

## **Legal Dimension of Governance Effect on Strategic Decision making and Business Risk Reduction in Small Enterprises, the Kingdom of Saudi Arabia**

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### **Abstract**

*Many small enterprises lack efficiency of strategic decision making which led to enterprises' performance risk, delay in enterprises' growth and development as result of misleading information for financial reports users. The study is an attempt to investigate to what extent the application of legal dimension of governance affects the strategic managerial decision making in small enterprises in the Kingdom of Saudi Arabia. The study aimed to identify whether the application of legal dimension of governance reduces business risk in the enterprises. The data analysis results show that there is a statistically significant relationship between the legal dimension of governance and the efficiency of strategic decision making in small enterprises in the Kingdom of Saudi Arabia. The results also confirm that The legal dimension of governance reduces business risk in small enterprises in the Kingdom of Saudi Arabia.*

**Keywords:** *strategic decision making - legal dimension of governance - risk.*

### **1. Introduction**

The legal dimension of governance means the rules through which a company is leaded and directed; those rules include mechanisms of regulating various relations between the board of directors and executives, shareholders and stakeholders by establishing specific procedures for facilitating decision making process and giving it a character of transparency and credibility in order to protect shareholders' and employees' rights. Small enterprises face challenges in making managerial and strategic rational decisions because most of the decisions made are characterized by riskiness and uncertainty in accordance with certain circumstances and information and existence of many probabilities without availability of opportunities of their occurrence or their effect on a company's performance.

These decisions are also taken by individuals whose powers and responsibilities differ and whose attitudes towards risks vary. The decision maker may tend to ignore risk or be overly optimistic and pessimistic, and delay making decisions and miss many future opportunities. Organizations whose growth is based on their ability to manage projects do not accept that decision-making process is uncontrolled or based on subjective impressions, due to the negative impact this has on the small enterprise projects objectives and their performance in general. Therefore, commitment to the legal dimension of governance helps in developing a logical strategy of decision-making process, supporting skills, and investing in dialogue mechanisms. This study aimed to

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clarify the impact of commitment to the legal framework of governance in making managerial and strategic decisions, to identify to what extent these companies adopt and apply the principles of governance and comprehensive disclosure of information that concerns all stakeholders, so that they can make decision on their business and investment and interest in the small enterprises efficiently. Therefore, this study is an attempt to shed light on the significance of organizational and legal dimensions of governance in making strategic decisions that have great impact on investors, stakeholders and economy as a whole.

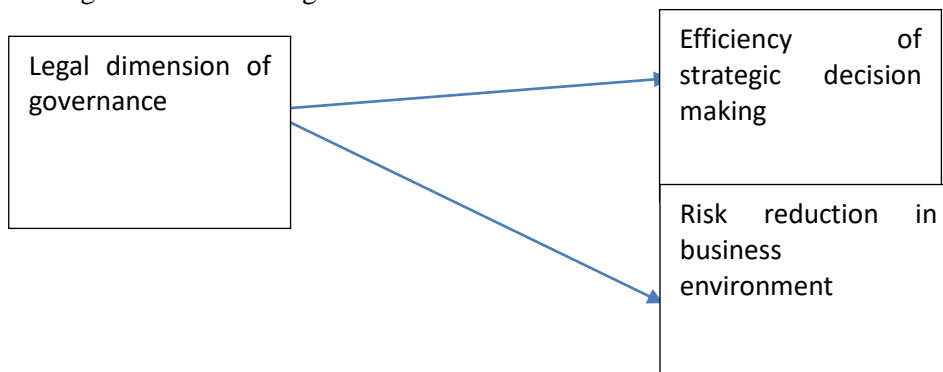
Al-Abbas (2012) investigates the role of corporate governance in reducing credit risk in the Saudi Banking Sector, Strategic Studies Center. The study concluded that the concept of governance is new in the Saudi environment, and that there are attempts to identify the mechanisms for applying it on the ground, and that audit committees in joint-stock companies play a role in applying it in the Saudi environment.

