



Corporate Governance Factors Affecting Donation: Evidence from Charitable Organizations in Malaysia

Suhaily Hasnan^{1*}, Maslinawati Mohamad², Zairul Nurshazana Zainuddin³, Zubaidah Zainal Abidin⁴

¹Faculty of Accountancy, Universiti Teknologi MARA, Shah Alam, Selangor, Malaysia, ²Faculty of Accountancy, Universiti Teknologi MARA, Shah Alam, Selangor, Malaysia, ³Faculty of Accountancy, Universiti Teknologi MARA, Shah Alam, Selangor, Malaysia, ⁴Faculty of Accountancy, Universiti Teknologi MARA, Shah Alam, Selangor, Malaysia. *Email: suhaily77@gmail.com

ABSTRACT

Charitable organizations are involved in activities of common concern to members and donors, but which normally benefit people beyond that membership. The survival of these organizations depends on donors and funders. The main objective of this study is to identify governance factors that affect donation. We posit that there are five governance factors related to donation. The governance factors are the board size, board members having professional qualification, board members with political connections, frequency of meeting, and website availability. Based on a sample of 98 charitable organizations, we found that the governance factors such as board members having professional affiliation and board members with political connections are significantly associated to donation received by the charitable organizations.

Keywords: Corporate Governance, Donation, Charitable, Non-profit Organizations

JEL Classifications: C21, M41, M15IT

1. INTRODUCTION

Charities exist in virtually all societies and the rise of charities as an economic force in today's society is well documented (Brower and Shrader, 2000). However, unlike profit-oriented entities, which are subject to securities market regulation and required to produce financial reports in compliance with the International Financial Reporting Standards, most industrialized countries impose minimal charity regulation and operate "underdeveloped" financial reporting standards (Wilke, 2003). Typically, charitable organizations are involved in activities that are of common concern to members and donors, but which normally benefit people beyond that membership (Saxon-Harold, 1990). Hence, the survival of these charitable organizations depends on donors and funders. The competition among charitable organizations and the desire to cultivate multiple revenue streams to resist donor capture requires these organizations to be transparent and accountable in their accounting disclosure (Cordery and Baskerville, 2007).

The purpose of this paper is to identify the governance factors that have an impact on donations in emerging countries, such as Malaysia. We identify five governance factors that affect donations - board size, board professionalism, board members with political connections, frequency of board meetings, and website availability. The results of this study can provide guidance to regulators in enhancing the level of corporate governance of the non-profit organizations in Malaysia.

This paper is organized as follows. Section 2 summarizes the common predictor variables of governance in prior research. The empirical results will be discussed in Sections 3 and 4 presents the discussion and conclusion.

2. GOVERNANCE FACTORS RELATED TO DONATIONS

Studies have found a positive relationship between the quality of board governance and non-profit organizational effectiveness

(Preston and Brown, 2004). The authors conjecture that charitable organizations that have a better quality of governance will be better in gaining public trust, and, hence, will be in a better position to secure donations from the public. A summary of the measurement of variables that will be used in this study is depicted in Table 1.

a. Board size

Some literature related to board size for profit organizations argues that a smaller sized board is better than a larger board size. A board membership exceeding seven or eight would be difficult to monitor (Lipton and Lorch, 1992); a smaller board size leads to cutting and downsizing (Jensen, 1993), and is more effective than a larger board size (Hermalin and Weisbach, 2003). Moreover, Owusu and Ganguli (2010) find that a smaller board size increases the likelihood of a company voluntarily reporting about its internal control.

In contrast, the literature concerning non-profit organizations indicates that board members may influence the efficiency of the organizations. Olson (2000) suggests that non-profit organizations with a larger board size are more efficient in gaining funds. In addition, a larger board size has a greater amount of information, which will help the organizations in terms of their advisory function and capacity to provide better monitoring. However, these are not the only elements needed by charitable organizations to obtain more donations.

b. Board professionalism

Board professionalism, qualification, knowledge, and experience are essential in making crucial decisions. According to Carpenter and Westphal (2001), a board of directors that has a mix of competencies and capabilities will have the tendency to increase the value of the role of the board execution. A study by Yermack (2006) regarding share prices states that directors with professional qualification can have a positive impact on the performance of the share price, particularly in accounting and finance. The same application can be applied to this study in the context of whether or not board professionalism can affect the ability of a charitable organization to attract the public to make donations to its organization.

