stage, may have to control and minimise risk. Thus, the owner and managers of small corporations should keep in mind that the corporate governance project is a continuous process and demands updates given the change in development stages.

9.3. Impact of government regulation on the performance of small corporations

The results discussed here provide an answer to RQ2: what is the relationship, if there is any, between government regulation and performance of small corporations?

9.3.1. Measurement of Government regulation of small corporations

Based on previous literature, the confirmative factor analysis found that five indicators can be used to measure government regulation of small corporations in Australia. These indicators are the small corporation owner/managers' perceptions in ten separate regulatory requirements, namely ASIC regulation, record keeping for tax purpose, directors' duties, information disclosure, OHS, superannuation, workplace relations, maternity leave, quality assurance and environmental protection. The findings are consistent with the literature on regulation of small corporations (PC 2006).

Regulation provides the foundations for the relationship between the State and the firm. The Australian literature suggests that regulation of Australian firms is directed to, and best suits the needs of, the largest companies (those that are public, listed and well-resourced) (Clarke 2007).

This bias in regulatory framework is particularly evident when it comes to self-regulation, a version of responsive regulation that it is conducive to the market and aimed a particular group, in this case listed public companies as exemplified by the Best/Good Practice Recommendations provided by the ASX to listed companies. These self-regulatory practices favour large, wealthy firms that enjoy plentiful in-house expertise and elaborate compliance systems; while small corporations with fewer resources are left with the costly and onerous task of complying with compulsory regulation (Milman 1999; Bebchuk and Roe 2004). The regulation of small corporations in Australia fails to adequately respond to the needs of small corporations and is preventing small corporations from performing at their best. It is therefore essential that Australia develops a system that is responsive to the business needs and aspirations of small corporations in order to facilitate optimal growth and business performance.

The need for reform and clarity is further enhanced by the Australian federal system. The models of Federalism range from cooperative to coercive; however, 'to understand better the interactions between federal and state governments in regulatory policy, one must separate economic regulation of specific industries from enforcement actions related to social regulations' (Teske 2004). In Australia corporate, tax law and intellectual property are federal concerns (Jensen and Webster 2004), on the other hand, business names and occupational health and safety are state concerns, whilst zoning and planning are local council matters. This study focuses on the federal economic regulation of small corporations (Teske 2004, p. 14).

As the UK Greenbury Report noted, 'the way forward as one sees it lies not in statutory controls, which would be at best unnecessary and at worst harmful, but in action to strengthen accountability and encourage enhanced performance' (Greenbury 1995). International research in terms of listed firms has shown that responsive regulation can produce more profitable firm performance (Chew 1997; Kaplan 1997) because it highlights transparency of process, enables clear disclosure of key information (Uren 2003), reduces information asymmetries (Stiglitz 2003) and enhances employee commitment (Mitchell 2003). It also allows for more efficient financial markets (Goergen 1998).

Corporations experience a life-cycle including their founding, development and maturity, and at each stage the correlative regulatory requirements should develop with the resources and activities of the company (Filatotchev et al. 2006; Clarke et al. 2007). This is particularly true for small corporations whose regulation needs are very different from large corporations. However, optimal regulatory practices should be addressed by companies at an early stage of their growth.

9.3.2. Impact of Regulation on performance of small corporations

The SEM models estimate the impact of government regulation, measured by the perception of small business owner/managers, on the financial performance and CSR of small corporations.

The impact of regulation on financial performance

The SEM model finds a positive impact of corporate governance on the financial performance of small corporations, meaning that firms which have perceived more government regulatory requirements tend to have better financial performance. The effect size is 0.26, indicating a close to medium effect. The results discussed here provide answers to RQ2a: what is the relationship, if there is any, between government regulation and the financial performance of small corporations?

This finding is supported by the Public Interest Theory, which states that regulation is beneficial for the small corporations given that they face a quasi-competitive market and the stricter regulatory requirements may help to develop a stable market place for the small corporations to compete (Kitching 2008).

This further supports the argument that regulated firms may require less monitoring and less uncertainty, thus saving some costs for small corporations to focus on their core business rather than conflict resolution (Becher and Frye 2012).

The moderating effect of size on the regulation-financial performance link

As reported in Table 7.24 and Chapter 8, Section 8.6, the number of FTEs has a positive moderation effect on the effect size of regulation and financial performance. This indicates that, though positive influencing the financial performance, regulation benefits the medium-sized businesses more than the micro- and small businesses.

The Resource Dependency Theory and the Public Interest Group Theory may explain the overall impact of regulation on financial performance and may potentially account for that in the micro- and small businesses. However, for the medium-sized small corporations, their favourable treatment from regulation may be better explained by the Private Interest Group Theory in which they are able to lobby the government for preferential treatments or restrictions on large listed companies. The medium-sized small corporations may also be explained by the "regulatory capture", in that, comparing with their smaller counterparts, they are in a better position in terms of resource and capacity to benefit from the Public Interest Group lobby as well as the loopholes in regulatory changes.

The impact of regulation on CSR

The SEM results show that the regulation has a positive impact on CSR, indicating that the stricter regulation perceived by the small corporation owner/managers, the more likely that small business owner/managers take into account the CSR in their business decision making. The results discussed here provide an answer to RQ2b: what is the relationship, if there is any, between government regulation and CSR of small corporations? The effect size is 0.29, which is close to a medium effect.

This may suggest that the regulators should put more requirements on the CSR of small corporations and preferably making it compulsory so that the small corporations can be more responsible for CSR (Kitching 2008). This further supports the argument that regulators do not have the same financial interests as shareholders who maximises shareholding wealth, rather they will focus on safety and soundness. Hence, stricter regulation will result in better CSR (Skeel 1999).

9.3.3. Government **regulation for small corporations**

Regulation is not necessarily a burden. As the results show in Chapter 8, regulatory requirements generally improve total assets, total sales and net profit, which confirms with the Institutional Theory (Refer to Section 3.2.3 in Chapter 3). Given that the market small corporations face in Australia is competitive or quasi-competitive, setting the standard in the forms of rules and regulations is of critical importance to each individual small corporation.

However, the ASIC regulation does reduce the total sales in small corporations. This may be due to the 'one size fits all model', which creates disproportionate and unnecessary burdens to be borne by the small corporations.

Moreover, the regulatory requirements do incur extra costs which jeopardise net profit growth in small corporations, with quality control the only exception. The top five deterrents of the net profit growth are superannuation management, ASIC regulation, maternity leave, environmental protection and occupational health and safety.

Based on the research findings and as per the answers to open-ended questions in the VU Small Corporations Regulation Survey 2012, the government regulatory reform proposal is developed including the small corporations are under-presented in the polity, de-regulating the 'red-tape', re-regulating the monopolies and factor industries, government taking a stakeholder approach to engage small corporations in regulatory reform, government should educate the small corporations and associated professionals who offer services to them.

i. The small corporations are under-presented in the polity

Most small corporations complained that their voices were never heard by the policy decision makers, so their interests were largely ignored. They advocate that there should be Small Business ministers sitting in the Federal Cabinet who are able to speak on behalf of small corporations. The political realities have repeatedly challenged such naïve ideals of small corporations. The governments' claim to represent small corporations before the vote was not properly audited for their promises to the small corporations. Though Australian Small Business Commission Mr. Mark Brennan was appointed to address such concerns and similar arrangements are in place in each state, the possibility for small corporations to be able to make joint efforts to lobby and petition for appropriate policies is yet to be explored.

ii. De-regulation on 'red-tape'

Small corporations responded to the survey call for de-regulation to cut red-tape on superannuation management, ASIC regulatory reporting requirements, environmental requirements, quality control, occupational health and safety, documenting GST, and other regulatory compliance requirements. In addition, small corporations requested that the regulators review the maternity leave associated costs and taxation (VU Small Corporations Regulation Survey 2012).

iii. Re-regulation

Small corporations indicated that they bear extra burdens due to an unfair market structure and market practices. Specifically, they point out that the monopolistic structure has to be broken so that small business can have a 'fair go'. An example is the Supermarket industry. Supermarket giants such as Woolworth and Coles were in an oligopoly position to receive favourable offers due to 'block ordering', in this regards, small corporations are unfairly disadvantaged (Armstrong, Li and Clarke et al. 2012).

Small corporations also called for re-regulation of the factor market, in particular the utility sector. A supermarket, for instance, has to abide by the Occupational Health and Safety regulation to keep the fridge on for 24 hours per day, 7 days per week, which takes up a significant proportion of their expenses.

Moreover, re-regulation should be applied to the professional service industries. Though there are price guidance for using professional services, such as lawyers and accountants, the price ranges were so loosely set and poorly defined that it left opportunities for the professionals to over-charge the small corporations due to information asymmetry.

iv. A stakeholder approach should be adopted in regulatory reforms

The stakeholders involved in the regulatory reforms include the governments/regulators, small corporations, industry associations, professional bodies, academics and the community.

