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THE EFFECT OF CEO DUALITY, BOARD COMPOSITION AND BOARD SIZE ON ORGANIZATIONAL PERFORMANCE OF COMPANIES LISTED ON THE KUALA LUMPUR STOCK EXCHANGE

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Abstract

This study examined the effect of CEO duality, board composition and board size on organizational performance of Bourse Malaysia or Kuala Lumpur Stock Exchange (KLSE) listed companies. For comparison purpose, this study examined these variables for main board companies as the proxy of large size companies, second board as the proxy for small size companies, and the whole market as proxy for developing country. This study employed 196 companies selected from the main board (96) and the second board (100) of KLSE and applied a simple regression analysis to describe the data of this study and MANOVA analysis model to test the effect of CEO duality, board composition and board size on organizational performance. We run these tests separately for main board, second board companies and the total market. The results indicated that the effects of multiple relationships between CEO duality and the three organizational performance variables (ROA, ROE, PER) before and after controlling by the age and industry are not significant for all three groups of board samples. While, the composition of outside directors was significant affects the firm performance for main board and combine board, but it is not significant for second board. Finally, board size is associated with higher firm performance. This evidence occurs only for main board. In general, the control variables, age and industry, do not affect significantly the relationships between CEO duality, board composition, and board size and organizational performance.

Key words: *CEO duality, board composition, board size, firm performance.*

INTRODUCTION

The managements of modern corporations do not generally hold substantial equity positions in the company. Simply, shareholders own the corporation; management runs it. For many shareholders, this is a distinct advantage. As noted, investors need not concern themselves with the routine operations of the companies in which they hold stock. This responsibility is the charter of the company's Chief Executive Officers (CEO) and its board of directors (Dalton & Kesner, 1987)

Until recent study, there is controversy regarding the impact of corporate governance on firm performance. Most of the empirical works have focused on two critical governance issues: First, one of the most

hotly debated issues in corporate governance is the question of whether the Chief Executive Officer (CEO) should also serve as the chairman of the board of directors and second, the composition and size of the board (Daily & Dalton, 1993). Researchers usually focus on large firms in developed countries. Very little studies have been done in developing countries. Thus, this paper is to provide another view on the impact of corporate governance mechanisms on organizational performance in developing country such as Malaysia.

Recent corporate scandals at such leading firms as Enron, WorldCom, Tyco, and Adelphia have only helped to rekindle this and other dialogues on the effectiveness of American corporate governance and the accountability of corporate executives (Faleye, 2003). The CEO is a corporation's chief strategist, responsible for initiating and implementing company-wide plans and policies. In the words of Fama and Jensen (1983), he heads the organization's decision management hierarchy.

On the other hand, the chairman is responsible for the working of the board, ensuring that all essential matters are on meeting agenda, ascertaining that the board adequately ratifies and monitors the strategy initiatives of the CEO, and overseeing the hiring, firing, evaluation, and compensation of the CEO. Thus, the chairman is the corporation's chief decision control agent. Since the chairman performs important control functions, it is often suggested that a separate person apart from the CEO should occupy this position (Faleye, 2003). Fama and Jensen (1983) suggest that CEO duality (that is, when the CEO also serves as chairman) violates the principle of separation of decision management and decision control and hinders the board's ability to perform its monitoring functions. Likewise, Jensen (1993) argues that separating the two positions is essential for board effectiveness since a chairman CEO cannot perform control functions "apart from his or her personal interest."

It is unfortunate that some management may act more in their own interests than in those of the shareholder. When this happens it suggests at a more practical level the failure of another group: the companies' boards of directors (Dalton & Kesner, 1987). The board of directors of a corporation plays an important role in protecting shareholder's interest. They are legally authorized to ratify and monitor managerial decisions (Fauzias et al.1999). It has been suggested that much of the board's inability to perform adequately in its role to control company management is related to its lack of independence from the very management it is enchartered to control (e.g., Kesner & Dalton 1986; Mintzberg 1983). Independent judgment by the board may be infrequent and two corporate practices may lead to this unjust act. This tendency not to intervene when company management behaves in a manner inconsistent with the interests of the shareholders may be related to CEO duality and board composition (Dalton & Kesner, 1987).