Many small enterprises lack efficiency of strategic decision making which led to enterprises' performance risk, delay in enterprises' growth and development as result of misleading information for financial reports users. As the appropriate and trusted information is very significant for making managerial and strategic decisions. The non-application of legal dimension of governance in small enterprises in the Kingdom led to problems in managerial and strategic decision making and this negatively affected the small enterprises' performance and growth. The lack of legal dimension of governance led to the failure of strategies and as result enterprises have not developed and many of them closed. Therefore, this study investigates to what extent the application of legal dimension of governance affects the strategic decision making and reduces business challenges.

## 2. Literature review

The legal dimension of governance is very important to ensure the efficiency of strategic decision making.

Figure (1): The legal dimension of governance and its relationship with the efficiency of strategic decision making and the risk reduction in business environment



### 2.1 Definition of governance

Michael (2005) defined governance as a case, process and orientation. It is also an immunity and protection system necessary for the control of movement, the direction and the safety of all actions and the fairness of behaviors inside the enterprise. It is such a managerial process exercised by the supervision management whether inside or outside enterprises through several stages. This process is based on ethics and conscience.

The definition includes the aspects of governance which are:

Wisdom: It provides direction and guidance.

Governing: It provides control over matters by establishing measures and restrictions.

Appealing: It includes referring to ethical and cultural reference and previous experience.

Litigating: It means seeking justice and preventing authority deviation and manipulation of shareholders' interests.

## 2.2 Advantages of the legal dimension of governance on managerial and strategic decision-making

The small enterprises that have applied the principles of corporate governance, this have been reflected positively on their performance in strategic management decisions and their performance on many objectives, the most important are (Zarqoun and Al-Omari, 2013):

1-Achieves transparency, justice, and protects the rights of shareholders in the company. This is done by establishing rules, regulations, and controls aimed at achieving transparency and justice.

2-Creates controls, rules and administrative structures that grant the right to hold the company's management accountable to the General Assembly and guarantee the enterprise's shareholders rights.

3-Develops investments by deepening investors' confidence in the financial markets.

4-Improves financial performance by holding management accountable to shareholders.

5-Imposes good and effective control over the performance of economic units to develop and improve competitiveness.

6- Combats unacceptable behavior, whether in the financial, administrative or moral aspect.

7-Ensures transparency in accounting and financial audit procedures to reduce and control corruption in the enterprise.

8-Develops, improves and helps decision makers such as managers and boards of directors to build a strategy.

9- Works to hold accountable and fight administrative and financial corruption in the enterprise in all its forms.

10- Applies the principle of good morals and humane and economic dealings between those who deal with the enterprise as ethical aspects are the most appropriate to support good governance.

## 2.3 Legal dimension of governance impact on performance efficiency

Al-Aziza (2009) explained the impact of the legal dimension of governance on performance efficiency in small enterprises as follows:

1-Cases of institutional success in America, Russia, and Asian countries.

2-The absence of a gap between management rewards and enterprise's performance.

3-Effectiveness of internal control procedures that cannot detect and prevent problems.

4-Strength of the Board of Directors can influence the executive and senior management and reduce the shortcomings in their ability to carry out successful management practices.

5- Provision of accuracy and transparency in preparing the final accounts.

6- Investors' ability to analyze and compare investment opportunities.

7- Strength of oversight by external parties of the enterprise, such as those in charge of drafting laws and auditors.

8-Reducing unethical practices by the Board of Directors, executive management and employees.

Governance helps small enterprises protect the interests of all parties, especially conflicting interests, preserve shareholders' rights, maximize the enterprise's profits and market value, and manage expected risk. Governance has internal and external components; the internal components are represented in the investment, legislative and regulatory environment and they consist of all the laws regulating enterprises' work and protection, in addition to the banking and supervisory environment. Internal components include the foundations that determine the decision-making mechanism and the distribution of powers and responsibilities within the enterprise between the Board of Directors and the executive director.

2.4 Dimensions of governance and their relationship with strategic decision-making:

Bou Al-Jazari (2015) investigates the role of governance mechanisms in financial decision-making, Algeria. The study concluded that the institution's achievement of a good turnover and market share with its competitors is the financial decisions that serve the objective of maximizing the owners' wealth and raising the market value of the shares, and they require mechanisms and principles of transparency, disclosure, accountability, and integrity as one of the most important elements needed by the financial statements and reports that ensure the proper application of the governance system.

