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Board Diversity and Compliance Practices

Diversidad del Consejo de Administración y Prácticas de Compliance
Diversidade do Conselho de Administração e Práticas de Compliance

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This study aimed to determine the incidence of diversity the board of directors in implementing compliance practices in Chilean companies. The research considers 1,322 reports on Social Responsibility and Corporate Governance. The results indicate that the degree of compliance practice adoption is partially explained by the diversity in the composition of the boards of directors of Chilean companies. Likewise, it was demonstrated that in Chile, there needs to be more concern on the part of the authorities in implementing practice for the composition of boards and that compliance is a mechanism that is increasingly present in the governance of companies.

Este estudio tuvo como objetivo determinar la incidencia de la diversidad del consejo de administración en la implementación de prácticas de cumplimiento en las empresas chilenas. La investigación consideró 1.322 informes sobre Responsabilidad Social y Gobierno Corporativo. Los resultados indican que el grado de adopción de prácticas de cumplimiento se explica parcialmente por la diversidad en la composición de los directorios de las empresas chilenas. Asimismo, se demostró que en Chile es necesario que haya mayor preocupación por parte de las autoridades en la implementación de prácticas para la composición de los directorios, y que el cumplimiento es un mecanismo cada vez más presente en el gobierno de las empresas.

Este estudo teve como objetivo determinar o impacto da diversidade do Conselho de Administração na implementação de práticas de conformidade em empresas chilenas. A pesquisa considerou 1.322 relatórios sobre Responsabilidade Social Corporativa e Governança Corporativa. Os resultados indicam que o grau de adoção de práticas de conformidade é parcialmente explicado pela diversidade na composição dos conselhos de administração das empresas chilenas. Mostraram também que no Chile há necessidade de maior preocupação por parte das autoridades na implementação de práticas para a composição dos conselhos, e que a conformidade é um mecanismo cada vez mais presente na governança corporativa.

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1. Introduction

Compliance has been a term with a clear definition of the obligations and procedures companies must carry out (Pascueli & Alcande, 2019). Gaudemet (2016) refers to it as a set of processes to ensure compliance with legal and ethical standards by companies, their leaders, and their employees. Additionally, studies on corporate governance compliance offer a wide range of qualitative and quantitative analyses that reveal the degree, scope, and dynamics of compliance (Okhmatovskiy, 2016; Shrives & Brennan, 2015), which brings with it benefits for those companies that contemplate these policies within their organization, because it implies better institutional performance, better service provision, and a higher standard of security and trust, which in turn generates greater prestige (Bedoya, 2017).

Practices related to compliance are incredibly beneficial, considering that adopting this type of policy positively influences the internal and external perspectives of public or private entities (Bedoya, 2017). For this reason, some describe it as a new global regulatory trend (Requena & Cárdenas, 2016; Michaelis et al., 2023) in the fight against regulatory non-compliance and prevention of criminal offenses.

Another concept that has been little explored in academic research is diversity, which goes beyond gender diversity and includes differences in age, ethnicity, sexuality, religious beliefs, and physical disabilities (Ghuri et al., 2021). Because, in those homogeneous councils, groupthink can be more limited; On the other hand, if there is gender diversity, the debates will be more intense, more profound, and interesting, and with a greater exchange of pluralist ideas (European Commission, 2012).

Studies related to diversity in the board regarding members of the female gender and foreign nationality indicate that these positively impact the organization's socially responsible behavior (Cuadrado et al., 2015). Likewise, Arenas et al. (2021b) point out that gender and nationality diversity encourages the adoption of good corporate governance practices within companies.

Relating this concept to Chilean companies, Arenas et al. (2021a) mention that the incorporation of the concept of gender, nationality, and age diversity on the boards of Chilean companies is insufficient because of the high homogeneity of its members, allowing the creation of a profile of the average Chilean director, which is mainly male, of Chilean nationality and reaches a high age range.

Based on the above, regarding the diversity and compliance variables, this research focuses on answering the following question: What is the incidence of board composition in the implementation of compliance practices in Chilean corporations?.