A related issue is the size of the board. The size of the board is related to the resource dependence perspective (Pfeffer & Salancik, 1978) and board size is often linked to board of directors effectiveness and recommend limiting the board size to fewer than seven or eight (Fuerst & Kang, 2000). The greater the reliance on the external environment, the larger the board of directors (Weir et al,. 2003). Small boards are most appropriate when directors serve primarily as administrators (Pfeffer, 1973). It might also be noted that small boards are more "manageable" from CEO's perspective (Chaganti et al., 1985).

Eisenhardt and Schoonhoven (1990) suggested that CEOs and directors be able to more directly influence organizational processes and outcomes in the small firm. This

suggestion is to be tested using second board companies on Kuala Lumpur Stock Exchange as proxy for small size firms. For comparison, therefore, this study examines the effects of CEO duality, board composition and board size on organizational performance of main board companies as proxy for large size companies, second board as proxy for small size companies, and the whole market as proxy for developing country.

The structure of this paper is as follows. First, we present the theoretical framework of the relationships between CEO duality, board composition, and board size on organizational performance and summarize the substantive empirical literature on this topic. Next, we explain the governance measures along with the rationale for our choice of specific performance measures. Third, we discuss our findings and finally the future research of corporate governance structures.

THEORETICAL FRAMEWORK

CEO Duality

Fama and Jensen (1983) have asserted that the inability of boards to exercise their legitimate governance role arises from board domination by firm managers. Specifically managers have been accused of defeating the system of checks and balances through their ability to influence board composition and tenure, and set agenda and control information flows.

Jensen and Meckling (1976) have suggested the impact of the separation of ownership from control on firm performance. In the broad arena of the impact of separation of ownership and control, CEO duality has come under particular scrutiny. In cases of CEO duality, the board of directors is the dual role of CEO as board chairperson. Another words, the CEO of the firm wears two hats, a CEO hat and the chairperson of the board of directors hat. Therefore, the top managerial officer of the corporation simultaneously serves as chairperson of the board which has the charter of monitoring and evaluating top management. This dual role would seem to suggest a certain conflict of interest (Dalton & Kesner 1987). Based on the separation of ownership from control, the main board structure recommendation is that the posts of CEO and chairman should be split (Weir, Laing, & Wright, 2003).

CEO duality has significant implications for organizational performance and corporate governance. Proponents of duality argue that duality should lead to superior firm performance. Organizational observers, however, are far less settled on the issue of a CEO and corporate performance linkage. Researchers views suggest that CEOs have a significant impact on the organizational performance. But, other researchers perspective in which environmental factors may constrain a leader's discretion to influence the organization. They argue that the effective CEO and performance linkages must depend on the context of succession event other contingent factors (Dalton & Kesner, 1985).

Board Composition

Members of boards of directors are commonly classified as either 'insiders' or 'outsiders'. An insider is a full-time officer of the corporation and is normally a CEO, president, or vice-president of the firm. Kesner & Dalton (1985) state that an inside director is an employee (usually a high level manager) of the firm and an outside director is not in the employ of the company. An outsider does not serve in a managerial capacity for the company in which he is a director. Board composition is ordinarily defined as the proportion of outside directors to total directors (Dalton & Kesner 1987). This ratio may be an important indicator of board independence. The issue is whether a board composed of a relatively high percentage of inside directors is likely – or even capable – of exercising independent judg-

ment in matters regarding the control of management (Dalton & Kesner 1987).

Those who are in favour of more non-executive directors on the board base their arguments on two theories: agency and resource dependency (Haniffa & Cooke, 2002). The premise of agency theory is that non-executive directors are needed on the boards to monitor and control the actions of executive directors due to their opportunistic behavior. Thus, non-executive directors are seen as the check and balance mechanism in enhancing boards' effectiveness (Haniffa & Cooke, 2002) and as monitors of management's performance and actions (Fama & Jensen, 1983). The resource dependence theory proposes that non-executive directors provide firms with links to the external environment due to their expertise, prestige and contacts (Haniffa & Cooke, 2002). This theory suggests that non-executive directors often see themselves in an advisory rather than a decision-making role but since they are respected for their wisdom and independence, they will be influential and listened to, although it may not be their function to actually institute policy.