Nevertheless, the regulatory impact analysis is a very useful tool, stakeholder views should be consulted at any stage of the regulatory reform development. In this regard, the academics may play a crucial role by serving as independent sources to generate evidence-base for policy development.

Moreover, governments and regulators should reinforce the private-public partnership model in the forms of liaison, partnering, funding and delegating power to the private sector, such as industry associations, in order to improve the governance and performance of small corporations.

v. Governments and regulators should engage with small corporations and educate them on corporate governance and government regulation compliance

Small corporations responding to the VU Small Corporations Regulation Survey 2012 generally reported that the regulators and the government agencies fail to communicate effectively with small corporations, nor had they provided sufficient and useful information for corporate governance and regulatory compliance. They complained that there are too many regulations and the changes of the regulations are too frequent. In order to facilitate the compliance of regulatory compliance requirements and effective corporate governance requirements, the regulators should:

- Develop user-friendly tools, web service, smart phone and the other multi-media to communicate the regulatory requirements. They should also continuously evaluate the effectiveness of such tools and make sure that the tax-payers' money are well paid.

- Offer training to professionals who deal with regulatory or corporate governance related matters. Through the training, the accountants, lawyers and other relevant professionals can improve their efficiency and consequently reduce the cost of small corporations.

- Provide guidance on corporate governance in small corporations. Corporate governance of small corporations still merits more research, with this study one of the few investigations. The government should acknowledge the imperative and positive impact of good corporate governance in small corporations, which may reduce business bankruptcy and the unemployment associated with it.

9.4. Impact of government regulation on corporate governance of small corporations

The SEM model shows that government regulation has a negative impact on corporate governance, and the effect size is 0.36, which is medium size effect. The results discussed here provide an answer to RQ3: what is the relationship, if any, between government regulation and corporate governance of small corporations?

This makes sense in that the stricter the regulatory requirements, the less resources and attention small corporations can give to corporate governance, which justifies a 'substitution effect' argument, and rejects the 'complementary effect' hypothesis (Becher and Frye 2012). The finding is consistent with the empirical research that regulations provide a substitute for traditional monitoring mechanisms (Adams and Ferreira 2006). The presence of regulators may substitute a traditional corporate governance mechanism related to controlling and monitoring, for instance, board structure, by reducing the effect of managerial decisions on firm performance.

9.5. Developing a responsive regulatory system for small corporations in Australia

The aforementioned results identified the unmet needs of small corporations in corporate governance and government regulation. This section addressed RQ4: How to develop a responsive regulatory system for small corporations in Australia?

Having identified the relationships between corporate governance, government regulation and performance of small corporations, how can corporate governance and government regulation jointly have a positive impact on the performance of small corporations? The policy alternatives include public ordering and private ordering and the hybrid (McCarthery and Vermeulen 2008). This section first discusses the policy alternatives, then provides details about responsive regulation and proposes a responsive regulatory system for small corporations in Australia.

9.5.1. Policy alternatives: Public offering vs. private offering

Given that the Agency Theory's omnipotent focus is on developing corporate governance mechanisms to solve the distributed shareholding problem in large corporations, it failed to consider the other stakeholders. From a legal perspective, governance requirements deserve scrutiny on balancing the expectation of the small corporations and that of the regulators.

Pioneers in small corporations related research intends to approach the governance issue from the contract-based and transaction cost perspectives (John Farrar 2008; McCahery and Vermeulen 2008). Farrar (2008) suggested a context-contingent approach for small business corporate governance while he developed the corporate governance codes for the non-listed companies in Hong Kong. Further, Farrar proposed a close-form corporation with limited liabilities as the potential solutions for the corporate governance of small family firms in Hong Kong (Farrar 2008).

McCahery and Vermeulen (2008) proposed a hybrid approach of corporate governance for non-listed companies, which include public ordering, private ordering and the combination of the two. Public ordering is also called hard law, which cover the legal requirements, rules and regulations. Private Ordering is the process of setting up of social norms by parties involved in the regulated activity, and not by the State. Private Ordering aims to achieve public goals, such as efficiency, enhancing the market, and protecting rights. Given the complexity of the corporate governance issue in small corporations and the heterogeneity of small corporations at large, the hybrid approach seems to be a better option. Specifically, governments, small businesses, and the other stakeholders should make joint effects to solve governance problems in the operation of small corporations, detailed proposal will be presented in the responsive regulation section below.

9.5.2. Developing a responsive regulatory system for small corporations in Australia

Since the influential work of the Chicago school of economics in the 1960s and 70s, economists, lawyers and social scientists have been interested in government regulation and its efficacy (Stigler 1961, 1971). The international literature has been concerned with regulation that is both ‘effective’ and ‘responsive’ in order to ensure that government is attuned to differing motivations of regulated actors (Ayres and Braithwaite 1993). Much of the literature has argued for less government intervention (Mercuro and Medema 1997) and for the need to formulate efficient legal rules to foster an optimum environment in which small corporations can flourish (Coase 1960).

The best regulatory strategy depends on context, regulatory culture, and history (Ayres and Braithwaite 1993, p.5). Cultural, social, economic and political imperatives are vital (Charkham 1995; Trompenaars 1998; Roe 2003; Clarke 2007)). In Australia, for example, the Hawke federal government introduced the notion of regulatory impact statements, and such statements are now commonplace in other contexts, such as the environment: efficacious regulation should speak to the diverse objectives of regulated firms, industry associations, and individuals within them (Ayres and Braithwaite 1993).

The responsive regulatory system model builds on the McCathery and Vermeulen's three pillars of regulation on governance of non-listed small businesses (2008 p. 12) and Ayres and Braithwaite's responsive regulatory model (1992, p. 21). It advocates that the regulation of small corporations should not be 'one size fits all', but responsive to the contextual contingencies and responsive to the compliance responses from small corporations. Though the responsive regulatory pyramid was first developed to address the regulatory compliance issues by Ayres and Braithwaite, it offers an excellent opportunity to present the self-regulated corporate governance and coerced regulation in a continuum.

Proper corporate governance mechanisms may serve as a self-regulatory mechanism, which requires the least regulatory cost, sitting at the bottom of the 'regulatory pyramid' (Ayres and Braithwaite 1993). While government regulation serves as enforcement or coercion, and demands a significant amount of resource and efforts to comply with, sits at the top of the pyramid. The other private arrangements in the form of customised contracts, optional guidelines, good practices, and corporate governance system serve as self-regulatory mechanisms. The hybrid may involve interactions between the external environment and internal environment of the small corporations, including regulation of corporate governance, optional guidelines, CSR, social networks, public-private partnership. Such requirements are responsive to the size of the small corporations, the development stage on the business life cycle, the industry that small corporations operate and business connections with the government and government agencies. Responsive regulatory system has a strong focus on generating incentives for regulatory compliance (Braithwaite 2006).

Given that the responsive regulatory framework has proven to be effective by a number of applications in regulatory design in Australia and overseas, for example, the Australian Taxation

Office (see a review of the application in Wood et al. 2010), it should replace the current 'one size fits all' model. It has to be implemented by joining the efforts of multiple parties, including the governments and their agencies, small corporations, industry associations and the community.

