

An Empirical Study on the Impact of Information Disclosure Quality of Listed Companies on the Resignation of Independent Directors

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Abstract. In recent years, there have been frequent scandals of financial information falsification in listed companies, independent directors have been held jointly and severally liable for large sums of money, and the recent wave of resignations of independent directors has led to extensive consideration by scholars. This paper is based on a comparison of the resignations of Kangmei Pharmaceutical and a comparative analysis of the resignations of independent directors of two companies, Dalian Shengya and Shougang Hotel. It is concluded that the correlation between disclosure quality ratings and independent director resignations is negative. It can therefore be inferred that the level of disclosure practiced by listed corporations is a decisive factor in the resignation of independent directors, which leads to further recommendations on the system of independent directors.

Keywords: Independent Directors; Quality of information disclosure; Reputation.

1. Introduction

1.1 Background and significance of the study

1.1.1 Research Background

On 12 November 2021, the Intermediate People's Court of Guangzhou ruled against Kangmei Pharmaceutical in the financial fraud case, awarding Kangmei Pharmaceutical 2.459 billion yuan in compensation for investment losses to 52,037 investors, while requiring five former or current independent directors to bear joint and several liabilities of 5% to 10%, involving a total joint and several compensations of approximately 369 million yuan, which would amount to 123 This is the first case in the country in which a securities group has sued for damages. This is the first case of securities group litigation in the country, signifying that the days when independent Listed company directors in China used to be free from civil liability to public investors are gone. [1] The "Kangmei Pharmaceuticals case", in which independent directors were held jointly and severally liable for misrepresentation by the company, stirred up a thousand waves and led to the resignation of independent directors, triggering a great deal of concern and heated discussion in the practical and legal communities of listed companies.

As an indispensable member of the board of directors of a listed company, an independent director should play a supervisory role in the standard of disclosure of information and take responsibility for the truthfulness of information disclosure, so the quality of information disclosure can affect whether an independent director resigns or not. In addition, the purpose of introducing the independent director system in China is to use the professional knowledge and experience of independent directors to monitor the accounting information of enterprises and ensure the truthfulness of accounting information disclosure.

1.1.2 Research significance

In recent years, there have been many scandals involving fraudulent disclosure of information by listed companies, and as a result, independent directors have been held jointly and severally liable for large sums of money, so it is of great significance to study whether the quality of information

disclosure will lead to a wave of resignations of independent directors, and it is also worthwhile to analyze and study the factors influencing independent directors' resignation. The study of the impact of independent directors on their quality will help to identify potential problems in advance through the professional knowledge and industry experience of independent directors and take appropriate proactive preventive measures before irregularities in accounting information disclosure occur. Ultimately, the goal of raising the standard of accounting information disclosure for Chinese listed firms will be accomplished.

1.2 Research ideas and framework

1.2.1 Review of the literature

Scholars at home and abroad mainly explore the functions of independent directors in corporate governance from two aspects: supervision and consultation. Based on the principal-agent theory, Fama and Jensen argue that independent directors, due to their externalities and independence, can effectively supervise the management's business behavior of the company and are an effective system to solve the agency problem between shareholders and management.

Ieetal, Shi Chunling and Wang Miao and other studies found that the good educational background and professional background of independent directors can help independent directors give full play to their advisory function, provide advice on the strategy formulation and investment decisions of enterprises, and have a better supervisory role on the quality of information disclosure.

Some domestic scholars have another "questionable voice" about the functions played by independent directors in China. Li Ming and Li Enzhu and others found that independent directors can enhance the overall independence and professionalism of the board of directors by monitoring and reviewing or providing professional advice, thereby achieving the purpose of risk avoidance and ensuring the truthfulness of information disclosure. Cao Chunfang et al. found through an empirical study that off-site independent directors' lower board attendance and access to information: led to a failure to perform their duties and thus the company's overinvestment was damaged the value of the company. [3]

Jaggi, Chen, Persons, Kelton, Andrea, and Md. Borhan Uddin Bhuiyan also found that the more independent directors there are on the board of directors, the higher the quality of accounting information disclosure. A study by Jaggi, Chen, Persons, Kelton, Andrea, and Md.

By combing through the existing relevant literature at home and abroad, it can be found that although scholars have conducted extensive research on the functional aspects of independent directors, whether the resignation behavior of independent directors is related to the information disclosure behavior of listed companies, these have not yet reached a unanimous conclusion. This article contends that there is a significant knowledge gap between investors and publicly traded corporations, and information disclosure is needed to prevent adverse selection and moral hazards caused by information asymmetry. In reality, most independent directors accept the position of independent directors because of their financial income, reputation, social status promotion, etc. They lack the discipline to tide over the difficulties with the company, and it is also difficult to access the comprehensive information disclosure of the company, and sometimes they are even unaware of the possible falsification of the information disclosure they have obtained, so most of them will choose to resign to avoid the harm to themselves when the company has problems. Therefore, it is worth studying whether the research on the information disclosure quality of listed companies has an impact on the resignation of independent directors.

