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## The Relationship between Corporate Governance and Profitability: A Study in Borsa Istanbul, Turkey

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### Abstract:

*Interest in the concept of corporate governance has increased dramatically in recent years, especially after scandals and crises in major international companies around the world, and also, profitability is one of the most important things that companies and their shareholders care about, as it is the criterion that shows the success and efficiency of management in leading investment, and profitability is the main goal of any An investor in any investment, as the biggest concern for any investor is to get the largest possible return on his investment. Therefore, work has been done through this study to discuss these two important concepts in one research, by studying the relationship between them, and corporate governance was considered as the independent variable and profitability as the dependent variable. The study was carried out on the companies listed within the corporate governance index at the Borsa Istanbul in order to ensure the existence of a relationship between corporate governance and profitability.*

*For the purposes of completing the study, statistical processes were used, such as regression analysis, ANOVA analysis, and correlation analysis. The study sample included 43 companies listed in the corporate governance index that have a corporate governance rating for eight years from 2013 to 2020, as the corporate governance index It currently contains 52 companies, but not all companies have ratings for eight years, as some of these companies are recent in the index.*

*Through the use of the SPSS statistical program in data analysis, the result of the study was that there is no clear and direct statistical relationship between corporate governance and corporate profitability.*

*At the end of the study, the researcher made some recommendations, the most important of which is the necessity of obligating all companies on the Borsa Istanbul to conduct an evaluation of their governance by recognized rating companies, because of the great impact of governance on companies' commitment to disclose transparently and not to manipulate and fraud with information and data, and recommended that studies Others on the relationship of governance with other non-profit matters in order to show the impact of governance on companies, and it was recommended that companies, shareholders and stakeholders continue to be educated about the importance of governance and work to benefit from the experiences of all countries and to draw lessons from the results that reached its application.*

**Keywords:** CG, P, CGR, PR

### 1. Introduction

Corporate governance is one of the modern concepts that should be applied by companies because of its importance in management and protecting the rights of shareholders and stakeholders, especially after the collapse of some giant companies in the United States of America and other countries, as a result of their use of complex accounting methods in order to conceal the loss and tamper with the rights of shareholders and stakeholders which led to the release of the Sarbanes Report, issued by the US Congress in 2002.

The concept of corporate governance represents the contractual relationship between the various parties, while others see from an accounting point of view that it focuses on how to maximize profitability and the value of the economic unit in the long term. Others view it from an ethical standpoint to protect the rights of minority shareholders. This consideration led to the emergence of various concepts of corporate governance (Hlehel and Karim, 2017).

Accordingly, the goal of maximizing profitability is one of the primary goals pursued by profit-oriented activities in general, as maximizing the profitability of these companies helps them to maintain their survival and continuity, support their financial position, and maximize property rights, which increases their ability to face the risks they may encounter, and this is considered The objective is an important tool for judging the efficiency of management and its effectiveness in using the available resources to achieve the highest possible profit.

The significance of corporate governance in global and national economies is becoming more widely recognized as an issue that promotes improved economic growth, financial performance, investment, and shareholder value. and curb conflicts of interest. Therefore, implementation must also only make sure shareholders' rights are protected, fair compensation for all stakeholders, and uphold societal norms also, as well as help enforce and maintain separate tasks on the board of directors.

Corporate governance and profitability relationships will be clarified by this study on the Borsa Istanbul companies, as corporate governance distinguishes between the rights and responsibilities of the board of directors, senior

management, shareholders and stakeholders, and in a way that affects the financial performance and profitability of the company for the better.

### *1.1. Problem Statement*

The problem of the study is the weakness of corporate management in making its decisions in some companies, and its weakness will lead to weak financial decisions for the company, and this leads to poor financial performance, which affects the profitability of these companies. As a result, the problem in this study focuses on the relationship between profits and corporate governance. The study problem revolves around determining corporate governance's effect on the profitability of companies listed on the Borsa Istanbul, and based on the above, the study problem can be formulated through the next most important question:

Is there a statistically significant relationship between corporate governance and the profitability of companies listed on the Borsa Istanbul?

### *1.2. The Importance of Study*

This study derives its importance from the importance of corporate governance in the world and in Turkey in particular, and its impact on profitability, as the success of business organizations is related to the extent to which they achieve profits compared to their competitors, and corporate governance plays a prominent role in this regard, and also contributes to reducing accounting practices innovation, as well as helping companies increase their ability to compete with their counterparts in the market. Where profitability is the primary goal of all organizations, and it measures the efficiency of management in using the resources available to them, so the effort of the financial management in the company is focused on the optimal use of resources to achieve the best possible return for their owners.