There are a few studies pertaining to private organizations that show that the professional board members can enhance firm performance (Haniffa and Cooke, 2002; Vafeas, 2005). In general, organizations having a higher number of professional board members will perform better than firms having a lower number of professional board members.

c. Board members with political connections

Political connection is a relational wealth inasmuch as the personal connections of managers with the government not only affects the firm's performance but also decisions such as charitable contributions. Previous studies define a politically connected board director as a member of parliament, a minister, military official, a head of state, a close relative of a top officer of a state, or a current or former officer of a central government (Faccio, 2006; Fan and Wong, 2006).

Previous literature shows that a politically connected board can increase the value of the firm; for instance, Agrawal and Knoeber (2001) find that directors with political experience are more prevalent in firms that have a stronger business relationship with the government. Claessens et al. (2006) posit that politically connected firms receive preferential treatment from the government in the form of capital investment and subsidy; thus, leading them to better performance. Goldman et al. (2009) show that the announcement of the nomination of a politically connected individual to a company's board of directors in the United States would lead to a positive stock return. The central assumption here is that owners or directors of firms have an incentive to intervene in politics if doing so can maximize their economic interests.

Therefore, our hypothesis is that a board with political connections will have a greater tendency of experiencing substantially higher donations than those without.

d. Frequency of board meetings

Research concerning corporate boards has found that the board process is the central driver of effective governance rather than the board structure or composition (Finkelstein and Mooney, 2003). The frequency of board meetings reflects the process in governance. Vafeas (2005) suggests that board activity, which is measured by board meeting frequency, is an important dimension of the board operations. The results indicate that the frequency of board meetings and firm value are inversely related, *ceteris paribus*, in that a higher frequency of board meetings follow poor corporate performance. Therefore, the hypothesized negative association between meeting frequency and past performance is likely to be non-linear, being more pronounced for poor performance than for good performance (Vafeas, 1999).

e. Website availability

The use of the Internet in marketing and promoting one organization can be beneficial. Websites manage to emotionally engage potential donors. It has been suggested that online donations significantly reduce the fundraising costs for non-profit organizations (Epner, 2004). Some charity organizations have earned a substantial income, for instance, recycling organizations; however, most depend on contributions from individuals who are convinced that the organization's programmes make a difference (Straughan and Pollak, 2008).

3. RESEARCH METHODOLOGY

This study aims to examine the relationship of the governance factors with donations received by charitable organizations. The dependent variable of this study is the donations received by charitable organizations measured by the natural log of the total income of charitable organizations. The independent variables comprise the governance factors; five variables are used to study the relationship, i.e., board size, board professionalism, board members with political connections, frequency of board meetings, and the website availability (Table 2). Our sample consists of 98 charitable organizations from

five different states - Kelantan, Kuala Lumpur, Sarawak, Selangor and Terengganu that have a complete set of annual report data from 2010-2013.

The research model is summarized as follows:

$$DON_i = \alpha + \beta_1 BSIZE_i + \beta_2 BPROF_i + \beta_3 BPOLI_i + \beta_4 BFREQ_i + \beta_5 WEB_i + \beta_6 FSIZE_i + \epsilon X$$

a. Measurement of control variables

In this research, the control variable is the organization size. The proxy used to measure the organization size is the total revenue collected by the charitable organization. This is consistent with the previous studies conducted by Ostrower (2007), Rehli and Jager (2011), and Schmitz et al. (2011).

4. RESULTS

This study aims to examine the relationship between governance and the donations received by charitable organizations (proxy for the total income of charitable organizations). The governance factors include total number of board members (BSIZE), board members with professional affiliations (BPROF), board members with political connections (BPOLI), total number of board meetings conducted in the financial year (BFREQ), and the availability of the charitable organization’s website (WEB). Ninety-eight charitable organizations from five different states were selected as the sample, as presented in Table 3.