This situation becomes relevant given that companies with diverse boards of directors are more profitable than companies with non-diverse boards (Al-Rahahleh, 2017). In addition, they must recognize that the existence of diverse perspectives and values that reflect various experiences, skills, and characteristics is a strength that supports sustainable growth (Al-Rahahleh, 2017). Conversely, compliance also leads to better company reputation, better performance, higher return on investment, and higher market valuation (Kaspereit et al., 2015; Pothisarn et al., 2023).

KEYWORDS

Diversity; board; compliance; fraud; corporate governance; crime prevention model.

PALABRAS CLAVE

Diversidad; consejo de administración; compliance; fraude, gobierno corporativo, modelo de prevención de delito.

PALAVRAS-CHAVE

Diversidade; conselho de administração; conformidade; fraude, governo corporativo, modelo de prevenção de crime.

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However, the objective of this study is to determine the diversity of the administrative council in the implementation of compliance practices in the issuers of publicly offered securities in the Chilean stock market in 2015 - 2021.

2. Compliance and diversity in the board

2.1. What is and what does compliance involve?

Compliance is the set of procedures and good practices organizations adopt to identify and classify the operational and legal risks they face, establishing internal prevention, management, control, and reaction mechanisms against them. Likewise, according to ISO 19,600, "Compliance" results from an organization fulfilling its obligations and becoming sustainable over time, integrating itself into the organization's culture in the behavior and attitude of the people who work for it (International Organization for Standardization, 2014).

Similarly, authors such as Solis (2007) define it as an independent function that, through appropriate policies and procedures, detects and manages the risk of non-compliance with external and internal regulatory obligations of an organization. Therefore, the term "Compliance" can refer, as its name indicates, to the regulatory, internal, and external compliance of companies, where, through the management of corporate strategies, they will allow, among other things, to prevent and avoid conducts criminal activities of organizations.

Compliance programs are a handy preventive tool for companies that want to protect themselves from fraud or other actions that could damage their integrity. In the same way, the Spanish doctrine mentions that although the cost of compliance is high for companies, the cost of non-compliance is even higher (Garat, 2018).

It is worth mentioning that the adoption of codes of good practice has been one of the most influential trends in corporate governance over the last 20 years (Cuomo et al., 2015; Aguilera & Cuervo, 2004) in developed and emerging economies. It brings with it benefits that will have an impact on the positive development of the organization once they are implemented, some of which are: the external image of the company is favored, greater confidence is generated for shareholders, the control environment in the company is collaborating, and legal and ethical practices are promoted in the market (Castagnino, 2019).

Additionally, it should be noted that compliance does not focus solely on financial regulations (Jackman, 2015), but instead focuses on four regulatory areas, namely, anti-corruption, organized crime, competition law (such as information management and data protection), and lobbying. The latter refers to the intervention of an "agent" to manage the interests of its contracting party and is related to compliance because, depending on the legislation of each country and its regulation, it can constitute an illegal and non-transparent act (Bedoya, 2017).

Compliance is currently one of the most innovative and incipient concepts to incorporate into the management strategies and vision of any organization since the obligation that falls on companies to contribute is increasingly clear to the fight against corruption through the adoption of internal mechanisms aimed at preventing or detecting the conduct of its members or linked third parties. For this reason, compliance has ceased to be a voluntary option for many organizations and has become a requirement to be integrated into their strategy and internal structures to comply with legal precepts or to be able to protect themselves in situations that would put the stability and continuity of the organization's activity in serious trouble.

As for Chile, in the corporate sphere, many companies and organizations, given the evolution of the market and its complexity, have seen the need to reinvent themselves or protect themselves against operational and legal risks. The preceding step is to safeguard the responsibility and image of the company, giving rise to a context of trust and stability for current and future investors.

Finally, it is essential to remember that today's corporate compliance standards provide a viable model to limit defamation and protect entities from wrongdoing (Christina & Fort, 2020). Likewise, consider that an effective compliance system throughout the organization allows an entity to demonstrate its commitment to compliance with relevant laws, including legislative requirements, industry codes, organizational standards, good governance standards, corporate best practices, ethics, and community expectations; thus, the opportunity for an organization to be successful and sustainable over time (International Organization for Standardization, 2014).