Resource dependence theory suggests that the effectiveness of the firm rests on the ability of key organizational members to act as boundary spanners. In their role as boundary spanners they interact with the environment in a manner that coopts "important external organizations with which they are interdependent (Pfeffer & Salancik, 1978). The point here is that carefully selected outside directors may be in a position to extract important resources from the environment that might be otherwise unavailable. Additionally, it is expected that these directors will support the organization, attend to its problems, and present it favorably to outsiders.

Another two perspective in which board composition is posited to affect firm performance are service and control. These two perspectives are not necessarily considered to be mutually exclusive (Pfeffer & Salancik, 1978). The service component suggests that outside board members provide counsel and advice to the CEO not necessarily available from inside directors. Beyond that, outside board members may, by virtue of their own experience, accomplishment, and exposure, enhance the reputation of the firm (Daily & Dalton, 1993). The second factor, control, suggests that increasing representation by outside directors as a means for better protecting shareholder interests (Daily & Dalton, 1993).

Firm performance

Boards of directors may also want to restrict the use of dual structure when performance is good. They monitor firm profitability as an important indicator of how well CEOs are performing (Fama & Jensen, 1983). When firm performance is good, strong boards may seek to avoid CEO entrenchment for four reasons. First, good firm performance enhances CEO status and power, strengthening CEOs' positions in firms and increasing the risk of entrenchment. Second, good performance creates organizational slack, facilitating CEOs' attempt to provide themselves or other managers with both financial and nonfinancial rewards that engender support (Jensen & Meckling, 1976). Third, because attributions of CEO effectiveness are often made when firms are successful (Meindl et al., 1985), there is less need to create a sense of managerial efficacy through duality; stakeholders may already perceive the firms' operations as legitimate. And fourth, because the boards of high-performance firms are less likely than other boards to replace their chief executives; their CEOs can institutionalize their power over time (Pfeffer, 1981). Vigilant boards are more likely to favor nonduality because of the increased potential for CEO entrenchment in high-performing firms.

Firm age

Literature on strategic and organizational change seems to argue that older firms should be more inert than younger firms (Hannan & Freeman, 1989). As firms age, numbers of routines, programs, and structures increase and become more internally consistent. Precedent gradually dictates an increasing portion of organizational action (Cyert & March, 1963). Others argue, however, that young firms, suffering from potential liabilities of newness, are less willing to make changes that might disrupt already tenuous links with suppliers, customers, and other stakeholders. Given the uncertainty of the relationship between age and strategic change. From this reason, we included it as a control variable.

HYPOTHESES

It would seem then that both CEO duality and board composition are at least potential threats to board of director independence. This in turn may lead to a certain level of board tolerance towards what some have referred to as managerial abuse of their fiduciary relationship with shareholders (Dalton & Kesner 1987). Borikhovich et al., (2001) state that directors who are also managers of the firm may have incentives to make corporate decisions that maximize their own utility, whereas outside directors have incentives to make decisions which signal their abilities as efficient decision-makers. CEO duality role is quite common, with approximately 80 percent of large firms employing the dual structure (Lorsch 1989). The reason for separating the posts of CEO and chairman is to prevent one person exercising too much power on board decisions. The mechanisms identified in the London Stock Exchange's Code of Best Practice would therefore be expected to mitigate the agency problems associated with weak internal governance. Firms that did not exhibit these structures are likely to be poor performers (Weir, Lang and Wright, 2003)

There is some consistency that the choice of the CEO duality structures could be strongly related to corporate performance but views differ diametrically regarding the direction of the impact. Whether the choice of these structures is related to corporate performance remains undetermined. Empirical studies to date provide mixed results on the effect of CEO duality on firm performance and a possible reason for the mixed results could be due to the influence of confounding variables (Gul & Wah, 2003). Examinations of large firms have reported no differences in financial performance across a number of indices as a function of board leadership structure (Daily & Dalton, 1993). Executives who concurrently serve as board members are unlikely to be able to set aside their interests as managers of the corporation when serving as directors and it would seem that greater concentrations of independent (outside) directors would best serve the financial interests of the shareholders (Daily & Dalton, 1993).