2.5 Organizational dimension of governance impact on information quality

Ayyash (2018) investigates the impact of governance in activating investment decision in capital markets, Larbi Ben M'hidi University, Oum El Bouaghi, Al Bashaer Economic Journal, Algeria. The study concluded that governance has an important role on encouraging investment in capital markets by achieving the best levels of quality in accounting information in terms of appropriateness, credibility, and comparability, and by increasing understanding and interpretation in light of the investment environment's needs for information, impartial disclosure, reducing its asymmetry for all parties, and information for evaluating available investment opportunities, comparison between investment alternatives, and decision-making regarding the employment of resources.

The organizational dimensions of corporate governance have an effective impact on the quality of information systems and strategic decision-making through the application and practice of supervision, control, and ethical behavior; the strategic dimension increases the company's response speed to the business environment and crises,; organizational dimensions are represented in the following:

A- Supervisory and controlling dimension

The supervisory and controlling dimension of small enterprise governance is activated through shareholder assemblies exercising shareholder rights and increasing their contribution to improve the degree of transparency, disclosure and strategic decisions and putting pressure on the board of directors to do better in their work and create reassurance and confidence for shareholders.

B- Moral dimension

Ethical behavior is important in activating the supervisory role and strategic decisions. Professional bodies ask to establish a guide to ethical behavior that focuses on moral values and integrity that guarantee the enterprise's good reputation and credibility, in addition to their commitment to the enterprise's values and internal regulations (Suleiman, 2012).

### C- Strategic dimension

Strategic control is one of the systems upon which governance is based to reduce agency problems that exist at various administrative levels. It includes the formal setting of objectives, measuring performance and feedback, thus evaluating strategies and ensuring whether they lead to improving the return on invested capital in the long term and achieving efficiency, quality, innovation and responding to the desires of and customer needs.

Strategic control also aims to develop objectives to compare the enterprise's performance and then take corrective measures; it means that the lower administrative levels, as an agent, agree with senior management to maximize stockholders' wealth.

#### 2.6 Definition of decision making

The decision-making process is defined as selecting the appropriate alternative that is chosen from the other alternatives according to several criteria in light of the availability of an available set of resources in order to achieve a specific objective (Al-Alaq, 2008). The decision-making process can be viewed as a behavior or function that depends on selecting from the proposed alternatives and evaluated according to the information and data in the work environment related to the problem in search of a suitable alternative (Boutros, 2009).

The decision-making process is directly related to management functions such as planning, organizing, directing and controlling in a process that takes place at all organizational levels and in all activities (Al-Attyani and Al-Nazer, 2015).

#### 2.7 Challenges facing decision making

The decision-making process takes place to address existing problems, confront certain potential situations and cases, or achieve established objectives (Hars, 2012), and faces organizational, social, political, and cultural challenges. The application of governance principles in its various dimensions contributed to going beyond providing appropriate information for making administrative and strategic decisions in small enterprises.

Musaleh (2017) investigates management information systems and their role in strategic decision making, a case study of Proapjakumalang University, Indonesia. The study concluded that management information system contributes to decision-making by providing high-quality information in terms of credibility, accuracy, and comprehensiveness and providing an integrated infrastructure. During decision making, senior management adopts a strategy of information system as part of the general strategy.

Khreis (2020) investigates the impact of applying governance on decision-making in private Jordanian universities in the northern region, Middle East University, Jordan. The study concluded that applying governance dimensions in a mandatorily has a positive impact on the availability of information and personal skills of decision makers. It also leads to developing effective communication mechanisms between shareholders and the Board of Directors and discussing decisions and available information.

Al-Heini (2018) investigates the role of accounting information in improving the efficiency of decision-making in small and medium enterprises: a field study on small projects in Jordan, Al-Balqa University. The study concluded that there is a statistically significant relationship between accounting information and the efficiency of decision-making, whether during planning and control, or when identifying alternatives or when comparing between them and choosing the best.

### 3. Study methodology

The study, in order to answer the following questions:

1. To what extent does the legal dimension of governance affect the strategic decision making efficiency in small enterprises in the Kingdom of Saudi Arabia?

2. What is the effect of legal dimension of governance on reducing business risk that face strategic decision making in small enterprises in the Kingdom of Saudi Arabia?