The significance of this study is to shed light on the profitability of companies listed on the Borsa Istanbul, specifically those included in the corporate governance index, in order to determine whether companies listed in the governance index have an advantage over companies not included in the index in terms of the existence of a relationship between the application of governance to this Companies and their profitability. In the event that there is a positive relationship between corporate governance and profitability, this study will be of great importance to encourage all companies on the Borsa Istanbul to implement the standards required for the implementation of corporate governance by the Borsa Istanbul in order to enter the companies listed in the corporate governance index.

## **2. Literature Review**

### *2.1. Preface*

In recent decades, many developed and emerging economies have recognized the importance of corporate governance, particularly in the aftermath of economic collapses and financial crises in a number of East Asian countries, Latin America, and Russia in the 1990s, as well as financial and accounting collapses in the United States. That year was the year 2001. With a rising number of countries in the world moving to a market economy, where the majority of economic growth is driven by private companies, corporate governance has become more important (Abu Al-Hajj, 2013).

Corporate governance is frequently mentioned in accounting literature, as it has recently emerged as a major factor in improving business, investment, and financial performance. In response, new systems have had to be implemented in departments across the business in order to uphold the rights of shareholders, investors, and society (Yan and Steven, 2014). In this chapter, we will clarify some issues related to corporate governance.

### *2.2. The Emergence and Development of Corporate Governance*

The subsequent crises caused by some companies' misleading statements increased the need for companies to develop work and avoid mistakes, such as those that occurred with Enron in 2001, when the giant company fell with assets valued at approximately \$64 billion, and this is the most bankruptcy process for an American company. At present, this has led to a great disappointment in people's confidence in general, due to the share price falling from \$90.75 to less than \$1 per share. In 2004, The World Bank, the IMF, and the OECD all collaborated to research corporate governance models and evaluate their potential efficacy in both emerging and developed markets. This study concluded with the formulation of standards for the corporate governance application, and the extent of its effectiveness in developed and emerging markets, and this study ended with the formulation of 'Principles of Corporate Governance', which are the criteria for applying corporate governance. As it includes specific principles such as (rights of shareholder, shareholder equal treatment, the stakeholder's role, transparency and disclosure, and the board of directors' responsibilities) (Freeland, C., 2007).

These standards were non-binding, and consisted of a set of basic and essential points aimed at providing guidelines for companies to improve and evaluate laws, regulations, and institutions.

And because of what happened in the global financial crisis, on 11/11/2008 the International Accounting Standards Board sent an official letter to the Twenty Summit, in which the heads of states informed the meeting of the importance of the role of the International Accounting Standards Board, as an independent body entrusted with the task of developing unified global standards. In identifying issues arising from the credit crunch. The letter included a detailed explanation of the steps taken to confront the crisis (Al-Qishi, ZahirShaher, 2006).

From here, matters began to take a new course in the field of linking administrative work and the mechanism of decision-making on the one side, and increasing the disclosure required by the principles of corporate governance, to appear in a form that can be announced on the other side, as well as attaching it to the nature of transparency in order to activate all the laws that have been issued. about this.

### 2.3. Reasons for the Emergence of Corporate Governance

The large-scale embezzlement and manipulation that occurred, causing harm to many shareholders and stakeholders and negatively affecting the performance of organizations, governments, and countries, necessitated a pause and consideration of a serious and forthright step to reclaim control, which led to the emergence of so-called corporate governance (Shahwan, 2013).

The following are some of the reasons for the emergence of corporate governance (Al-Azaiza, 2009):

- The disproportion between the performance of companies and the rewards obtained by the management.
- Organizational failure that occurred in many companies in Russia, America and countries of the Asian continent.
- The inability of companies to compete and the threat to their entities as a result of the inability to attract investors and capital.
- Inability of investors to access potential investment opportunities and analyze them properly.
- Inaccuracy in preparing final accounts, as well as a lack of transparency and clarity.
- Unethical practices of corporate boards and their employees.
- Weakness of the board of directors, which may have an impact on executive and senior management, which may have a deficit or shortcoming in their ability to carry out successful management practices.
- Ineffectiveness of internal control procedures that can detect and prevent problems.
- Weakness of external parties and their control over the facility, such as those in charge of setting laws and auditors.
- (Kaddouri, 2012) also indicates that there are other reasons for the emergence of corporate governance, which are:

Weakness of the legal system, with which it is not possible to carry out resolve of disputes and contracts implementation in a good manner, in addition to the low-quality information limits the ability to control and monitor and spreads corruption and distrust.

The emergence of many financial and administrative corruption cases through manipulation and misinformation in the financial reports.