2.2. Diversity of the board, how is Chile doing?

Diversity is not only correct, but also essential (Servaes et al., 2022); it refers to the human characteristics that distinguish individuals. Therefore, it can be understood as a heterogeneous group of members of various groups with different identities (Gama & Ramos 2020). Diversity has been progressively studied in administrative councils, particularly in terms of gender diversity (Mendoza et al. 2018). However, board heterogeneity should not be limited to gender (Nisiyama & Nakamura 2018). However, it must incorporate multiple diverse characteristics, such as directors' nationality, occupation, age, and ethnicity (Hillman 2015).

However, it must be taken into account that one of the issues most addressed by good governance codes at the international level is the composition and structure of the boards of directors. Different authors affirm that diversity motivates higher profits (Gordini & Rancati, 2017) and improves board independence and efficiency (Terjesen et al., 2016). Similarly, Rodríguez & Venegas (2018) mention that gender diversity leads to more robust business results and reduces risks by assuming better corporate behavior. In parallel, Abdullah (2014) points out that the spirit of diversity contributes to reducing the risk of groupthink by limiting managerial actions.

Regarding the incorporation of gender, nationality, and age diversity in the directories of Chilean companies, it should be noted that this is insufficient because of the high homogeneity of its members (Arenas et al., 2021b). However, the composition of companies' upper management levels is a relevant topic and is highly promoted by international organizations (Ben-Amar et al., 2017; Wang et al., 2016).

For example, studies related to female participation rates in the labor market indicate that, in Chile, between 2018 and 2021, there was a decrease of 3.2%, which can be explained by the health crisis

caused by the coronavirus and the economic recession. However, if we focus more generally on OECD countries, this decrease will only occur by 0.4% (Organization for Economic Cooperation and Development, 2022). On the other hand, Chile has a 14% female presence on its boards. Although it is above the 9% that Mexico showed in 2020, it is well below other developed countries such as the United States (28%), Spain (29%), the United Kingdom (35%), and especially France (45%). It should be noted that the boards of companies listed on the Chilean stock market have low diversity (Arenas et al., 2021a) in more developed countries, so there is still a long way to go.

Having said the above, diversity in senior positions is always an exciting topic (Kristanti & Iswandi, 2019), because better results can be achieved with a diverse board. However, not only should the gender variable be considered, but the topics of age and nationality should also be evaluated to discuss a diverse board.

In short, diversity within boards of directors is undeniable and offers clear benefits (De Leon, 2008). Therefore, this issue becomes relevant to implementing compliance practices in Chilean companies, considering that diversity is one of the dimensions of social responsibility on which the company is evaluated by its stakeholders (Sila et al., 2016, Kabara et al., 2023). Moreover, compliance also contributes to the socially responsible behavior of organizations (International Organization for Standardization, 2014), a vital resource for attracting investors and boosting economic growth.

3. Methodology

The research was conducted through a mixed approach, which consisted of collecting and analyzing quantitative and qualitative (Hernández et al., 2014). The type of research was descriptive-correlational (Hernández et al., 2014) and to evaluate the relationship between these variables, where the variation in one factor will not necessarily directly influence the other (Bernal, 2010). Regarding the research design, it should be noted that it was longitudinal (Hernández et al., 2014).

The universe of the study was extracted from the issuers of publicly offered securities that the Commission regulates for the Financial Market. Regarding the population, this corresponds to 1339 annual reports, of which, through a non-statistical probabilistic sampling for convenience, a sample of 1322 annual reports from entities that report the level of diversity of their boards of directors and their degree of trust was obtained from the adoption of compliance practices, according to General Regulation No. 386 on Social Responsibility, and No. 385 on Corporate Governance.

The analysis was carried out through multiple linear regressions, where incidence coefficients of the variables were determined: diversity of gender, nationality, and age, and their relationship with the degree of adoption of compliance practices, covering the periods 2015-2021.

Additionally, to more precisely identify the relationship between the variables under study, the economic sector and the Selective Stock Price Index (IPSA) were used as control variables, which allows for measuring the price variations of the largest and most liquid Chilean issuers listed on the Santiago Stock Exchange.

Table 1 presents the variables for the investigation, differentiating between the dependent, independent, and control variables. In addition, the criteria, description of the variables, type of measurement used in each, and references supporting the model are indicated.