The study verifies the following hypotheses:

1. There is a statistically significant relationship between the legal dimension of governance and the efficiency of strategic decision making in small enterprises in the Kingdom of Saudi Arabia?

2. There is a statistically significant relationship between the legal dimension of governance and business risk reduction in small enterprises in the Kingdom of Saudi Arabia?

3. There is a statistically significant relationship between the legal dimension of governance and the efficiency of performance in small enterprises in the Kingdom of Saudi Arabia?

The mean, Chi-square and T-test were used to measure the study sample individuals responses to the questionnaire that was distributed to them in small enterprises in the Kingdom of Saudi Arabia.

#### 3.1 Study method and tools

The analytical and descriptive approach was used to measure to what extent the commitment to corporate governance improves strategic decision making in small enterprises in the Kingdom of Saudi Arabia through collecting primary and secondary data from previous literature (previous research and studies) in addition to preparing a study tool a questionnaire designed to an electronic link and directed to a random sample of small enterprises in the Kingdom of Saudi Arabia. The link was also distributed to a number of a pilot sample of managers and employees of small enterprises in the Kingdom. It was also sent to a number of specialized experts to benefit from their opinions and suggestions, in order to verify the validity and reliability of the questionnaire. The validity and reliability of the tool was confirmed using the Cronbach Scale.

#### 3.2 Study population

The study population consisted of the small enterprises, including a group of commercial, service, and industrial enterprises in Khamis Mushait city.

#### 3.3 Study sample

The study sample was (73) individuals. (68) of the questionnaires which have been distributed to a random sample of the small enterprises were answered by (93%) of the study population.

#### 3.4 Study limits

Spatial limits: Khamis Mushait city.

Time limits: 2022/2023.

#### 4. Study results

##### 4.1 Data analysis

Table (1): The mean, degree of freedom, chi-square and t-test for the hypothesis one: There is a statistically significant relationship between the legal dimension of governance and the efficiency of strategic decision making in small enterprises in the Kingdom of Saudi Arabia

No.	Statement	Mean	DF	Chi-Square	T-test
1	The legal dimension of governance contributed to the effectiveness of decision making.	4	4	76.643 <sup>a</sup>	42.908
2	The legal dimension of governance means that there are systems for the relations between the basic parties in an enterprise.	4	4	63.214 <sup>a</sup>	41.812
3	The legal dimension of governance helps in developing the personal skills of decision makers.	4	4	58.000 <sup>a</sup>	42.565
4	The legal dimension of governance provides the shareholders with trusted information.	4	4	51.714	38.836
5	The legal dimension of governance contributes to the managerial, financing and investing decision making optimally in terms of source and cost.	4	4	39.071 <sup>a</sup>	35.812
6	The legal dimension of governance develops effective communication mechanisms between shareholders and the board of directors to discuss decisions and information available.	4	4	45.357 <sup>a</sup>	37.831
7	The legal dimension of governance contributed to the effectiveness of decision making.	4	4	59.214 <sup>a</sup>	42.830

Source: Prepared by the researcher using the field study data 2023.

The table (1) above shows values of the mean, degree of freedom and chi-square of the study sample answers for the statements as follow:

1. The mean was (4), degree of freedom (4), chi-square (76.643<sup>a</sup>) and t-test (42.908) for the statement (The legal dimension of governance contributed to the effectiveness of decision making). This result indicates that the degree of need was (great).
2. The mean was (4), degree of freedom (4), chi-square (63.214<sup>a</sup>) and t-test (41.812) for the statement (The legal dimension of governance means that there are systems for the relations between the basic parties in an enterprise). This result indicates that the degree of need was (great).
3. The mean was (4), degree of freedom (4), chi-square (58.000<sup>a</sup>) and t-test (42.565) for the statement (The legal dimension of governance helps in developing the personal skills of decision makers). This result indicates that the degree of need was (great).

4. The mean was (4), degree of freedom (4), chi-square (51.714<sup>a</sup>) and t-test (38.836) for the statement (The legal dimension of governance provides the shareholders with trusted information). This result indicates that the degree of need was (great).