Daily and Dalton (1993) find that CEO duality is not statistically and not important indicator of firm performance for small company. It is suggested that boards that separate the posts of chief executive officer and chairman will be better able to influence decisions (Weir et al., 2003). Gul & Wah (2003) study the association between US firms' earnings informativeness and board's leadership structure in terms of CEO duality. They find evidence that firms with the separation of the posts of CEO and chairman are associated with lower agency cost and may act as a substitute for the convergence-of-interests effect of insider shareholding when there is separation of the roles of CEO and chairman. Their study also shows that there is a negative (positive) association between increase in earnings only for firms with CEO duality at medium

(high) levels of insider shareholding. Accordingly, these arguments lead to our first hypothesis.

H1: CEO duality will be associated with lower firm performance.

The main board structure recommendations are that there should be a significant representation of non-executive (outside) directors and that the posts of CEO and chairman should be split. A significant representation is taken to be at least three non-executive directors. It is believed that this is the minimum number required for non-executive directors' views to carry weight at board meetings (Weir et al,. 2003). Board composition refers to the distinction between inside and outside directors and is traditionally operationalized as the percentage of outside directors (i.e., those not in the direct employ of the organization) on the board. Fama & Jensen (1983) argue that outside directors have greater incentives to make decisions that benefit shareholders than do inside directors. They maintain that the decisions made by outside directors signal the labor market concerning their abilities as decision control agents. Because most outside directors are major decision-makers at other organizations, concern for their reputations in the labor market provides them with incentives to act in the interests of shareholders.

Critics have argued that management generally dominates the board by its selection of outside directors, and by its control over the agenda of board meetings and organization provided to outside board members and they are called a pluralistic board (Fauzias et al. 1999). Empirical evidence particularly with respect to the role of outside directors is mixed. Molz (1988) finds that companies with a pluralistic board have higher average performance than companies with a managerial dominated (insiders) board. In another study, Schmidt (1982) finds that the inside/outside aspect of board composition is statistically insignificant as an explanatory variable in relation to corporate economic performance. However, Daily & Dalton (1993) find that board composition is statistically significant and important indicator of corporate financial performance for smaller firm.

Beyond that, outside board members may, by virtue of their own experience, accomplishment, and exposure, enhance the reputation of the firm (Daily & Dalton, 1993). An independent board that pursues shareholders' interests is indicative of effective internal monitoring. Thus boards with a greater proportion of non-executive directors will be more effective monitors (Weir et al., 2003). Borokhovich et al., (2001) study the relationship between the capital structure decision and the decision to hedge using interest rate derivatives and they show that outside members on a firm's board of directors have a significant impact on the decision to hedge using interest rate derivatives. There is a significant positive relation between the quantity of interest rate derivative use and the relative influence of outside directors. This evidence suggests that corporate interest rate derivative investments, on average, benefit shareholders.

Haniffa & Cooke (2002) examine the importance of outside directors as determinant of voluntary disclosures of Malaysian listed corporation. Board composition might be an interesting variable to consider because it will indirectly reflect the role of non-executive directors, that is, more disclosure may be expected if they do actually carry out their monitoring role rather than their 'perceived' monitoring role and they find significant evidence that associated board composition and the extent of disclosure. In a recent study, Park & Shin (2003) suggests that ordinary outside directors are not very helpful to the board in monitoring the firm's management of earnings. Fuerst

& Kang (2000) also find evidence that there is no improvement in operating performance or share value from having greater representation of outside directors, or having a larger board. Klein (2002) examines whether board characteristics of all large traded US firm are related to earnings management by the firm and he finds a significant negative relationship. He interprets that firms with large accruals inherent in their earnings structure are less inclined to have outside directors on the board. Accordingly, this reasoning leads to the second hypothesis.

H2: Proportion of outside directors will be associated with higher firm performance.

Small boards are most appropriate when directors serve primarily as administrators (Pfeffer, 1973). It might also be noted that small boards are more "manageable" from CEO's perspective (Chaganti et al., 1985). Therefore, it is expected that there is a positive relationship between the size of the board and the size of the organizations. With the coupling of organizational size and complexity, boards may provide an important linkage between the firm and the environment (Daily and Dalton, 1993). The greater the reliance on the external environment, the larger the board of directors (Weir et al,. 2003). Pfeffer (1973) finds the size of the board to be significantly related to total sales volume and reliance upon external funding. Chaganti et al. (1985) find that non-failed firms tended to have larger boards. Daily and Dalton (1993) find that board size is statistically significant and an important indicator of corporate financial performance for smaller firm. Fuerst and Kang (2000) find evidence that there is no improvement in operating performance or share value from having a larger board. Accordingly, this leads to our third hypothesis.