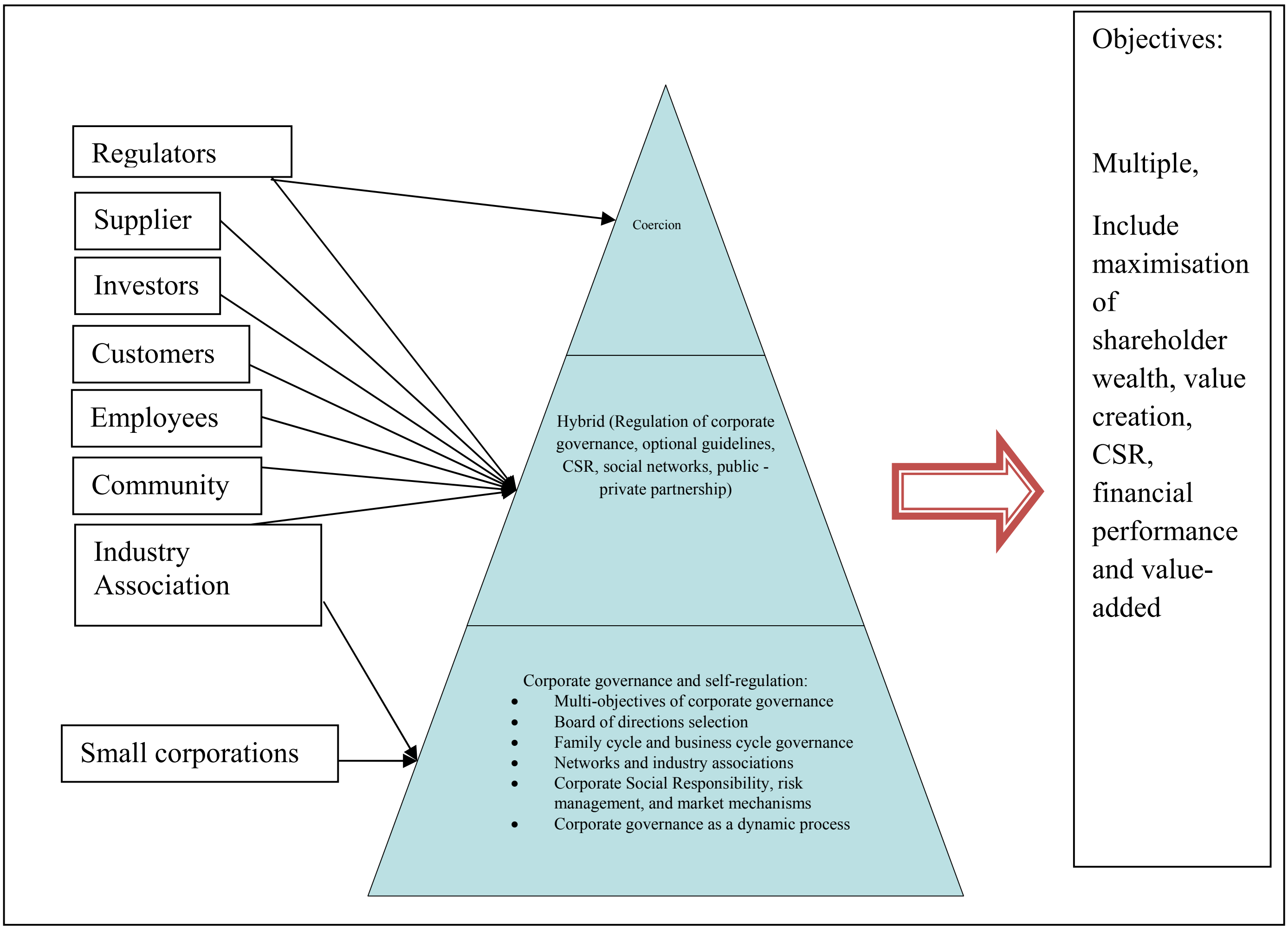


Fig 9.2 A responsive regulatory systems for small corporations in Australia

It incorporates the public ordering (through legislation and coercion), private ordering (through private arrangements) and the hybrid (through reactions to the regulation responsive of the contingencies such as firm size, development stage, and industry structure). One may see regulation as the external governance of corporate governance (Gillan 2006). Similarly, one can also view corporate governance as a special form of regulation - self-regulation (Jong et al. 2005).

9.6. Summary

This chapter discussed the results from Chapter 7 and Chapter 8 in relation to this study's research questions. The findings were compared with previous literature and relevant theories.

To answer RQ1, the research found a negative impact of corporate governance on the financial and social performance of small corporations in Australia. Though the findings may surprise some corporate governance researchers of large corporations, it complements contemporary knowledge and theories on small business governance that beside Agency Theory, Principal-Principal Theory and Stakeholder Theory should be of more relevance.

A list of corporate governance mechanisms for small corporations were developed, including the multi-purpose of corporate governance in small corporations, the role and selection of the board of directions, family cycle and business cycle governance, networks and industry associations, corporate social responsibility, risk management and market mechanisms, and corporate governance as a dynamic process.

To answer RQ2, the research found a positive impact of government regulation on the financial performance and CSR of small corporations. This result fits with Public Interest Theory and calls for further compulsory regulation of CSR to be beneficial to small corporations. A governance regulatory reform agenda to improve the performance of small corporations was proposed, including several ideas from small corporations, themselves, that they are under-presented in the polity, are looking for the de-regulation of 'red-tape', re-regulation of monopolies and factor industries. It was also argued that government should take a stakeholder approach to engage small corporations in regulatory reform; government should educate the small corporations and associated professionals who offer services to them.

To answer RQ3, the research found a substitution effect between corporate governance and government regulation for small corporations in Australia, which offers partial support that governance may serve in self-regulation, or equivalently, regulation may act as an external corporate governance mechanism.

To answer RQ4, the research develops a responsive regulatory framework for small corporations in Australia, which incorporates the public ordering (through legislation and coercion), private ordering (through private arrangements) and the hybrid (through reactions to the regulation responsive of the contingencies such as firm size, development stage, and industry structure). As a complement, one may see regulation as the external governance of corporate governance; and in similar vein, corporate governance as a special form of regulation — self-regulation.

The next Chapter is the concluding chapter which gives a summary of the results. It provides clear recommendations to Australian governments and regulators, small corporations and other stakeholders on how to improve the performance of small corporations in Australia. It also acknowledges the limitations of the study, and proposes future research directions.

CHAPTER 10 CONCLUSION

10.1 Introduction

Chapter 10 provides an overview of the thesis and summarises the main findings. It considers both the academic and practical contributions the study makes to the existing knowledge base on corporate governance, government regulation, financial performance and CSR of small corporations in Australia. This chapter also examines the theoretical, methodological and policy implications of the research, as well as potential limitations of the study. It concludes with a discussion of future research directions.

It is a major task to unravel the measurement and relationships among four latent constructs, namely corporate governance, government regulation, financial performance and CSR.

This thesis was organised by the analysis of each relationship. It first started with a review of the literature pertinent to the relationship between corporate governance and performance in Chapter 2, then a review on the literature relevant to the relationship between government regulation and performance in Chapter 3. Chapter 4 evaluated the context of corporate governance, government regulation and performance of non-listed small corporations in Australia. Chapter 5 summarised the empirical evidence on corporate governance mechanisms and performance using a meta-analysis approach, based on which the research hypothesis of relationships between corporate governance mechanisms and performance are developed quantitatively.

Due to the dearth of empirical studies between government regulation and performance of small corporations, the research hypothesis of the relationship between government regulation and performance was based on a systematic review. Drawing on the causal propositions, derived in Chapters 2 and Chapter 3 from the relevant theories and hypotheses developed from meta-analysis and systematic review, the conceptual framework was developed. Chapter 6 provided the details of the methodology. Chapter 7 reported the results of the impact of corporate governance on performance of non-listed small corporations in Australia. Chapter 8 submitted the results of the impact of government regulation on performance of non-listed small corporations in Australia. Chapter 9 discussed the results with reference to the theories and the extant empirical literature and offered recommendations for corporate governance and government regulation of non-listed small corporations in Australia.

This chapter proceeds as follows: first an overview of the thesis is provided in Section 2 summarising each chapter; Section 3 highlights the contributions of this thesis; Section 4 discusses the theoretical and policy implications of the research findings; Section 5 offers recommendations to the regulators, industry and professional associations, small corporations and academics; Section 6 acknowledges the limitations of this study and proposed future work; the last Section draws the research to a conclusion.

10.2 Thesis summary

Contents and findings from each chapter are summarised below.

10.2.1 Chapter 1

This thesis commenced with the proposition that the topic of interest is a pressing and significant one. As discussed in Chapter 1 and analysed further in Chapter 4, recent regulatory reforms suggest that corporate governance, government regulation and small corporations are becoming increasingly relevant to the achievement of economic development and social objectives in Australia and around the world. In a broader sense, this study has attempted to provide a comprehensive understanding of the corporate governance, government regulation, financial performance and CSR of small corporations.

The research in this specific field of interest was justified on practical and academic grounds. From a practical perspective, one catalyst for this research was the need for a decent understanding of corporate governance in small corporations. It is a pressing matter particularly as the corporate governance of corporations has been the foci for all corners of the market economy after the failure of Lehman Brothers, the US-subprime mortgage crisis in 2008 and the debt crisis in large corporations and business entities in Europe in 2012. Such failures, due in no small way to poor corporate governance, have had catastrophic and contagious effects on the global economy.

Further scrutiny of the issue demands a better understanding and specification of the role that multinational organisations, governments, regulators and corporations play in corporate governance reforms and, in particular, regulation of governance in the financial market. A question raised is: Is market regulation relevant to small corporations? This research offers an excellent opportunity to understand the perceptions of small corporations in Australia about the regulatory compliance requirements and their relationships to corporate governance and performance. Hence, this research responds to the call for an enriched understanding of corporate governance, government regulation and performance in small corporations in order to inform policy decision making in Australia.

10.2.2 Chapter 2

This chapter focused on reviewing the literature on corporate governance theories and performance of non-listed small corporations. The corporate governance theories, serving as the 'shoulder of the giants', informed the development of propositions about causal relationships between corporate governance mechanisms and performance in non-listed small corporations; while the empirical evidence based on a meta-analysis approach was summarised in Chapter 5.

The corporate governance theories were derived from research in large corporations. This chapter first discussed the relevance of corporate governance in small corporations, and then reviewed the good practice of corporate governance principles and guidelines pertinent to non-listed small corporations.

Section three examined theories relevant to the corporate governance of small corporations, namely the Agency Theory, the Stewardship Theory, the Stakeholder Theory, the Resource Dependence Theory, the Institutional Theory and the Network Governance Theory. The pioneers and propositions of each theory were reviewed. A critical analysis of the pros and cons of each theory was provided and summarised in Table 3. Then research gaps in research into corporate governance of small corporations were identified.

