

Governance: An International Perspective

Diane K. Denis and John J. McConnell (Eds)

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Governance: An International Perspective is a two-volume collection of articles published in academic journals, and is part of a series called 'Corporate Governance in the New Economy', comprising seven other books about several aspects of governance: Auditing, Ownership, Life Cycle of Corporate Governance, Political and Legal Perspectives of Corporate Governance, Governance & Expropriation, Governance in the Public Sector, and Directors & Boards. As other collections of articles, the book is oriented mainly towards academics, although it could also be of interest to students of accounting, finance, business or economics, and also to practitioners.

The two volumes contain 36 articles about several issues regarding governance in an international context. The articles have been published between 1990 and

2003 in prestigious research journals: *Journal of Financial Economics* (13 articles), *Journal of Finance* (9), *Journal of Political Economy* (3), *American Economic Review* (2), *Federal Reserve Bank of New York Economic Policy Review* (2), and one article from: *Journal of Financial and Quantitative Analysis*, *Journal of Corporate Finance*, *Economic Journal*, *Journal of Economic Literature*, *Journal of Economic Perspectives*, *Journal of Banking and Finance* and *Journal of Accounting and Economics*. The authors group the articles into seven different topics: Boards of Directors, Executive Compensation, Ownership and Control, Ownership Change Via Privatization, The External Control Market, Legal Systems & Corporate Governance and Financial Markets & Economic Growth. Although most of the articles have an empirical orientation, they also include four literature reviews. In the first volume they include what they call ‘first generation studies’, where they focus on studies that address questions regarding corporate governance and their relation to managers’ decisions and firm performance, without an explicit international setting. This, in a way, is something that surprised me as I was browsing through the papers in the first volume, as it did not respond to what I was expecting given the title of the book. In the second volume, they concentrate on what they call ‘second generation studies’ where the papers have a clearer cross-country perspective.

Given that this review is to appear in an accounting journal, probably the question to answer here is what the usefulness of this book is for accounting academics. And in answering this question, one must say that the book – although of great interest to an accounting audience – does not directly address accounting issues. Only one out of the 36 articles included in the book was published in what one could consider as a completely accounting-oriented journal, and the topics covered by the articles, although with many applications to accounting, do not directly answer accounting research questions. However, this should be viewed as a positive and very valuable characteristic of the book for accounting researchers, as the articles will help to identify interesting accounting questions related to governance structures, which have not been previously answered in the accounting literature. It also highlights an important point: that the relation between corporate governance and accounting numbers in an international setting is a forgotten stream of accounting research.

Research on the relation between governance mechanisms and accounting numbers is limited. Bushman and Smith (2001) and Sloan (2001) provide comprehensive literature reviews (not included in the coverage of the book) concluding that accounting researchers have failed to use their comparative advantage (vs. researchers in finance, business or economics) to investigate the different roles that accounting numbers play in corporate governance mechanisms. As pointed out by Sloan (2001), most of the accounting research on corporate governance has focused on managerial compensation. The relation between board characteristics (and also audit committees) with accounting numbers has also been studied. However, the role of accounting information in the other five corporate governance areas treated in the book (ownership and control,

privatisations, the external control market, legal systems, and financial markets and economic growth) has not received much attention from accounting researchers, and the analysis of the relation between corporate governance mechanisms and accounting numbers in an international context has been completely neglected.

Consequently, the role of accounting numbers on the issues on international governance identified by Denis and McConnell provides interesting research opportunities for accounting academics. For example, regulators are forcing firms to implement governance mechanisms to avoid accounting scandals. However, it is not even clear whether good governance and higher quality accounting numbers are positively correlated. Bushman *et al.* (2004) argue that good governance and good quality accounting numbers are substitutes. Others, like García Lara *et al.* (2006), take a different approach and show that there is a positive relation between better governance and the quality of accounting information. The effects of governance mechanisms will probably differ with the institutional settings, and mechanisms that can be useful in a certain setting to improve financial reporting might not be appropriate in other settings.

Overall, the papers contained in the two volumes can help accounting researchers to identify the key issues of interest in mainstream research in corporate governance. From this starting point, they will be in a better position to discover new researcher opportunities regarding the relation between corporate governance mechanisms and accounting numbers. The international differences in accounting quality, together with the differences in managers' incentives to manage earnings in different ways responding to the different international institutional frameworks, provide a reach setting to analyse how accounting numbers are used in corporate governance mechanisms. Also, and with this international setting in mind, accounting researchers should explore how governance mechanisms can be used to control accounting choice and to obtain better quality accounting numbers, all of this with the objective of reducing agency costs.

References

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