Table 1. - Description of variables included in the regression model

| <i>Dependent variables</i> | | | |
|--|---|---|---|
| <i>Variable</i> | <i>Description</i> | <i>Measurement</i> | <i>Reference</i> |
| Degree of adoption of compliance practices in companies: - Excellent - Well - Acceptable - Scarce - Deficient | Evaluation of the effect of implementing compliance practices. | The results obtained are assigned one of the defined quintiles to create a multinomial variable. | - Bedoya (2017) - Gaudemet (2016) - SVS (2015a) |
| <i>Independent variables</i> | | | |
| <i>Variable</i> | <i>Description</i> | <i>Measurement</i> | <i>Reference</i> |
| Gender diversity: - Proportion of women in the board | Measurement of the degree of gender diversity in the boards of organizations | $\frac{\text{Number of women on the board}}{\text{Total board members}}$ | - Kahloul et al. (2022) - Al-Rahahleh (2017) - Mateos de Cabo (2017) |
| Nationality diversity: - Proportion of foreign in the board | Measurement of the degree of nationality diversity in the directory of organizations | $\frac{\text{Number of foreigners in the directory}}{\text{Total board members}}$ | - Arenas et al. (2021a) - Kristanti and Iswandi (2019) - Ghauri et al. (2021) |
| Age diversity: - Proportion under 40 years in the board - Proportion older than 70 years in the board | Measurement of the degree of age diversity in the directory of organizations. | $\frac{(\text{Number directors} \leq 40 \text{ years} + \text{Number directors} > 70 \text{ years})}{\text{Total board members}}$ | - Kahloul et al. (2022) - Hillman (2015) - SVS (2015b) |
| <i>Control variables</i> | | | |
| IPSA | Recognize if the company is within the Selective Price Index of Chilean Shares (IPSA) | If it corresponds to a company IPSA = 0; otherwise No IPSA = 1 | - Grover et al., (2019) - Mendoza et al. (2018). |
| Economic Sector | Identify to which economic sector the analyzed companies belong | Primary Sector (Extraction); Secondary Sector (Industrial); Tertiary Sector (Services) = 1 | - Arenas et al. (2022) - Fernández and Sarria, (2018) |

On the other hand, in order to carry out the study, the data of the dependent and independent variables were transformed into a Likert scale. The data was extracted from the corporate governance and social responsibility reports reported to the Chilean regulator, considering practices closely related to compliance and the diversity of the board of directors. Below, in order to determine the incidence of the diversity of the board of directors in the implementation of compliance practices, the following

hypotheses to be evidenced are detailed:

H₁. Gender diversity has a positive and significant impact on the degree of adoption of Compliance practices.

H₂. Nationality diversity has a positive and significant impact on the degree of adoption of Compliance practices.

H₃. Age diversity has a positive and significant impact on the degree of adoption of Compliance practices.

Finally, below is the model with the study variables described in **Table 1**.

$$G^{\circ} \text{Adop. Compliance}_{it} = \beta_0 + \beta_1 \text{Gender Diversity}_{it} + \beta_2 \text{Nationality Diversity}_{it} + \beta_3 \text{Age Diversity}_{it} + \beta_4 \text{IPSA}_{it} + \beta_5 \text{Economic sector}_{it} + \epsilon_{it}$$

Where the hypotheses are validated with the coefficients:

H₁: Gender Diversity; H₂: Nationality Diversity; H₃: Age Diversity

4. Results

The results obtained from the analyses conducted in this study are discussed in the next section.

4.1. Diversity and Compliance: A descriptive analysis

Table 2 presents the descriptive statistics referring to the degree of adoption of compliance practices and the variables of gender, nationality, and age diversity of Chilean public-offering securities issuers. When analyzing the data obtained, it was possible to observe that the adhesion by these companies concerning the practices established in NCG N°385 related to compliance was, on average, 46.8%, which means that the companies adopted between three to four practices related to the said topic within its corporate governance. At the same time, the above was analyzed on a Likert scale, yielding an average of 2.9, indicating that Chilean societies have an acceptable degree of practice adoption.

Regarding the gender diversity variable, it can be noted that its average was 8.3%, demonstrating that Chilean boards of directors are homogeneous, since the number of men within them reaches an average of 7.1, and that of women is 0.6. Therefore, it is impossible to find a woman within an administrative council. In addition, taking it on a Likert scale resulted in an average of 1.6, which indicates a scarcity of deficient gender diversity within the boards.