10.2.3 Chapter 3

Chapter 3 reviewed the theories of regulation and empirical studies that focuses on the relationship between regulation and small firm performance. In Section One, the definitions of regulation were revisited, followed by identifying the need for regulation and the regulators, discussion of regulation of corporate governance in Australia and relevance of regulation to small firms.

Section Two critically evaluated theories of regulation, which included three major types of theories, namely Forces of Ideas Theory, Interest Theory and Institutional Theory.

Section Three examined six types of regulatory strategies, including Coercion, Market-based approaches, Government compensation, Self-regulation, Responsive regulation and Network-based regulation.

The empirical studies investigating the impact of regulation on small firm performance were reported in Section Four. Given the broad scope of regulation and constraints of data availability on small firms, the empirical evidence on the relationship between regulation and performance is yet to be established.

The last section summarised the theories of regulation and existing empirical studies on the regulation-performance relationships. Gaps were identified and a rationale for this study was provided.

10.2.4 Chapter 4

Chapter 4 summarised the context of the study. Firstly, the status quo of small corporations in Australia and their contributions to the Australian economy was discussed, followed by an analysis of government regulation, corporate governance and difficulties facing small corporations in Australia. Key terms were introduced in section 6. Section 7 acknowledges the research support from the ARC Linkage project team. This chapter concludes with a summary of the context of small corporations in Australia

10.2.5 Chapter 5

Chapter 5 summarised evidence on corporate governance mechanisms and performance by a meta-analysis approach; based on which the research hypothesis of relationships between corporate governance mechanisms and performance were developed quantitatively. Due to the dearth of empirical studies between government regulation and performance of small corporations, the research hypothesis of relationship between government regulation and performance were based on a systematic review. Based on the causal propositions derived in Chapter 2 and Chapter 3 from the relevant theories and hypotheses developed from meta-analysis and systematic review, the conceptual framework was developed.

10.2.6 Chapter 6

Chapter 5 outlined the conceptual framework for this research and developed research questions and hypotheses to be tested in the Chapter seven. Chapter 6 discussed the research design and methodology used to undertake this study, which steers different stages of the whole research project, including research questions, the literature review, conceptual framework, data collection, data analysis and discussion of the results.

The research design represents a positivist paradigm and uses quantitative research methods. The design was adopted to explore the research questions and hypotheses posed by the study and to achieve the objectives and aims, which were set forth and outlined in the introduction and Chapter 5. Unlike the listed companies, data collection from small firms is enormously difficult and prohibitive in cost, constraining the availability of data collection methods. A survey approach to testing the statistical hypotheses was considered necessary in order to generate preliminary data on the status quo of corporate governance, regulation and performance of small corporations in Australia across a range of constructs. Given that this is the first study in Australia to apply the legal definition from the Corporations Act (2001 Cth), there is neither prior knowledge nor suitable data available specifically about the characteristics of the small corporations. Thus the sample frame is unknown and the firms fall into the definition of a small corporation has to be determined *ex post*, hence the responses from large corporations were discarded from the study. Balancing practical matters such as cost, timeline and data availability, this study adopted a convenient survey approach to collect data – an online survey using Surveymonkey. The details of the SEM were provided as the major analytical approach for the examination of the relationships of interest.

10.2.7 Chapter 7

Chapter 7 reported the results from the major survey on small corporations. Characteristics of the small corporation and characteristics of the owners and/or managers respondents of small corporations were summarised first. Then the performance and corporate governance of small corporations were analysed and a performance measurement model was developed, followed by the path analysis model evaluating the impact of each individual corporate governance mechanism on corporate governance and the measurement model of corporate governance for small corporations. Structural equation modelling assessed the impact of corporate governance as a bundle of mechanisms on the performance of small corporations. The last sector summarises the results related to corporate governance and the performance of small corporations.

10.2.8 Chapter 8

Chapter 3 reviewed theories and empirical studies on government regulation, followed by the development of the hypothesis on the relationship between regulation and performance of small corporations in Chapter 5. This chapter reports the results from analysis of the measurement model of regulation, the impact of regulation on financial performance, CSR, and corporate governance of small corporations in Australia, and the mediation effects on the relationship between responsive regulation and firm performance. The last section summarises the results for regulation related models.

10.2.9 Chapter 9

Chapter 9 discussed the research findings from Chapter 7 and 8, and the theories and empirical studies in prior research which were reviewed in Chapter 2 and Chapter 3. The Chapter is structured around the sub-research questions of the research question 'What relationship, if any, is there between corporate governance, government regulation and performance of small corporations in Australia?'. As such, Section 2 to 4 addressed Sub-question 1- 'What is the relationship, if any, between corporate governance and performance of small corporations in Australia'; Section 5 analysed Sub-question 2 – 'How to develop a corporate governance framework for the small corporations in Australia in order to improve performance'; Section 6 and 7 discussed Sub-question 3 – 'What is the relationship, if any, between government regulation and performance of small corporations in Australia'; Section 8 discussed Sub-question 4 – 'What relationship, if any, is there between corporate governance and government regulation?'; and, Section 9 discussed Sub-question 5 – 'How to develop a responsive regulatory system for small corporations in Australia?'.

Section 2 specifically discussed the performance measurement of small corporations, covering the financial performance, the CSR and the relationship between financial performance and CSR; Section 3 discussed the corporate governance in small corporations; Section 4 discussed the impact of corporate governance on the performance of small corporations; Section 5 analysed the regulatory policy alternative: private ordering – network based governance; Section 6 discussed the measurement of regulation of small corporations; Section 7 discussed the impact of regulation on the performance of small corporations; Section 8 discussed the impact of regulation on corporate governance; Section 9 developed a responsive regulatory system for small corporations in Australia; and, Section 10 ended with a brief summary.

10.3 Contribution of the thesis

To the best of the author's knowledge, it is the first endeavour of any kind in small business research to systematically investigate corporate governance, government regulation and performance of small corporations and their intra-relationships.

Small corporations are the backbone of the Australian economy. However, the "one size fits all model" adopted by most of the corporations' law frameworks and the "comply or explain" mentality incurs a significant amount of unnecessary and disproportionate compliance burdens to small businesses. Worse still, non-listed small corporations are losers in the "corporate governance reform competition", given their resource constraints.

Evidence of the relationships between governance, regulation and performance of non-listed small corporations is at a dearth. Only in recent years has academia started researching the governance issues facing small corporations in North America and Europe. Existing empirical studies mainly focus on isolated governance mechanisms, while the interaction between different governance mechanisms has been ignored.

Moreover, theories on corporate governance are mainly centred on large corporations, which has largely been due to the American and European influence. A small corporations tailored corporate governance theory and practice in Australia is yet to be developed. The project concludes that it is dangerous to directly borrow corporate governance practices and apply large corporations' governance theory to their small counterparts. Theories on government regulation have failed to address the needs of small corporations.

This project addressed the aforementioned gaps by applying systematic review, meta-analysis, Path Analysis (PA) and Structural Equation Modelling (SEM). The systematic review identified relevant theories on the governance and regulation of small corporations. Grounded in the theories, meta-analyses were applied to synthesize the current academic literature in view to developing the conceptual framework. A structured online questionnaire was employed to collect data, yielding 391 responses. Multiple indicators have been adopted to measure the five latent constructs of governance, regulation, financial performance, social performance and sustainable performance. PA estimated the direct and indirect effects of governance mechanism on performance. SEM confirmed the hypothesized relationships, controlling for the variables of firm age, size, and development stage.

10.4 Implications of the research

This study merits theoretical and practical contributions, discussed as follows.

10.4.1 Theoretical implications

This study seeks to contribute knowledge in the field of corporate governance research in four main areas:

1) Empirical research for corporate governance, government regulation and the interactions between them has not been examined in previous literature (Crook et al. 2008; Foss and Klein 2009; Hodgson 2009; Williamson 2007). In addition, most existing work has focused on analysing one of the three major constructs proposed by Williamson, while a systematic quantitative investigation and results on this subject have been lacking in the field (Crook et al. 2008).
2) A systematic empirical examination of the impact of governance on the performance of small corporations met the criticisms that such research in Australia was long overdue (Farrar 2005). Existing research on firm performance has focused almost exclusively on

accounting and finance aspects. This study analysed performance factors such as strategic development (non-cost related growth) and corporate social responsibility.

3) Internationally, the state of research into the regulation of small corporations is not appropriately advanced. Nowhere to date has there been research that has as its central aim a review of regulation relevant to the ‘whole sector’ and which has focused on the ‘small corporation’ definition (Clarke A. 2007). This research project therefore assumes international significance.

4) The originality (and innovation) of this study lies in its treatment of corporate governance as a “bundle” and has applied latent variable modelling techniques to demystify the relationships amongst latent variables.