5. The mean was (4), degree of freedom (4), chi-square (39.071<sup>a</sup>) and t-test (35.812) for the statement (The legal dimension of governance contributes to the managerial, financing and investing decision making optimally in terms of source and cost). This result indicates that the degree of need was (great).

6. The mean was (4), degree of freedom (4), chi-square (45.357<sup>a</sup>) and t-test (37.831) for the statement (The legal dimension of governance develops effective communication mechanisms between shareholders and the board of directors to discuss decisions and information available). This result indicates that the degree of need was (great).

7. The mean was (4), degree of freedom (4), chi-square (59.214<sup>a</sup>) and t-test (42.830) for the statement (The legal dimension of governance contributed to the effectiveness of decision making). This result indicates that the degree of need was (great).

Table (2): The mean, degree of freedom, chi-square and t-test for the hypothesis two: There is a statistically significant relationship between the legal dimension of governance and the reduction of business risk in small enterprises in the Kingdom of Saudi Arabia

No.	Statement	Mean	DF	Chi-Square	T-test
1	The legal dimension of governance reduces the contradiction in the objectives between the parties related.	4	4	57.429 <sup>a</sup>	43.336
2	The legal dimension of governance provides quality in accounting information in terms of the appropriateness, credibility and comparability and increases the understanding and interpretation in light of business environment needs.	4	4	67.214 <sup>a</sup>	44.680
3	The legal dimension of governance enhances information comparability and increases understanding and interpretation in business environment.	4	4	58.571 <sup>a</sup>	41.553
4	The legal dimension of governance determines relations and boundaries separating between powers and responsibilities.	4	4	63.786 <sup>a</sup>	43.698
5	The legal dimension of governance enhances neutral disclosure of information and reduces its asymmetry for all parties.	4	4	37.286 <sup>a</sup>	37.617
6	The legal dimension of governance contributes to the control in small enterprises.	4	4	46.786 <sup>a</sup>	40.462
7	The legal dimension of governance helps to assess investment opportunities available and prefer	4	4	52.571 <sup>a</sup>	40.711



	between investment alternatives and make decision related to resource employment.				
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Source: Prepared by the researcher using the field study data 2023.

The table (2) above shows values of the mean, degree of freedom and chi-square of the study sample answers for the statements as follow:

1. The mean was (4), degree of freedom (4), chi-square (57.429<sup>a</sup>) and t-test (43.336) for the statement (The legal dimension of governance reduces the contradiction in the objectives between the parties related). This result indicates that the degree of need was (great).

2. The mean was (4), degree of freedom (4), chi-square (67.214<sup>a</sup>) and t-test (44.680) for the statement (The legal dimension of governance provides quality in accounting information in terms of the appropriateness, credibility and comparability and increases the understanding and interpretation in light of business environment needs). This result indicates that the degree of need was (great).

3. The mean was (4), degree of freedom (4), chi-square (58.571<sup>a</sup>) and t-test (41.553) for the statement (The legal dimension of governance enhances information comparability and increases understanding and interpretation in business environment). This result indicates that the degree of need was (great).

4. The mean was (4), degree of freedom (4), chi-square (63.786<sup>a</sup>) and t-test (43.698) for the statement (The legal dimension of governance determines relations and boundaries separating between powers and responsibilities). This result indicates that the degree of need was (great).

5. The mean was (4), degree of freedom (4), chi-square (37.286<sup>a</sup>) and t-test (37.617) for the statement (The legal dimension of governance enhances neutral disclosure of information and reduces its asymmetry for all parties). This result indicates that the degree of need was (great).

6. The mean was (4), degree of freedom (4), chi-square (46.786<sup>a</sup>) and t-test (40.462) for the statement (The legal dimension of governance contributes to the control in small enterprises). This result indicates that the degree of need was (great).

7. The mean was (4), degree of freedom (4), chi-square (52.571<sup>a</sup>) and t-test (40.711) for the statement (The legal dimension of governance helps to assess investment opportunities available and prefer between investment alternatives and make decision related to resource employment). This result indicates that the degree of need was (great).