The descriptive statistics of the independent and dependent variables are presented in Table 4. The total number of valid cases for donation is only 71 since the minimum value of log donation is set at 1.00; thus, charitable organizations with a total income of RM0.00 are not counted.

The analysis of skewness and kurtosis shows that board members with professional affiliation (BPROF), board members having political connection (BPOLI), and number of board meetings (BFREQ) are significantly non-normally distributed. Thus, to solve this problem, a transformation method proposed by Cooke (1998) and Rahman and Ali (2006), which is referred to as the Van der Waerden method, was used. Using this transformation procedure, variables from the actual observation were transformed to normal distributions by dividing the distribution into the number of observations plus one region on the basis that each region has equal probability (Cooke, 1998).

The correlation test was employed in order to determine the linearity of the relationship and describe the strength and direction of the linear relationship between the variables. The results shown in Table 5 indicate two significant positive correlations and two significant negative correlations. However, according to Cohen (1988), the correlations are considered as “small” since they range from 0.10 to 0.29. The threshold for the presence of severe collinearity is 0.80 (Cooper and Schindler, 1998). Therefore, none of the variables are excluded from the analysis.

Table 1: Variables and measurement for governance factors

Variable Acronym	Variable (proxy)	Measurement
BSIZE	Board size	Total number of board members
BPROF	Board professionalism	Percentage of board members with professional affiliation to total number of board members. Professional affiliation refers to members with professions in areas such as accounting, management, engineering, architecture and medical
BPOLI	Board members with political connections	Percentage of board members with political connections to total number of board members. Political connections refer to members being conferred awards by the Government of Malaysia
BFREQ	Frequency of board meetings	Total number of board meetings conducted in the financial year
WEB	Website availability	Availability of the website of the organization

Table 2: Measurement for independent variables

Variable Acronym	Variable (Proxy)	Measurement
BSIZE	Board size	Total number of board members
BPROF	Board professionalism	Percentage of board members with professional affiliations to total number of board members.
BPOLI	Board members with political connections	Percentage of board members with political connections to total number of board members.
BFREQ	Frequency of board meetings	Total number of board meetings conducted in the financial year
WEB	Website availability	Availability of the website. Charitable organizations that have a website will be coded 1 and 0 for not having a website

Standard multiple regressions were conducted to examine the relationship of the variables since the dependent variable in this study is a continuous data (log total income of charitable organizations). Since multiple regressions are very sensitive to outliers, extreme scores are excluded through the screening process resulting in one sample being excluded. The results from multiple regressions using the “Enter” method are presented in Table 6.

As shown above, the R² is 0.202, this indicates that 20.2% of the variation in the total income (Log-donation) of charitable organizations can be explained by the variation of the total number of board members (BSIZE), board members with professional affiliations (BPROF), board members with political connections (BPOLI), total number of board meetings conducted in the financial year (BFREQ), and the availability of the charitable organization’s website (WEB). Among the five governance factors, board members with political connections (BPOLI) show a significant

positive relationship at 0.05 (0.014) and board members with professional qualifications (BPROF) show a significant positive relationship at 1.00 (0.076) with the total donation received by the charitable organizations.

5. CONCLUSION

In this paper, we study the effect of the corporate governance characteristics of the charitable organization (measured by board size, board members with political connections, board members having professional affiliation, frequency of board meeting and the availability of website) on its performance (measured by total donation received). We test these predictions using the data from annual report of 98 charitable organizations from five different states (i.e., Kelantan, Kuala Lumpur, Sarawak, Selangor and Terengganu). Specifically, we find that board members having professional affiliation are positively associated with the total donation received by a charitable organization. Our empirical result is consistent with Haniffa and Cooke (2002) who find that board professionalism influences the ability of organizations in generating income. The results support the finding that organizations having a higher number of professional board members will perform better than firms having a lower number of professional board members. Although the board members of charitable organizations normally consist of volunteers rather than paid professionals, the presence of professional members on the board is important, as they are considered as an instrument in dealing with the organization’s environment; their competencies and capabilities are vital, especially in making significant decisions (Brower and Shrader, 2000). Besides, we also find that board members with political connections influence the donation received by the charitable organization. Claessens et al. (2006), claim that politically connected firms receive preferential treatment from the government in the form of capital investment and subsidy, which lead them to a better performance. Therefore, in this study, the matching of the competencies and capabilities of the board including the experiences and skills of the board members with the support from having political connections influence the performance of the charitable organizations.