H3: Greater numbers of total directors will be associated with higher firm performance.

DATA AND METHODOLOGY

Sample

The data for this study are collected from the latest KLSE Annual Companies Handbook Volume 25 (2002) and KLSE Annual Report 2001. This study employs 196 companies selected from the main board (96) and the second board (100) of KLSE. The companies are selected as they fit the selection criteria. All companies meeting these criteria are included in this study. This sample, then, constitute the population of firms meeting these parameters.

Independent variables

This study employs three independent variables, namely CEO duality, board composition, and board size. CEO duality is binary. It means that if a chairman is also chief executive, we put (1), and otherwise is (0). On the other hand, either one individual serves as both CEO and chairperson of the board (dual structure) or two different persons fill these roles (independent structure). This variable is derived from the Annual Report of Kuala Lumpur Stock Exchange or KLSE (2001).

The distinction between inside and outside directors determines the board of director composition. Inside directors include those active in the current management of the company. While, outside directors are those not in the direct employ of the company. Board of director composition is simply the ratio of total numbers of outside directors to total directors (inside and outside directors). These measures are believed to fully capture the service, resource, and control function of the board.

Finally, the third independent variable is board size. Board size is simply the total number of directors serving on the board. Total number of directors means all of inside directors and out inside directors. This information is also derived from Annual Report of KLSE (2001).

Dependent Variables

Financial performance is as proxy of firm performance. There is no consensus certainly about what constitutes the dependent variables of choice with regard to firm financial performance. It is unlikely that any single indicator could adequately capture the many aspects of such performance. Bourgeois (1980) suggests that the adoption of any particular set of indicators embroils the researcher in the set of problems of quantification and dimensionality. It is not to mention the issue of validity choosing the set of indicators which meet universal acceptance. Some researchers stress the apparent confusion in making such a selection the number of corporate performance measures that could serve as dependent variables is almost unpredictable. Finally, Cochran and Wood (1984) also realize that there is no consensus concerning the choice of dependent variables to measure organizational performance. They propose that organizational performance measures fall into one of two categories, namely accounting returns and market returns. In this study, we rely on three such indices as dependent variables, representing both accounting and market returns, namely return on assets (ROA) and return on equity (ROE) for accounting return and price earning ratio (PER) for markets returns.

Control Variables

This paper considers two variables that may possibly confound the relationships between independent variables and organizational performance, namely firm age and industry classification (industry sector). Both firm performance and certain governance structures may have some association with firm's age. Most literature on strategic and organizational change seems to argue that older firms should be more inert than younger firms (Hannan & Freeman, 1989). As firms age, numbers of routines, programs, and structures increase and become more internally consistent. Precedent gradually dictates an increasing portion of organizational action (Boeker, 1997). Others argue, however, that young firms, suffering from potential liabilities of newness, are less willing to make changes that might disrupt already tenuous links with suppliers, customers, and other stakeholders (Boeker, 1997). This may be particularly true in the case where founder directs the firm. Perhaps, newer firms are more likely to rely on CEO duality and more mature firms have a tendency to perform systematically better on the selected performance indices. Given the uncertainty of the relationship between age and strategic change, we include age as a control variable.

Industry effects may also confound the result. It is possible, for example, that the reported results do not reflect an association between board composition and firm performance, rather, it may be that certain industries – irrespective of board composition – differ systematically in their performance (Kesner & Dalton, 1985). Different industries have different style when they run their activities. We might suspect that management effects differ across industries (Daily & Dalton, 1993). In manufacturing industries, for examples, directors may see a greater opportunity for increasing the value of their investment. This, in turn, may enhance organizational performance. While, in service industries directors may feel that there are many difficulties for increasing the value of their industries, and as a result, they may be more aggressive for enhancing or creating the value of their investment. Besides that, board composition varies depending upon the institutional environment in which the firms operated. In this study, industry effect is not of primary interest, but the ability to test for such effects may strengthen the identification of differences among governance structures and the relationship to firm performance.

