

Analysis of Independent Director System and Effectiveness of Company Management

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Abstract: The establishment of independent director system can effectively supervise and manage, safeguard the rights and interests of legal shareholders, and improve the effectiveness of company management. In the meanwhile, the practice of independent directors in China still has a lot of problems and deficiencies, which requires continuous improvement and development. On the basis of relevant theories, this paper analyzes the current situation of independent directors in China and puts forward an empirical analysis on the effectiveness of the independent director system of company management. In addition, according to the conclusion of the empirical study, some policy suggestions are put forward on how to play the role of independent directors to achieve the purpose of improving the effectiveness of corporate governance.

1. Literature Review

1.1. Literature Review of Foreign Countries

1.1.1. Ineffectiveness of Independent Director System

With the study of the independent directors and company performance based on 217 non-financial listed companies in Vietnam from 2010 to 2014, Thi TuyetMai Nguyen, Elaine Evan and Meiting Lu^[1] used regression estimation method, and found that independent directors negatively impacted company's operating performance.

1.1.2. Effectiveness of Independent Director System

Abidin^[2](2010) took a random sample of listed companies in Malaysia and selected 75 companies as research samples. The research found that the size of the company's board of directors has an impact on performance, especially the size of the sole director has the most significant impact on performance.

1.1.3. Relationship between the Proportion of Independent Directors and Company Performance

Bouzouk^[3](2011), taking all listed companies on the Istanbul Stock Exchange of Turkey as samples, considering factors such as the size of the companies as controlling variables, concluded that the proportion of independent directors and their performance presents an obvious positive correlation.

1.1.4. Relationship between Independent Director's Compensation and Company Performance

Through research, Tian and Lau^[4](2001) found that there is no correlation between the remuneration of independent directors among external directors and the effective management of the company.

1.2. Literature Review in China

Experts and scholars in our country have different opinions on the effectiveness of the independent director system.

1.2.1. Ineffectiveness of Independent Director System

Dongzhi Yu and Wang Huacheng^[5] (2003) compared the before and after of the introduction of independent director system through research, and found that the introduction not only had unobvious improvement of the current financial situation, but had the opposite effect. Zheng Zhigang and Lv Xiuhua^[6] (2009) found that the company's sole director did not play its due role and became a "vase director".

1.2.2. Effectiveness of Independent Director System

Hu Xiaoming and Cao Yidan^[7] (2013) conducted empirical research after studying listed companies, and found that the proportion of the board of directors, the salary level and the number of people selected by the independent board of directors have more or less significant positive correlation with company management. Through research, Liu Liguo^[8] (2003), Wang Huaiming, Su Jinxiang^[9] (2007), concluded that the exertion of independent director system has a positive correlation effect on the company.

1.2.3. Relationship between the Proportion of Independent Directors and Company Performance

Zhang Aiping^[10] (2010) studied the relationship between educational background, age and proportion and company performance, and found that the proportion of independent directors has a significant impact on company performance. Zhu Liling^[11] (2014) and others' research results shows that the greater proportion of independent directors in shareholders is, the better indicators reflecting the company's performance are.

1.2.4. Relationship between Independent Director's Compensation and Company Performance

Wang Xinhong, Guo Qiaoli^[12] (2015) Through studying various characteristics of the independent director system, they concluded that the higher the average salary of independent directors, the more obvious the improvement in corporate performance.

According to the literature in china and abroad, to sum up, there is no identical conclusion. Even the experts and scholars have opposite opinions. The possible reasons are: different standards of management controlling utility, selections of different samples, or not setting some important variables that affect management utility.

1.3. Literature Review

Overall, foreign scholars have different views on the relationship between independent director system and corporate performance. Among them, the most studied part is the relationship among extent of independent directors percentage in the board of directors, the salary of independent directors and the company's performance. This article wants to analyze the effectiveness of independent director system for management through theoretical knowledge analysis. According to the actual situation of the effectiveness of the independent director system, this paper puts forward more targeted suggestions to improve and perfect the independent director system in our country.

2. Development Status of Independent Director System in China

The special background of China's introduction of the independent board system, which is different from other countries, is mainly reflected in the following aspects:

2.1. Prevent Internal Shareholder's Control and Safeguard Non-controlling shareholders

In China, a large proportion of the shares in listed companies are owned by state-owned shares and legal person shares, in addition, these shares are not tradable. Public ownership is only a small part, and these shares are largely dispersed. Controlling abuses are often conducted by manipulating BOD's decision-making wills.

2.2. Offset the Defects of the Board of Supervisors

In light of the main position of BOD, being as the voting and decision-making body of the company, BOD is aimed to discuss the major issues of the company, the supervisors however, cannot directly participate in the decision-making of the company. Without voting rights and voting rights in the shareholders' meeting, they cannot effectively restrict and exert pressure on the board of directors.

2.3. Enhance the Power of BOD

Unreasonable structure, low level of analysis in decision-making, lacking of necessary internal supervision, etc. are possible problems of a company's board of directors.

The proportion of internal directors in the board of directors of listed companies in China is too high.

In our country's board of directors, it often appears that the chairman and the general manager are held by one person.