10.4.2 Policy implications

This study is significant for policy decision-making in four aspects:

1) Small corporations play an important role in employing labour and boosting economic growth. A well-designed regulatory framework will enhance the impact of small corporations on the Australia economy;

2) The in-depth evidence of small corporation performance and industry regulation can assist key policy decision makers to allocate scarce public resources to the most needed regulatory requirements of the sector. This study acknowledged that there are relevant references on small business including: PC (2004, 2005, 2006, 2007a-b, 2008a-e, 2009a-b), ACCI (2005), AG (1997, 2006, 2007,2008, 2009a-b), ATO (2008), Blair (1998), Board of Taxation (2008), Bowen (2008), BRCWG (2009), BCA (2005), COAG (2006, 2007a-b, 2008a-b, 2009a-b), CRC (2008, 2009a-b), IPART (2006), Lattimore et al.

(1998), Mason (2007), NSW Government (2007), OECD (1997, 2005, 2007), OBPR (2007, 2008), Regulation Taskforce (2006), SBR (2009), Swan and Tanner (2008), VCEC (2007), Victorian Government (2008), and World Bank (2009). However, to the best of the author's knowledge, this study is the first of this kind to devote all of its research effort into focussing on governance, regulation and performance of small corporations;.

3) The regulatory framework to be developed from this project may shed light on the regulatory reform of small corporations in the future;

4) Equally, the results on corporate governance practices in non-listed small corporations will shed light on the development of guidelines for small business research in the future.

10.5 Recommendations

10.5.1 Recommendations on corporate governance of non-listed small corporations

Evidence derived from the empirical models was used to develop policy recommendations, which are summarised below.

Given the distinctive features of both small corporations and the institutional context of operating a business in Australia, corporate governance mechanisms tailored to the needs of the small corporations in Australia are proposed below. Such mechanisms include the role and selection of board of directions, family cycle and business cycle governance, networks and industry associations, corporate social responsibility, risk management and market mechanisms, and corporate governance as a dynamic process.

i. Corporate governance in small corporations serve multiple purposes

Corporate governance in small corporations serve multiple purposes given the multi-facet requirements they have. Such purposes include, but are not limited to, minority shareholder protection, value creation and value added, improvement in financial performance and CSR (Ingleey and Karoui 2013; OECD 2012). Small corporations may have to develop a holistic view that incorporates financial performance, social performance, innovation and growth in the performance measurement system.

ii. Board of directors' role and structure

Boards of directors in small corporations serve as controlling and service roles. They fill in the gaps in resources and expertise and they expand business opportunities by making use of personal and professional networks. Ideally, the board of directors should possess a specialisation in areas which are critical to the core business of the small corporations and have relevant industry expertise (Ingley and Karoui 2013).

Given the nature of block-holding and family ownership, small corporations may focus more on the diversity of the expertise and required industry experience of directions, while give lesser weight to the independence of the board (Adams and Ferrreira 2006).

iii. Family cycle governance and business cycle governance

The majority of small corporations are family owned (Armstrong et al. 2012). The corporate governance issue, hence, is complicated with the consideration of family cycles and business cycles. Toms (2012) has discussed the life cycle of corporate governance. Business type specific discussions include Bertoni et al. (2012) in High-tech firms, Uhlaner (2012) on family business, Filatotchev and Allcock (2012) on IPOs, Wu and Tihanyi (2012) on multinational firms and international firms, Yiu et al. (2012) on business groups, and Ayotte et al. (2012) on financial distress and bankruptcy. Given the complexity of both family cycles and business cycles, which could be benchmarked across a whole industry or sector, the small corporations may have resort to specialists for help in this regard.

Family governance concerns a number of issues, including succession planning, sustainability and social responsibility, and major events such as marriage and divorce of key family members.

iv. Network and industry associations

Recent developments in Network Theory have pinpointed the importance of networks in business development (Street and Cameron 2007; Perry 2012). Network and industry associations serve as a nexus for information exchange and sharing good practice amongst small corporations.

v. Corporate social responsibility, risk management and market mechanisms

External corporate governance mechanisms have to be considered as an integrated part of the corporate governance framework which includes corporate social responsibility, risk management and market mechanisms. Corporate social responsibility refers to the involvement and taking into account the key stakeholders in major business decision-making. Such stakeholders include employees, customers, suppliers, investors, environment, and philanthropy. Risk management may involve sound risk control systems, such as internal auditing, reporting and external auditing. Market mechanisms may include competition in the labour market for qualified employees, directors and executives, the product market, and the financial market.

vi. The corporate governance as a dynamic process

Contingency Theory argues that strategic management, in the form of corporate governance, is a dynamic process and should be contingent on the contextual factors such as industry environment and development stage. The majority of the businesses in the sample are at the established stage, where their governance needs would be more on the consolidation of the market position and product development; while those at the start up stage, may have to control and minimise risk. Thus, the owner and managers of small corporations should keep in mind that the corporate governance is a continuous process and demands updates given the change in development stages.

10.5.2 Recommendations on government regulation

Based on the research findings and as per the answers to open-ended questions in the VU Small Corporations Regulation Survey 2012, government regulatory reform proposals should note that small corporations are under-presented in the polity, de-regulating 'red-tape' and re-regulating monopolies and factor industries are important issues for small corporations. With government taking a stakeholder approach to engage small corporations in regulatory reform, it should also educate small corporations and associated professionals who offer services to them.

i. The small corporations are under-presented in the polity

Most small corporations complained that their voices are never heard by policy decision makers, so their interests have been ignored. They advocate that there should be one small business minister sitting in the cabinet who speaks on behalf of the small corporations. The political realities have repeatedly challenged the ideals of the small corporations. Government claims before an election to represent small corporations are not always met. De-regulation on 'red-tape'

Small corporations responding to the survey call for de-regulation to cut red-tape on superannuation management, ASIC regulatory reporting requirements, environmental requirements, quality control, occupational health and safety, documenting GST, and other regulatory compliance requirements. In addition, small corporations request that regulators review the maternity leave associated costs and taxation (VU Small Corporations Regulation Survey 2012).

ii. Re-regulation

Small corporations indicated that they bear extra burdens due to unfair market structures and market practices. Specifically, they point out that monopolistic structures have to be broken so that small business can have a ‘fair go’. An example is the Supermarket industry. Supermarket giants such as Woolworth and Coles occupy an oligopoly position, receiving favourable prices due to ‘block ordering’; in this regards, many small corporations are unfairly disadvantaged (Armstrong et al. 2012).

In addition, small corporations requested re-regulation of the factor market, in particular in the utility sector. For example, a supermarket has to abide by the Occupational Health and Safety regulation to keep the fridge on for 24 hours per day, 7 days per week, which takes up a significant proportion of their expense.

Moreover, re-regulation should be applied to the professional service industries. Though there is price guidance for using professional services, such as lawyers and accountants, the price ranges were so loosely set and poorly defined that it left opportunities for the professionals to over-charge the small corporations due to information asymmetry.

iii. A stakeholder approach should be adopted in regulatory reforms

Stakeholders involved in regulatory reforms include the governments/regulators, small corporations, industry associations, professional bodies, academics and the community. Nevertheless, regulatory impact analysis is a very useful tool; stakeholder views should be consulted at any stage of the regulatory reform development. In this regard, academics may play a crucial role by serving as an independent source to generate an evidence database for policy development.

Governments and regulators, moreover, should reinforce the private-public partnership model in the forms of liaison, partnering, funding and delegating power to the private sector, such as industry associations, in order to improve the governance and performance of small corporations.

iv. Governments and regulators should engage with small corporations and educate them on corporate governance and government regulation compliance

The small corporations responding to the VU Small Corporations Regulation Survey 2012 generally reported that the regulators and government agencies do not fail to communicate effectively with small corporations, nor had they provided sufficient and useful information for corporate governance and regulatory compliance. They complained that there is too much regulation and the changes of the regulations are too frequent. In order to facilitate the compliance of regulatory compliance requirements and effective corporate governance requirements, the regulators should:

- Develop user-friendly tools, web service, smart phone and the other multi-media to communicate the regulatory requirements. They should also continuously evaluate the effectiveness of such tools and make sure that the tax-payers' money are well spent.

- Offer training to professionals who deal with regulatory or corporate governance related matters. Through training, accountants, lawyers and other relevant professionals can improve their efficiency and consequently reduce the cost of small corporations.

A further area is guidance on corporate governance in small corporations. Corporate governance of small corporations still merits more research, with this study one of the few pioneering investigations. The Government should acknowledge the imperative for and positive impact of good corporate governance in small corporations, this may reduce business bankruptcy and the unemployment associated with it.

10.6 Limitations and future work

This study is subjected to four main limitations:

First, this study adopted a convenient online survey approach. This method may result in self-selection bias. Though the modeling process managed to compensate for the non-normality, missing variable bias and self-selection problem by introducing innovative statistical procedures, failing to adopt a random sampling approach may run the risk of violation of internal validity. Admittedly, a self-selection bias is always a challenge for any non-experimental types of research. A discussion of the specific consequences of self-selection bias can be found in Bethlehem and Biffignandi (2011).