### 2.4. Corporate Governance Concept

The concept of governance aims to clarify the interrelated relationships between all relevant parties and work on their integration. It also defines the policies and procedures related to supporting boards of directors and executive departments in the decision-making process in the business unit, and defines the hierarchy through which goals are set, ways to achieve them, and performance monitoring mechanisms (Hlehel and Karim, 2017).

There have been many opinions in the corporate governance literature about developing a specific definition for this concept, as it is related to and overlaps with a variety of economic, financial, regulatory, and legal fields, and there is no specific agreed definition, whether from organizations and state bodies or writers and researchers, as each definition is unique (Sharia and Al-Barki, 2014), and here are some of them:

- The International Finance Corporation (IFC) defined it as 'the organization of structures and methods is critical to guiding and supervising businesses and determine the distribution of rights and duties among the main participants in the company, such as CEO's, directors, the board of directors and shareholders, as well as emphasizing the policies and procedures related to issues of decision-making related to the affairs of the company.' (Kenza, 2014).
- Corporate governance has also been defined by the Organization for Economic Cooperation and Development (OECD) as 'the laws and procedures that manage and ensure the proper functioning of the company's business, as it clarifies the rights and duties and the mechanism for distributing them among the various relevant parties in the company, such as shareholders and the board of directors, and defines policies and procedures necessary in the decision-making process for the company's matters, and sets the objectives and strategies necessary to achieve them' (Manaseer, 2013).

### 2.5. Importance of Corporate Governance

The liberalization of financial markets as a result of the World Trade Organization agreements led to the opening of international markets, which allowed for huge profits, but it also exposed companies to competition. National business establishments have come to know that they need levels of capital that go beyond the capabilities of traditional sources of financing, to be able to grow and become capable of international competition. Thus, failure to attract sufficient levels of capital will threaten the very existence of the company. Furthermore, companies that are unable to attract capital risk becoming relegated to selling and supplying to multinational corporations on a global scale. Which leads to fear of the negative repercussions-as a result of the weak added value that companies achieve in relation to their products in this way-on the entire economies of the countries 'use in their modern forms'. The response came from the market control mechanism through the disclosure that the companies demanded, on the basis of which it gives a clear picture of the future market direction, and thus the possibility of imposing national controls (such as limiting market dumping and subsidies of all kinds...). Thus, governance has given a new dimension to international trade, represented by a vision of the various aspects surrounding corporate business strategies.

As a result of the great suffering that most companies in East Asia and the USA have faced recently due to financial and administrative difficulties, the concept of governance has received great attention from companies around the world, and it was discovered that the lack of corporate governance style can help those in charge of the company from within -

whether they are the board of directors, managers or public servants - from prioritizing their own interests over the interests of shareholders, creditors, and other stakeholders (Bo Chakhchokha and Ben Tawila, 2017).

Corporate management's interest in corporate governance has increased in order to enhance the reliability of the financial information disclosed in its financial statements to its beneficiaries, specifically shareholders and stock exchange dealers, in order to preserve their interests. In addition, in order for countries to achieve development and societal well-being, there has been an increase in interest in governance. (O Amr, 2014).

In addition, corporate governance measures improve corporate governance by assisting corporate managers and boards of directors to develop a sound strategy for the company, ensuring that mergers and acquisitions are not carried out except for sound reasons called for exclusively by the circumstances surrounding the companies. And to ensure that the systems that govern the determination of salaries, wages, bonuses and incentives reflect performance, that is, adopting the principle of increasing incentives as a result of increasing the company's profitability.

Corporate governance has gained great importance for researchers, shareholders and stakeholders, and this importance can be clarified as follows (Al-Hasnawi, 2018):

- The application of sound governance rules leads to evaluating share performance and maximizing profitability, generating confidence among investors and shareholders, and increasing the organizations' long-term ability to compete, given the transparency enjoyed by these companies in their transactions, accounting procedures, and financial auditing in all company transactions.
- The growth of shareholder wealth, and the increased competitiveness of firms in the global financial markets, particularly in the context of coordinating the development of new financial tools and mechanisms, and the emergence of acquisitions and mergers or sale of the main investor.
- Implementing the rules of governance gives companies greater ability to obtain the necessary financing, reduce capital costs, achieve better performance, and satisfactorily treat different categories of stakeholders.
- Implementing good corporate governance mechanisms is a possible solution to each agency's problem and reduces its costs.
- Avoid falling into accounting and financial problems, in a way that supports and stabilizes the activity of public companies in the economy.
- Providing protection for stakeholders, and preserving the rights of shareholders, especially the minority of shareholders.
- From the above, we can conclude that corporate governance is of great importance, represented in its great role in determining the foundations of the relationship between the stakeholders in the company, achieving justice and equality among them, ensuring shareholders' rights, and thus increasing investor confidence, attracting local and foreign investments, and reducing the cost of financing, and this in turn is due to benefit the economy of the entire country.