Data Analysis

We use a simple regression analysis to describe the data of this study and MANOVA analysis model to test the effect of CEO duality, board composition and board size on organizational performance. We run the tests separately for main board companies, second board companies and the total market. The regression analysis shows the descriptive statistics of the data, while MANOVA (Multivariate Analysis of Variance) demonstrate the effects of one or more independent variables on several (more than two) dependent variables simultaneously. The model of the analysis on this study is as follows:

$$\mathbf{Yi = \alpha_o + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e}$$

where,

Y_i = Return on asset; Return on Equity, and Price Earning Ratio as dependent variables.

X_1 = CEO duality

X_2 = Board of directors composition

X_3 = Size of board of directors

α_o = constant

e_t = error term is assumed equal to zero

RESULTS

For the main board and second board data, the number of directors (board size) ranges from 5 to 20, and the proportion of outside directors to total directors ranges from 33 % to 100 %. To reduce the potential loss of information using the heterogeneous firms, we classify the companies into eight categories based on the industry sectors classification provided in the Handbook of Kuala Lumpur Stock Exchange. The industry sectors namely are consumer products companies, industrial products companies, construction companies, trading/services companies, plantation companies, financial companies, properties companies, and technologies companies. Table 1 shows result of the three hypotheses testing. This study examines three hypotheses testing for main board, second board and combined.

Table 1: Result summary of hypotheses testing

	Hypotheses	Results
H1	CEO duality will be associated with lower firm performance	Not supported for all main and second boards
H2	the proportion (composition) of outside directors will be associated with higher firm performance	Supported only for main and combine boards
		Not supported for second board
H3	the greater number of total directors (board size) will be associated with higher firm performance	Supported only for main board
		Not supported for second board and combine boards

Table 2: Means, Standard Deviations, and Pearson Product-Moment Correlation

A. Main Board

Variables	Mean	SD	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) CEO duality	.385	.489							
(2) Board composition	.713	.204	-.328**						
(3) Board size	9.198	2.557	-.272**	-.033					
(4) Return on Asset	.068	.118	-.034	-.073	.060				
(5) Return on Equit y	.101	.224	-.058	. 131	-.132	.454***			
(6) Price Earning Ratio	35.387	58.898	-.199	.133	.053	-.040	-.060		
(7) Firm age	26.456	15.314	.067	-.132	-.255**	.106	.980	.026	
(8) Industry sectors	4.688	2.762	.004	.272**	.033	-.135*	-.048	.160	-.023

B. Second Board

Variables	Mean	SD	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) CEO duality	.480	.502							
(2) Board co mposition	.569	.174	-.371***						
(3) Board size	7.980	2.059	-.030	-.049					
(4) Return on Asset	.050	.112	-.151*	-.025	.078				
(5) Return on Equity	.056	.134	.055	.170**	-.170	.256			
(6) Price Earning Ratio	10.648	19.767	-.056	.181**	.244***	.224**	.227**		
(7) Firm age	10.206	9.166	.288**	-.118	-.018	-.103	-.065	.056	
(8) Industry sectors	2.510	1.396	.050	.015	.007	-.039	-.204**	-.139	.131*

C. Combined boards: Main Board and Second Board

Variables	Mean	SD	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) CEO duality	.434	.497							
(2) Board composition	.640	.202	-.357***						
(3) Board size	8.576	2.390	-.177**	.055					
(4) Return on Asset	.057	.106	-.094*	.015	.062				
(5) Return on Equity	.056	.282	-.018	.051	.073	.524			
(6) Price Earning Ratio	27.433	46.186	-.037	.084	.156**	-.033**	-.006***		
(7) Firm age	18.531	14.749	-.109*	.153**	.008	.062	.114*	-.028	
(8) Industry sectors	3.571	2.432	-.053	.313***	.131**	-.054	-.072	.171***	.245**

*** significant at 1 % level ; ** sign ificant at 5 % level; * significant at 10 % level

Table 2 shows the descriptive statistical analysis such as means, standard deviations, and Pearson Product-Moment Correlations of the variables. While Table 3 shows the MANOVA analysis for the three sample groups before and after controlling for age and industry. We use Wilks' Lambda multivariate tests of significance to indicate whether there are statistically significant differences among the groups on a linear combination of dependent variables. Tabachnick and Fidell (1996) recommend Wilks' Lambda for general use in MANOVA analysis.