This study, however, made the effort to correct the self-selection bias by applying sampling weights matching the number of small and medium sized businesses in respective local government areas based on postal codes and addresses provided by respondents.

Second, this study is not able to capture the longitudinal trends of the performance of small corporations in Australia, due to the unavailability of data. Ignoring the time factor in models that may inflate the impact of time-invariant variables on performance, subjecting to omitted variable bias. Consequently, the impact of the underlying and institutional factors may not be as significant as they actually are. In addition, failing to add the long-term impacts in the calculation of performance may make the results myopic.

Third, a heuristic approach has been taken in choosing the measurement indicators, which may result in a lack of objectivity. Though there was some subjectivity in selecting the measurement indicators, good practice has to be developed to recommend a selected list of variables which can be used as measures for particular types of research in similar settings.

Alternatively explorative factor analysis models may be used to search for an optimal governance structure for small corporations in Australia. This study managed to replicate the measures and indicators for small corporations identified from the prior literature on listed companies and found a negative impact of corporate governance on performance of small corporations. An alternative explanation, which may serve as a critical to this study, is that the measurement model for small corporations drawing from the literature of large listed companies does not work in this Australian cohort.

Fourth, the performance determination in this study was merely focused on the outcome, whilst measures of the process in which the determinants of performance have been transformed into outcomes were ignored. Failing to take into account the business operational level activities may only enable researchers to partially understand business performance.

Future work could focus on complementing this study in three areas:

First, a more rigorous sampling approach, coupled with a finer level of quasi-experiment design, may be used to collect more reliable information to represent the population.

Second, a longitudinal database could be developed in order to prepare for evidence-based policy analysis. The database should try to capture as many dimensions of the factors which affects the performance of small corporations, taking into consideration heterogeneous factors caused by differences due to industry, location and business characteristics. The data to be collected should also be adjusted for the advancement of technology and innovation and add in new information if necessary. A properly collected longitudinal database, with an ideal duration of 10 years (which is approximately the long term business cycle of the Australian economy, Australia Research Bank (2013)), would be able to provide further evidence on changes in productivity, efficiency and innovation, and add growth to the list of policy objectives.

Third, a thorough meta-analysis should be undertaken to systematically consolidate data and evidence that accumulates in future research. It could also be a good practice to prepare a toolkit suitable for evidence-based policy research in similar contexts in the future.

Fourth, practical resource constraints may hamper the performance of small corporations, such as market exiting pressure, lack of financing, skill shortage. Li and colleagues (2010, 2011a-b, 2012a-b) had investigated these issues in recent studies based on small samples. In the future, larger samples should be designed to solve these pressing policy issues.

Last but not least, in order to get a complete picture, it might be necessary to retrieve data documenting daily operations in small corporations, which can be synthesized with outcome and impact measures. A comprehensive research plan as such is exhibited in this study, could serve as a starting point, and be easily extended to meet such ends.

10.7 Conclusions

This research finds a negative impact of corporate governance on the financial and social performance of small corporations in Australia. Though the findings may surprise researchers interested in the corporate governance of large corporations, it complements and increases the relevance of existing theories on small business governance such as the Principal-Principal Theory and the Stakeholder Theory (but not Agency Theory).

Hence, a list of corporate governance mechanisms for small corporations were developed, including multi-purposes of corporate governance in small corporations, the role and selection of board of directions, family cycle and business cycle governance, networks and industry associations, corporate social responsibility, risk management and market mechanisms, and corporate governance as a dynamic process.

This research finds a positive impact of government regulation on the financial performance and CSR of small corporations. This confirms with the Public Interest Theory and calls for the compulsory regulation of CSR that would be beneficial for small corporations. A governance regulatory reform agenda to improve the performance of small corporations has been proposed, including greater representation of small corporations in the polity, de-regulating 'red-tape', re-regulating the monopolies and factor industries, government taking a stakeholder approach to engage small corporations in regulatory reform, education and training for small corporations and associated professionals who offer services to them.

This research, furthermore, finds a substitution effect between corporate governance and government regulation for small corporations in Australia, which offers partial support that governance may serve as a self-regulator, or equivalently, regulation may act as an external corporate governance mechanism.

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Appendix 1 Small business contribution to the Australian economy

	Small business contribution	Percentage of small businesses among all businesses
Total number	1,953,673	95.20%
Number of small businesses employing	750,042	88.39%*
Employment	4,764,000	47.65%
Entries	293,681	99.20%
Exits	311,227	98.74%
Wages and Salaries ($m)	116,386	29.57%
Sales and service income ($m)	772,057	31.85%
Operating profit before tax ($m)	109,264	40.17%
Value-added ($m)	290,348	34.46%

Appendix 2 Ethics approval

1. Ethics approval for Stage One of the ARC Linkage Project: Explorative study – interviews of CEOs/Managers of Small Corporations and Executives of Industry Associations.

MEMO

TO	Prof Anona Armstrong Centre for International Corporate Governance Research City Flinders Campus	DATE	19/03/2010
FROM	Prof Michael Muetzelfeldt Chair Faculty of Business & Law Human Research Ethics Committee		
SUBJECT	Ethics Application – HRETH 09/252		

Dear Prof Armstrong,

Thank you for resubmitting your application for ethical approval of the project entitled:

HRETH 09/252 Developing a responsive regulatory system for Australia's small business corporations.

The Chair of the Business & Law Human Research Ethics Committee resolved to **approve** the application, subject to submission of Year One, Year Two and CEO survey forms for approval as they are developed. All supporting documentation submitted to date has been accepted and deemed to meet the requirements of the National Health and Medical Research Council (NHMRC) 'National Statement on Ethical Conduct in Human Research (2007)'. Approval is granted from 19 March 2010 to 31 December 2012.

Continued approval of this research project by the Victoria University Human Research Ethics Committee (VUHREC) is conditional upon the provision of a report within 12 months of the above approval date (by **19 March 2011**) or upon the completion of the project (if earlier). A report proforma may be downloaded from the VUHREC web site at: http://research.vu.edu.au/hrec.php

Please note that the Human Research Ethics Committee must be informed of the following: any changes to the approved research protocol, project timelines, any serious events or adverse and/or unforeseen events that may affect continued ethical acceptability of the project. In these unlikely events, researchers must immediately cease all data collection until the Committee has approved the changes. Researchers are also reminded of the need to notify the approving HREC of changes to personnel in research projects via a request for a minor amendment.

If you have any queries, please do not hesitate to contact me at Michael.Muetzelfeldt@vu.edu.au.

On behalf of the Committee, I wish you all the best for the conduct of the project.

Prof. Michael Muetzelfeldt
Chair
Faculty of Business & Law Human Research Ethics Committee

2. Ethics approval for Stage Two of the ARC Linkage Project: Structured Online Survey

MEMO

TO	Prof Anona Armstrong Victorian Law School City Queen Campus	DATE	20/09/2010
FROM	Dr Nick Billington Chair Faculty of Business and Law Human Research Ethics Committee		
SUBJECT	Ethics Application – HRETH 09/252		

Dear Prof Armstrong,

Thank you for resubmitting your application for ethical approval of the project entitled:

HRETH 09/252 Developing a responsive regulatory system for Australia's small business corporations.

The Chair of the Business & Law Human Research Ethics Committee resolved to approve the application, including the use of the Small Business Survey. All supporting documentation submitted to date has been accepted and deemed to meet the requirements of the National Health and Medical Research Council (NHMRC) 'National Statement on Ethical Conduct in Human Research (2007)'. Approval is granted from 20 September 2010 to 31 December 2012.

Continued approval of this research project by the Victoria University Human Research Ethics Committee (VUHREC) is conditional upon the provision of a report within 12 months of the above approval date (by 20 September 2011) or upon the completion of the project (if earlier). A report proforma may be downloaded from the VUHREC web site at: http://research.vu.edu.au/hrec.php

Please note that the Human Research Ethics Committee must be informed of the following: any changes to the approved research protocol, project timelines, any serious events or adverse and/or unforeseen events that may affect continued ethical acceptability of the project. In these unlikely events, researchers must immediately cease all data collection until the Committee has approved the changes. Researchers are also reminded of the need to notify the approving HREC of changes to personnel in research projects via a request for a minor amendment.

On behalf of the Committee, I wish you all the best for the conduct of the project. If you have any queries, please do not hesitate to contact me at Nick.Billington@vu.edu.au

Kind Regards,

Dr Nick Billington
Chair
Faculty of Business and Law Human Research Ethics Committee

3. Ethics approval for Stage Three of the ARC Linkage projects – Interview with the regulators

VICTORIA UNIVERSITY | A NEW SCHOOL OF THOUGHT

MEMO

TO	Prof Anona Armstrong Victorian Law School City Queen Campus	DATE	2/8/2011
FROM	Dr Nick Billington Chair Faculty of Business and Law Human Research Ethics Committee		
SUBJECT	Ethics Application – HRETH 09/252		

Dear Prof Armstrong,

Thank you for submitting interview schedule for ethical approval of the project entitled:

HRETH 09/252 Developing a responsive regulatory system for Australia's small business corporations.