## 2.6. General Principles of Corporate Governance

The Organization for Economic Cooperation and Development (OECD) is one of the first organizations to discuss and research the issue of corporate governance. It issued (Principles of Institutional Control) in 1999, then in 2004, developed corporate governance principles, which have since been adopted by the majority of countries. (Yamen and Al Ramhi, 2016), and then, in April 2015, these principles were discussed at the OECD/G20 forum for corporate governance. After this forum, these principles were adopted by the OECD on July 8, 2015, and thereafter These principles were presented to the leaders of the Group of 20 on November 15-16, 2015 in Antalya, where they were approved and called the Principles of OECD/G20 Corporate Governance.

The objectives of these principles are to provide support to those responsible for setting policies in assessing and developing the legal, institutional and regulatory system for corporate governance, with the aim of enhancing economic efficiency, financial stability and sustainable growth. Basically, this is achieved through good incentives for executives, members of the board of directors, shareholders and all stakeholders, provided that this is done within the controls stipulated in this regard. The following is a review of the most important aspects of the new principles of governance (Federation of the Arab Securities Authority, 2015):

- The first principle: Assuring the existence of a general and effective corporate governance framework:

The importance of an effective corporate governance framework lies in encouraging companies to raise the degree of efficiency and transparency, clearly defining responsibilities for supervision and governance, and working to develop the governance structure, taking into account its impact on performance, in order to oblige all parties to implement laws, whether at the partial or total level. In addition to achieving integrity and efficiency in the markets, Compliance with legal and regulatory requirements in the practice of governance requires that the legislation clearly specifies the division of responsibilities between the different frameworks in the company while ensuring the achievement of the interests of the public, with the resources necessary to carry out its duties in a professional and objective manner (Suleiman and Muhammad, 2006).

- The second principle: Protecting the rights of shareholders:

As the financial markets seek to accumulate small savings and direct them to financing the activities of listed companies, the success of the market in this field lies in its ability to attract investors, which guarantees liquidity in the financial market, and for this reason, the rules of governance focus on protecting the rights of shareholders through the establishment of controls and mechanisms that shareholders enjoy ownership rights, access to all company information, actively participate in the meetings of the general assembly, vote on its resolutions, as well as any unusual operation that

affects the company's infrastructure. Also, the need to disclose the capital structure and the arrangements that enable some shareholders to obtain a degree of control that affects the company's policy, as well as giving them the opportunity to exchange consultations on issues related to their ownership rights to prevent abuse (Suleiman and Muhammad, 2006).

- The third principle: Fair treatment of shareholders:

Equality in the treatment of all shareholders is one of the most important governance controls, including the rights of minorities and the rights of foreign shareholders, and shareholders must receive adequate compensation in the event that their rights are exposed to risks.

- Fourth principle: The role of stakeholders in relation to the rules governing governance:

To find out the role of stakeholders in their contribution to finding different ways to secure the flow of external and internal capital to companies, whether in the form of property rights or credit, as well as the effective role of stakeholders and the company in its financial and administrative continuity. This is done by respecting the rights of stakeholders as defined in the internal and external laws of companies, and encouraging effective cooperation between companies and company stakeholders to create jobs and provide continuity for financially sound companies.

- Fifth Principle: Transparency and Disclosure (Taleb and Al-Mashhadani, 2011):

The importance of accounting disclosure of the rules regulating corporate governance highlights the rapid and accurate understanding of all data related to the material matters of the company, including the financial and performance position, property rights and corporate governance, in a way that enables shareholders to exercise their rights on a well-studied basis. Where disclosure and transparency help to attract capital and preserve the rights of shareholders, it leads to an increase in confidence between them and the board of directors. On the contrary, the weakness of accounting disclosure and transparency leads to the absence of market integrity, and to the practice of unethical behavior, which increases costs and affects profits.

- Sixth Principle: Board of Directors Responsibilities (Qabajah, 2008):

To determine the extent of the responsibilities of the board of directors, the rules of governance require the development of a set of guidelines to implement the tasks that these responsibilities include:

- Members of the Board of Directors must act in the best interests of the company and its shareholders by working with sufficient information and exercising due diligence.
- That all shareholders are treated fairly by the Board of Directors.
- High ethical standards must be followed, as well as consideration for stakeholders' interests.
- To ensure the integrity of the company's accounts and to disclose all available, correct, and timely information, the board of directors must complete the following tasks: developing a comprehensive strategic plan, supervising and controlling, and making the necessary changes.
- Accordingly, the formation of the board of directors must take into account the element of quality, that is, that its members have the skills and competence that qualify them to deal with various aspects of their ability, to make sound decisions, and to achieve the ability to follow-up and accountability through an effective system for evaluating and reviewing performance and assessing risks.