Table 3: Charitable organization according to states

State	Frequency (%)	Valid percent	Cumulative percent
Kelantan	9 (9.2)	9.2	9.2
Kuala Lumpur	13 (13.3)	13.3	22.4
Sarawak	20 (20.4)	20.4	42.9
Selangor	29 (29.6)	29.6	72.4
Terengganu	27 (27.6)	27.6	100
Total	98 (100)	100	

Table 4: Descriptive statistics for independent and dependent variables

Variable	N	Minimum	Maximum	Mean±SD
BSIZE	98	0.00	29.00	13.2143±6.28,736
BPROF	98	0.00	3.00	0.2143±0.67,732
BPOLI	98	0.00	5.00	0.2551±0.81,622
BFREQ	98	0.00	9.00	1.0000±1.14,873
WEB	98	0.00	1.00	0.2347±0.42,599
Log-donation	71	1.00	5.59	3.8864±0.96,484
Valid N	71			

Table 5: Correlation analysis

Variable	BSIZE	WEB	BPROF	BPOLI	BFREQ
Log-donation	BSIZE 1.00				
	WEB -0.106	1.00			
	BPROF 0.112	-0.114	1.00		
	BPOLI 0.093	0.173	-0.011	1.00	
	BFREQ 0.067	0.068	0.050	0.062	1.00

Table 6: Multiple regression analysis

Variable	B	Standard error	Beta	t	Significant	95.0% C.I for B	
						Lower	Upper
Constant	4.18	0.25		16.71	0.00	3.68	4.68
BSIZE	-0.027	0.016	-0.18	-1.63	0.107	-0.060	0.006
WEB	0.248	0.248	0.115	1.000	0.321	-0.248	0.743
BPROF	0.338	0.187	0.204	1.804	0.076	-0.036	0.712
BPOLI	0.438	0.173	0.289	2.527	0.014	0.092	0.785
BFREQ	0.218	0.142	0.173	1.538	0.129	-0.065	0.502
R ²	0.202						
N	97						

6. ACKNOWLEDGMENTS

The authors would like to thank the Faculty of Accountancy (Universiti Teknologi MARA), Accounting Research Institute (Universiti Teknologi MARA) and Ministry of Higher Education (MOHE) for providing facilities and financial support. Part of

this research is supported under MOHE Research Acculturation Grant Scheme.