The Chair of the Business & Law Human Research Ethics Committee resolved to **approve** the application, including the use of the Small Business Survey. All supporting documentation submitted to date has been accepted and deemed to meet the requirements of the National Health and Medical Research Council (NHMRC) 'National Statement on Ethical Conduct in Human Research (2007)'. Approval is granted from 18th July 2011 to 31 December 2012.

Continued approval of this research project by the Victoria University Human Research Ethics Committee (VUHREC) is conditional upon the provision of a report within 12 months of the above approval date (by **20 September 2011**) or upon the completion of the project (if earlier). A report proforma may be downloaded from the VUHREC web site at: http://research.vu.edu.au/hrec.php

Please note that the Human Research Ethics Committee must be informed of the following: any changes to the approved research protocol, project timelines, any serious events or adverse and/or unforeseen events that may affect continued ethical acceptability of the project. In these unlikely events, researchers must immediately cease all data collection until the Committee has approved the changes. Researchers are also reminded of the need to notify the approving HREC of changes to personnel in research projects via a request for a minor amendment.

On behalf of the Committee, I wish you all the best for the conduct of the project. If you have any queries, please do not hesitate to contact me at Nick.Billington@vu.edu.au

Kind Regards,

Dr Nick Billington
Chair
Faculty of Business and Law Human Research Ethics Committee

Appendix 3 Online Small Business Survey Questionnaire

INTRODUCTION

Please note that this questionnaire is Private and Confidential.

The purpose of this survey is to better understand the business practice and impacts of regulation as well as how they affect firm-level productivity. Please direct this email to the owner or principal decision makers of your firm.

Please note that the information obtained here will be treated strictly confidentially.

Please follow the instructions while answering the questions, if

a). a dropdown list is provided, please select your choice by clicking on your choice;

b). a text box is provided, please fill in the box with your comments;

c). a ratio or number is required, please provide a number.

We appreciate your time and efforts in contribution to this project.

The survey should take about 20 minutes. Now please turn to the next page.

SECTION A: GENERAL INFORMATION

1. When did your firm begin operations? ____________________________

2. What is the current legal status of your firm?

○ Public company ○ Private Company

○ Sole proprietor ○ Partnership

○ Others

3. Which industry does your business belong to?

○ 1 Agriculture, Forestry and Fishing ○ 2 Mining

○ 3 Manufacturing ○ 4 Electricity, Gas, Water and Waste Services

○ 5 Construction ○ 6 Wholesale Trade 7 Retail Trade

○ 8 Accommodations and Food Service ○ 9 Transports, Postal and Warehousing

○ 10 Information Media and Telecommunications ○ 11 Financial and Insurance Services

○ 12 Rental, Hiring and Real Estate Services ○ 13 Professional, Scientific and Technical Services

○ 14 Administrative and Support Services ○ 15 Public Administration and Safety

○ 16 Education and Training ○ 17 Health Care and Social Assistance

○ 18 Arts and Recreation Services ○ 19 Other Services

4. Where is your head office located?

○ 1 VIC ○ 2 NSW ○ 3 SA

○ 4 QLD ○ 5 NT ○ 6 ACT

○ 7 WA ○ 8 TAS ○ 9 NATIONAL

○ 10 OVERSEA

5. Is your company a listed company? (i.e. trades shares on the stock exchange)

○ 1 Yes ○ 2 No

6. The business life cycle consists 7 stages, as described in the choice below. What is the development stage of your business on the business life cycle?

○ Seed Stage (your business is just a thought or an idea.)

○ Start-Up Stage (your business is born and now exists legally.)

○ Growth Stage (your business has made it through the toddler years and is now a child.)

○ Established Stage (your business has now matured with a place in the market and loyal customers.)

○ Expansion Stage (a new period of growth into new markets and distribution channels.)

○ Decline Stage (changes in the economy, society, or market conditions can decrease sales and profits.)

○ Exit Stage (this is the big opportunity for your business to cash out on all the effort.)

7. How many sites does the business have in Australia?

○ 0 ○ 1 ○ 2

○ 3 ○ 4 ○ more than 5

8. Is your organisation a member of any industry or professional associations?

○ Yes ○ No

9. Please provide the names of industry associations you are a member of

---

10. What is your position within the firm?

○ Owner and Manager ○ Owner only

○ Manager only ○ Others

11. When did you first commence in that position?

- Less than 1 year
- 1-3 years
- 3-5 years
- 5-10 years
- more than 10 years

12. What is the highest level of education you have completed?

- 1 Post-grad degree (incl Doctors, Masters)
- 2 Grad diploma, grad certificate
- 3 Bachelor degree
- 4 Advanced diploma, Diploma
- 5 Certificate
- 6 Secondary
- 7 Primary
- 8 Others

13. What is your age category?

- Under 40
- 40-50
- 50-60
- 60-67
- above 67

14. What is your gender?

- Male
- Female

SECTION B: REGULATION-RELATED ISSUES

1. Does the business have its own constitution or does it use the model (Replaceable Rules) specified in the Corporations Act (the default arrangement)?

- 1. The business has its own constitution
- 2. The business uses the model in corporate Replaceable Rules
- 3. Not applicable

Other (please specify)

2. Are there any difficulties that you are aware of with the Replaceable Rules?

- Yes
- No

Other comments

3. Does your company have an overdraft?

- Yes
- No

4. Is your company a franchise?

○ Yes ○ No

5. Are the following sources of advice about regulation used by your business?

	Yes	No
Industry association	○	○
Lawyers	○	○
Accountants	○	○
Government agencies	○	○
Others	○	○

6. What is the proportion of your expenditure on each source of advice about regulation?

	Less than 5%	5%-9%	10%-14%	15%-19%	20%-24%	more than 25%
Industry association	○	○	○	○	○	○
Lawyers	○	○	○	○	○	○
Accountants	○	○	○	○	○	○
Government agencies	○	○	○	○	○	○
Others	○	○	○	○	○	○

7. How many days (equivalent) would you estimate your staff spent in the last financial year on meeting compliance? (e.g. filling forms, reading and understanding regulation)

○ 1. Less than 5 ○ 2. 6-10 ○ 3. 11-19

○ 4. 20-29 ○ 5. 30 + ○ 6. Unknown

8. How much would your firm have spent last year on meeting compliance? (Tax, Superannuation, environment, health and safety, taxation, and other documentation & reporting burdens)

○ 1. Less than $1,000 ○ 2. $1,001- $5,000 ○ 3. $5,001 - $10,000

○ 4. $10,001 - $ 20,000 ○ 5. $20,001 + ○ 6. Unknown

9. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1 = not Difficult at all	2	3	4	5 = most difficult	Not applicable
ASIC regulation	○	○	○	○	○	○
	○	○	○	○	○	○
	○	○	○	○	○	○
	○	○	○	○	○	○

Record keeping for tax purposes

Directors' duties

Information Disclosure

10. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1 = not Difficult at all	2	3	4	5 = most difficult	Not applicable
Occupational Health and Safety	O	O	O	O	O	O
Superannuation	O	O	O	O	O	O
Workplace relationships	O	O	O	O	O	O
Maternity leave	O	O	O	O	O	O
Quality assurance	O	O	O	O	O	O
Environmental protection	O	O	O	O	O	O

11. In summary, what would you nominate as being the three most problematic regulation issues small businesses are facing in Australia today? Please briefly describe each of the issues in ONE sentence per issue.

12. What remedies would you recommend to relieve small businesses from regulations?

SECTION C: BUSINESS OPERATION

1. During the financial year 2008/09, please indicate the following in dollar values

	0	<100,000	$100,001 to $300,000	$300,001 to $500,000	$500,001 to $700,000	$700,001 to $900,000	$900,001 to $1 m	$1m to $3m	$3m to $5m	$5m to $10m	$10m to $12.5m	$12.5m to $15m	$15m to $20m	$20m to $25m	$25m or more	N/A
total assets	○	○	○	○	○	○	○	○	○	○	○	○	○	○	○	○
total sales	○	○	○	○	○	○	○	○	○	○	○	○	○	○	○	○
net profit	○	○	○	○	○	○	○	○	○	○	○	○	○	○	○	○

2. In the 2008/09 financial year, what was the growth rate of the following

	0	less than 5%	5% - 9%	10% - 14%	15%- 19%	20% - 24%	25% - 30%	30% +	Not applicable
sales	○	○	○	○	○	○	○	○	○
net profit	○	○	○	○	○	○	○	○	○

3. Is each of the following customer types your customers?

	Yes	No
1. government or government agencies	○	○
2. large domestic firms (more than 50 employees)	○	○
3. small and medium size businesses	○	○
4. multinationals located in Australia	○	○
5. parent company or affiliated subsidiaries	○	○
6. not for profit organisations	○	○
7. overseas companies	○	○
8. Others	○	○

4. What is the percentage of your goods and services is purchased by each of the following customers in the recent 3 financial years?