## 2.7. The Correlation between Corporate Governance and Profitability

The concept of corporate governance is a concept related to the extent to which all institutions serve society and the state, and how the state is promoted through the application of the governance system in all institutions. Generally, the key purpose of the rules of governance is to maintain the survival of companies (Al-Ghazali, 2015).

The previous years have proven the importance of corporate governance, because of its merit in establishing fair rules, laws and foundations in the process of oversight over boards of directors, executive directors, and employees of companies, which contributed to preserving the rights of shareholders and stakeholders, whether they were material rights or not. morale (Shahwan, 2013).

Also, the presence of the founding first generation, the presence of board members with good characteristics and qualities, and the committees emanating from the board, such as the Audit Committee, all of these will positively reflect on the company's operational and financial performance, and on the performance of the shares as well., so that the company's added market value, rate of return on its investments, net profit margin, and operational return on assets are affected. And the rate of return on ordinary shares, And the degrees of vulnerability vary between companies based on the company's sector (Gurbuz et al, 2010).

The study (Kang &Kim, 2011) showed that earnings management practices were minimal in companies with a good governance system, which is also evidence of the positive role of governance on overall performance.

In the researcher's opinion, the main objective of governance is the optimal use of the company's human and financial resources, and it also aims to protect the company's assets and support the creation of competitive advantages, in order to ensure its development and continuity in activity and the recovery of its shares within the financial markets, and thus achieve the interests of the parties related to the company, including maximizing profitability.

## 2.8. Corporate Governance in Turkey

The concept of corporate governance was introduced in Turkey for the first time in 2002 by the Turkish Industrialists' and Businessmen's Association (TUSIAD). Although the research is limited to the Board of Directors, it constitutes the beginning of the corporate governance discussions in Turkey. Corporate Governance Principles, on the other hand, entered legislation after 2003 at the initiative of the Turkish Capital Markets Board. Although the principles based on the principle of 'apply or explain' were not mandatory for publicly traded companies, they consisted of four main

sections and their sub-sections: i) Shareholders, ii) Public Disclosure and Transparency, iii) Stakeholders, iv) Board of Directors (Güray&Başak, 2015).

In order to encourage the implementation of the principles in 2004, the CMB declared that companies trading in Borsa Istanbul are obliged to publish a 'Corporate Governance Compliance Report' together with their annual reports. The report allows companies to publicly disclose their level of compliance with the principles and the reasons for this, in line with the 'apply or explain' principle adopted by the CMB. Shortly after that, in 2007, Borsa Istanbul established the Corporate Governance Index (XKURY) to measure the profitability and income performance of trading companies according to their compliance levels.

With corporate governance gaining great importance for the business world in the international arena, the Investment Advisory Council of Turkey (YDK) established the Investment Environment Improvement Coordination Committee to work for the improvement of corporate governance practices.

In the same period, the OECD published Corporate Governance in Turkey: Pilot Study, which invited the CMB to further develop its corporate governance legislation, while praising all the innovations carried out by the CMB. As a result of all this, the first Communiqué (Serial: IV, No: 41) that mentions the concept of corporate governance was published in May 2008. The Communiqué is important in terms of two major regulations: a mandatory shareholder relations unit for listed companies, and the employment of an expert responsible for compliance obligations with the Turkish Capital Markets Board and corporate governance practices (OECD, 2006).

All these developments gained momentum with the appointment of the Turkish Capital Markets Board as the sole authority for the improvement of corporate governance practices by Decree Law No. 654. This Decree authorized the Capital Markets Board to make certain corporate governance articles mandatory and to detect and prevent violations of the law. With this new responsibility, the CMB published the Corporate Governance Communiqué (Serial: IV, No: 54) in October 2011, which also includes the fines to be paid in case of breach of corporate governance practices. Adjustments were made to the content and timing of the general assembly announcements in order to give shareholders sufficient time to make decisions. In order to prevent possible conflicts within the board of directors and to protect minority shareholders, the practice of Independent Board Members was introduced and made compulsory for companies (excluding banks) trading on BIST 30. With the entry into force of the Communiqué Serial: IV No: 56, this application has been extended to cover all joint stock companies trading (except for the Emerging Enterprises Market and the Custody Market) (Güray&Başak, 2015).