Table (3): The mean, degree of freedom, chi-square and t-test for the hypothesis three: There is a statistically significant relationship between the legal dimension of governance and the efficiency of performance in small enterprises in the Kingdom of Saudi Arabia

No.	Statement	Mean	DF	Chi-Square	T-test
1	The legal dimension of governance determines the gap between management wards and enterprises' performance.	4	4	52.214 <sup>a</sup>	40.679
2	The legal dimension of governance provides effective internal control procedures and detects mistakes.	4	4	53.357 <sup>a</sup>	40.655
3	The legal dimension of governance strengthens the board of directors and reduces the shortage in its ability.	4	4	48.357 <sup>a</sup>	39.390
4	The legal dimension of governance	4	4	55.214 <sup>a</sup>	42.679

	provides accuracy and transparency in preparing final accounts.				
5	The legal dimension of governance increases investors' ability to analyze and compare investment opportunities.	4	4	56.357 <sup>a</sup>	44.655
6	The legal dimension of governance strengthens an enterprise's external parties control.	4	4	43.357 <sup>a</sup>	32.390
7	The legal dimension of governance reduces unethical practices.	4	4	53.214 <sup>a</sup>	4.679

Source: Prepared by the researcher using the field study data 2023.

The table (3) above shows values of the mean, degree of freedom and chi-square of the study sample answers for the statements as follow:

1. The mean was (4), degree of freedom (4), chi-square (52.214<sup>a</sup>) and t-test (40.679) for the statement (The legal dimension of governance determines the gap between management rewards and enterprises' performance). This result indicates that the degree of need was (great).

2. The mean was (4), degree of freedom (4), chi-square (53.357<sup>a</sup>) and t-test (40.655) for the statement (The legal dimension of governance provides effective internal control procedures and detects mistakes). This result indicates that the degree of need was (great).

3. The mean was (4), degree of freedom (4), chi-square (48.357<sup>a</sup>) and t-test (39.390) for the statement (The legal dimension of governance strengthens the board of directors and reduces the shortage in its ability). This result indicates that the degree of need was (great).

4. The mean was (4), degree of freedom (4), chi-square (55.214<sup>a</sup>) and t-test (42.679) for the statement (The legal dimension of governance provides accuracy and transparency in preparing final accounts). This result indicates that the degree of need was (great).

5. The mean was (4), degree of freedom (4), chi-square (56.357<sup>a</sup>) and t-test (44.655) for the statement (The legal dimension of governance increases investors' ability to analyze and compare investment opportunities). This result indicates that the degree of need was (great).

6. The mean was (4), degree of freedom (4), chi-square (43.357<sup>a</sup>) and t-test (32.390) for the statement (The legal dimension of governance strengthens an enterprise's external parties control). This result indicates that the degree of need was (great).

7. The mean was (4), degree of freedom (4), chi-square (53.214) and t-test (40.679) for the statement (The legal dimension of governance reduces unethical practices). This result indicates that the degree of need was (great).

#### 4.2 Findings and recommendations

The researcher concluded the following results:

1. There is a statistically significant relationship between the legal dimension of governance and the efficiency of strategic decision making in small enterprises in the Kingdom of Saudi Arabia.
2. The legal dimension of governance reduces business risk in small enterprises in the Kingdom of Saudi Arabia.
3. The legal dimension of governance enhances the efficiency of performance in small enterprises in the Kingdom of Saudi Arabia.

Recommendations:

The study recommends the following:

1. Small enterprises in the Kingdom of Saudi Arabia should apply the legal dimension of governance.
2. Small enterprises in the Kingdom of Saudi Arabia should work to reduce business risk.

## 5. Conclusion

The study investigated the legal dimension of governance effect on strategic decision making and business risk reduction in small enterprises, the Kingdom of Saudi Arabia. Many small enterprises lack efficiency of strategic decision making which led to enterprises' performance risk, delay in enterprises' growth and development as result of misleading information for financial reports users. The study is an attempt to investigate to what extent the application of legal dimension of governance affects the strategic managerial decision making in small enterprises in the Kingdom of Saudi Arabia.

The study verified the hypotheses and concluded the following results:

There is a statistically significant relationship between the legal dimension of governance and the efficiency of strategic decision making in small enterprises in the Kingdom of Saudi Arabia. The legal dimension of governance reduces business risk in small enterprises in the Kingdom of Saudi Arabia. The legal dimension of governance enhances the efficiency of performance in small enterprises in the Kingdom of Saudi Arabia.

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