	0	less than 5%	5% - 9%	10% - 14%	15% - 19%	20% - 24%	25%- 30%	30% +	Not applicable
1. government or government agencies	○	○	○	○	○	○	○	○	○
2. large domestic firms (more than 50 employees)	○	○	○	○	○	○	○	○	○
3. small and medium size businesses	○	○	○	○	○	○	○	○	○
4. multinationals located in Australia	○	○	○	○	○	○	○	○	○
5. parent company or affiliated subsidiaries	○	○	○	○	○	○	○	○	○
6. not for profit organisations	○	○	○	○	○	○	○	○	○
7. overseas companies	○	○	○	○	○	○	○	○	○
8. Others	○	○	○	○	○	○	○	○	○

5. How long does it take for each of the following customers to pay you for your goods and services?

	less than 1 week	1 week to 2 weeks	2 weeks to 4 weeks	4 weeks to 8 weeks	more than 8 weeks
1. government or government agencies	○	○	○	○	○
2. large domestic firms (more than 50 employees)	○	○	○	○	○
3. small and medium size businesses	○	○	○	○	○
4. multinationals located in Australia	○	○	○	○	○
5. parent company or affiliated subsidiaries	○	○	○	○	○
6. not for profit organisations	○	○	○	○	○
7. overseas companies	○	○	○	○	○
8. Others	○	○	○	○	○

6. What is the number of your full-time (equivalent) employees

○ less than ○ 1-5 ○ 6-20

○ 21-50 ○ above 50

7. Is each of the following issues an extra burden to your business?

Yes NO

1. Access to financing (e.g., collateral required or financing not available from banks)

2. Cost of financing (e.g., interest rates and charges)

3. Contract violations by customers and suppliers

4. Cost of electricity

5. Cost of transportation

6. Access to land

7. Title or leasing of land

8. Rates of taxation

9. Tax administration

10. Customs and trade regulations

11. Business licensing and permits

12. Labour regulations

13. Skills and education of available workers

14. Uncertainty about regulatory policies

15. Compliance with new laws

16. Anti-competitive practices of competitors

17. Trade Pratice Act

Other cost to your business (please specify)

8. What is the percentage of cost each of the following issues incurred out of the total cost

	Less Than 5%	5%- 9%	10%- 14%	15%- 20%	25% and above
1. Access to financing (e.g., collateral required or financing not available from banks)					
2. Cost of financing (e.g., interest rates and charges)					
3. Contract violations by customers and suppliers					

4. Cost of electricity

5. Cost of transportation

6. Access to land

7. Title or leasing of land

8. Rates of taxation

9. Tax administration

10. Customs and trade regulations

11. Business licensing and permits

12. Labour regulations

13. Skills and education of available workers

14. Uncertainty about regulatory policies

15. Compliance with new laws

16. Anti-competitive practices of competitors

17. Trade Pratice Act

9. Does your firm consider the importance of the following stakeholders in business decision making process?

	Yes	No
1. customers		
2. suppliers		
3. employees		
4. financial investors		
5. philanthropy (incl. volunteering)		
6. enviornment		
7. adoption of Information and Communication Techniques		

10. How important is the weight of the following stakeholders in your business decision making?

Very Neutral Not so Not important Not

	Important		important	at all	applicable
1. customers	O	O	O	O	O
2. suppliers	O	O	O	O	O
3. employees	O	O	O	O	O
4. financial investors	O	O	O	O	O
5. philanthropy (incl. volunteering)	O	O	O	O	O
6. enviornment	O	O	O	O	O
7. adoption of Information and Communication Techniques	O	O	O	O	O

11. What is the percentage of total expenses that are allocated to product innovation and service upgrading in the past three financial years?

O 0   O less than 5%   O 5% - 9

O 10% - 14%   O 15%- 19%   O 20% - 24%

O 25% - 30%   O 30% +   O N/A

12. Does your organisation have a written strategic plan?

O Yes   O No

13. Do you offer any formal training to your permanent employees?

O Yes   O No

14. Thinking of your main product line or main line of services and comparing your production process with that of your closest competitor, which of the following best summarizes your position:

O My firm's technology is less advanced than that of its main competitor

O My firm's technology is about the same as that of its main competitor

O My firm's technology is more advanced than that of its main competitor

15. Over the last two years, what was the major means for your business to acquire technological innovations?

O Embodied in new machinery or equipment

O By hiring key personnel

O Licensing or turnkey operations from international sources international sources

O Licensing or turnkey option

○ Developed or adapted within the establishment locally the establishment locally

○ Transferred from parent the company

○ Developed in cooperation with client firms

○ Developed with equipment or machinery supplier

○ From a business or industry association

○ Trade Fairs and/or Study Tours

○ Consultants

○ From universities, public Institution

SECTION D: ABOUT THE BOARD

1. Does your business have a board of directors?

○ Yes

○ No(go to section E)

2. Please provide the number of directors on the board in your company

	0	1	2	3	4	5	6	7	8	9	more than 9
Total number of directors	○	○	○	○	○	○	○	○	○	○	○
executive directors	○	○	○	○	○	○	○	○	○	○	○
independent directors	○	○	○	○	○	○	○	○	○	○	○
female directors	○	○	○	○	○	○	○	○	○	○	○

3. Please select the sources of the directors of your firm

○ Founder/family member as executives

○ Consulters

○ Shareholders with significant amount of shares

○ Retired executives

○ Shareholders without significant amount of shares

○ No relationship with the firm at all

○ Suppliers

4. What is the average age of directors in your firm?

○ less than 50 ○ 50-60 ○ 60-67 ○ more than 67

5. How many shareholders does the company have?

○ 1-5 ○ 6-10 ○ 11-20

○ 21-30 ○ 31-40 ○ 41-50

○ more than 50

6. How many times does your board meet per year on average?

○ Never ○ once ○ twice

○ three times ○ four times ○ more than four times

7. To what extent are directors of your firm use their personal network to facilitate the development of your firm?

○ Very frequently ○ Often ○ Sometimes

○ Rarely ○ Never ○ Not applicable

8. What percentage of shares is owned by the largest shareholder?

○ less than 5% ○ 6%-10% ○ 11%-20%

○ 21%-30% ○ 31%-40% ○ 41%-50%

○ more than 50% ○ not applicable

9. Does your firm disclose information to the following?

○ government/regulators ○ shareholders ○ industry associations

○ bank and financial sources ○ public ○ none of the above

10. What information does your firm disclose?

○ 1. the financial and operating results of the corporation

○ 2. major share ownership and voting rights

○ 3. potential risk factors

11. Does your firm have a succession plan?

○ Yes ○ No ○ Not applicable

12. Is your company independently audited?

○ Yes ○ No ○ N/A

SECTION E: INSTITUTIONAL FACTORS

1. What are the following ratios?

the proportion of materials ordered from the 5 major suppliers

the proportion of products/services sold to the 5 major consumers

2. To what degree do you agree with the following statements (1 = strongly disagree, 5 = strongly agree)

	1 = strongly disagree	2	3	4	5 = strongly agree
1. my company is keen to have employees involved in decision making process	O	O	O	O	O
2. my company requires employees to know all the details of our products	O	O	O	O	O
3. we are able to forecast the sales accurately	O	O	O	O	O
4. my employees are all very experienced in meeting clients' needs	O	O	O	O	O
5. our customers are very loyal business partners	O	O	O	O	O
6. the percentage of market our product penetrated will be very stable in the future	O	O	O	O	O
7. it is feasible for us to monitor the market trends in the future	O	O	O	O	O
8. the volume of products demanded in our industry is stable in the future	O	O	O	O	O
9. we are able to predict the impact of technology changes on supplier market	O	O	O	O	O

3. Please evaluate the following issues based on your experience and perceptions

	Yes	No	N/A
1. is it adequate to evaluate the suppliers' strategies based on component prices	O	O	O
2. are the suppliers following the approved production and quality control procedures	O	O	O
3. are the major 5 suppliers expecting a long-lasting relationship	O	O	O
4. are the major 5 clients expecting a long-lasting relationship	O	O	O
5. whether the major 5 suppliers are shifting to other competitors in the short term	O	O	O

4. How often do your trade with the following stakeholders in total (times/year)

	Once	twice	3 times	4 times	5times	more than 5 times
5 major suppliers	O	O	O	O	O	O
5 major consumers	O	O	O	O	O	O

Acknowledgement

1. Would you like a copy of the final report?

O Yes - (Please go to Question 3.) O No

2. Would you like to be contacted with regards to following up researches?

○ Yes ○ No

3. Please provide your contact information below

Name: ______________________________

Company: ______________________________

Address 1: ______________________________

Address 2: ______________________________

City/Town: ______________________________

State/ Province: ______________________________

Zip/Postcode: ______________________________

Country: ______________________________

Email address: ______________________________

Phone number: ______________________________

Thank you very much for your time.