## 2.9. Turkish Principles of Corporate Governance

The principles of corporate governance issued by the Organization for Economic Cooperation and Development are the basic principles applicable in most countries in the world, and Turkey was one of the countries that adopted these principles, as it was based on them that the Capital Markets Board of Turkey issued the Turkish principles of corporate governance in 2003, and the last amendment to them was in 2005.

In the introduction to the principles, the Capital Markets Board mentioned the need for companies to be convinced of these principles, so that they can be applied in a completely voluntary manner. The Board is also keen on the need to disclose all aspects of corporate governance, such as (future plans for corporate governance, and whether all of these have been implemented governance principles or not and disputes resulting from non-implementation) within the annual report of companies. (Ararat & Ugur, 2006).

While the report's summary states that the Capital Markets Board's principles are implemented on the basis of the 'compliance or clarification' principle, the enforcement process is more complex than simply 'compliance or clarification.' Whereas, the principles approved by the Capital Markets Council contain the following (Hacimahmutoglu, 2007):

- Capital Markets Law.
- Turkish Commercial Law.
- All the circulars were issued by the Capital Markets Board.
- Regulations and rules.
- Recommendations are optional, not mandatory.

The principles of the Capital Markets Board consist of four main sections: shareholders, public disclosure and transparency, stakeholders, and the board of directors (CMB, 2003). The first section discusses the principles related to shareholder rights and fair treatment. This section includes topics such as: the right of shareholders to provide them with information and its evaluation, participation in general meetings of shareholders, voting, distribution of profits, and the rights of small shareholders.

In the second section, the principles related to the process of disclosing information of interest to shareholders are presented with high transparency, and work to establish and adhere to the relevant policies.

The third section also focuses on stakeholders. A stakeholder is defined as any party who is involved in the company's activities and objectives. Through this section, the mechanisms and principles that control and govern the relationship between stakeholders and the company are clarified.

The fourth section includes the principles related to the tasks, duties, obligations, processes, board of directors' structure, remuneration. As for the part related to the boards of directors, it clarifies that the boards of directors consist of executive members and non-executive members. Whereas, the executive member is the one who has duties in the company, and the non-executive member is the one who has no duties in the company.

### 2.10. BIST Corporate Governance Index

The Borsa Istanbul, which was founded in the year 1986, is one of the main players in the Turkish capital markets. Since its inception, this market has helped to develop the Turkish capital markets and economy. The name of the market was recently changed to Borsa Istanbul. This market was established on the thirtieth of December 2012, being a stock market, and The Borsa Istanbul brings together all of the Turkish capital markets' stock exchanges under one roof.

The Istanbul Stock Exchange contains several indicators and each of these indicators the company must meet certain conditions to be included, and one of the most significant of these indicators is the BIST Corporate Governance Index (XKURY), which contains companies that have applied the principles of corporate governance.

The BIST Corporate Governance Index is designed to measure the price and return performance of companies traded on the Borsa Istanbul Markets that have a corporate governance rating of at least 7 out of 10 overall and at least 6.5 for each major section.

### 2.11. Profitability Concept

Profitability is defined as the company's ability to earn and achieve profit during its operations in a specific period of time with the least possible risks (Daoud, 2012), or Investments and realized profits are linked together in terms of the relationships they have with one another. Total or partial units, and the profitability of a business is typically measured by how much profit is generated in relation to the amount of sales, or the profit and investments that went into the achievement of those sales (Al-Qaida, 2012).

I also knew that profitability refers to the efficiency of a method in achieving a certain result. If the result is attributed to the company's assets, then the profitability here is economic profitability, but if the result is attributed to the private capital owned, then the profitability here is financial profitability, but if it is attributed to the business number, the profitability here is commercial profitability (Saleh, 2002).

Another defined it as the ability to achieve a return from all commercial activities of an organization or institution, so it indicates the efficiency of the administration and its ability to make a profit using all available resources in the market (Burja, 2011).

In another definition, profitability is defined as the primary goal of all business organizations, and is necessary for their survival and continuity, a goal that investors aspire to, and an indicator that creditors are interested in when dealing with the organization. It is also an important tool for measuring the efficiency of management in using the resources available to it. Finance in the organization is directed primarily towards the optimal use of the resources available to it to achieve the best return for its owners (Levinthal, 2010).

It is also defined as a company's ability to generate profits as a return on invested capital, and it reflects profitability ratios and the company's competitive position, as well as the quality of management and the company's success or failure (Abdul Rahman, 2017).