2. Theoretical foundations

2.1 Principal-agent theory

Jensen and Meckling add that the owner of the business needs to hire a professional manager to run the business, while the ownership of the business remains with the owner and the right to claim

the residual value. The owners of the business are required to hire a professional manager to run the business, while the ownership of the business remains with the owners and they have the right to claim the surplus-value. The owners enter into a series of contracts that create an agency relationship between them. The shareholders of the business, as owners, aim to maximize the value of the business. Professional managers, on the other hand, do not have access to surplus value compared to the shareholders of the firm and are therefore more concerned with maximizing their benefits. Fama and Jensen add to this theory by suggesting that managers seek higher incomes, a better office environment, and more leisure time. When faced with the decision to take risks, managers will choose the level of risk that is favorable to them to avoid damage to their interests.

Bebchuk et al. argues that the development of capital markets has been accompanied by an inadequate system of protection for investors' interests, which has given rise to a proxy problem between major and minor shareholders. When there is no effective supervision of the majority shareholders, the majority shareholders may expropriate the interests of the minority shareholders out of their interests. And because the majority shareholder has more decision-making power, managers may conspire and act in ways that harm the interests of minority shareholders.

3. Definition of relevant concepts

3.1 The concept of independent directorship and the reasons for resignation

The independent director system optimizes the corporate governance structure. The Board of Directors consists of nine directors, three of whom are independent and composed of economic, financial, legal, and accounting professionals, respectively, holding important positions and serving on specialized committees. Independent directors play a full role in overseeing corporate governance and internal controls, and the Audit Committee of the Board of Directors, in coordination with auditors and company departments, makes management Proposals to help companies improve corporate governance and internal management in a targeted manner.

However, there have been numerous scandals in recent years when the financial information of Chinese listed firms has been disclosed in a way that is blatantly contradictory to the reality of the situation, such as the Kangmei Pharmaceutical and Jinya Technology cases. The majority of small and medium-sized shareholders' interests can be significantly impacted by the quality of information disclosure, which is why the system of independent directors was established. The rate of information disclosure violations of listed companies gradually decreased in the early 21st century and then started to increase, as shown by statistics of violations of listed companies in Shanghai and Shenzhen. As a result, it is crucial to control the quality of information disclosure, and independent directors, as significant figures in the internal governance of the company, bear the significant responsibility of directing the disclosure of financial information. Current research focuses on how independent directors' resignations affect listed firms' information disclosure quality. Using empirical research, we can examine how independent directors' performance affects the quality of accounting information disclosure. Descriptive statistics, correlation analysis, and regression analysis are all included in the empirical investigation. Through the empirical analysis, we can conclude that independent directors need to participate in company meetings frequently to obtain more information to provide more useful suggestions for better performance of their duties, which will also improve the quality of information disclosure of the company. The main objective of this paper is to analyze how to improve the quality of accounting information disclosure of listed companies in China. Accounting information disclosure by listed companies is an effective safeguard to promote the orderly operation of the capital market and safeguard the interests of investors. This paper studies the impact of independent directors on its quality, which is conducive to detecting potential problems in advance and taking corresponding active preventive measures through the professional knowledge and industry experience of independent directors before accounting information disclosure irregularities occur; it is conducive to better monitoring the behavior of managers from the perspective of improving the independent director system, thereby reducing the phenomenon of enterprises disclosing false

information and whitewashing financial statements. Ultimately, the purpose of improving the quality of accounting information disclosure of listed companies in China will be achieved. [7] Finally, some practical suggestions can be made based on the findings of the empirical study, such as further improving the remuneration system of independent directors and improving the selection and appointment mechanism of independent directors.

3.2 The meaning and role of information disclosure

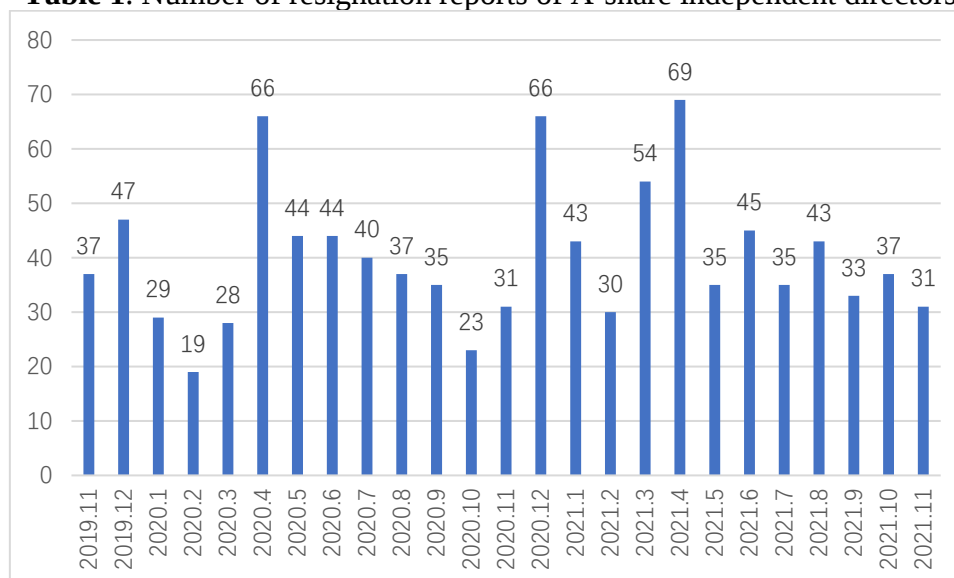
There is a significant information asymmetry between investors and publicly traded companies, and information disclosure is required to avoid adverse selection and moral hazards caused by the asymmetry. In reality, the asymmetry between the risks and benefits borne by independent directors is highlighted, and the responsibilities and risks borne by independent directors are externalized, which will awaken the independent directors' awareness of their rights, responsibilities, and risks, and they will resign to defend their rights. For example, the Kangmei Pharmaceuticals scandal forced independent directors to bear a massive amount of joint and several liabilities, even though most independent directors' salaries in listed companies are far less than one-thousandth of the amount of punishment. This phenomenon of risk and inequality of benefits merits further investigation, and will also promote the improvement of independent directors' performance and the level of information disclosure.