Regarding the diversity of nationality, an average of 10.7% was obtained, which reflects a homogeneous composition of the boards since, in general, if there are 6.9 Chilean directors, only 0.8 foreigners will be found, which shows that there is little to poor concern about integrating foreigners into their boards. Finally, on the topic of age diversity, an average of 25.9% was reached, which indicates that in Chilean boards of directors, there is no equity in the distribution of the ages of its members, since out of 5.8 directors who are between 41 and 70 years old, there are only 1.95 who are over 70 or under 40 years of age.

Table 2. - Descriptive Statistics Degree of Adoption of Compliance Practices

| Variable N= 1.322 | Mean | Min. | Max. |
|--|-------|------|--------|
| <i>Dependent variables</i> | | | |
| Degree of adoption of compliance practices | 46.8% | 0.0% | 100.0% |
| <i>Independent variables</i> | | | |
| <i>Gender</i> | | | |
| Degree of gender diversity | 8.3% | 0.0% | 80.0% |
| No. of male directors | 7.1 | 1.0 | 39.0 |
| No. of female directors | 0.6 | 0.0 | 8.0 |
| <i>Nationality</i> | | | |
| Degree of nationality diversity | 10.7% | 0.0% | 100.0% |
| No. of chilean directors | 6.9 | 0.0 | 38.0 |
| No. of foreign directors | 0.8 | 0.0 | 9.0 |
| <i>Age</i> | | | |
| Degree of age diversity | 25.9% | 0.0% | 100.0% |
| No. of directors under 30 years of age | 0.1 | 0.0 | 7.0 |
| No. of directors between 30 and 40 years old | 0.5 | 0.0 | 6.0 |
| No. of directors between 41 and 50 years old | 1.1 | 0.0 | 18.0 |
| No. of directors between 51 and 60 years old | 2.3 | 0.0 | 21.0 |
| No. of directors between 61 and 70 years old | 2.4 | 0.0 | 11.0 |
| No. of directors over 70 years of age | 1.4 | 0.0 | 11.0 |
| <i>Likert analysis</i> | | | |
| Degree of adoption of compliance practices | 2.9 | 1.0 | 5.0 |
| Degree of gender diversity | 1.6 | 1.0 | 5.0 |
| Degree of nationality diversity | 1.6 | 1.0 | 5.0 |
| Degree of age diversity | 2.7 | 1.0 | 5.0 |

4.2. Multiple Regression Analysis

In this section, correlation and multivariate regression analyses were carried out, where the incidence of the independent variables concerning the degree of compliance practice adoption can be identified.

Table 3 shows the correlations between the variables under study. It is worth mentioning that only those statistically significant relationships were considered; that is, those that reached a level of security between 95% (0.05*) and 99% (0.01**).

Table 3. - Correlations Analysis

| Variable N= 1.322 | Compliance practices | Gender diversity | Nationality diversity | Age diversity |
|-----------------------|-------------------------|---------------------|--------------------------|---------------|
| Compliance practices | 1.000 | | | |
| Gender diversity | 0.116*** | 1.000 | | |
| Nationality diversity | 0.079*** | 0.098*** | 1.000 | |
| Age diversity | 0.260 | -0.056** | -0.139*** | 1.000 |

Note. Bivariate correlations are significant at the 0.1 (*), 0.05 (**) and 0.01 (***) levels.

However, according to what is stated in **Table 4**, it was possible to observe that when applying Fisher's "F" global significance test, a $p \leq 0.05$ was obtained, which means that the variables under study are significant statistics. Regarding the adjusted definition coefficient (R^2 fitted), corresponding to 0.052, it can be noted that the degree of explanation of the model is low and limited since only 5.2% of the degree of adoption of compliance practices can be explained by the variable's diversity of gender, nationality, and age.

Regarding the incidence coefficients, it can be noted that both gender and age diversity were relevant factors that should be considered in the model since they present a level of significance $p \leq 0.05$, exerting an influence of 14.8%, and 6.2%, respectively in the degree of adoption of Compliance practices in Chilean public limited companies. Therefore, H_1 and H_3 are accepted. Regarding H_2 , this hypothesis is rejected because the results are inconclusive.