### 2.12. The Concept of Profit Management

Profit management is used as a measure of the quality of business results, as companies that have profit management have a lower quality of business results (Lee & others, 2005). In other words, profit management reduces the quality of business results. High-quality profits can be defined as permanent, continuous profits that are rich in useful information, and permanence means the ability to remain in the presence of profits in the long term or to be permanent and not transient profits, and continuity means that the profits gained from recurring activities are better quality than those gained from non-recurring activities, Rich in useful information means that there is sufficient information about future profits (Hermanns, 2006) and profits are of high quality when the forecast of the current level of profits is a good indicator of the expected level of profits in the coming years frequently.

It should be noted that management may choose an acceptable and appropriate accounting method or accounting estimate for the company's needs, and that compliance with accounting standards does not always imply that the financial statements are free of manipulation (Saleh & others, 2005), as companies work on managing profits to avoid announcing losses, reducing taxes, and influencing the price of the company's stock. There are extreme cases of profit management, where companies prepare fraudulent financial reports to hide crimes such as bribery, fictitious deals or illegal behavior (Mehmad&Nissim, 2008).

### 2.13. The Role of Corporate Governance in Limiting the Practice of Profit Management

The flexibility available in accounting standards facilitates the practice of profit management by the management of the enterprise and this is evident in many accounting aspects that the management of the enterprise does not hesitate to use as a means to influence the target profit figures that serve its desires and meet its aspirations, and among these aspects is the optional aspect of a basic principle. Accruals, the ability to make accounting estimates, changes in accounting policies, and the ability to disclose certain profit-related matters.

However, despite the space of freedom granted by accounting standards, this does not mean that there are no efforts by standard-setters to reduce this phenomenon, as the efforts of standard-setters to reduce the phenomenon of profit management are:

- The obligation to apply the standards accurately and not to deviate from them, including the disclosure requirements for each standard.
- Determining a specific timing for applying the standards.
- Encouraged the disclosure of optional and discretionary information

However, despite these clear efforts to reduce the opportunistic practices of management, these efforts remain limited, so it is necessary to have other methods and methods to discover the phenomenon of profit management and limit its practice.

Given the flexibility available in the accounting standards that enable the practice of profit management, it was necessary to search for ways through which to confront the phenomenon of profit management, especially after it caused the downfall and bankruptcy of many companies. The principles of governance have been activated, especially those related to the Board of Directors (as the Board is the one who carries out the profit management process), with the aim of limiting earnings management practices and their negative effects on the quality of the company's financial reports. It also makes the company's ability to continue in the future in permanent doubt. The term 'corporate governance' refers to a set of laws, rules, and guidelines that govern the relationship between the company's management and its shareholders and stakeholders, and aims to enhance transparency and appropriate disclosure with greater impartiality and objectivity.

### 3. The Hypotheses of the Study

- $H_0$  = There is no relationship between the Corporate Governance ratio and the profitability ratio.
- $H_1$  = There is relationship between the Corporate Governance ratio and the profitability ratio.

### 4. Data and Methodology

#### 4.1. Description of the Data and Variables Definition

In this section, the specificity of the effect of the governance ratio on the profitability rate will be studied, which will be included in the regression models, as the adopted methodology will study the sensitivity of the characteristics of the corporate governance ratio related to the profitability indicator. The researcher will conduct a performance test on the study sample for companies listed within the BIST CG index at the Borsa Istanbul. Note that the data from the study sample companies, which was obtained from the Istanbul Stock Exchange and from the corporate governance assessment website has been relied upon in order to ensure that the information is highly accurate and error-free.

the variables that will be analyzed through regression analysis, they are two variables: a future variable and a dependent variable, and the corporate governance ratio (CGR) is studied as an independent variable and the profitability ratio (PR) as a dependent variable.

- The Independent Variable: Corporate Governance Ratio (CGR):

Corporate governance is one of the most significant modern concepts that governs and regulates the relationship between stakeholders and departments that manage companies. The degree of corporate governance is measured by authorized rating companies in accordance with the Capital Markets Board's instruction and, to achieve an overall Rating of Corporate Governance, they allocate the following weights to the four main principles: Shareholders: 25% Disclosure and Transparency: 25% Stakeholders: 15% Board of Directors: 35%. Accordingly, the rate of governance assessment for each company is calculated.

The rate of governance was converted into a ratio by dividing the degree of governance obtained by each company by 100 in order to align with the profitability ratio, and the ratio of corporate governance was considered as an independent variable because it greatly illustrates the importance of governance.

The researcher expects that there is a positive relationship between corporate governance and profitability.