In the first hypothesis we suggest that the incidence of CEO duality will be associated with lower firm performance. The effects of multiple relationships between CEO duality and the three organizational performance variables before and after controlling by age and industry are not significant for all three groups of samples. Thus, hypothesis 1 is not supported.

Table 3. Wilks' Lambda coefficients of MANOVA analysis

Variables	Value	F-statistic	p-value	R squared
A. Main board (uncontrolled)				
Constant	.412	16.145***	.000	R^2 = .676
CEO duality	.847	2.050	.125	
Board composition	.091	1.553**	.018	
Board size	.294	2.483***	.001	
B. Main board (controlled by age and industry sectors)				
Constant	.880	1.450	.247	R^2 = .689
CEO duality	.899	1.199	.326	ΔR^2 = 0.013
Board composition	.081	1.568**	.017	
Board size	.272	2.524***	.001	
Firm's age	.932	.773	.518	
Industry sector	.927	.844	.480	
C. Second board (uncontrolled)				
Constant	.576	10.558***	.000	R^2 = .514
CEO duality	.964	.536	.660	
Board composition	.377	.756	.896	
Board size	.834	.674	.773	
D. Second board (controlled by age and industry sector)				
Constant	.777	3.925**	.015	R^2 = .487
CEO duality	.977	.318	.812	ΔR^2 = .027
Board composition	.393	.686	.954	
Board size	.830	.660	.786	
Firm age	.965	.499	.685	
Industry sector	.919	1.197	.323	
E. Combined of main board and second board (uncontrolled)				
Constant	.753	11.682***	.000	R^2 = .473
CEO duality	.986	.506	.679	
Board composition	.320	1.377**	.017	
Board size	.904	.524	.960	
F. Combined of main board and second board (controlled by age and sector)				
Constant	.915	3.239**	.025	R^2 = .459
CEO duality	.988	.435	.729	ΔR^2 = .014
Board composition	.324	1.336**	.029	
Board size	.890	.594	.922	
Firm age	.949	1.890	.136	
Industry sector	.956	1.624	.188	

*** significant at 1 % level ; ** significant at 5 % level; * significant at 10 % level

The second hypothesis suggests that the proportion (composition) of outside directors will be associated with higher firm performance. For main board and combine boards the results are significant at 5% level even before and after controlling for age and industry. But, it is not significant for second board before and after controlling by age and industry. Thus, hypothesis 2 is partially supported since the result for small size firms (second board) is not significant.

Finally, the third hypothesis suggests that the greater number of total directors (board size) will be associated with higher firm performance. The result for main board is significant at 1% level even before and after controlling for age and industry. But, for the second board and combine boards, the result is not significant. Thus, hypothesis 3 is also partially supported. The results can be summarized as follow:

Based on these results, it can be concluded that control variables, age and industry, do not contribute and do not affect significantly the relationships between CEO duality, board composition, and board size and organizational (firms) performance. We summarize the results of these tests on Table 4 as follows:

Table 4: Summary of significance test of CEO duality, board composition, and board size

Boards/Variables	CEO duality	Board composition	Board Size
Main Board:			
Uncontrolled	not significant	significant	significant
Controlled	not significant	significant	significant
Second Board:			
Uncontrolled	not significant	not significant	not significant
Controlled	not significant	not significant	not significant
Combined:			
Uncontrolled	not significant	significant	not significant
Controlled	not significant	significant	not significant

DISCUSSION

CEO Duality

The results of this study offer some important insight regarding the effect of CEO duality, board composition, and board size on organizational performance specifically financial performance e.g., return on asset (ROA), return on equity (ROE), and price earning ratio (PER). Based on the insignificant results for all main board and second board companies given on table 3, we conclude that there is a tendency for Malaysian's firms to adopt CEO duality structure since the dual structure does not have any association with lower performance. Our findings are consistent with those reported in England where legally mandated separation of the chair-person and CEO has not been found to have any significant impact on firm performance (Chief Executive, 1989).

Even though most literatures (Fama & Jensen, 1983; Jensen & Meckling, 1976; Dalton & Kesner, 1987 and Weir et al., 2003) suggest the separation of this dual function, this study shows otherwise. One of the probable reasons is may be because most of previous research is done in developed countries. But, in developing country like Malaysia, the organizational culture and environment could be one of the determinant factors that influence the result. The CEOs and directors in developing country may be are less constrained by organizational systems and structures as compared to developed country such as the United States and United Kingdom.