Likewise, when analyzing the control variables, it can be noted that only the effective stock price index (IPSA) is a relevant factor because it is the only one that presents statistical significance. The standard error was 0.327, which was the margin of error in the model equation.

Once the incidence of each variable concerning the degree of adoption of compliance practices was identified, considering the significant control variables and their standard errors, the model equation was created, as shown in **Table 4**.

Table 4. - Multiple Regression Analysis

| Variable N= 1.322 | Coefficient | Standard error | R^2 Fitted | Global significance |
|-----------------------|-------------|-------------------|--------------|------------------------|
| (Constant) | 2.796*** | 0.225 | 0.052 | 0.000 |
| Gender diversity | 0.148*** | 0.040 | | |
| Nationality diversity | 0.014 | 0.035 | | |
| Age diversity | 0.062** | 0.027 | | |
| IPSA CV | Yes | | | |
| Economic sector CV | No | | | |

Note. The variables are significant at the 0.1 (*), 0.05 (**) and 0.01 (***) levels.

5. Discussion of Results

Based on the results obtained, Chilean companies have little gender diversity on their boards of directors. This is confirmed by Arenas et al. (2022), who point out that stagnation is observed in Chile in terms of the diversity of the board of directors. According to Terjesen et al. (2015), government and political institutions are essential for developing norms to promote gender equality. Furthermore, Al-Rahahleh (2017) notes that one of the reasons for low gender diversity on boards is a lack of awareness of its potential benefits.

Likewise, regarding the nationality variable, a situation similar to the previous topic is presented since, on average, it is not possible to find a foreigner in Chilean companies, thus reflecting the homogenization of the directories, which can be detrimental to the entity. According to Abuhijleh et al. (2020), a greater diversity of nationality in the members of the board of directors has a positive impact on the company's commitment to social responsibility activities.

Concerning the age topic, the boards of Chilean securities issuers are mainly composed of members between the ages of 41 and 70, so there is limited age heterogeneity within the executive committee. According to Arenas et al. (2022), the diversity of Chilean boards is concentrated in the age range 50–70 years. However, this topic is yet to be explored in different investigations of diversity. Therefore, it was not possible to determine trends in this subject.

Now, regarding the level of adoption of compliance practices, this is acceptable among Chilean securities issuers, as pointed out by Pascueli & Alcande (2019), who affirm that compliance functions within companies are of moderate relevance in Chile because it is necessary to strengthen this field according to international trends, where the objective is not only the formal control of legal obligations but also allows the development of operations, decision-making, business management, and the prevention of risks. In addition, compliance programs in Chile have evolved in their treatment and importance, mainly since the enactment of Law No. 20,393 establishes the responsibility of legal persons and their subsequent modifications.

In contrast, Severino & Acuña (2019) mention that low compliance is the cause companies do not have better knowledge of the new actions they must carry out internally, which does not allow the generation of the necessary conditions for compliance with the actions declared in the standard. Bedoya (2017) states that only these preventive mechanisms currently allow companies to position themselves better and guarantee transparency in the services provided.

Finally, the variables studied explain only 5.2% of the model. Therefore, the remaining 94.8% is explained by variables that are not considered, which positively and significantly influence gender and age diversity, accepting H_1 and H_3 based on the coefficient of determination (adjusted R^2). The results are inconclusive regarding the diversity of nationality; thus, H_2 is rejected. In this context, Liang et al. (2023) point out that in specific markets, there could be a positive association between compliance and governance, clearly defining the market and industry to be analyzed.

6. Conclusion

According to the results obtained, the degree of compliance practice adoption is acceptable, while the degree of diversity on the board of directors is still insufficient. Additionally, gender and age diversity have a positive and significant impact on the adoption of compliance practices, exerting an influence of 14.8% and 6.2%, thus accepting H1 and H3. Regarding the diversity of the nationality variable, the results were not conclusive; therefore, H2 was rejected.

Additionally, through this research, the need for related regulations to promote diversity in decision-making bodies and strengthen standards of compliance and prevention of economic crimes was evidenced in Chile.

Finally, regarding diversity, future researchs should consider related issues such as ethnicity, religion, or sexual orientation. Similarly, more quantitative research is expected regarding the impact of compliance on different financial variables, such as accountability.

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