Many members of the company's board of directors are directly appointed by the government. Many of them are not proficient in business and management. The direct consequence of the above main problems is the failure of the board of directors.

3. Problems of Independent Directors Policy in China

There are many problems in the practice of China's independent director system, which have directly affected the development of the independent director system after it was introduced into China, mainly in the following aspects:

3.1. The Professional Quality of Independent Director Mismatches the Quality Required

In reality, it is popular that the sources of the company's sole directors are becoming more and more single and even similar. The company has not combined their own circumstances to select experts with professional knowledge and experience to feed their corporate governance needs.

3.2. Unreasonable ownership Structure of Listed Companies

The internal structure of China's listed companies are characterized by the "one-share hegemony" of major shareholders. On average, state-owned shares and corporate shares (indirectly controlled by the government) account for 70% of the total share capital of listed companies. Apart from that, major shareholders control two-fifths of the listed shares at the same time, which makes it easier to entitle various interests towards identical shares under the economics market. The abnormal structure of equity can effortlessly unbalance the rights in company management.

3.3. Obstruction of Information transmission and Absent of Communication Mechanism

One prominent problem in the management system among listed companies in China is non-transparent information disclosure. Many companies have not timely and accurately updated the information that the company should disclose when operating according to the regulations of the system, and this indicates that the independent director have no advantages over the perspective of information disclosure. The sole director is part-time in the board of directors, not full-time in the company. Lacking of the comprehensive understanding of the company's management planning, it is difficult for them to put forward persuasive suggestions when involving in decision-making and discussions.

3.4. Functions Conflict between Independent Directors and Supervisory Board

The supervision of the sole director and the supervision of the board of supervisors have overlapping areas, i.e. there are overlapping management parts in the company's finance and legitimacy. Such a situation is easy to lead to conflicts in supervision, resulting in waste of resources, duplication of work or mutual shirking of responsibilities when things go wrong. On the contrary, it may increase the supervision cost and reduce the company's management efficiency.

4. Suggestions on Perfecting Independent Director System of Listed Companies in China

4.1. Increase the Proportion of Independent Directors

Through theoretical analysis and case analysis, it can be concluded that the increase in the proportion of independent directors can improve the company's performance, which makes management more efficient. The higher the proportion of independent directors in the board of directors is, the more says they have and the more influence they can exert on major shareholders in the company's decision-making.

4.2. Improve the Incentive Mechanism for Independent Directors

Through research and theoretical discussion, the higher the salary of independent directors, the better the performance of their company and the better the company's performance, which also shows that the management efficiency of the company has been improved.

4.3. Establish Personnel Files of Independent Directors

For independent directors, the securities regulatory department shall set up an independent personnel file supervisor to train and evaluate candidates for independent directors. Only candidates passed the training and evaluation can they meet the requirements of BOD in listed companies.

4.4. Establish and Improve the Integrity System of independent directors and the Market Exclusion Mechanism

In 2016, the State Council issued the Guiding Opinions on Establishing and Perfecting Joint Incentive and Joint Disciplinary System for Faithfulness to Accelerate the Construction of Social Integrity. Some people think that if a person is listed in the list of violating trust and other common disciplinary, he should not act as the director, supervisor or senior manager of a listed company.

4.5. Improve the Employment Mechanism of Independent Directors

The recommendations of controlling shareholders and management can be changed into those of small and medium shareholders. Because some companies hire independent directors to gain the experts' reputation in order to enhance their reputation.

Under the new normal, China's economy will maintain a steady and positive development trend. Under the good trend, the number of companies continues to increase, and corporate governance and internal control systems still need constant progress and development. As an important part of corporate governance, independent director system should play a greater role.

5. Conclusion

Over the years, practices in Britain and the United States have proved that the independent director system has played a positive role in the effective management of the company as well as a series of reputations and development prospects. However, after the introduction of China's general situation, the adjustment of the combination of China's economic backgrounds and present atmosphere is needed as long as the sole independent director intends to make a difference. This article focuses on the analysis of the factors that will affect the effectiveness of the independent board system for management, including the selection and appointment of personnel, the follow-up compensation issues, the perfection of the system and government factors. In theory, it can be seen that the independent board system is effective for management. Through the analysis of the current situation of the development of the independent director system in China, it is found that the existence of the independent director system in our country is not suitable for the professional and corporate culture needs, the system in our country is not perfect enough to effectively safeguard the independent director, the public in our country is not clear about the connotation of the independent director, and awareness of its position is also vague and unprofessional. These problems seriously affect the effectiveness of the independent director system in management.

The establishment and improvement of independent director system is a complicated systematic project, in order to make it play its due role. Many relevant supporting measures have been taken to assist in the implementation. At the same time, corresponding institutional environment and cultural background are also needed. Rome was not built in a day. Similarly, in our economic system, the independent board system cannot be perfected in one day. This article is based on the actual situation in China, combined with the special status of independent directors and the factors affecting them, to put forward suggestions on perfecting appropriate laws and regulations, perfecting the incentive policies of independent directors and establishing procedures for selecting independent professionals, so as to make the independent director system play a more effective role in management performance.

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