- The dependent variable: profitability ratio (PR):

The net profit margin ratio is considered one of the most important ratios for shareholders in terms of measuring the return on their money. It is calculated by dividing net profit by sales, as it is also an evaluation of management's efficiency in leading the company, which is supposed to be strengthened through the application of corporate governance principles, which is assumed to have an effect on the dependent variable in this study, which is profitability.

As a result of dividing the net profit by the sales, the dollar amounts have been converted into a percentage in line with the corporate governance ratio.

#### 4.2. The Research Methodology

In this research, descriptive and analytical statistics will be used to work on studying and analyzing data and verifying hypotheses, and this will be done through the use of the SPSS program in order to verify the existence of an impact of the corporate governance ratio on the profitability ratio. The profitability ratio will be the only dependent variable, and the corporate governance ratio will be the only independent variable.

And the regression equation will be used:  $PR = a + b (CGR)$

Where the equation variables are:

(PR) it basically is the dependent variable.

(A) it basically is alpha (constant) for models.

(CGR) it basically is the independent variable.

As for the research hypotheses, we can say that if the correlation coefficient is  $0.05 \leq a$ . There is a strong statistical relationship between the independent variable (CGR) and the dependent variable (PR).

##### 4.2.1. Regression Analysis

If we have a set of data  $(X_i...Y_i)$  and we assume for some reason that the variables  $x$  and  $y$  have a linear relationship, we can plot the data on a graph and draw a straight line through it. Certainly, the well-known equation for this relationship is  $y = mx + b$ . after that the slope,  $m$ , and  $y$ -intercept,  $b$ , can be reach.

It is not necessary to plot data in order to determine the constants  $m$  (slope) and  $b$  (y-intercept) of the equation  $y = mx + b$  if we expect the data to have a linear correlation. Instead, we can run the data through a statistical procedure called linear regression to find these constants. (Muhamad, 2012).

(The summation indices on  $x$  and  $y$  have been omitted, as have the summation limits, which are 1 to  $n$ .)

According to the enter Method, we will use linear regression to test our hypotheses. We will:

- Use the value of the independent variable to predict the value of a dependent variable.
- Describe how changes in one independent variable affect the dependent variable.

The following are the figures that will be produced as a result of regression analysis:

- R: Correlation coefficient, which indicates the strength and direction of the relationship between the dependent and independent variables.
- R-square: Represents the percentage change in the dependent variable explained by the regression equation, or the proportion of the total variation in the dependent variable explained by variation in the independent variable.

The F-test is a statistical test in which if the null hypothesis is true, the test statistic has an F-distribution. It evaluates the ability of the independent variable to affect the dependent variable. The F ratio is used to determine statistical significance; if the F ratio percentage is significant, it means that the independent variable has a high ability to predict the dependent variable's values. This ratio is considered significant if (sig) F is small, as it is in all statistical tests.

T-test: This is a statistical test that rejects the null hypothesis if the level of significance of T is less than a certain threshold.

## 5. Hypotheses Testing

Table (1) below shows facts about the selected companies. a sample of the community listed companies in Borsa Istanbul, it appears that the significance level of 48%, which is more than 5%, is suggesting that there is no relationship between the CGR and the rate of profitability, so we accept the hypothesis  $H_0$  and say there is no relationship between the corporate governance and profitability.

Equation of companies:  $PR = -0.187 + 0.48 (CGR)$ .

R Square	Std. Error of Estimate	Significance Regression	Accepted Hypothesis
0.001	0.18337	48	$H_0$

Table 1: Hypotheses Testing of 43 Companies

## 6. Conclusion

Through the study, it was found that all the companies listed in the corporate governance index at the Borsa Istanbul have fully adhered to the principles of corporate governance approved by the Capital Markets Council, as all of them have received ratings higher than 7, which means that they have obtained good and very good ratings. But at the same time, there are many large Turkish companies that have a long history and a great reputation inside and outside the Turkish market, but they are not included in the corporate governance index and the reason may be that they did not apply to the rating companies to be evaluated, as they do not have the desire to enter the corporate governance index.

Through the study and the statistical tests that were carried out, and testing the hypothesis of the study, it was concluded that there is no clear statistical relationship between corporate governance and corporate profitability for an eight-year period from 2013 to 2020 for the study sample companies, which numbered 43 companies and were included in the corporate governance index in the Borsa Istanbul.

The researcher believes that the reason for the lack of a clear and explicit relationship between corporate governance and profitability in Turkish companies, is that Turkish companies are large and old companies and these companies are highly organized and disciplined, and therefore the concept of governance was a support for their system and not the basis, but it is certain that It did not have an impact on profitability, as it has an impact on creating a system for companies to ensure that there is no manipulation and fraud in the presentation to stakeholders and the disclosure of its results with complete transparency.

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