REFERENCES

- Agrawal, A. Knoeber, C.R. (2001), Do some outside directors play a political role? *Journal of Law and Economics*, 44, 179-198.
- Brower, H.H., Shrader, C.B. (2000), Moral reasoning and ethical climate: Not-for-profit vs. for-profit boards of directors. *Journal of Business Ethics*, 26(2), 147-167.
- Carpenter, M.A., Westphal, J.D. (2001), The strategic context of external network ties: Examining the impact of director appointments on board involvement in strategic decision making., *Academy of Management*, 44(4), 639-660.
- Claessens, S., Feijen, E., Laeven, L. (2006), Political connections and preferential access to finance: The role of campaign contributions. *Journal of Financial Economics*, 88(3), 554-580.
- Cohen, J.W., (1988), *Statistical Power Analysis for the Behavioral Sciences*. 2nd ed. Hillsdale, NJ: Lawrence Erlbaum Associates.
- Cooke, P. (1998), Introduction: Origins of the Concept in Regional Innovation Systems-the Role of Governances in a Globalized World. London: UCL Press, p2-25.
- Cooper, D.R., Schindler, P.S. (1998), *Business Research Method: Statistics and Probability*. Singapore: McGraw-Hill International Edition.
- Cordery, C.J., Baskerville, R.F. (2007), Charity financial reporting regulation: A comparative study of the UK and New Zealand. *Accounting History*, 12(7), 6-27.
- Epner, S. (2004), Surviving fundraising on the internet. *Nonprofit World*, 22(2), 17-19.
- Faccio, M. (2006), Politically connected firms. *American Economic Review*, 96(1), 369-386.
- Fan, J.P.H., Wong T.J. (2006), Politically connected CEOs, corporate governance and post-IPO performance. *Journal of Financial Economics*, 84(2), 330-357.
- Finkelstein, S., Mooney, A.C. (2003), Not the usual suspects: How to use board process to make boards better. *Academy of Management Executive*, 17(2), 101-113.
- Goldman, E., Rocholl, J., So, J.(2009), Do politically connected boards affect firm value? *Review of Financial Studies*, 22(6), 2331-2360.
- Haniffa, R.M., Cooke, T.E. (2002), Culture, corporate governance and disclosure in Malaysian corporations. *Abacus*, 38(3), 317-349.
- Hermalin, B.E., Weisbach, M.S. (2003), Board of Directors as an Endogenously Determined Institution: A Survey of the Economics Literature. Working Paper, Center for Responsible Business.
- Jensen, M.C. (1993), The modern industrial revolution, exit and the failure of internal control systems. *Journal of management*, 22(3), 409-438.
- Lipton, M., Lorsch, J.W. (1992), A modest proposal for improved corporate governance. *Business Lawyer*, 48(1), 59-77.
- Olson, D.E. (2000), Agency theory in the not-for-profit sector: Its role at independent collages. *Nonprofit and Voluntary Sector Quarterly*, 29(2), 280-296.
- Ostrower, F. (2007), Nonprofit governance in the United States: Findings on performance and accountability from the first national representative study. Available from: <http://www.urban.org/publications/411479.html>. [Last accessed on 2011 Dec 27].
- Owusu. A., Gangguli. G. (2010), Voluntary reporting internal control systems and governance characteristics: An analysis of large US companies. *Journal of Managerial Issues*, 22(3), 383-408.
- Pollach, I., Treiblmaier, H. And Floh, A. (2005), Online Fundraising for Environmental Nonprofit Organizations. In *System Sciences, 2005. HICSS'05. Proceedings of the 38th Annual Hawaii International Conference*. p178.
- Preston, J. B., and Brown, W. A. (2004), Commitment and performance of nonprofit board members. *Nonprofit Management and Leadership*, 15(2), 221-238.
- Rahman, R.A., Ali, F.H.M. (2006), Board, audit committee, culture and earnings management: Malaysian evidence. *Managerial Auditing Journal*, 21(7), 783-804.
- Rehli, F., Jager, U.P. (2011), The governance of international nongovernmental organizations: How funding and volunteer involvement affect board nomination modes and stakeholder representation in International Nongovernmental Organizations. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, 22(4), 587-612.
- Saxon-Harold, S.K.E. (1990), Competition, Resources and Strategy in the British Nonprofit Organizations, *The third sector: Comparative Studies of Nonprofit organizations*. Berlin,: Walter de Gruyter & Co., p31-44.
- Schmitz, H.P., Raggo, O., Vijfeijken, T.B. (2011), Accountability of transnational NGOs: Aspirations vs. practice. *Nonprofit and Voluntary Sector Quarterly*, 41(6), 1175-1194.
- Straughan, B., Pollak, T.H. (2008), The broader movement: Nonprofit environmental and conservation organizations, 1989–2005. Available from: <http://www.urban.org/publications/411797.html>. [Last accessed on 2011 Dec 27].
- Vafeas, N. (1999), Board meeting frequency and firm performance. *Journal of Financial Economics*, 53(1), 113-142.
- Vafeas, N. (2005), Audit committees, board and the quality of reported earnings. *Contemporary Accounting Research*, 22(4), 1093-1122.
- Wilke, B. (2003), Monitoring Charitable Organizations: Criteria and Assessment Methods, Paper Presented at the OECD/DAC Workshop Development Partners in Evaluation, 25-26 March 2003, Paris.
- Yermack, D. (2006), Board members and company value. *Financial Markets Portfolio Management*, 20(1), 33-47.