The verdict in the Kangmei Pharmaceuticals case, in which the independent director assumed joint and several liabilities of more than 100 million yuan, immediately sparked a heated debate on the profession and system of independent directors from all sides of the market, highlighting the significant demonstration effect of the Kangmei Pharmaceuticals case, which will make listed companies and independent directors think deeply, and from which it can be concluded that It is worthwhile to conduct an analysis and come to the conclusion that the quality of information disclosed by a publicly-traded company is too risky and of dubious authenticity, which may lead to independent directors not believing in the financial position of the company and lead to the resignation of independent directors.

4. A comparative study on the resignation of independent directors of listed companies

Since the advent of independent directors in China at the turn of the twenty-first century, research on independent directors has concentrated on the effects of independent directors on the governance of publicly traded companies, the market response, and the causes of and behaviors associated with independent directors' resignations. Numerous empirical studies have demonstrated a negative correlation between the resignation of independent directors and the effectiveness of corporate information disclosure. In addition, the scholar Tang Qingquan et al. pointed out in 2007 that independent directors tend to have a proactive risk-averse attitude. Therefore, we will compare the resignation of independent directors of listed companies at both general and specific levels. We will first compare the trends in the number of resignations of independent directors of listed companies before and after the fraudulent disclosure case of Kangmei Pharmaceuticals, and then we will select two companies to compare the quality of their disclosure and the resignations of their independent directors.

Firstly, we will take the case of Kangmei Pharmaceutical's fraudulent disclosure case, which caused significant joint and several liabilities to independent directors, as a time point for the resignations of independent directors before and after the time point, as shown in the table below.

Table 1. Number of resignation reports of A-share independent directors


The statistics show that 45 independent directors of listed companies resigned in the month following the Kangmei Pharmaceutical case. Comparing the data in the table with previous years, we can see that the number of 45 resignations is not the highest ever, but compared with the number of around 30 resignations in the previous three months, it shows that the Kangmei Pharmaceutical case has given a certain impetus to the increase in resignations of independent directors.

In addition, we will compare the resignations of independent directors between two listed companies with different disclosure quality. After a series of screenings, we have selected two companies for comparison, Dalian Sunasia, and Btg Hotel, where we have selected data from the CSMAR database, except for the resignations of independent directors which were manually extracted by team members from the WIND database.

Table 2. Btg Hotels' Resignation data and evaluation data

Btg Hotels	
Information disclosure quality evaluation	A
Percentage of independent directors	37.5%
Number of independent director who esigned	0

Table 3. Dalian Sunasia's Resignation data and evaluation data

Dalian Sunasia	
Information disclosure quality evaluation	C/D
Percentage of independent directors	33.3%
Number of independent director who esigned	3

Based on the aforementioned table, we can deduce that, for a given percentage of independent directors on the board, listed companies with better disclosure tend to have independent director resignation rates that are lower, which makes sense given that independent directors typically have a risk-averse mindset. It has been discovered that the independent directors' resignations have a negative impact on how well-listed corporations disclose their financial information. Good quality of information disclosure will reduce the resignation rate of independent directors.

5. Conclusion

Independent directors are the calling card to ensure the independence, impartiality, and standardized operation of a company's board of directors and are an important factor influencing investors to make investment decisions. A comparative analysis of two companies, Dalian Shengya and Shougang Hotel, led to the following conclusions: there is a negative correlation between the quality of information disclosure and the resignation of independent directors, and there is an asymmetry between the risks taken by independent directors and the benefits received, with most independent directors being unwilling to take the maximum risk for a very small benefit. In addition to this, independent directors may choose to resign early in order to protect their reputation when they anticipate the imminent disclosure of unfavorable news about the company, or when they expect the company to perform poorly in the future. Independent directors with higher reputational capital are more likely to resign early when they anticipate a decline in the company's future performance.

The quality of information disclosure by listed companies needs to be monitored by independent directors, and our group believes that the link between information disclosure and independent directors should be strengthened so that the vice of information asymmetry does not develop, resulting in independent directors being in a state of ignorance when a scandal of disclosure falsification occurs in a listed company, and then carrying huge joint and several liabilities, which is a possible direction for our future research.

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