Although organization theory helps explain the general case of CEO duality, agency theory does have an explanatory power under specific circumstances, specifically in Malaysian companies. Certainly, one approach in agency theory to this is to separate the CEO from the chairperson of the board. But in Malaysia, we assume that under this structure, the founder of the companies becomes chairman and CEO of the firm could maintain presence as chairperson, but the CEO would have operational authority and does not have much influence on firm's performance.

Board Composition

One of the main purposes of this study is to test whether a relationship exists between board composition and the organizational performance. The second hypothesis that the proportion of outside directors will be associated with higher firm performance is supported only for main and combine boards, proxy for large size firms as suggested by Molz (1988), Borokhovich et al. (2001) and Klein (2002). The result is not significant for the second board, proxy for small size firms which is consistent with study done by Schmidt (1982) but contrary to study done by Daily & Dalton (1993).

Although this study suggests a relationship between board composition and performance (specifically on main board and combined board), there remains some question about what aspects of outside directors lead to this association. It is mentioned earlier that an increase in performance might be a function of the expertise brought to the company by outside board members or a function of the companies' attempts to manage interdependence by appointing outside directors. These factors are not mutually exclusive and the observed effects may be some function of board. Perhaps better performing companies have a systematic tendency to select a higher proportion of outside board members. The continuing controversy over the merits of various board compositions, the effects of board composition on organizational performance and other outcome variables may be fruitful areas of future research.

Board size

Board size is hypothesized to be associated with higher firm performance. In this study, the effect of board size on firm performance is only significant for main board, proxy for large size firms and not significant for combine boards, proxy for developing country. We conclude that large size firms in general are expected to have large size board (Chaganti et al., 1985) and have better performance. Using sample from developing country such as Malaysia would then give insignificant results in terms of the effect of board size on firm performance compared to study done in developed countries such as US and UK. This finding provides some evidence that need further evaluation by future researchers to find a probable reason for this mixed result.

The result for second board as proxy of small firms is not significant which is contrary to findings by Daily and Dalton (1993). We suggest that an effective means for overcoming the liability of size is through the inclusion of outside directors. The expertise and resources kept by these individuals may counter any disadvantages experienced as a result of the modest resource base experienced by many small firms.

CONCLUSION

This study examines the effects of CEO duality, board composition and board size on organizational performance of Malaysian Bourse listed companies. We compare the effects of CEO duality, board composition and board size on organizational performance on main board as proxy for large companies, second board as proxy for small companies, and combined main board and second board as proxy for developing country. Our findings are consistent with some past studies and not consistent with some of the previous research done in developed countries.

This study has several limitations. A potential limitation lies in the selection of the firms. We only employ 96 firms of main board and 100 firms of second board. The sample firms examined in this study, therefore, constitute a small population. Publicly traded corporations may not be representative of those corporations not publicly traded or those small firms who voluntary elect to utilize a board of directors. These firms do, however, provide a sensible sample of firms for initial explorations of the firm governance structure or performance relationship. Another limitation is that we do not control for size as it is may be one of the potential confounds in this study. Future research should consider size as control variable since the data used involve large firms and small firms. We propose that future research should consider more than one-year period to assess organizational performance because the proportion of directors is unlikely to substantively affect the performance of an organization in the short run. It does seem reasonable, however, that the posited benefits of outside directors should become evident over time (Kesner and Dalton, 1985).

The listed companies of KLSE (now is Bourse Malaysia) are selected because comparable data for those corporations not publicly traded and private firms are not readily available. Additionally, the independent variables in other than publicly trade corporations may be insensible for examinations of this nature. Because control appears to be at issue, it is likely that little or no variability will exist in the number of outside directors.

There remain other theoretical as well as empirical issues. This study relies on selected sample of KLSE listed companies which encompasses firms of a variety of board structure and firms performance. Future research should be more selective on these dimensions. Not only may firms operating under those conditions have different

proportions of CEO duality or independence structures, but the choice of structure may impact performance differently as well. Fama and Jensen (1983) have noted that CEO duality likely signals the absence of separation of decision management and decision control. These results, therefore, may provide empirical support for some strongly worded admonitions about governance structure that includes the same individual serving simultaneously as CEO and board chairperson of a firm.

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